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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16594

In the Matter of

EQUITY TRUST
COMPANY,

Respondent.

BRIEF OF THE DIVISION OF ENFORCEMENT IN SUPPORT OF ITS PETITION FOR REVIEW

DIVISION OF ENFORCEMENT
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The Division of Enforcement respectfully submits this brief in support of its Petition for Review of the Initial Decision dated June 27, 2016 ("ID"), rendered by Administrative Law Judge Carol Fox Foelak ("ALJ"). The Initial Decision dismissed the charges against Respondent Equity Trust Company ("Equity Trust") under Section 8A of the Securities Act of 1933. The ALJ found that the first two elements under Section 8A – that Ephren Taylor ("Taylor") and Randy Poulson ("Poulson") committed nonscienter primary violations and that acts or omissions by Equity Trust were a cause of these violations – were established. The ALJ also found, however, that the Division did not prove the third element – that Equity Trust "knew or should have known that its conduct would contribute to the primary violations" – and dismissed the charges.

PRELIMINARY STATEMENT

Although Equity Trust claims to be merely a passive custodian of self-directed Individual Retirement Accounts ("IRAs") with limited duties, its conduct was far from passive. Equity Trust partnered with, endorsed, and recommended Taylor and Poulson, issuers who offered high-risk promissory notes and are now serving lengthy prison sentences, without doing any due diligence. And as Equity Trust knew from its own experience, fraudsters have repeatedly targeted Equity Trust's self-directed IRAs. Despite this knowledge, Equity Trust aggressively marketed self-directed IRAs to low and middle-income investors as a "fountain flowing with money," suitable for "everyone," and a surefire route to tax-free riches. Equity Trust's unreasonable conduct was a cause of the primary violations of Taylor and Poulson.

The evidence presented during the eight-day hearing proved that Equity Trust crossed the line and did not act passively. Section 8A requires evidence that Equity Trust "knew or should have known" that its conduct would contribute to the primary violations, and the evidence was more than sufficient to meet this standard.

First, Equity Trust knew that its conduct would contribute to Taylor's and Poulson's violations due to its knowledge of a key aspect of the Taylor and Poulson frauds: the false marketing and sale of the promissory notes as "secured." Taylor and Poulson provided no security for the notes which the investors believed were secured. Equity Trust, however, processed the Taylor and Poulson notes as "secured" despite knowing of the absent security. Equity Trust also knew that Taylor, in front of an audience of thousands, made materially false statements about Equity Trust's role in order to lend himself credibility.

Second, and alternatively, the "should have known" element – which requires evidence of negligent or unreasonable conduct – was satisfied by substantial evidence that Equity Trust acted highly unreasonably and far outside the bounds of a passive custodian. Equity Trust unreasonably promoted and endorsed Taylor and Poulson as "referral sources" who could be counted on to generate account openings, without conducting any due diligence. In breach of its role as a passive custodian, Equity Trust sales representatives promoted Taylor and Poulson by attending their solicitation events, and investors testified that those representatives recommended and promoted Taylor and Poulson.

The ALJ made numerous errors in applying the "knew or should have known" element, beginning with an incorrect determination of the appropriate standard of care. Rejecting unrefuted evidence of the duties of an IRA custodian, the ALJ adopted an "Investor Alert" issued by the SEC staff as a "convincing statement of the Commission's view." ID at 34. The Investor Alert, however, was issued by the staff, ***not*** the Commission, and, in any event, merely gave generalized descriptions of what IRA custodians may do in the context of warning investors about the risks of self-directed IRAs.

Compounding these errors, the ALJ skirted past the issue of whether Equity Trust complied with its duties, finding that this issue was "not relevant" to the "should have known" element because, under any circumstance, Equity Trust would not have "known of the fraud." As in all Section 8A causing cases, however, issues of reasonableness and negligence – and not knowledge of fraud – are fundamental. The ALJ erred by replacing the reasonableness inquiry that has long been part of Section 8A causing cases with a knowledge requirement. The evidence of Equity Trust's unreasonable conduct, moreover, was more than sufficient to establish the third element.

Given the evidence of Equity Trust's unreasonable conduct, which was far outside the scope of a passive custodian, the ALJ's dismissal of the charges and finding that Equity Trust's conduct was nothing more than the innocuous "promotion of its own business model" can be expected to have ramifications throughout the lightly regulated self-directed IRA industry. The Initial Decision will be viewed as a green light to self-directed IRA custodians to engage in the same kinds of promotion, endorsement, and negligent conduct engaged in by Equity Trust. The consequences could be additional and unnecessary risk to the approximately $94 billion held nationwide in self-directed IRA accounts.

For these reasons, the Initial Decision should be reversed and appropriate sanctions should be imposed.

STATEMENT OF FACTS[1]

EQUITY TRUST COMPANY

Equity Trust, a privately held company based in Westlake, Ohio, is owned by Richard Desich Sr. ("Desich Sr.") and his two sons, Jeffrey Desich ("J. Desich"), and Richard Desich, Jr. ("Desich Jr."). Since August 2008, Michael Dea has been President and, until the end of 2015, Chief Financial Officer. Tr. 649-650.

Equity Trust was incorporated under South Dakota law on February 11, 2003, and is a public trust company regulated by the South Dakota Division of Banking. Upon its formation, Equity Trust took over the self-directed IRAs administered by Mid-Ohio Securities Corp. ("Mid-Ohio Securities"), a broker-dealer founded by Desich Sr. in 1974. DE 598 at 37-42.

The Internal Revenue Code allows Equity Trust to serve as a custodian of IRAs because it is regulated by the South Dakota Division of Banking. 26 U.S.C. § 408(a)(2). Equity Trust promotes itself as a so-called "self-directed" IRA custodian, meaning that it is willing to take custody of and administer non-traditional assets such as "real estate, notes, private placements, tax lien certificates and much more." DE 801 at 12. Most banks offering custodial services do not permit IRA accounts to hold non-traditional assets. DE 39 ¶¶ 19, 32; DE 801 at 12. As Equity Trust states on its website, a "self-directed IRA is technically no different than any other IRA (or 401k)." DE 801 at 12.

As of 2011, U.S. investors were estimated to hold approximately $94 billion in self-directed IRAs. RE 46 at 2.

[1] In this brief, "DE" means Division Exhibit; "RE" means Respondent's Exhibit; and "Tr." means the transcript of the hearing held in December 2015. Two exhibits – DE 36 (Taylor dep.) and DE 824 (Poulson "Extravaganza" transcript) – are minuscripts and are cited with the internal page number in parentheses after the "DE" citation.

KNOWLEDGE THAT FRAUDSTERS TARGETED SELF-DIRECTED IRA ACCOUNTS

Mid-Ohio Securities, like Equity Trust, was repeatedly targeted by fraudulent promoters and, as a result, Mid-Ohio Securities was investigated and sanctioned by regulators. In October 2009, Desich Sr. agreed to withdraw his state securities license to resolve an investigation by Ohio authorities. DE 848 at 3-4 (2009 Ohio Sec. Div. Cease-and-Desist Order: "at least thirteen particular investment programs...turned out to be fraudulent").[2]

After the Desiches moved their self-directed IRA business from Mid-Ohio Securities (a registered broker-dealer) to Equity Trust (an unregistered entity), fraudulent promoters continued to target Equity Trust. Equity Trust declared fraudulent investments to be "administratively not feasible" and placed them on its "Do Not Process" list, which categorized them as "Ponzi Scheme/Fraud," "SEC Investigated," "Pending Litigation," or "Cease & Desist Found." DE 578 *passim*. *See also* Tr. 742; 1589-1590. By 2012, the Do Not Process list contained over 800 investments, including BBC Equities, the fraudulent investment fund run by John Bravata (DE 578 at 3; DE 853); Refco (DE 578 at 1); DBSI, Inc. (DE 578 at 4); and Robert Langguth (DE 443 at 11; DE 592).[3]

Dea acknowledged that the Do Not Process list showed that Equity Trust has been "custodying assets for issuers who turned out to be engaged in a Ponzi scheme or investment fraud." Tr. 742-743. *See also* Tr. 278 (Marsh: administratively not feasible "'was code for basically 'we don't want to process your investment, we think it is a fraud'"). Additional

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[2] In October 2003, the Commission found violations by Mid-Ohio Securities of the net capital rule, and imposed a cease-and-desist order and penalty. DE 829. State regulators and the NASD also investigated and sanctioned Mid-Ohio. DE 841 (Hawaii); 655 at 27-29 (Vermont); 848 at 2-3 (Maine); 655 at 19-21 (NASD).

[3] The ALJ asserted that "it is not clear" that the Kenneth Starr who used Equity Trust is the same person who was prosecuted in a 2011 criminal case. ID at 11, n. 12. Dea, however, testified that he knew that Starr was "running a big Ponzi scheme." Tr. 703.

evidence and caselaw reveal occurrences of fraud in Equity Trust accounts. DE 658 at 2 (2006 Ohio Sec. Div. Order); DE 840 at 3 (2014 Alaska Div. Bkng. Order); *Rome v. Roop*, 2014 WL 1491480, at *1-2 (Col. Div. Sec. Apr. 3, 2014); *Casey Charles*, 2011 WL 6094422 (Md. Sec. Div. Nov. 28, 2011) (fraudulent promoter "convinced investors that Equity Trust [] was a reputable IRA custodial company").

After real estate, promissory notes constitute the second largest category of Equity Trust's asset base – approximately $1.2 billion as of 2012, with nearly $550 million in unsecured notes. DE 579; Tr. 652. The SD Division of Banking warned Equity Trust that its high concentration of promissory notes "increase[s] the risk of fraud." DE 596 at 6. *See also* DE 595 at 6 (March 2010 exam noting "non-performing promissory notes" and "over 8,000 non-performing notes"); DE 595 at 7 (Equity Trust's "high concentration of alternative account holdings…heightens compliance risk."); DE 39 ¶ 34-36.

EQUITY TRUST PROMOTED SELF-DIRECTED IRAs WITH NO WARNINGS AND SENT SALES REPRESENTATIVES TO ISSUER EVENTS

Equity Trust's website and marketing materials, including *Proven Wealth Building Secrets*, a book written by the Desiches, promote self-directed IRAs as get-rich-quick vehicles suitable for all. DE 802 at 117; DE 548 at 15 (self-directed IRAs are for "Everyone!"); DE 548 at 22 (**"Equity Trust Company…actually encourage[s] you to invest in the very areas that other custodians won't allow!"**) (emphasis in original). *See also* DE 801 at 55; DE 802 at 125, 93, 113, 121; DE 764 at 2; DE 543 at 3. Equity Trust's website referred to Desich Sr. as "the Guru" and promoted self-directed IRAs as "a fountain flowing with money." DE 801 at 55.

Equity Trust gave no warning to investors that self-directed IRAs can be targeted by fraudsters or that promissory notes can be risky. DE 39 at ¶¶ 34-36; DE 801-804 (pages from Equity Trust website from 2008-2011); DE 597 at 11.

Sales representatives like Robert Batt and Irene Berlovan were required to open a minimum of forty accounts per month, and their compensation and evaluation was tied to the number of account openings. Tr. 202; 389; 664; DE 611. The most effective method for sales representatives to increase account openings was to establish relationships with outside referral sources, also known as centers of influence ("COIs"). Tr. 663; 1242. Issuers and investment sponsors like Taylor and Poulson were coveted referral sources. DE 191.

Sales representatives were encouraged to attend issuer events in order to generate leads and account openings. DE 518 at 1; DE 600 at 2; DE 602 at 4. Batt attended events, including investment sponsor events, "every four to six weeks." Tr. 304. Berlovan also attended events where COIs and issuers were present. Tr. 1203-1204; DE 191.

Sales representatives were not trained to provide disclaimers. Tr. 211; 304; Tr. 1215-1216; 1219; Tr. 1206. Instead, sales representatives were told "[h]ow to dress, how to act [], like not sitting behind the booth, how to be approachable." Tr. 226-227; DE 605 at2; 606 at 2; 610 at 5, 7. Equity Trust knew that at these events, which were often presented as educational, the investment sponsors were promoting promissory notes and soliciting investments. Tr. 1276, 1343, 1335-1336.

Equity Trust did not seek or obtain approval from the SD Division of Banking to send sales representatives to issuer events. Tr. 1181. Indeed, by having its sales and marketing departments under the umbrella of an affiliate, Equity Trust prevented its regulator from knowing about and examining activities such as sending representatives to issuer events. Tr. 1179-1182.

