SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 53136 / January 18, 2006

Admin. Proc. File No. 3-11953

In the Matter of the Application of

ALVIN W. GEBHART, JR.
and
DONNA T. GEBHART

c/o Charles F. Goria
Goria & Weber
7863 La Mesa Blvd. Suite 201
La Mesa, CA 91941

For Review of Disciplinary Action Taken by
NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION -- REVIEW OF DISCIPLINARY PROCEEDING

Violations of Securities Laws and Conduct Rules

Fraudulent Sale of Securities

Sale of Unregistered Securities

Failure to Provide Written Notice to, and Obtain Prior Approval from, Member Firm Employer Regarding Private Securities Transactions

Registered representatives of member firm of registered securities association engaged in private securities transactions without giving prior written notification to, or obtaining prior approval from, member; sold unregistered securities; and made material misrepresentations and omissions in the sale of securities. Held, association's findings of violation and the sanctions imposed are sustained.

APPEARANCES:

Charles F. Goria, of Goria and Weber, for Alvin W. Gebhart, Jr. and Donna T. Gebhart.

Marc Menchel, James S. Wrona, and Michael J. Garawski, for NASD.

Appeal filed: June 15, 2005
Last brief received: September 21, 2005

I.

Alvin W. Gebhart, Jr. ("Gebhart") and his wife Donna T. Gebhart ("D. Gebhart"), both formerly associated with Mutual Service Corporation ("MSC"), an NASD member firm, appeal from NASD disciplinary action. NASD found that, from 1997 to 2000, the Gebharts violated the antifraud provisions and registration requirements of the federal securities laws, as well as NASD rules, in offering and selling over $2 million in unregistered promissory notes. 1/ NASD barred Gebhart and fined D. Gebhart $15,000 and suspended her for one year. 2/

In its decision, NASD found that the promissory notes were securities, that no registration statement was in effect as to the notes, and that no exemption applied to the Gebharts' sales. NASD found further that the sales of the notes constituted private securities transactions and that the Gebharts neither provided MSC with written notice of the sales nor obtained MSC's prior, written approval as required by NASD rules. Additionally, NASD found that the Gebharts violated the antifraud provisions by, among other things, recklessly representing to their clients that the notes would be secured by deeds of trust on real property that contained sufficient equity to pay all claims in the event of default, when, in fact, deeds of trust for most of the notes were never recorded and the properties were substantially overencumbered, with the result that the

---

1/ NASD found that the Gebharts violated Section 5 of the Securities Act of 1933 (requiring registration of certain securities), Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder (prohibiting fraud in the offer and sale of securities), and NASD Conduct Rules 2110 (requiring adherence to just and equitable principles of trade), 2120 (prohibiting fraud in the offer and sale of securities), and 3040 (prohibiting involvement in a private securities transaction outside the regular course or scope of employment without providing prior written notice to the member firm).

2/ NASD imposed two separate one-year suspensions on D. Gebhart (one year for private securities transactions and sales of unregistered securities and one year for violations of federal and NASD antifraud provisions) that were to be served concurrently. NASD also assessed costs against the Gebharts, jointly and severally, in the amount of $5,141.21.

notes were generally unsecured. We base our findings on an independent review of the record, except with respect to those findings not challenged on appeal.

II.

This case involves promissory notes issued by MHP Conversions, LLC ("MHP"). MHP was formed in late 1996 to facilitate the conversion of mobile home parks to resident ownership by Community Service Group ("CSG"). CSG, owned by James Scovie and his wife, would identify the owners of mobile home parks and solicit their interest in selling the park, meet with residents and solicit their interest in purchasing the park using various "special financing" options, and broker the transfer of ownership. By 1995, CSG began effecting the transfer of ownership by purchasing the parks itself and then helping the residents buy the property from CSG. MHP was created by Scovie and his associate, a real estate broker named David Mounier, supposedly to facilitate this operation by serving as the issuer of promissory notes that were sold to individual investors to raise the funds necessary for the purchases of these parks. MHP does not appear to have had any employees of its own and was operated by Scovie and CSG personnel in the CSG office.

The Promissory Notes Issued by MHP

The notes issued by MHP had one-year terms (because closing was normally expected to occur within one year of the notes' issuance) and paid interest rates of 18% for new investments and 14% on reinvested funds. 3/ Each promissory note stated that it would "ultimately be secured by a deed of trust" on the park to be purchased, but that "[u]ntil such time as said deed of trust is recorded, the sole asset of [the issuer] will be a deed of trust for the property known as Eastern Trailer Park . . . in the amount of $100,000." 4/ The notes also stated that they were "non-recourse to Payor," i.e., the notes on their face warned investors that their only remedy for default was against the property securing the note and not against the issuer. No registration statement was filed with the Commission by MHP for the notes it issued.

3/ New investments earned 11% interest per annum, calculated and paid monthly, and a 7% "bonus" paid at maturity; clients who reinvested their funds after maturity could choose between earning 10% per annum with a 4% maturity bonus, or 11% per annum with a 3% bonus. Before MHP was formed, CSG issued certain promissory notes with essentially identical terms, but those notes are not at issue in this proceeding, as explained in note 8, infra.

4/ All notes issued by MHP purported to be secured by this interest in Eastern Trailer Park, which was described only as "located at 213 El Cajon Blvd, El Cajon, CA consisting of a 33 space trailer park"; however, the record indicates that MHP never owned an interest in Eastern Trailer Park.

The record is ambiguous as to whether MHP was conducting a legitimate business during the period at issue. The record indicates that, for most of the three years of MHP's existence, noteholders received their promised interest payments, and MHP returned the principal to at least some investors who decided not to reinvest their funds when their notes matured. However, the characteristics of the MHP note program are consistent with those of a "Ponzi" scheme, in which returns are paid to investors out of funds raised from subsequent investors, rather than from profits generated by any real business. Because the books and records of MHP are not part of the record, the source of funds used to pay investors is unknown.

Irrespective of the initial success of MHP, it is clear that MHP's latter years, at least, were marred by fraud: it is undisputed that very few of the deeds of trust purportedly securing the MHP notes were recorded, despite representations to the contrary. It is also clear that, by the time MHP ultimately collapsed in early 2000, most, if not all, of the mobile home parks supposedly serving as security for the MHP notes were substantially overencumbered.

The Gebharts Learn About the Trailer Park Note Program

Gebhart, who had worked for Prudential Insurance Company from 1980 to 1994, began working at Mutual of New York ("MONY") in early 1994 selling variable annuities and mutual funds. 5/ While working at MONY, Gebhart met Jack Archer, a fellow MONY salesman. 6/ Archer had learned about CSG's park-conversion business from Mounier, one of his financial advisory clients, and in 1994 began assisting CSG in finding buyers for the promissory notes. Gebhart testified that Archer, an ex-Marine and Vietnam veteran, was highly regarded by MONY office staff and supervisors, and that he "had no reason to think anything different of him."

In late 1995, Archer had a short discussion with Gebhart in which Archer briefly described CSG's trailer park program and asked if Gebhart would be interested in it. 7/ Gebhart responded equivocally, but when Archer contacted him again to ask if he knew anyone who might be interested in investing, Gebhart said that he would call some of his clients and find out if they were interested in purchasing notes from Archer. 8/

5/ Gebhart was registered as an investment company products / variable contracts representative. He became registered as a general securities representative on December 10, 1997.

6/ Archer was a named respondent in these proceedings but defaulted and, based on that default, was barred by NASD from associating with any member firm.

7/ Gebhart testified that Archer described it as a "program that did mobile home park conversions where people became owners of their parks."

8/ By early 1996, Gebhart had introduced three of his clients to Archer, each of whom eventually purchased notes from Archer: one client invested $25,000 on January 19,

(continued...)

The Gebharts Join MSC

In late January 1996, Gebhart left MONY to join MSC. Soon after, on February 14, 1996, D. Gebhart also became associated with MSC. 9/ The Gebharts opened a branch office in Rancho Bernardo, California, where they sold insurance and mutual funds and provided financial planning services.

During their first year with MSC, the Gebharts received from MSC a compliance manual and marketing materials, and Gebhart acknowledged that he read and understood the compliance policies and procedures in the manual. Included in that manual was a requirement that "outside business activities must always be reported to the Compliance Department," and, in the case of private securities transactions, await written approval before proceeding to "engage in private securities transactions outside the regular course or scope of their association or employment." A later version of the manual, the contents of which the Gebharts acknowledged by signature in September 1996, further clarified MSC's policy on private securities transactions, noting that representatives may not offer any security not listed on MSC's approved product list, including "alleged non-securities 'deals,'" without "advance written specific permission" from MSC.

On October 2, 1996, the Gebharts themselves invested $7,000 in notes issued by CSG. 10/ Soon after, on October 23, 1996, Archer contacted the Gebharts to ask if they were interested in selling notes directly to their clients. The Gebharts had a lengthy discussion with Archer about the details of the note program. Gebhart testified that, during that discussion, Archer "explained the entire program," including "the due diligence that [Archer] had done

---

8/ (...continued)
1996; another invested $10,000 on April 26, 1996; a third client invested $10,000 on May 10, 1996 and $20,000 on October 3, 1996. Gebhart received $5,720 as a "finder's fee" for introducing these clients to the program. Although NASD's complaint and the record developed encompass Gebhart's involvement in, and potential liability for, these earlier sales of CSG-issued notes, in its two decisions (issued by an NASD Hearing Panel and its National Adjudicatory Council), NASD based findings of violation exclusively on the Gebharts' actions with respect to the notes issued by MHP from 1997 to 2000.

9/ D. Gebhart was registered as an investment company products / variable contracts representative when she joined MSC; she became registered as a general securities representative on April 27, 1998.

