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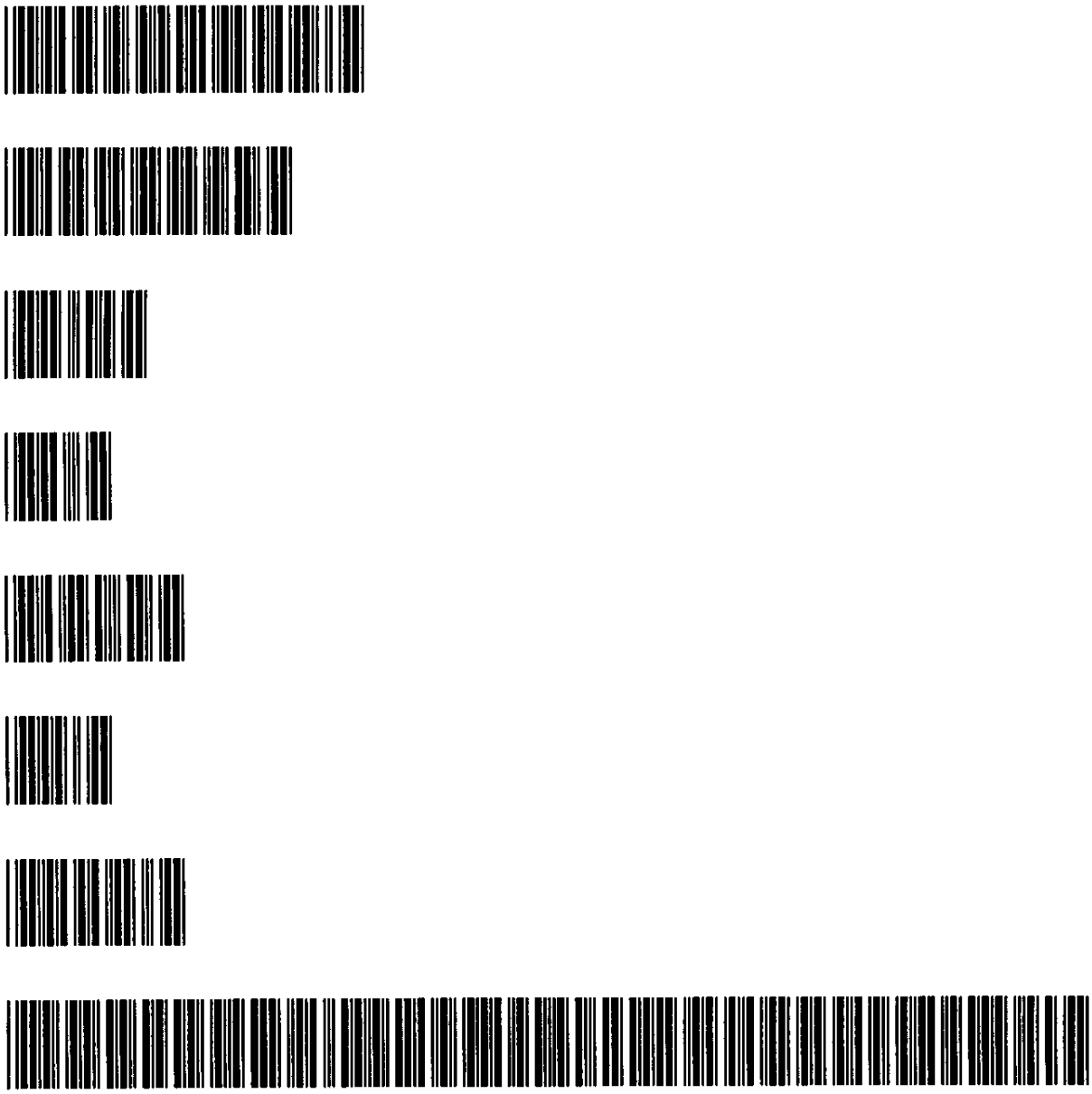

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UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

vs.

ALLIANCE LEASING CORPORATION, et al.,

Defendant.