Scott Kelly of the SD Division of Banking testified that Equity Trust never asked him if it was appropriate to send sales representatives to issuer events; that he did not know that Equity

Trust sent sales representatives to issuer events; and that this would have been relevant to his exams. Tr. 1181-1182. S. Kelly also did not know about Batt's attendance at Taylor's Wealth Tour in 2009. After being shown the video of Batt's appearance, S. Kelly testified that it was "certainly a bad business practice;" that it "looks like Mr. Taylor used Mr. Batt to market his product;" and that "Mr. Batt should have clarified that he's not a banker and that he doesn't endorse Ephren Taylor's products." Tr. 1186-1187.

DUTIES OF A REASONABLE IRA CUSTODIAN

The Ries report summarizes the duties of a reasonable IRA custodian. DE 39 (Ries). As shown below, the duties described in the Ries report are consistent with Equity Trust's customer agreements, its internal policies, its regulatory framework, and its representations to customers. DE 39 *passim.*

First, a reasonable IRA custodian should not endorse or recommend any investment, promoter, issuer or investment strategy, without conducting any due diligence. Equity Trust's policies and customer agreements all express the prohibition on endorsement and recommendation. DE 49 at 15; DE 53 at 2; DE 40 at 54; DE 751 at 36-37 (§ 8.05(b)); DE 39 at ¶¶ 20, 31-32.

Second, a reasonable custodian should avoid conflicts of interest and act in the best interests of its customers. DE 49 at 11 (Trust Co. Policy: "A custodian has a duty to avoid conflicts of interest and self-dealing."). The policy derives from FDIC Trust Examination Manual and requires "a fiduciary's duty of loyalty." *Id. See also* DE 57 at 1 (Equity Trust employees cannot "engage in any activity that is, or appears to be a conflict of interest"). In addition, the Internal Revenue Code requires that IRA custodians administer accounts "for the exclusive benefit of an individual or his beneficiaries." 26 U.S.C. § 408(a). *See also* DE 49 at

11 (Trust Co. Policy: accounts must be administered "solely in the best interests of [the] beneficiaries").

Third, a reasonable custodian should hold and administer the customer's assets, which includes taking title to the assets and maintaining indicia of ownership, and transfer funds out of a custodial account until the documents evidencing the customer's intent have been received. DE 39 at ¶¶ 23-24, 29-30; DE 49 at 14; Tr. 699-700 (Dea); Tr. 1191 (S.Kelly: Equity Trust is expected "to have documentation that the asset exists and it's in their possession."). Account documentation supporting its customers' investment intent must be obtained before transferring funds to an issuer. DE 53 at 3 (Equity Trust must maintain "applicable documents pertaining to the client investment" and "review the documents for completeness.").

The Direction of Investment ("DOI") form tells Equity Trust the customer's investment intent. Tr. 721; DE 40 at 54; Tr. 393-394 (Batt: DOI is "how you execute an investment"). When a promissory note is marked as "secured" by an asset other than real property on the DOI, Equity Trust must obtain the "Original Note Stating the Associated Collateral and a UCC filing to Evidence Security or Title to the Collateral with Lien Attached." DE 53 at 12; DE 40 at 35 (DOI: documents "must be submitted" with DOI include note "clearly stating collateral"). If the DOI states that the note is secured by real property, Equity Trust must obtain the "Original Note and Executed Deed of Trust/Mortgage." DE 53 at 11-12. *See also* DE 40 at 35 (DOI).

Equity Trust repeatedly acknowledged to customers its obligation to hold the documents evidencing its customers' investment. DE 790 at 2 ("Does Equity Trust Company need to hold all original documents? Yes, as a custodian, we are required by law to hold all original documents."); DE 764 at 8 ("All records pertaining to the investment (such as real estate deeds, original notes, operating agreements for LLCs) are retained by Equity Trust for safekeeping");

DE 801 at 27 ("An investment at Equity Trust isn't final until all records pertaining to the investment (such as real estate deeds, original notes, operating agreements for LLCs, etc.) are sent to Equity Trust for safekeeping.").

Starting in at least 2009, Equity Trust widely circulated a promotional document that told investors that that Equity Trust must receive the "Promissory Note and Security Document" ***before*** any retirement funds are transferred out of the custodial account:

> **How it Works:**
> 1. Open and Fund IRA
> 2. Find an Individual or Entity Interested in Borrowing Money
> 3. Submit Promissory Note Direction of Investment Form to Request Funding
> 4. Send Original Promissory Note and Security Document to Equity Trust for Safe Keeping
> 5. Funds are Sent to Borrower

DE 856 at 4 (Guide emailed to at least 53 customers between June 2009 and April 2011).

Fourth, a reasonable IRA custodian should periodically review customer assets, weigh risk, and reasonably respond to red flags. *See, e.g.*, DE 39 ¶ 28; DE 823 at 2 (Div. of Banking, *Account Review Guidance*: "A comprehensive account review includes both an administrative and investment review"); DE 598 at 14 (in application to SD regulator, Equity Trust agreed to "Review the assets of each trust account at least once during each period of twelve months").

In 2009, in response to the Division of Banking, Equity Trust developed a more robust review policy, which included primary and secondary reviews. DE 53; DE 594 at 4; Tr. 1167-1168 (Div. of Banking recommendation led to improvement of review program); Tr. 1629 (Dea: reviews were to "get our arms around some of the bigger relationships to make sure that everything appears to be in order"); Tr. 1193 (Div. of Banking testimony that Equity Trust's compliance culture was "reactionary as opposed to proactive"). *See also* DE 595 at 5; DE 596 at

4 (2009 & 2011 Div. of Banking exams warning about risk, the need for comprehensive audit programs, and concerns about staffing levels).

Equity Trust was not supposed to process investments without complete investment documents. DE 53 at 3; Tr. 901-902; Tr. 906-907.[4] The primary review also included a background check on the investment and investment sponsor, and if negative information was material it would be investigated. DE 53 at 3. In conducting secondary reviews, Equity Trust ensures that "ETC is holding all the required documents, whether they have been properly executed, if necessary, and if expected income is being generated by the investment." *Id.* at 6. If documentation is missing, the investment or investment sponsor is to be placed on "hold." *Id.* at 9; DE 39 at ¶ 52 (missing documents a red flag). The investment or investment sponsor would be placed on the Do Not Process list for any number of reasons, including being charged by a regulator or criminal authority. DE 578 (Do Not Process list); Tr. 741-742.

EQUITY TRUST AND EPHREN TAYLOR

From April 2008 through December 2009, a total of 81 Equity Trust customers made 94 investments in the Taylor Notes, for a total of approximately $5.3 million. DE 40 at 19, 21. These investments defaulted, resulting in almost a complete loss for investors. DE 40 at 3.

Taylor, through City Capital, a public company, and other entities he owned and operated (collectively, "City Capital"), raised funds from investors through the issuance of secured and unsecured promissory notes that paid interest rates from approximately 10% to 20% for terms of primarily nine months to three years, as well as two equity investments (the "Taylor Notes"). DE 40 at 10-19.

[4] The first time that Equity Trust informs an investor of any missing documents and that it is the customer's responsibility to obtain account documentation is ***after*** Equity Trust processes the investment and transfers the funds to the issuer. *See, e.g.*, DE 763 at 67; Tr. 1081-1084.

Taylor's violations included the misappropriation of investor funds (DE 40 at 3-4; DE 36 at 8 (28); DE 3 at 45-50), and the misrepresentation on the DOI that many of the notes were secured by City Capital or other entities owned by Taylor. *Infra* 20-22. In fact, almost all of the Taylor Notes were unsecured. Finally, Taylor made false statements to investors about Equity Trust's role at the October 2009 New Birth Church event. *Infra* 15-19.[5]

Equity Trust Promoted Taylor

In early 2008, Batt responded to an online inquiry from Taylor, and during the next two years Taylor became a prized referral source, or COI, of Batt's. *See* DE 36 at 12 (43-44); DE 796 at 36 (2.15.08 Batt note: "tlk to ephren, he could be a bi[g] COI"); DE 15 (4.6.09 Batt to Taylor email: "I am here to make it happen for you guys"); DE 23 (8/11/09 Batt to Taylor email: "THANK YOU FOR MAKING ME #1 LAST MONTH—LETS MAKE MONEY TOG[E]THER !!!"); DE 362.

In their initial conversation, Taylor told Batt that self-directed IRAs were "big moneymaker[s]" for City Capital, but that he was unhappy with the slowness of the IRA custodians he was using. DE 36 at 12 (44-45). Taylor said he was "focusing on speed" and looking for a custodian that could "expedite the process." *Id.*; DE 796 at 36 (2/15/08 Batt note: "[Taylor] has used pensco and entrust, but does not like their transaction times"). As Taylor soon discovered, Equity Trust was "[s]ignificantly faster" in processing investments than other custodians and over time "[i]t actually got faster...[to] about two weeks." DE 36 at 13 (46-47).

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[5] The parties conducted a deposition of Taylor at the prison in Texas where he is serving a 223 month sentence for his conviction in the parallel criminal case. The video of the deposition was admitted into evidence and played in its entirety before the ALJ. DE 36-37.

In 2008, Equity Trust Was Warned That Taylor Was a "Crook"

In October 2008, at Equity Trust's Accelerated Wealth Building Boot Camp, an accountant named Al Aiello, now deceased, was an invited speaker. DE 821 at 3-4 (line 4). J. Desich, Dea, and Equity Trust's National Speaker Edwin Kelly also attended this event. DE 20; Tr. 600. When Aiello noticed E. Kelly reading an Ephren Taylor book, Aiello told E. Kelly "that guy's a crook." Tr. 600-601. Aiello explained that one of his clients loaned Taylor $600,000, which Taylor never paid back, and that Taylor refused contact with the client. Tr. 601. E. Kelly was "taken aback," and told Aiello "that's a problem" because Equity Trust had "clients who are holding assets that Ephren Taylor is investing in." *Id.* E. Kelly immediately informed J. Desich about his conversation with Aiello. Tr. 602-603. J. Desich told E. Kelly to "tell Mike Dea," which E. Kelly did. Tr. 603-04. E. Kelly did not recall any follow up from J. Desich or Dea. Tr. 604.[6] Shortly thereafter, a Taylor representative contacted E. Kelly to arrange a webinar. E. Kelly declined based on Aiello's "crook" allegation. Tr. 604-605.

Batt Gave Credibility to Potential Taylor Investors

Taylor testified that if a potential investor needed a "credible independent source," then Batt "help[ed] the closing process. . .[and] gave us a boost of credibility." DE 36 at 30-31 (116-117). Batt also provided "additional convincing" to hesitant investors. DE 36 at 16 (59). *See also* DE 36 at 16 (58) (if investor was "getting cold feet," Batt "brought a different level of credibility"). Investors reported to Taylor that they had "talked to the bank" and that "[Batt] had great things to say" about Taylor and City Capital. DE 36 at 16 (58-59). For Taylor, Batt

[6] The ALJ dismissed the significance of these conversations as "not memorable so as to constitute red flags putting Desich and Dea on notice that Taylor was a crook." ID at 10. This fails to give sufficient weight to the accusation of Equity Trust's own guest speaker who called Taylor a "crook" and to Equity Trust's own National Speaker who was alarmed by and relayed that warning to other senior officers of Equity Trust.

provided a "transference of a credibility from Equity Trust []to City [Capital]." DE 36 at 16 (58).

Taylor Emphasized Equity Trust in Sales Pitches

As Equity Trust knew, self-directed IRAs and Equity Trust itself were integral to how Taylor pitched his promissory notes to investors. DE 36 at 11 (39). Taylor also promoted his relationship with Equity Trust and self-directed IRAs in public statements and in the press. DE 13 at 5-6 (2009 Bankrate.com article); DE 13 at 1 (1/5/09 Taylor email to Batt: "Should I get an Endorsement deal with Equity Trust"); DE 36 at 29 (112).

One of Taylor's key promotional tools was a booklet titled *3 Simple Steps to Double Your Return Retirement,* known as "the Whitepaper." Equity Trust received copies of the Whitepaper (DE 272; 35 at 1; 509), and it was given to numerous investors (DE 662-667), including Dorothy Sims. DE 728 at 1. The Whitepaper emphasized City Capital's "close working relationship" with Equity Trust and stated that Equity Trust "understand[s] these unique self-directed investments and the kind of boost they can mean to your retirement plan." DE 35 at 14.