10/ The Gebharts also made five subsequent investments in notes issued by MHP: $5,939.51 on February 13, 1997; $6,462.17 on March 9, 1998; $13,417.92 on September 2, 1998; $6,918.98 on March 29, 1999; $15,000 on May 20, 1999; and $14,550.62 on September 30, 1999. Although the Gebharts' note purchases total nearly $70,000, the record indicates that some of these note purchases were simply reinvestments of funds from matured notes.

behind it and he explained that the firm running it had gone through the necessary documentations [sic], that it had been approved by the IRS to be held in pensions, other reinforcement docs, things like that." Gebhart also testified that Archer told the Gebharts that "all of the governmental agencies were involved, even San Diego County." According to D. Gebhart, Archer told them that "the parks were in good shape"; "had a lot of equity in them"; were only "45 to 55 percent leveraged"; and "had ten investors or less [sic]" per park. D. Gebhart also testified that in that meeting she "wanted to make sure that these notes or trust deeds were secured and [Archer] assured us that they were always secured . . . . I don't remember word-for-word what the man said, but he came to us and he was a pension administrator, a Pacific Life former manager, and we always looked at him as being probably further up in the – obviously more experienced in stuff than we had [sic]."

Gebhart testified that Archer told the Gebharts that the notes did not present "a security issue" because they were second deeds of trust and the parks "always" had fewer than ten investors. 11/ Gebhart also testified that Archer told him that, in 1994, Archer had a conversation about the notes with a MONY compliance officer, who told Archer the notes could be sold "without objection." 12/ Nevertheless, Archer suggested the Gebharts contact MSC's compliance department before selling the notes "to avoid the selling away problem" and encouraged the Gebharts to be open and forthcoming with their firm.

The Gebharts Contact MSC's Compliance Department

That same day, Gebhart telephoned MSC's compliance department and spoke to the Director of Compliance, Michael Poston. Gebhart testified that he had a relatively lengthy conversation with Poston in which Gebhart explained the program in detail, disclosed that he would be receiving commissions on the sales, and answered "a lot" of questions from Poston.

11/ The Gebharts never knew, and never asked, about the holders of the first deeds of trust secured by the mobile home parks. They also never knew, or asked about, whether the properties were encumbered by any other liens.

12/ In a deposition in a related civil case, Archer testified that he approached a MONY compliance officer, whose name and appearance he forgot, about the notes at the conclusion of a compliance seminar in August 1994. Archer "told the gentleman that I had a client who was converting mobile home parks to resident ownership and that I was going to be or was considering raising – arranging loans between my two clients, Dave Mounier from Community Service Group and my other client base. . . ." The compliance officer asked several questions and supposedly concluded that "he did not see a problem with it." However, Archer also testified that there was no discussion about whether the notes were securities, and admits that, although the compliance officer recommended that Archer run the program by the MONY compliance department, Archer never did so. It is undisputed that Archer never submitted written notice of his activities to MONY, and never received written approval from MONY to sell the notes.

According to Gebhart, Poston said the program "sounded like a good idea" and asked to see more information. Poston, on the other hand, testified that the call was "a casual five-minute conversation" in which Gebhart told him "very little" about the promissory notes. Although Poston's recollection of the phone call is markedly different from that of the Gebharts, the parties agree that Poston did not give permission to the Gebharts to sell the notes during that telephone call.

The next day, the Gebharts sent a brief letter via overnight courier to Poston enclosing a package of materials about CSG and its mobile home park conversion business, which Archer had provided in his recent meeting with the Gebharts. 13/ The Gebharts testified that they forwarded to Poston "everything that Mr. Archer gave [them]," including a sample promissory note and a "brochure" created by Scovie and Mounier that included a printout from CSG's website describing its park-conversion business, several local newspaper articles that reported successful park conversions, and several one-page descriptions of converted parks. Gebhart also recalled sending Poston a copy of "pro forma" financial information for one park conversion that provided a brief projected cash flow analysis and an investment summary that sketched the outlines of CSG's plan to borrow funds to convert the park. MHP was mentioned in these materials only in that the company's name appeared on the cover of the brochure along with CSG's. It is undisputed that Poston never responded to the Gebharts' letter and never gave either oral or written permission to the Gebharts to sell the notes. 14/ It is also undisputed that the Gebharts made no further efforts to inform Poston or anyone else in MSC's compliance department about their plans to sell the notes, and that no one in the firm's compliance department ever authorized those sales either orally or in writing.

13/ The Gebharts' letter to Poston consisted of four sentences:

> Pursuant to our phone conversation, [sic] this morning, please find enclosed the information on the Trailer Park Program. Please review this information, and please let me know what you think of it.
>
> Should you have any questions, please do not hesitate to call me. Thank you.

14/ Poston's recollection of the materials he received differed from the Gebharts' description. Poston testified that the package contained only three or four newspaper articles and a few abstracts of converted parks; he "didn't know what to make of it," and thought that the "whole letter . . . looked like a joke, practically." The Hearing Panel made no credibility finding related to the telephone conversation between the parties, but found that it "believed [Gebhart's] testimony that the material he sent to Mr. Poston at Mutual Service included everything he had received from Mr. Archer. . . ." We need not resolve the disparity between the testimony of the Gebharts and Poston because, as we noted above, the parties agree on the critical facts: neither Poston nor anyone else in MSC's compliance department gave permission to the Gebharts to sell MHP notes either during the telephone call or in response to the Gebharts' letter.

The Gebharts Sell MHP Notes

Hearing nothing from Poston since their October 1996 phone call, 15/ the Gebharts began offering and selling promissory notes issued by MHP to their clients in early 1997. All the clients to whom the Gebharts offered and sold MHP notes were individuals. The Gebharts' presentations were based on the information they received from Archer, on the payment history of their own note, and on visits the Gebharts paid to two trailer parks. 16/ When asked about what investigation he conducted before presenting the MHP notes to clients, Gebhart responded:

> I did visit two parks, the one in my town where I lived and also the one in El Cajon. I felt in talking with Jack [Archer] and his representations, the documentation that I had received from him, the things that I sent to Mutual Service Corporation letting them know, thinking if there was an issue, they would be in touch with me. If there wasn't [sic] something I wasn't doing right, they would say, "Fix this. Do that." I would do that. So up until the first note, I thought I had done what I believed was the proper due diligence.

Both of the Gebharts together usually made a presentation to clients regarding the notes and normally distributed copies of the CSG brochure and a sample MHP note to their clients. 17/ The brochure briefly described CSG's business and included several local newspaper articles on CSG's park conversions and some cursory descriptions of properties converted by CSG; it contained no information on MHP other than its address and telephone number (which it shared with CSG) or on the MHP notes. Information on the MHP note program that clients received

---

15/ When asked why he waited a few months after calling Poston before making his first sale, Gebhart responded, "There was no – I don't know. There was no parks. There was no clients. There was nobody – we just didn't do it."

16/ Gebhart testified in a civil deposition in a related case:

> What we did is I went up to the Flinn Springs trailer park, drove in, looked around to see the quality of it, to see if it's there, if it's a bona fide piece of real estate, there were mobile homes on it, people living in those mobile homes, whether it was upkept – kept up. Same thing in Aviation. I drove in, looked around, see if there's people living there, if mobile homes were there. In fact, they were.

17/ D. Gebhart testified that she considered Gebhart to be the "overseer" and her "mentor." He tended to do most of the talking during client presentations, but she did much of the "detail work." They shared responsibility for fielding client phone calls, reviewing correspondence and client account statements, and were "both familiar with their [clients'] investments or strategies," so that if Gebhart were unavailable, D. Gebhart could "answer their questions."

therefore came only from the sample MHP notes themselves and from oral presentations by the Gebharts.

The Gebharts considered the MHP notes to be one of a “variety of investment strategies” and offered it to their clients as one alternative that would “fit in [their] portfolio[s], based on their objectives.” The Gebharts presented the MHP program as an option for some investors who needed a substantial, fixed monthly income. For example, investor Maribeth Trogdon, a recent widow with two dependent children whose only income was from a part-time teaching job, testified in a deposition in a related civil case that the Gebharts recommended that she invest a large portion (more than a third) of the life insurance proceeds from her husband’s death into MHP notes to replace her husband’s income. 18/ Notes that Trogdon made in preparation for the deposition state that “[t]he investment was presented to me as a proven, long term way for me to receive a substantial monthly income.” Investors also testified that the Gebharts told them that the Gebharts had invested their own money in the notes and that the program had been so far successful. Investor Donald Townsend, a retiree looking to supplement his retirement income “to take care of the bills,” testified that Gebhart represented that MHP was “basically solvent and steadily growing[,] obtaining more parks[,] and had been paying the monthly interest with no problems.” At the hearing, Gebhart confirmed that he believed the trailer park program was a successful venture because he “didn’t hear any complaints” from the three clients he had referred to Archer in early 1996.

Investors also testified that the Gebharts informed them that the MHP notes would be secured by recorded deeds of trust, and that the parks would serve as sufficient collateral to secure all investments in the event of default. For example, Townsend testified, “I was told that [MHP] would purchase the mobile home parks with the money that’s being loaned to them and that they would eventually secure the property with trust deeds. . . .” Investor Larry Tickel, a disabled former Wal-Mart store manager, testified that the Gebharts assured him that “there was no risk because [the note] was secured by a deed of trust and then that [the parks] would not be overbought. So that way, if they had to sell the place, we would still get our money back.” 19/ The Gebharts’ recollection of their statements to clients is consistent with the testimony of their

---

18/ Although NASD declined to rely on investor testimony in its decision because the Hearing Panel made no credibility determinations as to investor testimony given at the hearing or in civil depositions, we choose to include it. The Hearing Panel made no finding that the investors’ testimony was unreliable and actually made use of investor testimony in at least one instance in its decision. Further, where, as here, there are similarities among the investors’ testimony regarding the salespersons’ behavior, the reliability of that testimony is strengthened. See Frank J. Custable, Jr., 51 S.E.C. 643, 648 (1993). Given that the Gebharts’ own testimony is also consistent with that of the investors, we find no reason to ignore this evidence.

19/ Following up, the NASD attorney asked Tickel, “Is that what Mr. Gebhart told you, that there was no risk?” Tickel responded, “Right.”

clients. Gebhart testified that he told clients, "If they invested into [an MHP note] they would get a recorded deed of trust. If the worst case scenario came down they would be part owners of that park." D. Gebhart similarly testified, "If [clients] asked us about it, either [Gebhart] or I would say the type of thing it is; they are mobile home park conversions. We would give them the knowledge we had about them and we would tell them that they would own a piece of the park . . . . [I]f it was like worst case scenario, if something happened and the park were to default, we all would own a portion and we could be able to sell the park and we would all get cashed out."