Batt Helped Taylor "Close" the $1.3 Million Dorio Investment

The single largest investment in City Capital's history was $1.3 million in retirement funds held in an AIG account controlled by a Texas resident named Anita Dorio. Dorio first met Taylor at her church in Houston, Texas, and, at Taylor's urging, she opened an Equity Trust account. Dorio and her husband, however, were "initially very skeptical." DE 36 at 30 (115).

In early 2009, Dorio's investment advisor, Richard Wheeler, sent her a letter expressing concern about the City Capital investment. Tr. 817; DE 830. Wheeler's letter warned Dorio about moving her money into private placements because the "income stream is NOT guaranteed" and she may not be able "to get out of the investment program." DE 830. *See also* Tr. 817; 820. Dorio then called Batt to discuss Wheeler's letter.

After the call, Batt emailed Taylor that he had "a conference call with Anita [Dorio] today and it was a good call." DE 14. Referring to Wheeler's letter, Batt wrote:

> The letter basically trashed commercial real estate and said don't transfer out... 'you will regret it.' It was so cheesy it sounded like a 1st grader wrote it. I said 'Anita....how can you comment on something you know nothing about....how can this broker comment on real estate when he has never done it'. She said 'great point' lets do it.

Id. Batt's email to Taylor concluded: "I am on it...I will close it." *Id. See also* DE 36 at 30 (115) (Taylor: "[Batt] was able to dismantle the financial advisor on the call, get the Dorios settled, calmed down, and get their confidence in the deal that was on the table. He got that sold and he got on the phone and got the money transferred over.").

The ALJ found that Batt's conduct in connection with the Dorio investment "constituted a recommendation to invest" with Taylor. ID at 36.

Batt Trained City Capital Employees

In June 2009, Batt visited City Capital's headquarters in Raleigh, NC, to train City Capital employees on self-directed IRAs and Equity Trust's account documents. DE 36 at 18 (67-68); Tr. 418-419. Equity Trust's policy encouraged such visits to issuers (Tr. 231), and Batt's PowerPoint at the time recommended that investors "Do a Deal with City Capital"; DE 368 at 28; Tr. 419.

Batt conducted an additional training for City Capital personnel on October 12, 2009, right before Batt's appearance at Taylor's Wealth Tour at New Birth Church. DE 796 at 270.

Batt's Attendance at Taylor's New Birth Church "Wealth Tour"

In October 2009, Batt proposed to his supervisors that he be permitted to attend an event of Taylor's at the New Birth Church near Atlanta, which was part of Taylor's "Wealth Tour."

Batt told his supervisor Marsh that he would appear on stage with Taylor, "pitch 4000 people," and have "5-10 minutes speaking time." DE 367; DE 363; Tr. 401-402; DE 509. As the event would provide an opportunity to open new accounts, Batt received approval to attend. Tr. 235-236. Batt instructed Equity Trust's marketing department to send "800 packets ASAP," which included new account applications. DE 356; Tr. 398; 390. Batt was provided no training or guidance in advance of the event. Tr. 235.

On October 20, 2009, Batt attended Taylor's Wealth Tour in front of an audience of thousands. Batt was seated in the front with a brightly colored "Wealth Tour" badge clipped to his lapel. DE 800-J (Batt photo); RE 32 ("Wealth Tour" logo); DE 36 at 56 (217-218) ("Wealth Tour" referred to the "brand for all of [Taylor's] speaking engagements."). Taylor introduced his "special guest" Batt as "my banker" and added that "if you have any questions specifically about what I do, I figured, why not just bring the expert with me?" DE 800-B (video); DE 9 at 3-4. Taylor then told the New Birth Church audience that "you know it's something when the bank flies out your banker to hang out with you." *Id.* Batt stood, smiled broadly, and waved to the audience. DE 800-B (video); 800-H -L (photos).

Taylor also referred to Batt as his "qualified, educated, and informed financial professional" (DE 9 at 29-30; 800-C), and said that "if you don't have one or if you don't like the [financial advisor] you have because they've been losing all your money, I brought mine with me. He's right there. Robert, you might get bombarded, they might have the security escort you out right now." DE 9 at 30.

Batt knew that Taylor's statements about him were false. Tr. 408. Batt appeared to enjoy being in the spotlight and attendees viewed his presence as an endorsement of Taylor. Tr. 22-23; 1352-53; DE 800-B (video). *See also* DE 36 at 20 (74) (Taylor: "to have a representative from [Equity Trust] in the audience, it wasn't going to get any better than that. That was the . . . endorsement I needed – to make it happen.").

Following the service and the next morning, Batt and City Capital employees spoke with potential investors and helped them complete account opening documents. *See, e.g.*, DE 712 at 5-8 (Jones DOI); RE 179 at 20-23 (Turner DOI); DE 684 at 129-132 (Wells DOI). Neither Batt nor Equity Trust ever told investors that Taylor's statements were false. Tr. 406; 413. At the New Birth Church event, Taylor raised "a couple of million dollars," which gave Taylor and City Capital "a significant capital injection." DE 36 at 23 (86).

When he returned to Ohio, Batt told Marsh and others about the false statements made by Taylor at the event. Tr. 411-412. Batt was not reprimanded. Tr. 245-246; Tr. 292; Tr. 771-772; DE 518 at 6.

Several days after the event, Batt sent Taylor a congratulatory email: "you are awesome...thank you thank you." Taylor responded: "Ha! We make it rain?", and Batt replied: "From the National Weather Service: Weather Bulletin: - Category 4 Hurricane named 'Ephren' just hit Cleveland OH." DE 26.[7]

Investors Testified That Equity Trust Endorsed Taylor

Lawrence Hill is a sixty-four year old truck driver from Jacksonville, Florida. Hill met Taylor in 2008 and initially told Taylor that he was "pretty happy where I am," and "wasn't too sure" about moving his retirement funds. Tr. 171-172. Taylor then told Hill that "I'm going to give you the number of a company called Equity Trust, and ask for Robert Batt." Tr. 171. The next day, Hill called Batt and told Batt that "I talked with Mr. Taylor from City Capital, and I

[7] As the ALJ states, the New Birth event was "the first and only time" Batt and Taylor met face to face. ID at 15. Batt, however, repeatedly tried to arrange meetings with Taylor. DE 18; Tr. 368-369; 316; Tr. 371-372; DE 27; DE 796 at 30, 22 (7/31/08 Batt note: Taylor "might be visiting in August").

was just checking to see how was the company." Tr. 172. Batt responded "Mr. Hill, it's a good company and he's getting people right now 10 percent on their investment." *Id.* Hill "got kind of excited" with Batt's endorsement of Taylor because "10 percent sounded a little better" than the 4% he was getting, and Batt made Hill feel comfortable with Taylor. Tr. 173. Hill then invested with Taylor through Equity Trust. Tr. 166-167; DE 40 at 10, 13.

Ronald Jones, a high school teacher in Georgia, met Batt at New Birth Church. Jones testified that Batt was "very glowing in the remarks about Mr. Taylor." Tr. 111. Batt told Jones that Taylor was "[a] child prodigy," that Taylor has "done well on Wall Street" and that Taylor "has a very good reputation." *Id.* Batt also told Jones that Taylor was doing "good work" and was engaged in "urban revitalization." Tr. 145. Batt "absolutely" had an effect on Jones' decision to make the investment. Tr. 113. Jones testified that "clearly, ... Equity Trust did endorse Mr. Taylor and City Capital Corp." Tr. 159. *See also* Tr. 156 (Equity Trust was "endorsing City Capital Corp. and Ephren Taylor"). Jones then invested with Taylor through Equity Trust. Tr. 120, 98; DE 40 at 13.

Crystal Turner, an unemployed medical technician with five children, heard Taylor's presentation at New Birth Church. She testified that having "a banker there to support Ephren" helped make the decision to invest a "slam dunk." Tr. 1395-1396. When Taylor finished speaking, Turner approached Batt, who told her that "he had been to several different places with Ephren." Tr. 1354. Turner "was comforted to know that he had been doing several tours with him, had been to different places with him." Tr. 1354. *See also* Tr. 1353. Turner then invested with Taylor through Equity Trust. Tr. 1365-1368.

Lillian Wells also attended New Birth. After hearing Taylor speak, she approached Batt to inquire about self-directed IRAs generally. Tr. 23-24. Although Wells did not ask about investing with Taylor, Batt told her that "what I'll need to do is to get you with an appointment set up and everything," and walked Wells over to meet Taylor. Tr. 24-25. Batt motioned to Taylor, and told Taylor that Wells "was interested in setting up an account." Tr. 24-25. Taylor then had someone come over and schedule an appointment for Wells. Tr. 25. Wells then invested with Taylor through Equity Trust.

Equity Trust's Website Promoted Taylor

Equity Trust launched a landing page for City Capital that went live in August 2009. DE 338; 322-324; 331-332; 334; 338; 525. Taylor recalled seeing the landing page live as recently as either 2013 or 2014, and he was aware of two or three investors who viewed the landing page. DE 36 at 19 (71), 81 (312-313).[8] The landing page, which displayed the Equity Trust logo at the top and, in large bold font, the text "City Capital Corporation – Wealth Builder Network." The landing page included links to Equity Trust's self-directed IRA opening application and DOI, and included Batt's picture and contact information. *Id.*

Taylor testified that the landing page was "a huge credibility booster." DE 36 at 19 (70). He regarded the web site as "a little section on the Equity Trust Web site and now we're officially in bed together, so – we spun and touted that a little bit with our marketing materials and the clients and customers." DE 36 at 19 (70). City Capital sales staff "screen-captured" the landing page and used it in their marketing materials. Tr. 70-71.

[8] The ALJ stated that the City Capital landing page "reached the beta stage" and that the "parties dispute whether it ever went live on the Equity Trust website." ID at 14. This "dispute," however, did not arise until the hearing when Equity Trust suddenly changed its position. Tr. 484. Until that point, including throughout the investigation, Equity Trust had repeatedly admitted that the City Capital landing page went live. *See* DE 575 (City Capital landing page was "active on the ETC website"); Answer ¶ 37 (7/9/15: "...there were a total of approximately 50 visits to this landing page prior to the time ETC stopped doing business with Taylor"); Resp. Pre-Hearing Brief dated Nov. 23, 2015 at 7-8; 31 ("the page went live back in 2009").

Batt Closely Tracked Transfers and Disclosed these Transfers to Taylor and City Capital

In dozens of emails, Batt regularly provided confidential customer information to City Capital, including amounts that had been transferred to Equity Trust, the timing of transfers to Equity Trust, Batt's efforts to expedite transfers, and whether he lost contact with potential investors. *See, e.g.*, DE 275; 277; 282-285; 288-294; 297-301; 304-305; 307-308; 310-311; 318; 321; 327; 329-330; 335-336; 339-340; 343; 349-353; 359; 378-379; 381-387; 391-393; 397-399; 401-407. *See also* DE 36 at 15 (54-55). These updates were contrary to Equity Trust's privacy policy. DE 46 at 20-21.

Taylor testified that having "that type of data and intelligence...would alert us to any issues. If a client kind of fell off the radar, couldn't be reached, one of the sales guys could swing back around and try to do a save or recoup." DE 36 at 15 (54-55). These updates from Batt also allowed City Capital to "cut down the processing time tremendously." *Id.*

Equity Trust Knew That Half of the "Secured" Taylor Notes Were Unsecured

Many of the DOIs for the Taylor notes showed that the customers intended for the notes to be secured. DE 40 at 5-6. For the customers' intent to be met, the Taylor Notes would have to "clearly stat[e]" the collateral and be accompanied by a security agreement. DE 40 at 35; DE 53 at 3, 14. Despite Equity Trust's knowledge that the security agreement was absent, Equity Trust released its customers' retirement funds to Taylor. DE 40 at 5-6. City Capital knew that by marking the DOIs as secured, the Taylor Notes would be more attractive to investors. *See, e.g.*, DE 24; Tr. 1407-1408 (Sims: "a secured note, it protects you against risk").

Equity Trust created a "special procedure" for City Capital – undisclosed to customers – allowing Equity Trust to circumvent its own policies and process "secured" notes without a security agreement. DE 444 at 4-5 (line 15). *See, e.g.*, DE 661 (collection of 15 City Capital investment packages with letter from City Capital to Equity Trust's "Investment Processing Team": "There has been no security agreement needed thus far"); DE 719 at 130-131. For nearly twelve months, Equity Trust processed "secured" Taylor Notes without asking for or receiving a security agreement. DE 40 at 30.