The Gebharts did not have, and did not pass on to clients, any specific information about MHP's or CSG's management, income, or financial condition. Nor did the Gebharts possess, determine, or recite to clients any specific information about the properties that were to be purchased with the investors' borrowed funds other than the address of the parks to be purchased. According to D. Gebhart, she didn't require more specific information because "[i]t was always our understanding that [MHP] wouldn't have done a conversion on a park that wasn't – that didn't have good cash flow and that would be a deal worth them doing." D. Gebhart testified that she simply "had faith with everybody that was involved that it was a good program."

When a client decided to purchase an MHP note, the Gebharts would collect a check from the client, make a copy of that check, and then call Archer. Archer, who had told the Gebharts not to contact MHP or CSG directly, served as the "middle man" between the Gebharts and MHP/CSG: Archer would deliver the clients' checks to MHP and then return a promissory note to the Gebharts, who would then transmit the MHP note to their clients, usually by mail. 20/ MHP did not provide copies of the deeds of trust supposedly securing the notes unless an investor requested one, and very few investors made such a request. 21/ The Gebharts recalled seeing at least one copy of a client's trust deed, but did not recall seeing any recording information. The Gebharts testified that they maintained records of the MHP note purchases in their client files and in their office transaction logs.

20/ The Gebharts corresponded with their customers using letterhead that stated "Securities offered by Mutual Service Corporation." At least one investor testified in a deposition in a related civil case that, when she asked the Gebharts how she could be sure the money she was putting toward the MHP note "isn't being sent to Tahiti," the Gebharts replied that MSC "looks at all our business . . . and would tell them if there was anything incorrect by law."

21/ The Gebharts never requested, nor received, a copy of the deeds of trust securing their own promissory notes.

The Gebharts understood that Archer was sharing his commissions with them. 22/ For investments of new money into an MHP note, Archer paid the Gebharts a commission of 6-7%; for MHP notes purchased with reinvested funds, the Gebharts received 3-4%. 23/ Archer paid the Gebharts their commissions with checks drawn on his personal bank account.

MSC's 1997 Audit of the Gebharts' Office

From January through August 1997, the Gebharts sold eleven MHP notes totaling $378,195, including a $5,939.51 investment of their own money. On August 20, 1997, the Gebharts completed a Compliance Survey in which they acknowledged that they received and understood MSC's compliance procedures, notified MSC of any outside business relationships, and did not engage in any private securities transactions. The Gebharts did not report their MHP note sales, or the commissions they earned for those sales, to MSC. 24/

On November 17, 1997, MSC audited the Gebharts' office as part of MSC's normal practice. The Gebharts testified that they made available to the auditor their transaction logs, which contained line item entries for their clients' MHP note purchases, and client files, some of which contained copies of MHP notes. If the auditor noticed the MHP transactions, he did not raise any concerns. At this time, the Gebharts each completed an audit questionnaire that requested information on whether the Gebharts, among other things, received compensation from outside sources, participated in the offer of promissory notes, or split commissions with any person. The Gebharts checked "no" in response to all of these questions and did not otherwise report any of their MHP transactions on the form.

22/ The record contains inconsistencies about the Gebharts' knowledge of the commissions that they understood Archer to be earning. Gebhart testified that before he sold his first MHP notes, he understood that he "would be getting 50 percent" of what Archer made. However, Gebhart also testified that he did not know how much Archer was being paid by MHP and did not ask, considering it a "private issue."

23/ Gebhart testified that Archer renegotiated the amount of commission the Gebharts were paid: it decreased from 7% to 6% for new money and from 4% to 3% for reinvested money in January 1998; this seems to correspond to a decrease in commissions that MHP paid to Archer.

24/ The Gebharts earned $7,401.00 in commissions for their sales in 1997.

The Gebharts' Sale of MHP Notes in 1998 and 1999

The Gebharts continued to offer and sell MHP notes to their clients throughout 1998: customers purchased over $425,000 in notes that year, 25/ for which the Gebharts earned over $50,000 in commissions. Nevertheless, the Gebharts completed MSC's Compliance Survey in July 1998 in which they made no disclosures about their sales of MHP notes and certified that they had not engaged in any private securities transactions without written approval from MSC's Compliance Department.

On September 14, 1998, the Gebharts instructed their administrative assistant to contact MSC's operations department to inquire whether funds held in a tax-qualified, 403(b) retirement account could be used to purchase an MHP note. The Gebharts' assistant faxed a sample MHP note to a staff member in MSC's operations department, and, upon MSC's request, also provided MHP's contact information. On September 24, 1998, the Gebharts received a fax from the operations department approving the MHP notes for holding in a 403(b) account and giving instructions on filing the necessary paperwork before funds could be released. The client on whose behalf the Gebharts made this inquiry ultimately decided not to invest in the MHP notes, but Gebhart testified that two other clients later did so using retirement account funds, and the paperwork for these purchases cleared MSC's operations department without comment. It is undisputed, however, that MSC's compliance department, which was given the responsibility for approving outside business activities in the firm's compliance manual, was not involved in the review of these transactions; moreover, as the Gebharts' administrative assistant testified in a civil deposition, the inquiry to MSC's operations department was made for the sole purpose of finding out what paperwork was needed to effect the transaction.

On February 1, 1999, the Gebharts completed MSC Representative Questionnaires in anticipation of a second visit from MSC's auditor. 26/ The Gebharts certified on the questionnaires that they had not engaged in any private securities transactions. These forms also asked whether the representative "issued or participated in any offering of general partnership interests, commercial paper, promissory notes, or joint venture participations" other than through the firm; both the Gebharts checked "yes" and wrote in "2nd deeds of trust." 27/ In response to this same question in 1997, the Gebharts had checked "no." When asked why he gave a different

---

25/ This amount excludes the $36,469.60 that the Gebharts themselves purchased in 1998.

26/ Although the Gebharts testified that, as with the 1997 audit, they made available to the auditor their transaction logs and client files that contained some evidence of MHP transactions, the auditor, if he took note of them, did not comment on the transactions.

27/ D. Gebhart also added "Investment by Rep. & Clients" after "2nd deeds of trust" in her response to this question.

answer to the same question in 1999 than he did on an identical form in 1997, 28/ Gebhart replied, "The only answer is I had a better understanding of the form then." D. Gebhart testified that in 1997 she believed the question sought information only on new activity that had not before been disclosed to MSC, whereas in 1999 she thought that because they "started doing more of them" they should disclose it on the form. 29/

In late 1999, the Gebharts each completed a Compliance Survey in which they acknowledged that they had not engaged in any private securities transactions without prior written approval from MSC's Compliance Department. 30/ The Gebharts sold over $1.5 million in MHP notes in 1999, 31/ earning $75,723.00 in commissions.

MHP Collapses

The Gebharts sold another $213,731.51 in MHP notes in early 2000. On January 15, 2000, Scovie was diagnosed with brain cancer. In April 2000, MHP ceased making interest payments on the notes. In an April 4, 2000 letter to MHP noteholders, Scovie stated that his absence from the daily operations of CSG and MHP was causing "cash flow problems" and that he intended to liquidate all assets and distribute proceeds to the companies' creditors. The Gebharts learned in May 2000 that MHP had secured only $605,000 worth of notes with recorded deeds of trust and that, as they reported in a letter to MSC describing the collapse of the MHP note program, "all of the mobile home parks appear[ed] to be substantially overencumbered." When MHP collapsed, the Gebharts' clients had over $1.5 million invested in outstanding notes, and the Gebharts themselves had about $36,000 invested. MSC launched an

---

28/ As noted previously, in 1998 the Gebharts had also acknowledged by signature, on a different form, that they had "not engaged in private securities transactions as defined in MSC's Policy and Procedures Manual without written approval from the MSC Compliance Department."

29/ Although the auditor testified that he discussed the "2nd deeds of trust" with the Gebharts and was told that the Gebharts and "only a few" of their clients had invested in the deeds through a "third party," neither of the Gebharts recall the discussion with the auditor. It is undisputed, however, that the auditor conducted no further inquiry into the matter and did not raise the issue with Poston, his supervisor. The Hearing Panel found it "unlikely that [the auditor] irrefutably remembered the audit and the conversations that he had with the Respondents."

30/ MONY's compliance department became aware of Archer's sales of MHP notes in mid-1999, informed Archer that his activities constituted private securities transactions, and insisted that he terminate his relationship with MHP. Archer did not tell the Gebharts about MONY's determination.

31/ This figure excludes the $36,469.60 in MHP notes the Gebharts purchased themselves.

investigation of the matter, with which the Gebharts fully cooperated, which resulted in their termination by MSC on August 11, 2000.

The Gebharts took steps to recover the money that they and their clients had invested, including eventually filing a petition for involuntary bankruptcy against MHP and suing their own professional liability insurer, with the result that the Gebharts' clients recovered approximately 84% of their losses. The Gebharts also may have recovered some portion of their own investment, although the record is unclear as to the extent of that recovery. 32/

III.

The Gebharts are charged with the fraudulent sale of unregistered securities without approval from MSC, in violation of the federal securities laws and regulations and NASD rules. Because all of these violations depend upon a finding that the promissory notes issued by MHP were securities, we turn first to that question.

Securities Act Section 2(a)(1) defines the term "security" as, among other instruments, "any note." 33/ In Reves v. Ernst & Young, 34/ the Supreme Court stated that "the phrase 'any note' should not be interpreted to mean literally 'any note,' but must be understood against the backdrop of what Congress was attempting to accomplish in enacting the Securities Acts." 35/ "Congress' purpose in enacting the securities laws was to regulate investments, in whatever form they are made and by whatever name they are called," and Congress "enacted a definition of

---

32/ Although the record indicates that the Gebharts participated in the bankruptcy, they claimed below that they declined to recover the funds they had invested with MHP in order to maximize recovery by their clients. They further claim to have paid, out of their own funds, substantial legal fees to help their clients recover their investments. The Gebharts, however, have introduced no evidence to support these assertions, leaving us without a basis on which to credit them.

33/ 15 U.S.C. § 77(b)(a)(1).

34/ 494 U.S. 56 (1990).