In October 2009, Equity Trust's compliance director, Sandra Sarudis, told Batt and others that Equity Trust had improperly processed notes without security agreements, and that just because notes were processed that way in the past "doesn't mean [they] should have been...[T]he terms of the note may have been overlooked." DE 374 at 1.

Batt's supervisor Marsh responded to Sarudis that he and Batt would "see if we can navigate this land min[e]" and expressed concern that Equity Trust, by demanding security agreements, could be seen "to have changed the process midway." *Id.* Marsh's solution was to propose telling City Capital "ok now moving forward we overlooked the prom notes and now need this." *Id.* Sarudis responded that Equity Trust "did not change our process midway...this appears to have been overlooked...we SHOULD have asked for it last time." Sarudis accurately stated the problem: "I am very concerned that we did not ask for collateral on the prior note seeing that the client stated it secured." *Id.*

Batt and Marsh, however, were worried only about the reaction of Taylor and City Capital. Batt informed Taylor of the issue in an email, cc'ing Marsh:

> The current direction of investments show the notes are secured. However, looking at the prom notes they do not show by what or mention what is secured. If the notes are unsecured please check unsecured on the DOI's. If the notes [are] secured please list in the prom note a quick paragraph of what the notes are secured by. Keith Marsh and I appreciate your business – let's make money together! PS- when are you coming to Cleveland, I have a nice Brazilian steak house I want to take you and Kinetra too.

DE 27.

By early 2010, after J. Desich and Dea became involved, Equity Trust "updated" its records to show that the notes were unsecured. DE 410 at 1; DE 434 at 1; *see also* DE 420. Equity Trust also unilaterally changed the designation of 13 customers' quarterly account statements from "secured" to "unsecured," but never told customers the reason. DE 40 at 10-14 (column P=Yes; column M=No; and column N=Yes); DE 731 at 6; Tr. 1410-1411. For 23 other Taylor noteholders, however, Equity Trust neglected to make any change. DE 40 at 10-14 (column P). As a result, those account statements continued to state the note was secured when it was not. DE 40 at 10-14 (column P=Yes; column M=No; and column N=Yes). *See also* DE 40 at 11, 16; Tr. 805-806; 814; (Dorio "absolutely" understood she had a secured note and her account statements at all times indicated she had "secured" notes).

Equity Trust Had Access to Negative Public Information Regarding Taylor

City Capital's public filings disclosed that, in 2008 and 2009, City Capital's debt was skyrocketing, it had almost no assets or income, and had an unsustainable business model consisting of, in the word of an internal auditor, "basically issuing notes for cash." Tr. 1741-1742; RE 2; DE 538 at 7, 43, 64, 79, 106, 275; DE 537 at 6 (City Capital SEC filings reflecting "going concern" opinion dating in a 2007 Form 10-K).

In addition, a blog called Ripoff Report, which was reviewed by Equity Trust in connection with its account review procedures, included a post in 2007 describing Taylor as "dishonest." DE 810. *See also* 811-813; Tr. 707 (Dea: Equity Trust reviews "all publicly available information"); 728-729, 737. Forbes Magazine reported on March 3, 2009 that Taylor's "touch has been less than golden [with City Capital]: For the trailing 12 months ended last September, the company lost $2.9 million on sales of $305,000." DE 814 at 2. A 2006 article in the Kansas City Business Journal disclosed "a lawsuit filed against Taylor by area investors and a contractor who claim they were swindled in one of his earlier East Side housing ventures . . . [Taylor] faces a default judgment after failing to respond to repeated requests for discovery." DE 809. Numerous other lawsuits alleged that Taylor failed to pay promissory notes and fraudulently induced an investment. DE 819 at 16; DE 818; DE 817; DE 820.

Equity Trust Continued to Process City Capital Investments Even After Putting It on the Do Not Process List

Equity Trust flagged City Capital for a review in December 2008, although the review of City Capital did not start until September 10, 2009 due to a lack of audit staff. DE 526; DE 566 at 5 (backlog of reviews); DE 566 at 2 (reflecting 53 investments that triggered a secondary review in 2008); Tr. 1576-1580 (Dea: in 2009, "we didn't really have the support staff"); DE 594 at 5; DE 595 at 7; DE 596 at 4.

On December 29, 2009, Equity Trust placed City Capital on its "hold" list because of the number of matured and unpaid promissory notes; a going concern opinion from City Capital's auditor contained in SEC filings; and a high level of debt that was apparent from the company's SEC filings. Tr. 1585-1589; DE 519 at 2; Answer ¶ 44.

In early January 2010, Dea, Taylor and others were on a call in which, according to Taylor, he was accused of "running a fraud." DE 36 at 26 (99-101). On January 14, 2010, Sarudis emailed Taylor, copying Dea, to confirm that "we cannot accept any new investments with City Capital regardless of their structure due to the concentration level." DE 31 at 2. Equity Trust moved City Capital from the "hold" list to the Do Not Process list in either January or February 2010. DE 526; 517; 519; DE 469 at 4.

From January 2010 through October 2010, Equity Trust processed 21 renewals, extensions, or conversions of Taylor Notes. During this time, it learned additional adverse information concerning Taylor, including two separate lawyer's letters stating their clients had not been repaid by Taylor and a blog post warning of Taylor's "scam." DE 461; DE 485; Tr. 896; DE 487. Investors were never informed of the decision to put Taylor on the Do Not Process list.

EQUITY TRUST AND RANDY POULSON

From January 2007 through May 2011, a total of 34 Equity Trust customers made 41 investments with Poulson, for a total of approximately $984,998. DE 41at 2. Most of these investments defaulted, resulting in a complete loss for 33 of 41 investments. *Id.*

Poulson's company issued promissory notes purportedly secured by real property that paid interest rates from approximately 12% to 20% for terms of six months to five years (the "Poulson Notes"). DE 41 at 2; DE 743 at 39-42. Poulson represented to investors that the investments would be used to purchase, maintain, and improve the respective properties, including making payments on the existing mortgages. DE 267 at 32.

Poulson misappropriated a significant amount of the funds for his personal use. DE 267 at 32; DE 41 at 2-3; Tr. 502-504. In addition, investors believed that real property secured the Poulson notes, and the investors were provided a draft mortgage. DE 41 at 29; Tr. 503; DE 751 at 50; Tr. 1260-1263; Tr. 1077-1078; DE 743 at 41. However, Poulson did not disclose his unrecorded mortgages, which do not appear in public searches. DE 41 at 4, 29; Tr. 1098; Tr. 1274; DE 41 at 4; Tr. 1766.

Poulson's investors believed that the mortgages securing their notes were recorded, but they were not. DE 41 at 4; Tr. 1766; DE 41 at 29; Tr. 503; DE 751 at 50; Tr. 1260-1263; Tr. 1077-1079; DE 743 at 41. Unrecorded mortgages are "pretty much worthless." Tr. 1263.

Equity Trust Promoted Poulson

Equity Trust sales representatives Irene Berlovan, and later Robert Yurgalewicz, were assigned to work with Poulson as their COI. An Equity Trust marketing department employee named Jeanne Arnholt, and E. Kelly, also worked with Berlovan to sponsor and promote Poulson.[9]

Equity Trust's goal was to "partner" with Poulson and to "support" him from a "marketing perspective." DE 146 at 1; DE 145. To this end, Arnholt emailed J. Desich that "Randy Poulson is a client and had consistently been referring people to us," and added that Berlovan was "very attentive to [Poulson's] needs" and that she's "done a great job with him." DE 150 at 1. *See also* DE 149; 147. In September 2009, Poulson was added to the approved guest speaker list. DE 581 at 8-9. At this point, Equity Trust had 19 Poulson Notes that were not fully executed and 17 with unrecorded mortgages. DE 41 at 17-18.

Berlovan and Edwin Kelly Appeared at Poulson's April 2009 "Extravaganza"

In mid-March 2009, Arnholt talked with two supervisors, Jeffrey Bartlett and Brad Hemstreet, about having E. Kelly address a Poulson promotional event, entitled "Poulson Russo 4 Day Live Interactive Liquidation Extravaganza" scheduled for April 2009. DE 746. Arnholt emailed E. Kelly and Berlovan that Bartlett "likes the idea but wants to see what they actually pull together." DE 152 at 2-3. On April 1, 2009, Poulson asked Berlovan about "Edwin Kelly's availability to speak at my upcoming 4 day live event in April," and asked Berlovan to "mail me 200 of your business cards ASAP!" DE 142 at 11; DE 153 at 4. Berlovan emailed back within

[9] Poulson learned about Equity Trust from attending real estate seminars of Ronald LeGrand, a real estate promoter who was repeatedly investigated and subject to orders by state banking authorities, and charged by the SEC with fraud. Tr. 497-499; DE 845-847; DE 591. Desich Sr. also credits LeGrand, an approved speaker for Equity Trust who frequently spoke at its events, with inspiring Equity Trust's aggressive promotion of self-directed IRAs. DE 838A at 2; DE 581 at 8; DE 582 at 1, 9, 12, 14, 18; DE 583 at 2, 5-8; Tr. 672-673.

an hour: "I have dropped 200 cards in the mail it will go out tomorrow. Also I believe Edwin [Kelly] will be attending [the April 2009 event]." DE 153 at 3.

A "Speaker's Agreement" between Equity Trust and Poulson regarding the "Liquidation Extravaganza" stated that "product sales are encouraged and IRAs will be made available," and that "Self-directed retirement accounts will be made available to the audience during the presentation!" DE 142 at 1, 5. In addition, product sales at the event would be split with Poulson. DE 142 at 2. Equity Trust paid Poulson $4,819 under this agreement. DE 142 at 2; DE 186 at 23 (line 395); Tr. 612-613.

Berlovan had a booth just outside the main conference room where she had Equity Trust materials. Tr. 1221. During the event, Poulson warmly introduced Berlovan to the audience as a member of his "power team," and added that "[t]here is no better company [than Equity Trust] that is out there that truly understands exactly what it is we do, and caters to individuals just like us in this room. With that, I don't want to steal any of her thunder, but here she is from Ohio. Flew all the way in with her team. Irene Berlovan." DE 824 at 69 (270).

Berlovan then took the microphone from Poulson and addressed the audience: "Thanks so much, Randy. That was a very, very nice introduction there. I'm very excited to be here and that Randy invited Equity Trust Company. It's a very, very neat concept to be able to utilize [] your IRA money just as you use your money today. To go ahead and build your future income." *Id.*

Berlovan concluded by saying, "I help individuals and I also help investment sponsors like Randy. So if you have clients, if you're a CPA and you need someone to be your primary contact, I can be that for you, as well. Okay? So I'm excited. Thank you." *Id.* at 69 (271); DE 262-A (video of Poulson's introduction and Berlovan's remarks); DE 262-C, D, E (photos).

Berlovan gave no disclaimers and never refuted Poulson's claim that Equity Trust was part of his "power team," a phrase meaning "partner[ing] up" to "get business" from the relationship. Tr. 1219; 1221; Tr. 518-519; Tr. 1764-1765. Poulson also promoted E. Kelly's presentation the next day, which Poulson referred to as "one if the best presentations that I've seen," (DE 824 at 69 (269)), and referred to Equity Trust's presence at the event repeatedly. DE 824 at 64 (251) (Poulson: "Equity Trust is in the hall. They'll be presenting tomorrow."); DE 824 at 64 (253) (Poulson: "Irene [Berlovan] is out in the hallway. Go introduce yourself to her. . .. She'll be introducing herself to us later this evening or first thing in the morning, and Edwin [Kelly] will be making a two hour presentation about self-directed Roth IRAs tomorrow evening. This is how you utilize private money.").

On her post-event evaluation form, Berlovan reported that there were 100 attendees, that 5 accounts were opened at the event, 2 accounts were "fully funded," and 48 "qualified leads" were brought back. DE 264 at 6; Tr. 1241. *See also* DE 264 at 1-5.