35/ Id. at 63. Reves involved the definition of a security in the Exchange Act. The Court noted that the Securities Act contained a virtually identical definition and reaffirmed that the coverage of the two statutes may be considered the same. Id. at 61 n.1.

'security' sufficiently broad to encompass virtually any instrument that might be sold as an investment." 36/ Thus, we focus on whether the notes in question resemble an investment. 37/

The "family resemblance" test adopted in Reves controls our inquiry into whether a note constitutes an investment and is therefore subject to regulation under the securities laws. The test identifies four relevant factors: 1) the motivations that would prompt a reasonable seller or buyer to enter into the transaction; 2) the plan of distribution of the instrument; 3) the reasonable expectations of the investing public; and 4) the presence or absence of a factor such as another regulatory scheme that significantly reduces the risk of the instrument, thereby rendering application of the federal securities laws unnecessary. 38/ A note is presumed to be a security under this test, 39/ and that presumption may be rebutted only if the four-factor analysis reveals either that the note bears a strong resemblance to certain types of notes recognized as non-securities or that the note should be added to this list. 40/

The Gebharts state incorrectly that "the initial test is whether the subject instrument is includable within one of six categories of notes that are automatically deemed to be non-securities" and that the "second test" is the "four-part" or "family resemblance" test. The four-factor inquiry governs whether a note resembles one of the categories of notes deemed non-securities as well as whether a note should be added to that list because "[i]t is impossible to make any meaningful inquiry into whether an instrument bears a 'resemblance' to one of the instruments identified [as non-securities] without specifying what it is about those instruments that makes them non-'securities.'" 41/ Accordingly, we apply the four-factor analysis to evaluate the Gebharts' claim that the notes, as notes purportedly secured by deeds of trust on real property,

---

36/ Id. at 61 (emphasis in original).

37/ McNabb v. SEC, 298 F.3d 1126, 1131 (9th Cir. 2002).

38/ 494 U.S. at 66-67.

39/ Id. at 67.

40/ Id. The Court deemed the following notes to be non-securities: 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, a short-term note secured by an assignment of accounts receivable, the note that simply formalizes an open-account debt incurred in the ordinary course of business, and the note evidencing a loan by a commercial bank for current operations. Id. at 65 (quoting Exchange Nat'l Bank v. Touche Ross & Co., 544 F.2d 1126, 1138 (2d Cir. 1976) and Chemical Bank v. Arthur Anderson & Co., 726 F.2d 930, 939 (2d Cir. 1984)).

41/ Reves, 494 U.S. at 65-66 (emphasis in original); see also id. at 67 (stating that a showing that a note bears a strong resemblance to one of the categories of notes considered non-securities is to be made "in terms of the four factors" identified by the Court).

fall within the category of "notes secured by a mortgage on a home" that are deemed non-securities. 42/

As discussed below, this four-factor analysis reveals that the MHP notes do not sufficiently resemble a "note secured by a mortgage on a home" to be considered a non-security under that category. The Supreme Court contemplated only mortgage-backed notes issued in the context of a traditional face-to-face transaction between a borrower and commercial or consumer lender. 43/ We find, based on the four Reves factors, that the MHP notes do not fit within this classification. 44/

42/ Cf. SEC v. Wallenbrock, 313 F.3d 532, 537-40 (9th Cir. 2002) (applying four-factor test to notes ostensibly secured by accounts receivable even though defendant argued that the notes were exactly like the "short-term notes secured by an assignment of accounts receivable" excluded from the definition of a security in Reves); see also Mercer v. Jaffe, Snider, Raitt and Heuer, P.C., 736 F. Supp. 764, 769 (W.D. Mich. 1990) (rejecting argument that the "first mortgage notes" at issue were per se non-securities and that the court need not even consider the four-factor "family resemblance" test given that the Supreme Court listed "the note secured by a mortgage on a home" as a non-security), aff'd on other grounds sub nom. Schriemer v. Greenberg, 931 F.2d 893 (6th Cir. 1991) (Table) and aff'd on other grounds, 933 F.2d 1008 (6th Cir. 1991) (Table).

43/ See Mercer, 736 F. Supp. at 769-70 (stating that the Supreme Court in Reves intended the example of a "note secured by a mortgage on a home" to apply only to mortgage-backed notes in the context of a traditional face-to-face loan transaction between a borrower and commercial or consumer lender, and concluding that, in terms of the Reves factors, the "first mortgage notes" at issue bore little resemblance to the mortgage-backed note given by a borrower to his lender in a typical home equity loan transaction); see also Pollack v. Laidlaw Holdings, Inc., 27 F.3d 808, 812 (2d Cir. 1994) (finding, for reasons that would become clear as the court addressed the Reves factors, that the instruments at issue did not sufficiently resemble the traditional note secured by a home mortgage to be exempt from regulation under the securities laws).

44/ The Gebharts argue, citing Proschaska & Assocs. v. Merrill Lynch Pierce Fenner & Smith, Inc., 798 F. Supp. 1427, 1430 n.2 (D. Neb. 1992), that we must consider the notes on the basis of what they would have been but for the fraud and that, but for the fraud, the notes resembled "notes secured by a mortgage on a home." The Reves analysis, however, demonstrates that the notes were bought and sold as "investments" regardless of the fraud. Thus, the notes are subject to regulation as securities. See Reves 494 U.S. at 68-69 (stating that the fundamental essence of a security is its character as an investment).

1. Motivations of Seller and Buyer

The first Reves factor is an objective inquiry into "the motivations that would prompt a reasonable seller and buyer to enter into [the transaction.]" 45/ The instrument is likely to be a security if the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate. 46/ The note is less sensibly described as a security if the note is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties, or to advance some other commercial or consumer purpose. 47/

a. Seller's motivation

MHP sold the notes to raise money for the general use of a business enterprise; it used the noteholders' funds to purchase trailer parks as part of its core business of converting such parks to resident ownership. 48/ We reject the Gebharts' contention that this use is not a general business use because noteholders provided their funds "as purchase money loans for the purchase of specific real estate." The noteholders testified explicitly that they did not care in which park MHP invested their money. MHP's use of their money constituted a general business use notwithstanding that MHP purportedly gave each noteholder an interest in a specific park in return for their funds; at the core of the transaction, the noteholders, in return for a high rate of interest, provided MHP with funds for its business of financing trailer park purchases. 49/

45/ Wallenbrock, 313 F.3d at 538 (alteration in original).

46/ Reves, 494 U.S. at 66.

47/ Id.

48/ See Stoiber v. SEC, 161 F.3d 745, 749-50 (D.C. Cir. 1998) (finding that the seller's "use of the note money to buy an inventory of commodities" was "appropriately viewed as a general business use" "[b]ecause the purchase of commodities for reselling was at the core of [seller's] business"); Frank Thomas Devine, Securities Exchange Act Rel. No. 46746 (Oct. 30, 2002), 78 SEC Docket 2528, 2536 (finding that the seller's use of investors' money to buy viatical insurance contracts was "appropriately viewed as a general business use" because the purchase of such contracts "was at the core of [seller's] business").

49/ See Wallenbrock, 313 F.3d at 538 (finding that an issuer sold notes for the general use of a business enterprise even though investors provided the issuer with half the cost of a specific account receivable and received a note purportedly secured by that receivable because, at the core of the transaction, the investors, seeking to make a significant profit, provided the issuer with cash for its business of buying accounts receivable).

b. Buyer's motivation

The noteholders' testimony that they invested in the notes for the promised 18% return in the form of interest payments establishes that the noteholders were interested primarily in the profit the notes were expected to generate. 50/ "'[P]rofit' in the context of notes" means "'a valuable return on an investment,' which undoubtedly includes interest." 51/ The noteholders' desire for a valuable return on an investment is further evidenced by their testimony that they viewed the notes as investments rather than real estate loans and purchased the notes as "part of my investment portfolio" or to "supplement my income with monthly distribution." Further evidence of the noteholders' investment intent stems from their reliance on the Gebharts for financial planning and investment advice and the Gebharts' recommendation of the notes in connection with this advice. 52/ We reject the Gebharts' contention that a desire for profit did not motivate the noteholders because "they were not promised any capital appreciation; nor was the rate of interest keyed to the profits of the enterprise." In Reves, the Supreme Court declined to limit the definition of profit to either "capital appreciation" or "a participation in earnings." 53/

2. Plan of Distribution

The second Reves factor is an examination into the "plan of distribution" of the note "to determine whether it is an instrument in which there is common trading for speculation or

---

50/ See John P. Goldsworthy, Exchange Act Rel. No. 45926 (May 15, 2002), 77 SEC Docket 2025, 2035 (finding that the customers who purchased the notes were motivated by a desire for profit because most of the customers identified the promised ten percent interest rate as a primary reason for investing in the notes); Devine, 78 SEC Docket at 2536 (stating that the noteholders purchased the notes "with the expectation of profit based on the 21% to 25% interest rates purportedly offered").

51/ Reves, 494 U.S. at 68 n.4.

52/ See Robin Bruce McNabb, 54 S.E.C. 917, 922 (2000) (stating that the fact that the customers obtained the notes from a financial advisor as part of an investment portfolio is also evidence of investment intent); Stephen J. Gluckman, 54 S.E.C. 175, 180-81 (1999) (stating that further evidence of investment intent stemmed from the investors' reliance on the respondent, their "financial advisor," for recommendations and suggestions on instruments to add to their investment portfolios).

53/ Reves, 494 U.S. at 68 n.4; see also SEC v. Edwards, 540 U.S. 389, 395-96 (2004) (rejecting notion that "profits" for purposes of determining whether an instrument constitutes an "investment contract" are limited to either capital appreciation or a participation in earnings).

investment." 54/ The requisite "common trading" is established if the instrument is offered and sold to a broad segment of the public. 55/ The Gebharts sold over 100 notes worth more than $2 million to about forty-five clients. Archer sold notes to a similar number of customers. We find that such sales constitute sales to "a broad segment of the public." 56/ The fact that the investors who purchased notes from the Gebharts were not linked in any way except as customers of the Gebharts and MSC further supports this conclusion. 57/ Accordingly, the distribution of the notes to a "broad segment of the public" establishes common trading. 58/

We reject the Gebharts' contention that no common trading existed because there was no secondary market in the notes, no client sold the notes to a third party, and the notes expressly prohibited resale without the issuer's permission. The notes do not expressly prohibit resale in

---

54/ Stoiber, 161 F.3d at 750 (citing Reves); McNabb, 298 F.3d at 1132 (same). The Gebharts state incorrectly that a plan of distribution requires common trading for speculation and investment. Reves refers to common trading for speculation or investment. The noteholders bought the notes as investments. See, e.g., infra text preceding note 64.