Berlovan Gave a "Glowing Endorsement" of Poulson

Joseph Gatto, a retired engineer, met Poulson at a New Jersey real estate investors club. Tr. 1256-1257. Gatto testified that Poulson recommended Equity Trust as "his IRA custodian of choice" because the investments were "easier to get through." Tr. 1258-1259. Gatto testified that Poulson had "a stack of [Berlovan's] cards and he would pass them out." Tr. 1262. Gatto told Berlovan that "this is my career savings, 20 years in the government. This is all I have." Tr. 1261. Berlovan made "glowing remarks about Randy" and assured Gatto that she "has many clients with Randy, never had a problem, he's a great guy, she knows him, she works with him." Tr. 1261. Berlovan further assured Gatto that Poulson "knew what he was doing, he was knowledgeable." Tr. 1262.

Gatto took his phone conversation with Berlovan as "a ringing endorsement of Mr. Poulson," (Tr. 1341), and testified that Berlovan's "glowing recommendation" of Poulson was "pretty much a deciding factor" in Gatto's decision to invest with Poulson through Equity Trust. Tr. 1262.

Equity Trust Sponsored Poulson's Dinner Series

In an August 2009 email entitled "Real Estate Wealth Alliance [REWA] Business Sponsorship Opportunity," Poulson invited Equity Trust to sponsor his "monthly dinner events." DE 160 at 1. Poulson's invitation arose "as a result of your continued strategic alliance with us." *Id.* Among the benefits to sponsorship were "a table at each REWA Dinner Event to set-up a display of your informational pieces and/or products," and "exclusive access" to those in attendance. DE 160 at 11, 1. The "sponsor" would also be "fully endorsed" by Poulson. DE 160 at1.

Berlovan emailed a colleague that the proposed sponsorship was "a great opportunity" because Poulson "has brought us numerous clients and when we attended his event in April Edwin [Kelly] sold 18 CD sets." DE 160 at 1; Tr. 1223:6-9. Arnholt responded that it "seems very reasonable for $600 to sponsor." DE 165 at 1.

In September 2009, Arnholt emailed Poulson that Equity Trust would "do the $600 level sponsorship for your events." DE 168 at 5. Poulson responded that "I greatly appreciate your willingness to sponsor our Real Estate Wealth Alliance." DE 168 at 4; Tr. 527. On September 6, Poulson again thanked Arnholt and Berlovan "for agreeing to sponsor our monthly dinner events for the next year in the amount of $600.00." DE 169 at 3. Poulson also requested "250-300 folders containing information about Equity Trust and IRAs that you want distributed to our audience on September 16." *Id.* at 2. Arnholt told Poulson that she would "work with our marketing coordinator to get you the packets as requested below." *Id.* In approving the sponsorship, Berlovan's supervisor noted that the purpose was "generating accounts – would like to support." DE 174 at 1. Berlovan and E. Kelly planned to attend the dinner series in person once the series "ramped up." *Id.* at 2.

Poulson later sent Berlovan lists of attendees at the dinner events, in addition to attendance lists of attendees at April 2009 Extravaganza and another June 2009 event. DE 183; 184. Berlovan used the names to pursue leads. DE 174 at 2; DE 796 at 210, 219, 243, 253 (Berlovan's notes of follow-ups with Poulson event attendees).

Equity Trust Solicited Poulson's Sponsorship and Presence at Equity Trust Events

In August 2009, Equity Trust invited Poulson to sponsor and speak at an Equity Trust "networking" event in Orlando, Florida. DE 163 at 3-4. Poulson responded that he "would like to sponsor this event" and asked "whether or not we may have the opportunity to present/speak in front of the entire audience?" DE 163 at 1. Arnholt suggested that Poulson speak at "an early morning session" or "a lunch." *Id.* As for the lunch, Arnholt told Poulson: "It's a bit more $10,000 (but I might be able to take it down a bit for you) or a breakfast sponsor." *Id.* Arnholt then told Poulson that a lunch sponsorship "guarantees you an audience." *Id.* The following month, Poulson was approved and placed on the Guest Speaker List. DE 581 at 8-9.

Poulson emailed Berlovan that he would "welcome the opportunity" to present at the Orlando event. DE 144 at 2; DE 168 at 4. When Poulson said he could not attend, Arnholt proposed that Poulson be a "break sponsor," DE 168 at 4, which would include "Signage and marketing info and logos – and mentions etc." DE 168 at 2-3. Poulson responded that he would "love to sponsor one of the breaks for $750.00" and that he "would love to participate on a larger scale next year." DE 168 at 2.

Equity Trust and Poulson then discussed the details of the break sponsorship, which included passing out Poulson's materials and preparing a sign. DE 168 at 1; DE 169 at 3; DE 181; DE 182. Arnholt later confirmed to Poulson his status as a "Networking Break Sponsor," and that she "reduced the cost for [Poulson]." DE 169 at 1. Poulson and Equity Trust agreed to net the $600 owed to Poulson for sponsoring his REWA dinners against the $750 Poulson owed Equity Trust for the break sponsorship; Poulson ended up owing Equity Trust $150 (which he never paid). DE 188 at 1-3; DE 193.

On March 31, 2010, Arnholt repeatedly solicited Poulson's sponsorship of the 2010 Equity University Networking Conference Sponsorships. DE 193 at 2; DE 243 at 1-2.

Equity Trust Knew that No Recorded Mortgages Secured the Poulson Notes

In June 2010, Equity Trust's secondary review showed that all 25 Poulson investments had "Inadequate Documentation on file to support investment" and no Poulson investments had "Adequate Documentation." DE 256 at 3. Six months after this finding, and after additional Poulson investments were made, Mary Juristy, a compliance manager, emailed Poulson a two-page "Requested Document List" showing the missing mortgages. DE 209, 212 at 2-3.

Poulson became concerned that, because he did not have the recorded mortgages, his scheme would be uncovered. Tr. 540. Poulson then emailed Juristy that he would pull together the documents "within a month or so," (DE 214 at 1), but continued to give Juristy excuses throughout December 2010 and January 2011. DE 217 at 1; DE 221; DE 224; DE 225.

In February 2011, after telling Juristy that he had to "re-create some of the documents from scratch," (DE 226 at 1), Poulson sent some promissory notes and extensions, but not the absent recorded mortgages. Juristy made no further inquiries. DE 256 (review conducted in 2011 shows document deficiencies with 25 of 33 Poulson Notes); DE 245; Tr. 544-545.

Despite the missing documents, Robert Yurgalewicz, the Equity Trust sales representative who took over from Berlovan, began soliciting referrals from Poulson. Poulson responded that he "will be sure to begin referring clients to you that are interested in opening an IRA with ETC." DE 194 at 1; DE 41 at 11-14. From 2010 through late 2011, Equity Trust continued to advise Poulson of referrals and provided a substantial amount of confidential customer information, even though Equity Trust knew of the widespread document deficiencies. DE 205; DE 208; DE 231-232; DE 239-240; DE 201; DE 204; DE 244.

In another review begun on July 11, 2011, Equity Trust noted that 25 of 33 investments had inadequate documentation. DE 256 at. 2. There were also 13 matured and unpaid notes. DE 256 at 2. During the 2011 review, Juristy admitted that, with respect to Poulson's initial secondary review, "I [] don't think a background was actually done since I did not see it on the sheet to inquire about during my interview." DE 245 at 1. On November 17, 2011, Equity Trust's risk committee put Poulson on the "hold" list. DE 256 at 2.[10]

Several weeks later, Equity Trust received a grand jury subpoena from the U.S. Attorney's Office for the District of New Jersey, seeking information about Poulson. DE 248. Poulson was placed on the Do Not Process list on October 25, 2012. DE 578 at 28.

[10] Although the ALJ found "no evidence" to support a finding that Equity Trust told a customer who extended after May 2011 about "Poulson's status," the ALJ nevertheless "found that Equity Trust did not fail to communicate Poulson's status to the customer." ID at 27 n.30. This is contradicted by the evidence. Equity Trust's policy was to never tell customers the reason for a "hold" or Do Not Process decision (DE 442), which was confirmed by investor testimony. For example, the first time Gatto heard that there was a problem with Poulson was when the FBI knocked on his door. Tr. 1272; 1275; 1277.

ARGUMENT

I. DETERMINING LIABILITY FOR CAUSING UNDER SECTION 8A OF THE SECURITIES ACT OF 1933

Section 8A of the Securities Act authorizes the Commission to impose sanctions if it finds that "any person is violating" the securities laws; the same section also authorizes sanctions against "any other person that is, was or would be a cause of the violation, due to an act or omission the person knew or should have known would contribute to such violation[.]" 15 U.S.C. § 77h-1(a). Causing liability is designed "to provide a flexible remedy against persons who commit isolated infractions and present less threat to investors than do persons against whom injunctive relief is sought." *KPMG Peat Marwick LLP*, S.E.C. Rel. No. 1360, 2001 WL 47245 at *20 (Jan. 19, 2001).

Causing liability requires three elements: (1) a primary violation; (2) acts or omissions by the Respondent that were a cause of the violation; and (3) that the Respondent knew or should have known that its conduct would contribute to the primary violations. *Robert M. Fuller*, Rel. No. 8273, 2003 WL 22016309, *4 (Aug. 25, 2003), *pet. denied*, 95 F. App'x 361 (D.C. Cir. 2004).

The ALJ correctly found that the first two elements were established. Taylor and Poulson committed nonscienter primary violations through a "course of business that operated as a fraud on the purchasers of [their] notes." ID at 31. In addition, Equity Trust's "account-opening, investment processing, record-keeping, and marketing activities" constituted acts or omissions by Equity Trust that were a cause of these primary violations. ID at 32. The ALJ, however, found that the third element – that Equity Trust "knew or should have known" that its conduct would contribute to the primary violations – was "unproven." ID at 32.

The evidence proves that the "knew or should have known" element was satisfied. Section II *infra* shows that Equity Trust "knew" that its conduct would contribute to the primary violations, and Section III *infra* demonstrates that, in the alternative, Equity Trust, at a minimum, "should have known." Section IV *infra* summarizes the appropriate sanctions that should be imposed.[11]

II. EQUITY TRUST KNEW THAT ITS CONDUCT WOULD CONTRIBUTE TO THE PRIMARY VIOLATIONS

A. Knowledge of Taylor's Primary Violations

Equity Trust had actual knowledge of significant conduct constituting two of Taylor's primary violations: the marketing and sale of his promissory notes as secured when they were unsecured; and Taylor's misrepresentations about the role of Batt and Equity Trust during his Wealth Tour promotion at New Birth Church.[12]

Equity Trust knew of the absent security behind the Taylor Notes from the DOIs it received from City Capital. In February 2009, Equity Trust received 6 DOIs marked secured that were not accompanied by any security agreement, and that number more than doubled to 13 the next month. DE 40 at 30. By October 2009, Equity Trust had custody of 35 investments that it knew, based on the DOIs, were supposed to be secured but were in fact unsecured. *Id.* Equity Trust knew that because the DOIs were marked "secured," the promissory note should "clearly state" the collateral and be accompanied by a security agreement. *Supra* 20-22. But Equity Trust knew that the Taylor Notes referenced no collateral and there were no security agreements.

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[11] In evaluating the evidence, the Commission conducts an "independent, *de novo* review of the record." *Timbervest, LLC*, Rel. No. 4197, 2015 WL 5472520, at *1 (Sept. 17, 2015); *see also* 5 U.S.C. § 557(b).

[12] Equity Trust had knowledge of Taylor's and Poulson's violations through its employees and officers. *See, e.g., In re Parmalat Sec. Litig.*, 474 F. Supp. 2d 547, 550 n.12 (S.D.N.Y. 2007).

In an internal email in October 2009, Equity Trust's chief compliance officer wrote that she was "very concerned" because the security agreements "SHOULD" have been obtained and "this appears to have been overlooked." DE 374. Equity Trust nevertheless continued working with Taylor and processing his investments. *Supra 23-24.*

This was a material aspect of Taylor's scheme to defraud investors who believed they were acquiring secured, as opposed to unsecured, notes. *Application of Coastline Financial, Inc.*, Rel. No. 34-41989, 1999 WL 798874, at *3 (Comm. Oct. 7, 1999) (difference between a secured and unsecured note is "highly material"; "for a noteholder the difference between a secured and unsecured note can easily be the difference between being repaid and not"). *See* DE 24; Tr. 1407-1408; DE 808 at 1 (Equity Trust website: an unsecured note "is a higher risk than a secured note").