55/ Stoiber, 161 F.3d at 750 (citing Reves); McNabb, 298 F.3d at 1132 (same).

56/ See Jim Newcomb, Exchange Act Rel. No. 44945 (Oct. 18, 2001), 76 SEC Docket 172, 177 (finding that respondent engaged in a plan of general distribution by selling ninety notes worth $1 million to more than forty-seven investors); cf. Eagle Trim, Inc. v. Eagle-Picher Industries, Inc., 205 F. Supp. 2d 746 (E.D. Mich. 2002) (finding no plan of distribution for a single note given by the purchaser of assets to the seller in exchange for a loan to finance the purchase because plaintiffs did not allege that the note was offered to any other party, that there was any common trading, or that the note was acquired for speculation or investment purposes); Singer v. Livoti, 741 F. Supp. 1040 (S.D.N.Y. 1990) (finding no plan of distribution for a single note given to a single lender).

57/ Deal v. Asset Mgmt. Group, Fed. Sec. L. Rep. (CCH) ¶ 97,244 (N.D. Ill. 1992), 1992 U.S. Dist. LEXIS 13011, at *12-13 (stating that allegations of a plan of distribution involving an offering to at least six investors who were not linked in any way except as customers of the defendant firm gave rise to a reasonable inference that the investors were from a broad segment of the public).

58/ An additional factor supporting the finding of common trading is that the Gebharts sold the notes to individual investors. Courts have indicated that the sale of notes to individual investors suggests common trading due to "the purchasing individual's need for the protection of the securities laws." See SEC v. Global Telecom Services, LLC, 325 F. Supp. 2d 94, 114-15 (D. Conn. 2004) (stating that "where the notes are sold to individual investors rather than 'sophisticated institutions,' common trading has been found"); see also Stoiber, 161 F.3d at 751 (stating that respondent's sales to individual investors rather than "sophisticated institutions" suggested common trading).

any way, and the absence of secondary trading is not determinative. As discussed above, the sale of the notes to numerous individual investors, representing a broad segment of the public, establishes common trading. 59/

3. Reasonable Expectations of the Investing Public

Under the third Reves factor, we "must determine whether the promissory notes in question are reasonably perceived by the investing public as securities." 60/ "Whether notes are reasonably perceived as securities generally turns on whether they are reasonably viewed by purchasers as investments." 61/ We "must look to a reasonable investor, not the specific individuals in question." 62/ "When a note seller refers to notes as 'investments,' prospective purchasers may reasonably regard them as investments, absent contrary indications." 63/ Here, the Gebharts characterized the notes as investments repeatedly. For example, the Gebharts wrote one prospective investor that they were "attach[ing] additional information about the trailer park investment," included the notes on another investor's "Suggested Investment Choices and Considerations," and listed the notes on client statements entitled "Investment Portfolio."

59/ See Goldsworthy, 77 SEC Docket at 2036 (stating, where the notes did not prohibit secondary market trading, that the lack of proof of such trading was "not determinative," and finding that the sale of the notes to individual retail customers indicated common trading); cf. Banco Espanol de Credito v. Sec. Pac. Nat'l Bank, 973 F.2d 51, 55 (2d Cir. 1992) (finding no common trading in loan participations sold only to institutional investors because prohibition on resale without the express written permission of the issuer prevented loan participations from being sold to the general public and thus limited eligible buyers to those with the capacity to acquire information about the debtor).

60/ McNabb, 298 F.3d at 1132. Courts "will consider instruments to be 'securities' on the basis of such public expectations." Reves, 494 U.S. at 66. This factor, therefore, is described as a "one-way ratchet." It allows notes that would not be deemed securities under the other three factors nonetheless to be treated as securities if the public has been led to believe they are, but does not allow notes which would otherwise be deemed securities to escape regulation. Stoiber, 161 F.3d at 751.

61/ Stoiber, 161 F.3d at 751.

62/ McNabb, 298 F.3d at 1132; Wallenbrock, 313 F.3d at 539. We note, however, that the third Reves factor "is closely related to the first factor – motivation for the transaction – and thus considerations discussed vis-a-vis that factor also come into play here." Wallenbrock, 313 F.3d at 539. We highlighted the noteholders' investment intent, as exemplified by their testimony that they viewed the notes as investments rather than real estate loans, in considering the first factor. See supra text following note 51.

63/ McNabb, 54 S.E.C. at 924 (citing Reves, 494 U.S. at 69 and Stoiber, 161 F.3d at 751).

Gebhart also testified that he recommended the notes as "a type of investment vehicle," that he "indicated it would fit in [clients'] portfolio[s], based on their objectives," and that he "presented [the notes] as one alternative, as an investment strategy that might meet [clients'] goals." We find that prospective purchasers would reasonably view the notes as investments, and that therefore the investing public would reasonably perceive the notes as "securities." 64/

4. Need for Application of the Federal Securities Laws

The fourth and final factor in the Reves analysis is whether some factor, such as the existence of another regulatory scheme, significantly reduces the risk of the instrument, thereby rendering application of the federal securities laws unnecessary. 65/ The Gebharts argue that California real estate law provides such an alternative regulatory scheme by regulating offers or sales of notes secured by trust deeds encumbering the same real property. The protections afforded by California law to lenders making real estate loans secured by trust deeds, however, do not render the protections of the federal securities laws unnecessary to individual investors investing in unsecured notes recommended and sold to them by securities professionals. 66/

64/ See McNabb, 54 S.E.C. at 924 (finding that investing public would reasonably consider the notes at issue to be investments where seller listed notes as "invested assets" on a noteholder's balance sheet and identified himself as a Registered Investment Advisor in correspondence pertaining to the notes); Devine, 78 SEC Docket at 2536-37 (finding that investors reasonably understood that the notes at issue were investments where seller testified that the loans were "investment money," used the term "to invest" in connection with making the loans, and detailed how his clients "invested . . . risk capital" in the notes). We reject the Gebharts' contention that the investing public would not consider the notes to be investments because the noteholders could only receive the stated fixed interest rate. See Pollack v. Laidlaw Holdings, Inc., 27 F.3d 808, 814 (2d Cir. 1994) (finding that the fixed interest rate neither justified characterizing the noteholders' motivations as anything but investment nor altered the reasonable expectations of investors, pursuing a conservative investment strategy through registered securities professionals, that they were protected by the federal securities laws).

65/ Reves, 494 U.S. at 67.

66/ See Pollack, 27 F.3d at 814-15 (2d Cir. 1994) (finding that New York law governing collateralized mortgages did not reduce the risk of purportedly secured mortgage participations bought for passive, unsophisticated investors by their investment adviser because the "[i]nvocation of protections that might apply to the more usual mortgage loan distorts the character of these transactions" where the investors "held uncollateralized, speculative participations in mortgages and had not engaged in the usual process for extending such a loan"); McNabb, 54 S.E.C. at 924-25 (finding that "the protection of the federal securities laws should apply to the holder of the note secured by a deed of trust"

(continued...)

We also reject the Gebharts' argument that a significant risk-reducing factor existed because the notes "were to be collateralized." Collateralization can be a risk-reducing factor, 67/ but these notes were not actually collateralized. Most notes stated only that they would "ultimately" be secured by a deed of trust on property usually described only as "the property located in [city], [state]." These properties, moreover, turned out to be overencumbered. Furthermore, MHP did not record the deeds of trust. Fictitious collateralization does not reduce the risk of the instrument such that application of the federal securities laws is unnecessary. 68/

* * *

We conclude, based on the above analysis, that the MHP notes constituted investments, and therefore securities, and thus fall outside the category of "notes secured by a mortgage on a

---

66/ (...continued)
despite respondent's argument that the note was "subject to regulation by the California Department of Real Estate"). We note that the cases on which Reves relied in discussing the fourth factor involved an alternative scheme of federal – not, as here, state – regulation. McNabb, 54 S.E.C. at 925 n.29 (citing Reves, 494 U.S. at 69); see also II Louis Loss & Joel Seligman, Securities Regulation 931 (3d ed. 1999) (stating that "the existence of a body of state regulation should be given little or no deference in determining whether an instrument is a security").

67/ Bass v. Janney Montgomery Scott, Inc., 210 F.3d 577, 585 (6th Cir. 2000). We note that collateralization does not necessarily render the instrument a non-security.

68/ Wallenbrock, 313 F.3d at 539 (finding that no factor reduced the risk of notes purportedly secured by accounts receivable because the "so-called collateralization" was a fiction); McNabb, 54 S.E.C. at 924 (rejecting reduced risk argument with respect to a promissory note secured by a deed of trust because there was "no evidence that the deed of trust was recorded" and no "evidence as to the value of the property subject to the deed of trust"). We reject the Gebharts' reliance on Singer, 741 F. Supp. at 1050, where the court deemed the note "a note secured by a real estate mortgage" and therefore a non-security despite the failure to record the mortgage because the note, but for the fraud, would have been "one of many commonplace and successful conventional mortgage loan transactions." These notes were not commonplace conventional mortgage loan transactions.

home" considered non-securities. 69/ This analysis also demonstrates that the notes should not be added to the list of notes recognized as non-securities. 70/

IV.

Having found that the MHP notes are securities, we turn to an analysis of the Gebharts' liability under the securities laws and regulations for their involvement in offering and selling the notes.