Equity Trust also knew of another primary violation: while pitching his notes at the New Birth Church to an audience of thousands of potential investors, Taylor made false and misleading statements about Equity Trust in order to project an air of legitimacy. Taylor referred repeatedly to Equity Trust and Batt, stating that Batt was his "banker" and a "qualified, educated, and informed financial professional" who could respond to "questions specifically about what I do." DE 9 at 3-4; 29-30; 800-C. Batt failed to correct any of these misrepresentations during his trip to Taylor's Wealth Tour, and Batt widely shared Taylor's false statements with supervisors and other colleagues at Equity Trust. Equity Trust processed 17 new investments for Taylor investors after the New Birth Church event, including from attendees at that event. DE 40 at 13-14; *supra* 15-17.

Equity Trust does not dispute that Taylor's statements were false. Tr. 404; 408; Answer ¶ 39. The ALJ, however, found that the Division "exaggerated" the significance of the episode and that Taylor merely "point[ed] out Batt in the audience and referr[ed] to him as his 'personal banker.'" ID at 35 n.39. The ALJ's benign view of the events at New Birth Church, however, is contradicted by the evidence.

Taylor clearly was making a sales pitch, and he told the congregation, "I run an investment fund. We're always looking for new investments." DE 9 at 28. By spotlighting Batt and Equity Trust early in his pitch, Taylor sought to legitimize himself and increase sales. Taylor boasted that "you know it's something when the bank flies out your banker to hang out with you." DE 9 at 4. Taylor also claimed that Batt was "a joy with our firm," and mentioned Batt and Equity Trust throughout his remarks. DE 9 at 4, 30 ("I brought my [financial advisor] with me. He's right there. Robert, you might get bombarded."), 67, 75. At the end of his remarks, Taylor told the crowd "if you're really looking to make a change in your life just see anybody that has...a Wealth Tour Live badge." DE 9 at 80.

Batt, of course, prominently wore a Wealth Tour Live badge and, as the video shows, appeared to be delighted at being singled out by Taylor. DE 800-B (video), 800-J (photo). Witnesses testified that Batt's presence was significant to their investment decision. One witness testified, for example, that she was impressed that Taylor's "personal banker" flew out to be with Taylor at the Wealth Tour. Tr. 1353-1354 (Turner: "I'm thinking this is legit because you don't often get big established banks sending their people to do business with a black guy in a predominantly black church. So it kind of made feel like this is . . . really good.").

Taylor's false statements about the role of Batt and Equity Trust were material. *See also Harding Advisory LLC*, Rel. No. 734, 2015 WL 137642, *60 (Init. Dec. Jan. 12, 2015) ("As a general matter, misrepresentations and omissions are material when they pertain to an independent professional on whose expertise investors rely.") (pet. for review granted on Feb. 23, 2015).

B. Knowledge of Poulson's Primary Violations

Poulson's primary sales pitch was that the promissory notes issued by his company were secured by mortgages on real estate. From July 2007 through May 2011, Equity Trust failed to collect the recorded mortgages that it was required to collect for the Poulson Notes.

By no later than June 2010, after Equity Trust conducted a secondary review of Poulson investments, Equity Trust knew that all 25 of the Poulson Notes under review – total face value of $719,000 – lacked recorded mortgages. DE 256 at 3; DE 198-199. Recorded mortgages are a critical component of promissory notes secured by property, and even unrecorded mortgages, as one witness testified, are worth only the "value of the paper…if there is no recorded lien against the property." Tr. 1766. *See* Tr. 1262-63. This is critical because Poulson's violations included failing to disclose unrecorded mortgages to prospective investors and failing to record the mortgages of those who invested with him. Tr. 1098; Tr. 1274; DE 41 at 29.

A reasonable custodian would have put Poulson on "hold" status right away, as its own policies required. DE 53 at 9. Equity Trust, though, despite knowing by no later than the June 2010 secondary review that there were no recorded mortgages, many of which were on the same properties, continued to process 9 new Poulson Notes through May 2011, and continued to process extensions for 8 Poulson Notes a total of 10 times into 2012. DE 41 at 4. Equity Trust finally stopped processing Poulson's investments as a result of another review started in July 2011 when it again learned that Poulson had never provided recorded mortgages. DE 245; DE 256 at 2; Tr. 544-545.

III. EQUITY TRUST SHOULD HAVE KNOWN ITS ACTS AND OMISSIONS WOULD CONTRIBUTE TO THE PRIMARY VIOLATIONS

While Equity Trust's knowledge is sufficient to satisfy the third element of causing liability, Equity Trust also "should have known" it was contributing to the primary violations. In analyzing whether Equity Trust "should have known," the ALJ erred by requiring knowledge of the fraud and then deriving a standard of care based on an investor alert. The Division presented a clear basis for determining the conduct of a reasonable custodian at the hearing and the evidence proved that Equity Trust acted highly unreasonably. Because Equity Trust did not act passively, any of the protections applicable to a passive custodian do not apply.

A. The ALJ Applied an Incorrect Standard of Care

1. The ALJ Incorrectly Required Knowledge of the Fraud

The ALJ erroneously framed the causing inquiry as whether Equity Trust had actual knowledge of the fraud. ID at 32. For example, the ALJ held that "unless Equity Trust assumed the role of investigator, it is unclear how it would have known of the fraud." *Id.* (knowledge of City Capital's troubles "is not the same as knowing that Taylor was engaged in fraud;" even if Equity Trust complied with standard of care, "it still would not have had knowledge of Poulson's fraud").

Even though knowledge can satisfy the third element (and as shown above Equity Trust had the requisite knowledge), the ALJ's formulation of "should have known" is a sharp departure from precedent. The "should have known" element does not require proof that the party causing the violation would have had actual knowledge of fraud and improperly elevates the level of proof required to demonstrate causing under Section 8A. Indeed, the phrase "knew or should have known" in Section 8A is "'classic negligence language,'" *KPMG, LLP v. SEC*, 289 F.3d 109, 120 (D.C. Cir. 2002), and "'negligence is sufficient to establish 'causing' liability...in cases in which a person is alleged to 'cause' a primary violation that does not require scienter.'" *Howard v. SEC*, 376 F.3d 1136, 1141 (D.C. Cir. 2004).

Negligence is "[t]he failure to exercise the standard of care that a reasonably prudent person would have exercised in a similar situation." *Thomas R. Delaney II*, Rel. No. 755, 2015 WL 1223971, at *44 (Init. Dec. Mar. 18, 2015) (Finality Order Apr. 29, 2015); *Vernazza v. SEC*, 327 F.3d 851, 861-62 (9th Cir. 2003) ("the standard of care...is ultimately one of 'reasonable prudence, whether it usually is complied with or not.'"); *Daniel Bogar*, Rel. No. 502, 2013 WL 3963608, at *24 (Init. Dec. Aug. 2, 2013) (causing liability established although "none of [the Respondents] acted with knowledge" but there was "a failure to exercise reasonable care"); *Albert Glenn Yesner, CPA*, Rel. No. 184, 2001 WL 587989, *35 (Init. Dec. May 22, 2001) (although Respondent "did not act knowingly, recklessly, or with conscious intent," his conduct was "unreasonable" and therefore a cause of company's violations of Sections 17(a)(2) and (a)(3)).

By requiring proof that Equity Trust knew of the fraud, the ALJ elevated the standard to one of knowledge or extreme recklessness, not negligence. *See, e.g.*, *SEC v. Steadman*, 967 F.2d 636, at 641-42 (D.C. Cir. 1992) (extreme recklessness could be found where there was "a danger...so obvious that the actor must have been aware of it").

2. The OIEA Alert Is Not Evidence of the Standard of Care

The ALJ incorrectly adopted an Investor Alert issued by the SEC's Office of Investor Education and Advocacy ("OIEA") in September 2011 as the "most convincing statement of the Commission's view of standards applicable to IRA custodians such as Equity Trust." ID at 34.

The OIEA alert, however, was not "a statement of the Commission's." It was never considered or approved by the Commission and, for that reason, explicitly states that it is "neither a legal interpretation nor a statement of SEC policy." RE at 46 at 5. In any event, the OIEA alert does not even purport to express any standard of care. Instead, it is merely a generalized statement that self-directed IRA custodians are passive and do not evaluate investment decisions. It says nothing about an IRA custodian, such as Equity Trust, that endorses and promotes issuers and makes recommendations. And using the OIEA investor alert as an element to clear Equity Trust of wrongdoing undermines the broader intent of the Alert, which was to warn investors of the risks of investing through self-directed IRAs.[13]

3. Ries Established the Duties of a Passive Custodian

Before and during the hearing, there was little dispute between the parties as to the duties of a passive custodian. Both the Division and Equity Trust agreed that, as a general matter, a reasonable custodian should remain passive; refrain from endorsing or promoting investments or investment strategies; take custody of documents evidencing the customers' intent; avoid conflicts of interest; adopt policies and procedures; and reasonably respond to red flags. These duties were consistent with the opinion of the Division's expert, William Ries. Prior to and during the hearing, Equity Trust never disputed Ries's qualifications or his opinion regarding the duties of a passive IRA custodian. The ALJ admitted Ries's expert report with no objection or cross-examination from Equity Trust.[14]

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[13] The ALJ also stated that the OIEA alert was "consistent" with an investor alert issued by the North American Securities Administrator Association ("NASAA"). NASAA's general counsel, however, testified that the NASAA investor alert was not a statement of the standard of care and was intended solely as a warning to investors of the risks of fraud associated with self-directed IRAs. Tr. 1833, 1835, 1825-26, 1843.

[14] Instead, Equity Trust relied on the rebuttal report of Terry Prendergast that argued that Ries's report failed to consider a South Dakota statute that, in Prendergast's view, relieved Equity Trust of any liability. RE 223. The ALJ did not rely on the Prendergast report, nor did the ALJ base her ruling on the statute cited by Prendergast. In any event, another Division

Ries's report, moreover, comports with Equity Trust's point that a "custodian's duties are typically determined by the terms of the custody agreement." DE 39 ¶ at 20. Ries's conclusions were also consistent with the testimony of S. Kelly, an examiner Equity Trust's banking regulator. Tr. 1156-1200.

Without support, the ALJ asserted that the duties expressed in the Ries report were "essentially made up of whole cloth" and "did not address current industry practice but rather aspirational best practices." ID at 33 n.37; 34. The fallacy of these assertions is demonstrated by the fact that Equity Trust itself never made either point when it had the opportunity and incentive to do so. The ALJ, moreover, failed to identify which aspect of the Ries report was "made up" or "aspirational." In fact, Ries's report was grounded in unimpeachable sources: customer agreements, South Dakota law, Equity Trust's own policies and procedures, the Internal Revenue Code and certain OCC and FDIC authorities. DE 39 *passim*; DE 105 at 1 (1/19/10 Equity Trust risk committee minutes: "the FDIC trusts exam manual is on-line... the SD exam follows it verbatim"). As a result, the Ries report should be relied upon as evidence of the duties and standard of care of a reasonable custodian.

B. Equity Trust Acted Unreasonably

The ALJ did not evaluate the reasonableness of Equity Trust's conduct. Instead, the ALJ erred by asserting that although Equity Trust's conduct "may have been undesirable" and "inconsistent" with Equity Trust's representations to its customers, these factors "do not bear on" whether Equity Trust should have known of the primary violations. ID at 35.

The ALJ's assertion that the reasonableness of Equity Trust's conduct is "not relevant" (*id.*) to the "should have known element" is wrong. On the contrary, the issue of whether Equity

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expert, Tom Simmons, demonstrated that the statute cited by Prendergast did not apply and that Prendergast failed to consider that Equity Trust was not acting as a passive custodian. DE 836.

Trust "should have known" that its conduct would contribute to the primary violations depends on whether, in light of its own negligent practices and interactions with Taylor and Poulson, it was reasonable for Equity Trust to fail to recognize it was contributing to their frauds.

As shown below, the evidence proves that Equity Trust in multiple different respects disregarded the duties of a passive custodian and acted highly unreasonably. By doing so, Equity Trust exposed its customers to additional risk and contributed to the primary violations. *See, e.g.*, *Thomas R. Delaney II*, 2015 WL 1223971, at *48 (Respondent "should have known that, by not acting with reasonable care . . . [Respondent] contributed to the circumstances where particular personnel could commit such violations.").

1. Equity Trust Acted Unreasonably by Endorsing and Recommending Taylor and Poulson Without Conducting Due Diligence or Warning Investors

Equity Trust acted unreasonably by endorsing, promoting, partnering with, and recommending Taylor and Poulson without conducting any due diligence and without informing investors of negative information. The ALJ, though, found that it was Taylor and Poulson "who promoted Equity Trust, not *vice versa*." ID at 35-36. This finding is contradicted not only by substantial evidence of Equity Trust's promotion and endorsement, but by the Initial Decision itself, which found that Batt's conduct relating to the Dorio investment with Taylor "constituted a recommendation to invest."[15] ID at 36.

The evidence of Equity Trust's endorsement and recommendation of Taylor and Poulson is significant. DE 36 at ¶¶ 37-46. For Taylor, Batt helped "close" deals by making positive

[15] The ALJ also stated that Equity Trust's promotion of self-directed IRAs was "not inconsistent" with its representations that it was passive. ID at 35, n.38. This ignores the broader point that Equity Trust's unreasonableness should be considered in light of both its specific promotion of Taylor and Poulson, and its aggressive and over-the-top promotion of risky investments where it knows its accounts have been targets of fraud.

comments to customers that gave them comfort in investing with Taylor; Batt trained City Capital personnel at its headquarters in North Carolina and again in a webinar on how to promote self-directed IRAs in their solicitations; Batt attended Taylor's New Birth Church event wearing one of Taylor's Wealth Tour badges and was falsely introduced as Taylor's banker, which gave investors comfort to invest with Taylor; Equity Trust hosted a landing page for City Capital; Batt made highly positive comments about Taylor to investors; and Equity Trust acquiesced in Taylor's promotion of Equity Trust in his sales materials. *Supra* 11-23.

For Poulson, Equity Trust's marketing department literally "partnered" with and "sponsored" Poulson; Equity Trust financially sponsored Poulson's monthly dinner events in exchange for Poulson using Equity Trust as his exclusive custodian; Berlovan attended one of Poulson's event and allowed Poulson to refer to Equity Trust as part of his "power team," after which attendees invested with Poulson; Poulson sent Berlovan the contact information for attendees after the event she attended; and Berlovan made "glowing" remarks about Poulson. *Supra* 24-31.

Equity Trust's promotion and recommendation happened both as part of its business model and as a result of its failing to have appropriate policies in place. DE 39 at ¶ 39. For example, as part of its business model, Equity Trust actively sought to partner with issuers in order to gain referrals, which led to account openings. These relationships foreseeably led to a significant conflict of interest for Equity Trust's sales representatives who were beholden to big issuers like Taylor and Poulson for account openings. *Supra* 5-8.

In spite of this conflict of interest, Equity Trust unreasonably failed to provide appropriate training or oversight to client-facing sales representatives like Batt and Berlovan on how to navigate working with issuers without endorsing them. *Supra* 7. The resulting promotion and recommendation of Taylor and Poulson is not surprising, and best summed up in an email that Batt sent to Taylor that captures the attitude of the sales representatives: "Let's make money together!" DE 27; DE 13. The conflict also led Equity Trust's representatives to regularly providing confidential customer information to Taylor and Poulson without customer authorization, which served to facilitate Taylor's and Poulson's ability to expeditiously obtain investor funds to fuel their frauds. *Supra* 20, 31.

Because Equity Trust did not act passively, the reasonableness of its conduct must be judged in light of its promotion and recommendation of Taylor and Poulson. This means that Equity Trust cannot hide behind the purported industry norms of a passive custodian, or behind provisions in its custodial agreement stating that Equity Trust does not evaluate investments or issuers.[16]

Indeed, as Ries testified, if custodians "take on duties and responsibilities that are outside the scope of the duties and responsibilities set forth in the custody agreement, the custodian is responsible for performing those additional duties in accordance with the standard of care applicable for the services provide." DE 39 at ¶ 22. "A custodian that endorses or recommends investments acts in a fiduciary capacity and as a result owes fiduciary duties to the principal with respect to providing such advice. As such, the custodian would be required to exercise

[16] Two Courts have rejected Equity Trust's arguments about the scope of its duties. *See Bentley v. Equity Trust Co.*, 2015 WL 7254796, at *1 (Ct. App. Ohio Nov. 16, 2015) ("broad exculpatory clauses, including a provision in which Equity Trust disclaims any fiduciary duties" do not preclude investors' tort claims "based on duties of conduct that are imposed by law"); *Mid-Ohio Securities Corp. v. Estate of Burns*, 790 F. Supp.2d 1263, 1265 (D. Nev. 2011) (upholding arbitration award; "Mid-Ohio was required to perform basic due diligence with regard to its customers' holdings, and [] it failed to do so.... Mid-Ohio should have realized that [issuer] was a fraud based on several red flags"). The ALJ erred by finding that *Bentley* and *Burns* "do[] not support the Division's position." ID at 36-37.

reasonable care, skill and caution in recommending an investment which would include investigating the investment being promoted or endorsed." DE 39 at ¶ 33.

Similarly, courts have regularly held that financial institutions acting outside the scope of industry norms or customer agreements take on duties commensurate with the additional conduct. For example, courts have held that brokers holding nondiscretionary accounts, which do not typically have duties beyond executing orders, have additional duties if they exceed the scope of that nondiscretionary relationship by, for example, giving investment advice. *See, e.g.*, *Anwar v. Fairfield Greenwich, Ltd.*, 745 F. Supp. 2d 360, 376-77 (S.D.N.Y. 2010) ("if the relationship between the parties develops beyond a nondiscretionary one – if, for example, one party begins giving investment advice – the duties increase").

In *Anwar*, a broker argued that he owed only limited duties to customers the customer accounts were nondiscretionary. *Id.* Because it was alleged that the broker made recommendations to his customers, the court found that even nondiscretionary brokers have a duty to recommend only after "studying [the investments] sufficiently to become informed as to [their] nature, price and financial prognosis." *Id. See also Ward v. Atl. Sec. Bank*, 777 So. 2d 1144, 1147 (Fla. Dist. Ct. App. 2001) ("while Stockholder had a non-discretionary account with Bank and had a long history of making his own investment decisions," the Bank's conduct in failing to sell Stockholder's shares as originally instructed and in offering advice meant that "Bank owed Stockholder a fiduciary duty of loyalty and care."); *Capital Bank v. MVB*, 644 So. 2d 515, 518-520 (Fla. Dist. Ct. App. 1994) (in a lender-borrower relationship, finding duties where the bank's agent "expressly invited [the customer's] reliance by urging [the customer] to trust him and by reassuring [the customer] that he was part of the [bank's] family" and the bank "also fostered [the customer's] perception that the bank was his financial advisor, by repeating that the bank's plans would benefit [the customer's] business."); *Global Enter. Group Holding, S.A. v. Ottimo*, 2010 U.S. Dist. LEXIS 145126, at *16 (E.D.N.Y. June 8, 2010) (clearing brokers, which traditionally perform only ministerial tasks, take on additional duties where their conduct exceeds the normal scope of a clearing broker's duties); *McDaniel v. Bear Stearns & Co.*, 196 F. Supp. 2d 343, 353 (S.D.N.Y. 2002) ("where a clearing firm moves beyond performing mere ministerial or routine clearing functions and becomes actively and directly involved in the introductory broker's actions, it may expose itself to liability with respect to the introductory broker's misdeeds"); *Srein v. Frankford Trust Co.*, 323 F.3d 214, 222-23 (3rd Cir. 2003) (finding additional duties where custodian was acting as more than a "'plain vanilla' custodian of assets").

Equity Trust's choice to be an active, as opposed to passive, custodian, meant that it acted unreasonably in promoting and endorsing Taylor and Poulson without doing due diligence, and in failing to warn investors of the risks associated with those investments. *See, e.g., Anwar v. Fairfield Greenwich Ltd.*, 118 F. Supp. 3d 591, 614 (S.D.N.Y. 2015) (broker's conduct could result in the additional duty to perform due diligence and the duty to warn of risks of the investment).

And given Equity Trust's knowledge that fraudsters targeted self-directed IRAs, and Equity Trust specifically, Equity Trust was well aware that promoting issuers – contrary to the conduct of a passive custodian – would have entirely foreseeable consequences of contributing to primary violations. Equity Trust should have known that by allowing its ill-prepared sales representatives to establish relationships with and appear alongside Taylor and Poulson it was contributing to their frauds.

2. Equity Trust Acted Unreasonably by Failing to Respond to Significant Red Flags

Equity Trust had knowledge of numerous red flags that, taken together or separately, should have – and would have for a reasonable custodian – created reason for suspicion and/or alerted Equity Trust to the primary violations of Taylor and Poulson. *See, e.g., Iowa Pub. Empls. Ret. Sys. V. Deloitie & Touche LLP*, 919 F. Supp. 2d 321 at 331-32 (S.D.N.Y. 2013) ("[C]ourts must examine such red flags in the 'aggregate,' which prevents defendants from 'secur[ing] dismissal by cherry-picking only those allegations susceptible to rebuttal and disregarding the remainder.'" (quoting *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 658 (S.D.N.Y. 2007)).

The red flags for Taylor include the description of Taylor as "a crook" by a credible source; that the customers sought secured notes but only received unsecured notes; that Taylor did not provide security agreements with the promissory notes; Taylor's false representation that Equity Trust was his "personal banker" and an investment adviser before thousands of potential investors at the New Birth Church event; that Taylor used his relationship with Equity Trust to promote himself; that Taylor was selling promissory notes with interest rates of 10-15% to unsophisticated investors; that Taylor failed to pay on almost all of the promissory notes (DE 40 at 6-7, 33); and that the financial statements for Taylor's entities included going concern opinions, which at the very least is one of the most significant indicators that a company is on the brink of bankruptcy. *Supra* 22-23.

The red flags for Poulson include that 25 out of 25 Poulson investments were missing key documents in the recorded mortgages (DE 256 at 3); that numerous notes were secured by the same unrecorded mortgages; that Poulson could not provide Equity Trust the required documents in response to its June 2010 audit and review of his investments; that Poulson failed to pay on almost all of the promissory notes (DE 40 at 6-7, 33; DE 41 at 3-4, 19); and that that Poulson used his relationship with Equity Trust to promote himself.[17] *Supra* 25-30.

In addition, any due diligence of Taylor and Poulson would resulted in Equity Trust learning additional negative information, such as the publically available lawsuits and press involving Taylor, the "going concern" opinions for Taylor's companies dating to 2007 (*supra* 22-23), and that Poulson had not in fact recorded any mortgages and that the Poulson Notes were severely undersecured by the properties (*supra* 24-25, 30-31).

3. Equity Trust Failed in Its Basic Duties to Hold Adequate Documentation

Equity Trust's failures to hold the security documentation for Taylor and Poulson, and to conduct appropriate reviews of Taylor and Poulson investments, violated the duties of even a passive custodian, much less an active one.[18] DE 36 at ¶¶ 47-52. These failures allowed Taylor to obtain additional investors through misrepresentations that the notes were secured when they were unsecured, and they allowed Poulson to continue misrepresenting to investors that they properties were secured when they were not. Even Equity Trust's policies required it to follow up on these red flags, such as the missing documentation, by discontinuing investments with

[17] The ALJ states that "by the time Equity Trust knew or should have known that its conduct might be a cause of Poulson's violation it had stopped processing new investments." ID 37. This is contradicted by the evidence. Equity Trust knew about Poulson's violations at least by June 2010. *Supra* 30-31. Despite this knowledge, Equity Trust continued to actively solicit and accept referrals from Poulson, which a reasonable custodian would not have done under the circumstances. Equity Trust did not cease these activities until shortly before it received a grand jury subpoena in November 2011 (DE 248), and did not put Poulson on the on the Do Not Process list until October 2012.

[18] The ALJ asserts that "unrebutted evidence" shows that "no other SDIRA custodian was performing the level of review of customer accounts that Equity Trust pioneered." ID at 34. Apart from the testimony of Dea, however, no evidence exists as to what level of reviews other custodians were doing. And there is persuasive evidence that Equity Trust was not the "pioneer" it claims to be. Scott Kelly, Equity Trust's regulator, testified that Equity Trust's reviews were the result of the Division of Banking's recommendations and that Equity Trust's compliance culture was "reactionary as opposed to proactive." Tr. 1193.

Taylor and Poulson until the deficiencies were addressed. DE 39 at ¶ 52 (missing documentation a red flag for a custodian). *See also* Tr. 908 (Jeffrey Bartlett: "'Why is missing documentation...something that Equity Trust seeks to obtain? [W]e consider that a red flag that...there may be some problems with that investment because they are not providing the documents that are required...that's when we try to get them all in, and otherwise we cease doing business with them.'").