A. Offer and Sale of Unregistered Securities

Sections 5(a) and 5(c) of the Securities Act provide that, unless a registration statement is in effect or an exemption applies, it shall be unlawful for any person, directly or indirectly, to offer or sell a security through the use of any means or instrumentality of transportation or communication in interstate commerce or of the mails. 71/ A prima facie case for a violation of Section 5 is established by a showing that (1) no registration statement was in effect or filed as to the securities; (2) a person, directly or indirectly, sold or offered to sell the securities; and (3) the sale was made through the use of interstate facilities or the mails. 72/ A showing of scienter is not required. 73/

69/ Cf. William F. Wuerch, 50 S.E.C. 811, 812 n.2 (1991) (finding that notes secured by an assignment of accounts receivable sold to the general public as an investment constituted securities, even though "short term notes secured by an assignment of accounts receivable" are deemed non-securities, because the Supreme Court, by stating that Congress' purpose in enacting the securities laws was to regulate investments, in whatever form they are made and by whatever name they are called, intended to exclude from the definition of a security only those notes issued in a purely commercial or consumer context) (emphasis in original) (citations omitted); see also William Louis Morgan, 51 S.E.C. 622, 626-27 (1993) (finding notes "securities" because respondent's notes "were sold to members of the general public as investments" and the Supreme Court intended to exclude only notes issued in a purely commercial or consumer context).

70/ See Wallenbrock, 313 F.3d at 540 (declining to add notes to the list of notes exempted from the federal securities laws "because the indicia of an investment are so strong").

71/ 15 U.S.C. §§ 77e(a)(1), 77e(c).

72/ See SEC v. Continental Tobacco Co., 463 F.2d 137, 155 (5th Cir. 1972).

73/ Swenson v. Engelstad, 626 F.2d 421, 424 (5th Cir. 1980) ("The Securities Act of 1933 imposes strict liability on offerors and sellers of unregistered securities.").

As explained above, the MHP notes were securities. From 1997 to 2000, the Gebharts sold over $2 million of these securities to approximately forty-five clients, and stipulated that they made use of the mails in connection with those transactions. The Gebharts have also stipulated that no registration statement was in effect for the notes. Because NASD has made a prima facie case that the Gebharts violated Section 5, the burden shifts to the Gebharts to prove the availability of any exemptions. 74/ They have not argued or shown that any exemption applies. Accordingly, we conclude that the Gebharts violated Section 5 of the Securities Act. 75/

B. NASD Conduct Rule 3040

NASD Conduct Rule 3040 provides that an associated person who intends to participate in a securities transaction outside the regular course or scope of employment must give prior written notice to his or her employer describing in detail the proposed transaction and stating whether he or she may receive selling compensation. If selling compensation is to be received, the associated person may not engage in the transaction unless the employer gives its prior approval in writing. A showing of scienter is not required for a violation of Rule 3040.

The record establishes that the Gebharts violated NASD Rule 3040. MHP notes were not sold by MSC and did not appear on the firm's approved transaction list. Although the Gebharts provided some oral and written information on the MHP note program to MSC, it is undisputed that they never disclosed the details of their commission arrangement with Archer. Further, even if the Gebharts provided to MSC all the documentation they possessed about the program, the submission of those materials did not satisfy Rule 3040 with the specificity required. The most complete version of the CSG/MHP promotional materials contained in the record, although including information about successful park conversions, does not describe even in general terms the workings of the promissory note investment. Indeed, the materials were never intended to describe that aspect of the transaction: the brochures were created to serve as "promotional material that was used by MHP at trade shows" to distribute to park owners in order to promote park conversions. 76/ The "pro forma" financial information gave projected cash flow figures for a sample park conversion, but offered no detailed information on the workings of the

---

74/ See SEC v. Zubkis, No. 97 Civ. 8086, 2000 U.S. Dist. LEXIS 1865, at *6 n.6 (S.D.N.Y. Feb. 23, 2000) (citing SEC v. Ralston Purina Co., 346 U.S. 119, 126 (1953) and Byrnes v. Faulkner, Dawkins and Sullivan, 550 F.2d 1303, 1310-11 (2d Cir. 1977)).

75/ Further, because we have consistently held that a violation of a Commission or NASD rule or regulation is inconsistent with just and equitable principles of trade, we find that the Gebharts' sale of the unregistered MHP notes also constitutes a violation of NASD Conduct Rule 2110. See Devine, 78 SEC Docket at 2538 n.30; Gluckman, 54 S.E.C. at 185.

76/ Mounier testified that "mobile home park owners would have a convention, and we would set up a booth and obtain . . . interest from various park owners."

promissory note program beyond the anticipated purchase price of one park and the expected interest rate to be paid on the notes. The Gebharts did not provide information specific to any of the investments they actually sold to their clients. Moreover, even if the Gebharts had provided complete and explicit written notice of their intended involvement with the notes – which they did not – it is undisputed that the Gebharts never received written or even oral approval from MSC's compliance department to sell the notes.

The Gebharts assert that they reasonably believed they had MSC's authorization to proceed with the MHP note sales because they interpreted the silence of Poston and MSC's auditor as the firm's tacit conclusion that the MHP notes were not securities. Assumptions that the Gebharts may have drawn from MSC's silence, however, cannot substitute for the written permission clearly required by Rule 3040 and the relevant MSC policies, which unequivocally prohibit representatives from selling securities without prior, written permission from their firm. 77/ The Gebharts argue that their violation of Rule 3040 was unintentional, claiming that they believed they were in compliance with another NASD requirement, Rule 3030. Rule 3030, which applies to outside business activities not involving the sale of securities, requires written notice to the firm, but, unlike Rule 3040, does not require prior, written permission before associated persons participate in the activity. However, even assuming the Gebharts believed they were in compliance with Rule 3030, 78/ and not subject to Rule 3040, a violation of Rule 3040 does not require a finding that it was done knowingly (or with any other degree of scienter); consequently, the Gebharts' belief is irrelevant. We therefore find that the Gebharts violated Rule 3040. 79/

77/ The Gebharts also argue that they received further apparent approval for their MHP note sales when MSC's operations department faxed its approval to hold an MHP note in a 403(b) retirement account. However, this "approval" was limited to the discrete issue of how to process an investment of 403(b) funds into an MHP note, was not routed through any compliance personnel, and could not have been reasonably construed as blanket approval of the Gebharts' sales activity.

78/ The Gebharts were not charged with violating, and have not been (and are not here) found to have violated Rule 3030. However, we note, in response to the Gebharts' argument about Rule 3030, that their stated belief in their compliance with the rule is at odds with the rule's requirements. Rule 3030 requires "prompt written notice" of the activity in the form prescribed by the firm. The details of MSC's policy with respect to outside business activities evolved over time but always required, at the least, written notice of compensation received for the activity. It is undisputed that the Gebharts never disclosed in writing the compensation they expected to earn for their sales of MHP notes.

79/ As noted supra note 75, a violation of another Commission or NASD rule or regulation is inconsistent with just and equitable principles of trade. We therefore find that the Gebharts' sale of the MHP notes without prior, written approval from MSC also constitutes a violation of Conduct Rule 2110.

C. Fraudulent Misrepresentations and Omissions

Exchange Act Section 10(b), Exchange Act Rule 10b-5, and NASD Rule 2120 all prohibit fraudulent and deceptive acts and practices in connection with the offer, purchase, or sale of a security. Violations of these provisions may be established by a showing that persons acting with scienter misrepresented or omitted material facts in connection with securities transactions. 80/ A fact is material if there is a substantial likelihood that a reasonable investor would have considered the fact important in making an investment decision, and disclosure of the omitted fact would have significantly altered the total mix of information available. 81/ Scienter may be established by a showing of recklessness, 82/ which involves an "'extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the [actor] or is so obvious that the actor must have been aware of it.'" 83/

The Gebharts offered and sold over $2 million in MHP notes to their clients. In doing so, the Gebharts told their clients that investments in the notes would be secured because second deeds of trust on the properties purchased with client funds would be recorded, and because in the event of a default on the MHP notes, clients could recover their investments by foreclosing on the properties and liquidating the collateral. These representations were false: second deeds of trust purportedly securing the MHP notes were not recorded, and, had they been recorded, the properties would have been substantially overencumbered. MHP's only purported asset pending recordation of the deeds, a $100,000 deed of trust on Eastern Trailer Park, apparently never existed. Moreover, the Gebharts failed to disclose to clients that, in making these representations and recommending the MHP notes, the Gebharts relied upon the vague and conclusory statements made in the marketing materials used by the issuer to induce trailer park owners to convert to tenant ownership, upon the bald representations of Archer (who stood to gain substantial commissions on each sale), upon site visits the Gebharts made to two parks that

---

80/ Basic Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976).

81/ Basic, 485 U.S. at 231-32; TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); see also SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963) (stating that a fundamental purpose of the federal securities laws is "to substitute a philosophy of full disclosure for the philosophy of caveat emptor").

82/ See, e.g., Robert M. Fuller, Securities Act Rel. No. 8273 (Aug. 25, 2003), 80 SEC Docket 3539, 3546 n.20, petition denied, No. 03-1334 (D.C. Cir. 2004).

83/ The Rockies Fund, Inc. v. SEC, No. 04-1255 (D.C. Cir. Nov. 15, 2005), 2005 U.S. App. LEXIS 24521, at *12 (citing Steadman v. SEC, 967 F.2d 636, 641-42 (D.C. Cir. 1992) (quoting Sundstrand Corp. v. Sun Chemical Corp., 553 F.2d 1033, 1044-45 (7th Cir. 1977))).

confirmed nothing but proof of the parks' existence, 84/ and upon the absence of complaints from the customers to whom they had already sold notes. The Gebharts never disclosed to clients that they performed no meaningful investigation of the notes or their issuer, nor did they disclose to clients that they did not understand the details of the transactions they were recommending. 85/ These misrepresentations and omissions, which bore directly on the level of risk involved with an investment in MHP notes, were material. We therefore conclude that the Gebharts misrepresented and omitted material facts in connection with the offer and sale of securities. 86/

We also find that, in making these material misrepresentations and omissions, the Gebharts acted recklessly and, therefore, with the requisite scienter. Securities professionals have a duty to investigate offerings before presenting and selling them to clients, 87/ and must have a reasonable basis for recommending that customers purchase those securities; they may not "deliberately ignore that which [they have] a duty to know and recklessly state facts about matters of which [they are] ignorant." 88/ The Gebharts failed to discharge this duty to their clients because, despite numerous warning signs or "red flags" that demonstrated a need for a thorough investigation, the Gebharts made no meaningful effort to perform one before recommending MHP notes to their clients.

84/ It is unclear what information the Gebharts hoped to, or did, find on these two site visits that would bear on the viability of the promissory notes or their issuer.

85/ As noted supra note 11, the Gebharts knew nothing about the holders of the first deeds of trust secured by the mobile home parks nor whether the properties were encumbered by any other liens. Moreover, the Gebharts did not know, or attempt to determine, into which bank accounts client money went, how cash flowed through MHP, or whether any of the park conversions that their clients' notes purportedly financed actually happened. For example, the Gebharts never knew or asked about whether funds would be placed in escrow. When Gebhart was asked at the hearing about his knowledge of any escrow arrangement, he replied, "What is an escrow account, ma'am?"

86/ Misrepresentations and omissions are also inconsistent with just and equitable principles of trade and violate NASD Conduct Rule 2110. Robert Tretiak, Exchange Act Rel. No. 47534 (Mar. 19, 2003), 79 SEC Docket 3166, 3180.

87/ Richard H. Morrow, 53 S.E.C. 772, 779 (1998) (citing Hanly v. SEC, 415 F.2d 589, 595-96 (2d Cir. 1969)).

88/ Hanly, 415 F.2d at 596; see also Jay Houston Meadows, 52 S.E.C. 778, 785 (1996) (holding that salesman of registered broker-dealer "had an obligation to investigate and verify consistently optimistic assertions before repeating them to others," especially in light of "the several suspicious circumstances that were present").

CSG and MHP were small, relatively unknown entities engaged in a business with which the Gebharts had no experience; MHP came into existence only a few months before the Gebharts began selling the notes it issued. Furthermore, Archer paid the Gebharts their commissions with personal checks and told the Gebharts that they were not to contact CSG or MHP directly, and that all communication with the companies must be channeled through Archer. The Gebharts had no access either to the books and records of the companies or to the principals or even office staff; Gebhart testified that although he contacted the offices of MHP a few times, the staff "kept referring [the Gebharts] back to Jack Archer." 89/

Moreover, the form of the MHP notes themselves should have raised questions: the notes were vaguely worded and offered no description of the property supposedly serving as collateral other than "the property located in [city], [state]." The notes also stated that MHP itself owned but one asset, worth only $100,000, and that this would be the sole source of collateral for the notes until they were eventually secured by recorded deeds of trust. At a minimum, this feature of the notes should have alerted the Gebharts to the risk of loss when more than $100,000 in notes were sold. In addition, the interest rates offered by the MHP notes, combined with the commissions that the Gebharts knew MHP was paying to them and to Archer, added up to a substantial payout (up to 28% or more for new note purchases); 90/ nevertheless, the Gebharts made no effort to determine whether MHP would be able to afford the cost of servicing the notes. 91/

Notwithstanding these facts, the Gebharts performed virtually no investigation of the MHP notes or their issuer before recommending the MHP notes as essentially risk-free to clients based on the recordation of deeds of trust for the notes and the sufficiency of the collateral. The Gebharts made no effort to ensure that the deeds of trust purportedly securing the MHP notes

---

89/ Cf. Meadows, 52 S.E.C. at 785 (finding that salesman of a registered broker-dealer made misrepresentations that were reckless, based in part on a denial of unrestricted access to the issuer's records even though salesman claimed "not to have been troubled by this development").

90/ The Gebharts did not know that MHP paid Archer 10% on each new note sale; they knew only that they shared 50% of Archer's commissions. Accordingly, the Gebharts may have believed that MHP paid Archer as much as 12-14% in commissions for new note sales, given that they earned 6-7%, resulting in a total 32% payout by MHP for new notes.

91/ The Gebharts presented testimony from a witness they offered as an expert on real estate transactions; this witness asserted that the interest rates combined with broker commissions payable on "second trust deed hard money loan[s]" in the late 1990s were between 20 and 33 percent. We note that, even if the MHP notes could be characterized as "second trust deed hard money loans," a return this substantial on its face, even if common for this type of note, should still have prompted the Gebharts to confirm that MHP could afford the cost of servicing the notes.

were recorded; they were never provided, nor did they request, a copy of a deed of trust that had been recorded. The Gebharts also made no effort to confirm that the parks contained sufficient equity to discharge the note obligations. Although the Gebharts "were of the understanding" that generally the parks were not to be encumbered with debt totaling more than 45 to 55 percent of the property's value, 92/ the Gebharts never sought or examined any information or documents that normally help to confirm the value of real property, such as an appraisal, escrow instructions, or title report. Furthermore, the Gebharts did not keep track of the number or amount of investments their own clients made into each park and did not know or ask how many of Archer's clients were investing in those same parks. The Gebharts also never investigated the nature or extent of the first trust deeds against the parks, nor whether any other liens existed against the properties purportedly serving as collateral for the notes. 93/

As indicated, the Gebharts do not deny making the misrepresentations and omissions that are the basis for this aspect of the case, but claim that they did so without the scienter necessary to support a finding of fraud. The Gebharts claim that they, like their customers, were victims of the fraud of others. According to the Gebharts, they offered and sold the notes in "good faith," which they assert is supported by the finding of NASD's Hearing Panel, which heard their testimony and concluded that the Gebharts

> truly believed that they had fulfilled their responsibilities to assure that MHP and CSG were appropriate investments, based on (i) the information they received from Mr. Archer, whom they believed to be reliable; (ii) the information they gathered about mobile home conversions from [the U.S. Department of Housing and Urban Development ("HUD")] and other municipal and state agencies; (iii) their one-year personal payment history with the MHP promissory note; and (iv) Mutual Service's lack of response to the information concerning the mobile home conversion provided to it. 94/

92/ It is unclear whether even this limited understanding, which D. Gebhart testified she gathered from representations made by Archer, was accurate: Archer testified in a civil deposition that he did not recall ever telling the Gebharts that the loan-to-value ratio on the parks would be in that range; his conversations with Scovie indicated only that the ratio would be less than 85%. Of course, ultimately the Gebharts learned that the loan-to-value ratio of these properties actually exceeded 100%.

93/ This information would have been important because holders of notes recorded prior in time have priority over later lienholders in the event of default.

94/ The Hearing Panel found that the Gebharts acted with negligence, but not with the scienter necessary to find fraud, in offering and selling the notes. In finding recklessness rather than negligence, NASD's National Adjudicatory Council (the "NAC") concluded that the four factors identified by the Hearing Panel provided "scant reasons for the

(continued...)

However, we conclude that the factors identified by the hearing panel do not support a finding of good faith. First, the information the Gebharts received from Archer, no matter how reliable they deemed him to be, was inadequate to provide a reasonable basis for recommending the notes to others. We have long held that "a salesman may not satisfy his duty to investigate the securities he recommends by relying 'blindly' on information supplied by persons connected with the issuer." 95/ Second, contrary to the Hearing Panel's finding, the record does not support a finding that the Gebharts sought information from HUD or any other government agencies about mobile home conversion programs or financing therefor. 96/ Even if it did, general information about mobile home park conversions would have shed no light on the specific conditions under which the MHP note program was being operated. Third, the personal investment the Gebharts made despite their own failure to investigate the notes cannot render reasonable the Gebharts' actions in light of the numerous red flags in this case. 97/ Finally,

---

94/ (...continued)
Gebharts to believe they had fulfilled their duty to investigate." The NAC also noted that the evidence established that the Gebharts acted with "more than just empty-headedness," and engaged in an "extreme departure from the standards of ordinary care."

95/ Morrow, 53 S.E.C. at 779-80 (citing Hanly v. SEC, 415 F.2d 589, 597 (2d Cir. 1969)); see also Sorrell v. SEC, 679 F.2d 1323, 1327 (9th Cir. 1982) (holding that reliance on assurances from attorney and another broker does not excuse broker's own lack of investigation).

96/ D. Gebhart testified in one instance that the Gebharts "had found out about the HUD housing," but it is unclear whether she is simply referring to information Archer gave them or to some independent research the Gebharts conducted. Because the Gebharts make no mention of an investigation of the HUD financing elsewhere in these proceedings, we decline to find that the Gebharts investigated the role of government entities in CSG's or MHP's activities.

97/ See John R. Brick, 46 S.E.C. 43, 49 n.16 (1975) ("Brick stresses the fact that he bought the stock himself. Moreover, he recommended Thorne [stock] to his father-in-law. But his willingness to gamble with his own money and with that of his father-in-law did not give him a license to make unfounded recommendations to clients."); see also Dane S. Faber, Exchange Act Rel. No. 49216 (Feb. 10, 2004), 82 SEC Docket 530, 543 ("A registered representative's willingness to speculate with his own funds despite his knowledge of adverse financial information does not excuse his failure to disclose material information to his customer.") (citing Richard J. Buck & Co., 43 S.E.C. 998, 1008 (1968), aff'd sub nom. Hanly v. SEC, 415 F.2d 589 (2d Cir. 1969)). We further note that one year of success, by itself, cannot form the basis for a prediction of future success; for example, NASD Rule 2210, like many Commission rules, has long

(continued...)

MSC's failure to respond to the Gebharts' communications about the MHP note program does not excuse their own failure to make appropriate inquiries before recommending the notes. 98/ Put simply, even an "honest belief in an issuer's prospects does not in itself give [one] a reasonable basis for recommending the [investment] to others." 99/

In sum, we find that the record does not support a finding of good faith. We conclude, as discussed above, that the actions of the Gebharts in recommending the notes, based on material misrepresentations and omissions of material fact, were done with recklessness, in violation of the antifraud provisions.

V.

Under Exchange Act Section 19(e)(2), we may reduce or set aside sanctions imposed by NASD if we find, having due regard for the public interest and the protection of investors, that the sanctions are excessive or oppressive or impose an unnecessary burden on competition. 100/

NASD Sanction Guidelines recommend imposition of a fine between $5,000 and $50,000 for private securities transactions and a one-year suspension or a bar where, as here, the sales exceeded $1,000,000. 101/ The Guidelines recommend a fine between $2,500 and $50,000 for

---

97/ (...continued)
prohibited securities sellers from predicting or projecting performance and from implying that past performance will recur.