Yet, Equity Trust continued to contribute to Taylor's and Poulson's violations even after they were placed on the hold or Do Not Process lists and new investments were no longer permitted. For example, Equity Trust permitted 14 Taylor Notes and 2 Poulson Notes to be renewed, extended, or modified after they were placed on Do Not Process list (DE 40 at 15-19); and each of those events was a separate securities transaction that constitutes a primary violation. This conduct allowed Taylor and Poulson to prolong their frauds.

IV. THE COMMISSION SHOULD IMPOSE SANCTIONS

If the Initial Decision is reversed and Equity Trust is found liable, then appropriate sanctions should be imposed. Equity Trust should disgorge all payments, including fees, it received in connection with the Taylor and Poulson accounts, plus prejudgment interest. The Division has calculated disgorgement based on account fees and other fees paid to Equity Trust at $180,336.18, which is broken down as follows: $89,042.74 paid directly by Equity Trust customers who invested in Taylor Notes (DE 797 at 1-63; 798 at 162-357); $62,598.81 paid directly by City Capital directly (DE 40 at 7); and $28,694.63 paid directly by Equity Trust customers who invested in Poulson Notes (DE 798 at 1-161). The calculations of the amounts paid directly by Equity Trust customers are summarized on Attachment A, which summarizes DE 797 & 798 and was submitted to the ALJ in post-hearing briefing.

In addition, the Commission should impose a civil penalty for conduct after July 22, 2010, when Section 8A was amended to permit penalties in causing cases. Equity Trust committed approximately 21 causing violations within the applicable period. In particular, Equity Trust processed 9 new investments in Poulson Notes (DE 41 at 9-10, lines 35-43); extended 10 Poulson Notes (DE 41 at 11-14, lines 3, 9-11, 14, 22-23, 30); and replaced two Taylor Notes (DE 40 at 18, lines 72-73; DE 807 (account statements reflecting replacements for first time on 12/31/10 statement); DE 491 (email shows replacement processed at Equity Trust after October 20, 2010)). Considering the egregiousness of Equity Trust's conduct, First Tier, Second Tier, or Third Tier penalties are appropriate. *SEC v. Reserve Management Co.*, 2013 WL 5432334, *19 (S.D.N.Y. Sept. 30, 2013) ("the Second Circuit and district courts in this circuit have imposed second and third tier penalties for violations of Section 5 of the Securities Act, even though scienter is not an element of a violation of that statute"). For the benefit of their customers who were victims of the Taylor and Poulson frauds, the Court should order the establishment of a Fair Fund.

Equity Trust also should be required to retain an independent compliance consultant for a period of three years. The compliance consultant, who would be retained and compensated by Equity Trust, and whose appointment and terms of engagement should be acceptable to the Division, would review Equity Trust's policies and procedures as they relate to the standard of care. 15 U.S.C. § 77h-1(a).

CONCLUSION

The Division of Enforcement respectfully requests that the Commission reverse the Initial Decision, find that Equity Trust is liable under Section 8A of the Securities Act, and impose appropriate sanctions.

Dated: New York, NY
September 15, 2016

Respectfully submitted,

DIVISION OF ENFORCEMENT

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Attachment A:
Fees Paid to Equity Trust by Taylor/City Capital Customers

Taylor/City Capital Investor	Div Ex Number	2009	2010	2011	2012	2013	2014	2015
Albert Hines								
Alex Mendano	798:284-288			$360.00	$360.00	$360.00	$200.00	
Alfonso Glenn								
Anita Dorio	797:1-4		$260.00	$260.00	$0.01			
Anita Dorio	797:10-13		$260.00	$260.00	$0.07			
Ann M. Walton								
Bettie J. Richardson Dixon	798:186-190	$260.00	$260.00	$260.00	$260.00			
Betty J. Wilson								
Beverly A. Dotson								
Bradley Goodsell	798:211-214	$440.00	$440.00	$440.00	$0.05			
Carolina Saravia								
Clara Hawley	798:219-223	$360.00	$360.00	$360.00	$360.00	$190.00		
Clarence Courtney								
Corzell White	798:344-347	$300.00	$300.00	$300.00	$56.66			
Crystal Turner	798:331-332			$66.05	$1.00			
Darrilyn B. Bryant-Hudson	797:30-34 & 798:229-233		$640.00	$26.56				
Deborah Degree	798:176-180	$440.00	$440.00	$440.00	$440.00	$190.00		
Denita L. Miller								
Dennis Ramsue								
Diana J. Wiberg-Donnell	798:191-193		$390.00					
Diana Wiberg Donnell	797:43-46		$440.00		$53.18			
Diane C. Moorman	798:292-295		$360.00		$185.73			
Diane Callaway								
Dorothy Sims	798:305-307		$440.00		$4.11			
Dovie C. Hines								
Ernest Walker								
Faustina Davis	798:173-175		$300.00	$141.14				
Freeman Wyche II	798:354-357		$343.10	$0.00	$439.00	$490.00	$465.00	
Gail Burks	798:162-164	$310.00	$128.58		$1.00			
Gennet Thompson								
Gennet Thompson	798:329-330		$260.00	$6.93	$1.00			
Glenn McKinney	798:279-283			$300.00	$300.00	$190.00	$195.00	
Gloria Butler	797:47-52		$440.00	$440.00	$75.00			$395.00
Gloria Daniels								
Gloria Jean Murray								
Harroll Chisom								
Hector F. Palacios								
Hollie McCollister	798:274-278	$190.00	$190.00	$265.00	$190.00	$390.00		
Ivan Stokes Sr.								
Izetta Jenkins								
Jeanette M. Thomas	798:326-328	$300.00	$300.00	$0.01	$1.00			
Jeffrey Martin	798:270-273		$360.00	$12.56	$1.00			
Jennifer Suitt	798:314-316		$260.00	$293.47				
JoAnn White	798:348-353		$440.00	$284.76	$1.00			
Joseph F. Bailey								
Kathryn Farmer	798:201-205	$410.00	$260.00	$90.67		$300.00		
Kauisha Smith	798:308-313	$190.00	$300.00	$375.00	$300.00	$300.00	$195.00	
Kelvin E. Robinson	798:299-304	$440.00	$440.00	$515.00	$440.00		$195.00	
Kenneth E. Turner								
Larease Rivers								
Latasha Lewis	797:35-38 & 798:266-269			$375.00	$300.00	$249.94		
Lawrence Hill Sr.	797:17-21 & 798:224-228	$440.00		$515.00	$440.00	$71.45		
Leroy Butler Jr.	797:53-58		$360.00	$360.00	$75.00			$395.00
Lilian Wells	798:341-343			$440.00	$44.78			
Lucy A. Stokes								
Mae R. Sanders								
Marcus Earl								

Attachment A:
Fees Paid to Equity Trust by Taylor/City Capital Customers

Marisa E. Miller Hampton								
Mary Jane Dinish	798:181-185	$440.00	$440.00	$440.00				
Mary-Ellen Lee	798:234-239	$310.00	$260.00	$335.00	$190.00	$190.00	$195.00	
Maxine Griffin	798							
Maxine Griffin	797:22-25 & 798:215-218		$640.00	$640.00	$0.78			
Mazen P. Musallam	798:296-298	$440.00						
Melissa Williams								
Michael Carnes								
Michael Evans								
Michael K. Feast	797:5-9 & 798:206-210	$440.00	$440.00	$440.00	$440.00	$164.15		
Neomia Coleman	798:169-172		$190.00	$190.00	$168.03			
Phyllis Shumate								
Rajaram Srinivas								
Renee Amos								
Rhonda Howard								
Richard W. Tahara	798:317-322	$360.00	$440.00	$440.00	$360.00			
Ronald C. Jones	797:14-16		$109.99	$340.00	$61.92			
Saundra W. Williams								
Sharon Rutledge								
Shirley T. Bailey								
Shirley W. Evans	798:198-200	$300.00	$300.00		$0.04			
Stanley E. Miles	798:289-291	$360.00	$32.05		$1.00			
Thomas Rucks	797:39-42		$360.00	$360.00	$171.29			
Thomas Taylor Jr.	798:323-325		$94.00					
Valter Cipollari Jr.	798:165-168							
Virginia Wallace	798:333-340		$1,850.00	$79.00	$1.00			
Wanda Gong	797:59-65		$360.00	$360.00	$360.00	$360.00	$375.00	$195.00
Wendy Bert								
Wesley Lee								
William R. Lee	798:240-265	$650.00	$600.00	$580.00	$600.00	$600.00	$630.00	
Willie Jacobs								
Yvette Price								
Total		$7,380.00	$15,087.72	$11,391.15	$6,683.65	$4,045.54	$2,450.00	$985.00

Total 2009-2015 For 48 Taylor Accounts: $48,023.06

Average for 48 Taylor Accounts: $1000.48 per account

Missing Statements for 41 Accounts

Estimated Fees on Account of Missing Statements: $1000.48 x 41 = $41,019.68

Total Estimated Fees for All Taylor Accounts = $89,042.74

Attachment A:
Fees Paid by Poulson Customers

Poulson Investor	Div Ex Number	2009	2010	2011	2012	2013	2014
Adam Farrington							
Andrea Clark	798:14-16		$190.00	$190.00			
Barbara Nowacki	798:84-85					$0.18	
Brian Spencer	798:124-125			$240.00	$67.17		
Carol Noe	798:78-80	$190.00		$190.00	$1.00		
Charles Milk	798:63-67					$208.10	
Christine Gallagher	798:33-35	$177.00				$190.00	
Colleen Conrad	798:17-20			$190.00	$190.00	$200.00	
David Dalrymple	798:21-24		$300.00	$115.53	$74.75		
David Dalrymple							
Deborah Overman-Plante	798:91-108	$360.00	$360.00	$360.00	$600.00	$600.00	$630.00
Denise Savary	798:112-116					$300.00	$195.00
Elaine Gulliford	798:47-49			$190.00	$97.00	$0.00	$0.00
Gary Smith	798:117-123	$300.00	$360.00	$360.00	$360.00	$440.00	$375.00
Heidi Valery	798:143-144			$240.00	$0.06		
Hien Nguyen	798:68-74				$440.00	$740.00	
James Behan	798:4-5			$200.00			
James Gallagher							
John Gulliford	798:43-46			$260.00	$260.00	$190.00	
Joseph Gatto	798:36-42	$650.00	$285.97			$600.00	$665.00
Joseph Ricci	798:109-111			$300.00	$200.90		
Joseph Sharman							
Julie Wiedis	798:152-161		$360.00			$210.00	
Karen Tilley	798:138-142			$300.00		$300.00	
Keri Dupree	798:25-32						$515.00
Laura Farrington							
Mark Halpern	798:50-59				$440.00		$440.00
Mark Jones	798:60-62	$43.33		$42.56	$1.00		$49.00
Mei Sun	798:126-137	$300.00	$300.00	$440.00	$440.00	$440.00	$460.00
Michael Banski	798:1-3						
Norman Noe	798:75-77	$190.00		$190.00			
Ronald Nowacki	798:81-83					$0.21	
Sandra Bryant	798:6-13		$689.00	$689.00	$689.00	$609.00	$564.00
Serge Ohotin	798:86-90	$221.67	$190.00	$190.00	$190.00	$190.00	
Walter Wall	798:145-151	$650.00					$630.00
Total		**$3,082.00**	**$3,034.97**	**$4,687.09**	**$4,050.88**	**$5,217.49**	**$4,523.00**

Total 2009-2014 for Poulson Accounts: $24,595.43

Average for 30 Poulson Accounts: $819.84 per account

Missing Statements for 5 Accounts

Estimated Fees on Account of Missing Statements: $819.84 x 5 = $4,099.20

Total Estimated Fees Paid for All Poulson Accounts = $28,694.63

CERTIFICATE OF COMPLIANCE

I hereby certify pursuant to Rule 450(d) that the Division of Enforcement's Brief on Review of the Initial Decision dated September 15, 2016 complies with the length limitations set forth in the Commission's Order dated August 16, 2016. The Division's Brief is 15,832 words, not including Attachment A.

David Stoelting

CERTIFICATE OF SERVICE

I hereby certify that on September 15, 2016, I filed the Division of Enforcement's Brief on Review of the Initial Decision dated September 15, 2016 with the Office of the Secretary of the Commission via facsimile at (202) 772-9324, and to alj@sec.gov, and served copies on the following person by email and by overnight courier to:

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