98/ See Donald T. Sheldon, 51 S.E.C. 59, 88 n.130 (1992) (stating that duties owed by securities professional to customers are "not abridged by a failure on the part of his supervisors"), aff'd, 45 F.3d 1515 (11th Cir. 1995); Justine Susan Fischer, 53 S.E.C. 734, 741 n.4 (1998) (holding that "[a] broker has responsibility for his or her own actions and cannot blame others for [his or] her own failings"). For the same reason, we do not credit the Gebharts' similar argument that the bank holding the custodial accounts of some clients should shoulder the blame, and thereby exonerate the Gebharts, because the bank did not ensure the trust deeds securing the MHP notes were recorded.

99/ Sheldon, 51 S.E.C. at 70 n.41 (citing Gilbert F. Tuffli, 46 S.E.C. 401, 405 (1976)); see also James E. Cavallo, 49 S.E.C. 1099, 1102 (1989), petition denied, 993 F.2d 913 (D.C. Cir. 1993) (Table) ("A salesman's honest belief in an issuer's prospects does not warrant his making exaggerated and unfounded representations and predictions to others.").

100/ 15 U.S.C. § 78s(e)(2). The Gebharts do not claim, and the record does not show, that NASD's action imposed an undue burden on competition.

101/ NASD Special Notice to Members 03-65 (Oct. 2003). The guideline provides that the first step is to assess the extent of the selling away, including the dollar amount of sales,
(continued...)

selling unregistered securities and, in egregious cases, a suspension of up to two years or a bar. 102/ For reckless or intentional misrepresentations or omissions of material fact, NASD Sanction Guidelines recommend a fine between $10,000 and $100,000 and a suspension between ten business days and two years; in egregious cases, the Guidelines recommend a bar. 103/ Using these Guidelines, NASD found that Gebhart's sale of unregistered securities and private securities transactions supported a bar; NASD also found that a bar was warranted for Gebhart's fraudulent sales of securities. D. Gebhart was sanctioned with two one-year suspensions for those same violations and assessed a total fine of $15,000. 104/

We have held repeatedly that engaging in private securities transactions and selling unregistered securities are both serious violations. 105/ NASD Rule 3040 protects investors from unsupervised sales as well as securities firms from liability and loss resulting from such sales. 106/ Its violation deprives investors of protections they have a right to expect, such as a firm's oversight, due diligence, and supervision. 107/ Similarly, the keystone of the Securities Act, Section 5, serves to protect the public in the offer and sale of new securities issues; 108/ its registration provisions set forth basic requirements for the protection of investors. 109/ The Gebharts' misconduct illustrates the potential for harm to public investors through unsupervised

---

101/ (...continued)
the number of customers, and the length of time over which the selling away occurred. The second step is to consider the other factors described in the principal considerations for the guideline and the general principles applicable to all guidelines. The presence of one or more aggravating or mitigating factors may increase or decrease sanctions.

102/ NASD Sanction Guidelines 30 (2001 ed.).

103/ NASD Sanction Guidelines 96 (2001 ed.).

104/ Although NASD found that D. Gebhart "played a less substantial role," we believe that the record would support a finding that D. Gebhart's responsibility for these violations was equivalent to that of Gebhart.

105/ See, e.g., Gerald James Stoiber, 53 S.E.C. 171, 180 (1997); Excel Financial, Inc., 53 S.E.C. 303, 313 (1997).

106/ Chris Dinh Hartley, Exchange Act Rel. No. 50031 (July 16, 2004), 83 SEC Docket 1239, 1247; Gluckman, 54 S.E.C. at 192.

107/ Hartley, 83 SEC Docket at 1247-48; Ronald W. Gibbs, 52 S.E.C. 358, 365 (1995).

108/ First Heritage Investment Co., 51 S.E.C. 953, 959 (1994).

109/ Independent Securities Corporation, 47 S.E.C. 780, 784 (1982).

securities transactions and the sale of unregistered securities, and warrants substantial sanctions. 110/

The Gebharts, in addition to engaging in private securities transactions and selling unregistered securities, also engaged in fraud. "[C]onduct that violate[s] the antifraud provisions of the federal securities laws is especially serious and subject to the severest of sanctions under the securities laws." 111/ Here, the Gebharts offered and sold over $2 million worth of notes to their clients while representing falsely that the notes would be secured by deeds of trust on real property that was more than adequate to cover the amounts the clients were investing. The notes, in fact, were largely unsecured, and the collateral proved seriously inadequate to cover the sums invested.

There were also several aggravating factors present in this case that NASD identified. Among other things, NASD found that the Gebharts attempted to create the impression that their member firm approved their sale of the notes by writing to customers of the firm on letterhead stating "Securities offered by Mutual Service Corporation." 112/ We further note that, as NASD found, the Gebharts' misconduct also resulted in significant monetary gain for themselves.

We reject the Gebharts' contention that the sanctions are excessive because "they did all they could do to avoid the risk of engaging in the sale of unregistered securities." The Gebharts argue that they notified their firm in advance of their sales of the MHP notes and that "[b]oth MONY and MSC determined the legal status of the notes as being non-securities." This latter assertion is unsupported by the record and, for that reason, we do not credit it with any mitigative effect. The Gebharts' interpretation of Poston's silence as a tacit determination of the notes as non-securities cannot substitute for express approval by the firm (or a decision by the firm that approval is not required) and does nothing to excuse their violation. Further, the Gebharts' own judgment that the MHP notes were not securities, based on Archer's assertion that MONY "did

---

110/ See, e.g., Anthony H. Barkate, Exchange Act Rel. No. 49542 (Apr. 8, 2004), 82 SEC Docket 2443, 2455 (upholding bar for violating Rule 3040), aff'd, 125 Fed. Appx. 892 (9th Cir. 2005).

111/ Marshall E. Melton, Investment Advisers Act Rel. No. 2151 (July 25, 2003), 80 SEC Docket 2812, 2825.

112/ Cf. Barkate, 82 SEC Docket at 2454-55 (upholding bar where respondent created the impression that his employer sanctioned the sale of the instruments, sold instruments directly to customers of his employer, engaged in the misconduct over a nine-month period, and generated $6.8 million in sales).

not see a problem," does not diminish their failure to provide written notice to their firm informing it of their activities and allowing it to make its own determination on this issue. 113/

The Gebharts cite their spotless disciplinary history, contrition, 114/ and cooperation with NASD's investigation, all of which we have considered, as did NASD, in mitigation. The Gebharts also note that they have made substantial efforts to assist their customers in recovering their funds by filing a petition for involuntary bankruptcy against MHP and suing their own insurance carrier. Although we recognize that the Gebharts' efforts resulted in significant recoveries for their customers, we note that the Gebharts had an interest in recovering their own funds and, presumably, avoiding personal liability for their actions. 115/ In sum, we agree with NASD that the mitigating factors identified by the Gebharts do not outweigh the aggravating circumstances present in this case.

113/ Joseph J. Vastano, Jr., Exchange Act Rel. No. 50219 (Aug. 19, 2004), 83 SEC Docket 2015, 2023 (rejecting salesman's argument that it was a mitigating factor that his supervisor told him the product was not a security and finding that salesman's "belief that the [product] was not a security or the assertions of others that it was not, are not relevant in determining whether the [products] were securities or whether he should have given [his firm] written notice to permit [it] to make an independent determination of that issue."), reconsid. denied, Exchange Act Rel. No. 50691 (Nov. 18, 2004), 84 SEC Docket 426; see also Gilbert M. Hair, 51 S.E.C. 374, 377 (1993) (rejecting respondent's reliance on "his own judgment and that of the issuer" for his belief that the notes were not securities). We also point out that the Gebharts' reliance on Archer's confidence that the notes were not securities is further undermined by the fact that, at the same time, Archer encouraged the Gebharts to solicit MSC's permission to sell the notes notwithstanding MONY's apparent approval.

114/ We note that the mitigative effect of the Gebharts' contrition is diminished by their argument that the MHP note program would have been successful absent Scovie's fraud and that other actors failed to fulfill their obligations and thus allowed the fraud to escape detection. See Vastano, 83 SEC Docket at 2025 (finding that respondent's argument that the instrument would have been successful absent the fraud had no impact on his obligation to give notice to his firm); Mike K. Lulla, 51 S.E.C. 1036, 1040 (1994) (upholding bar because "the fact that others also might have been remiss in their duties does not mitigate [respondent's] responsibility").

115/ As noted supra note 32, the Gebharts have not provided evidence of expenses they incurred, or recoveries they declined, in their efforts to recoup customer losses. Although efforts to help defrauded customers recover their losses are acknowledged and encouraged, those efforts do not always justify a reduction in sanctions. See Hartley, 83 SEC Docket at 1247 ("We do not consider that Hartley is deserving of a reduction in sanctions because his clients may be able to recover some of their losses.").

Under these circumstances, where the Gebharts, without notice to or approval from their firm, sold over $2 million in unregistered securities to dozens of investors over the course of more than three years based on fraudulent misrepresentations and omissions, we find that a bar is manifestly warranted against Gebhart. Similarly, on this record, we find that the suspension and fine imposed on D. Gebhart are well within the range of sanctions appropriate for the selling away of unregistered securities involving fraud. We therefore find that the sanctions NASD imposed against the Gebharts are neither excessive or oppressive, and we sustain NASD's findings of violation and imposition of sanctions. 116/

An appropriate order will issue.

By the Commission (Chairman COX and Commissioners ATKINS, CAMPOS, and NAZARETH); Commissioner GLASSMAN not participating.

Nancy M. Morris
Secretary

116/ We have considered all of the arguments of the parties. We reject or sustain them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 53136 / January 18, 2006

Admin. Proc. File No. 3-11953

In the Matter of the Application of

ALVIN W. GEBHART, JR.
and
DONNA T. GEBHART

c/o Charles F. Goria
Goria & Weber
7863 La Mesa Blvd. Suite 201
La Mesa, CA 91941

For Review of Disciplinary Action Taken by

NASD

ORDER SUSTAINING DISCIPLINARY ACTION

On the basis of the Commission's opinion issued this day, it is

ORDERED that the disciplinary action by NASD against Alvin W. Gebhart, Jr. and Donna T. Gebhart, and NASD's assessment of costs be, and they hereby are, sustained.

By the Commission.

Nancy M. Morris
Secretary