CASE NO. 98-CV-1810-J (CGA)

ORDER GRANTING RECONSIDERATION

ORDER ADOPTING AMENDED SUMMARY JUDGMENT ORDER

This matter comes before the Court on Motions for Reconsideration by the Securities and Exchange Commission ("SEC") and Prime Atlantic, Inc. ("Prime") with regard to the Court's Order Granting Summary Judgment dated March 20, 2000. For the reasons set forth below, the Court GRANTS reconsideration and adopts the AMENDED Order Granting Summary Judgment and Final Judgment against Prime and Alliance attached hereto as Appendix A.

BACKGROUND

The parties are well familiar with the factual background of this case. The Court therefore declines to repeat those facts herein and instead incorporates the facts as set forth in the March 20, 2000 Summary Judgment Order.

In the instant motions for reconsideration, both the SEC and Prime seek clarification and amendment of the Court's March 20, 2000 Order. Prime asks the Court to reconsider the following:

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(1) the Court's determination that the Alliance Leasing Program is a security, (2) the Court's determination that Prime knew or was reckless in not knowing that Prime's 30% commissions came from investor funds, (3) the Court's treatment of Prime's "good-faith reliance on counsel" argument, and (4) the Court's ultimate determinations as to disgorgement, interest, and penalties. The SEC, on the other hand, urges the Court to amend its Order such that (1) the civil penalties assessed against Prime reflect the increased statutory maximums as amended by 17 C.F.R. § 201.1001, and (2) the Court's determination regarding the propriety of injunctive relief against the Prime Defendants is clear.

DISCUSSION

A. The Court's Authority to Reconsider its March 20, 2000 Summary Judgment Order

As a preliminary matter, the SEC argues that neither Rule 60(b)(1) nor Rule 60(b)(6) authorizes the Court to reconsider its summary judgment order as to Prime. Rule 60, in relevant part, states:

> On motion and upon such terms as are just, the court may relieve a party or a party's legal representative from a final judgment, order, or proceeding for the following reasons: (1) mistake, inadvertence, surprise, or excusable neglect; . . . or (6) any other reason justifying relief from the operation of the judgment.

FED. R. CIV. P. 60(b). Relief under Rule 60(b)(6), however, is extremely limited. Twentieth Century-Fox Film Corp. v. Dunnahoo, 637 F.2d 1338, 1341 (9th Cir. 1981)("In order to bring himself within the limited area of Rule 60(b)(6), a petitioner is required to establish the existence of extraordinary circumstances which prevented or rendered him unable to prosecute an appeal."). The bottom line is that reconsideration under Rule 60(b) is appropriate if the district court "committed clear error or the initial decision was manifestly unjust[.]" School Dist. No. 1J v. ACandS, Inc., 5 F.3d 1255, 1263 (9th Cir. 1993), cert. denied, 512 U.S. 1236 (1994).

Because the Court appreciates the importance of its findings in this case and their impact on related pending litigation, the Court exercises its discretion to reach the substantive merits of the Prime's arguments on its motion for reconsideration. Id. at 1262 ("[D]enial of a motion to reconsider is [reviewed] for abuse of discretion."). The Court is cognizant of the fact that the "mountains of paperwork" submitted in connection with this case leave room for errors of the magnitude that Prime

suggests. Accordingly, the Court will not deny Prime's or the SEC's motions for reconsideration on procedural grounds.

B. Prime's Objections to the Court's Summary Judgment Order Dated March 20, 2000

1. Prime Argues the Court's Finding that the Alliance Leasing Program was a Security was Erroneous

Prime argues that the Court erred in determining that the Alliance Leasing Program was a security as defined in 15 U.S.C. § 77(b)(1) and 15 U.S.C. § 78c(a)(10). Specifically, Prime argues that the evidence relied on by the Court to demonstrate that horizontal commonality existed under the second prong of the Howey test was inadequate. SEC v. W.J. Howey Co., 328 U.S. 293 (1946).

As a preliminary matter, the Court notes that the second prong of the Howey test, a requirement that the investment of money be in a "common enterprise," is satisfied by a finding of either horizontal or vertical commonality in the Ninth Circuit. SEC v. R.G. Reynolds Ent., Inc., 952 F.2d 1125, 1130 (9th Cir. 1991); see also SEC v. Eurobond Exchange, Ltd., 13 F.3d 1334 (9th Cir. 1994) (finding "common enterprise" prong satisfied upon a showing of only vertical commonality). Notably, Prime does not contest the Court's conclusion that vertical commonality exists. Since only one form of commonality is actually required under the Howey test in the Ninth Circuit, the Court's determination that the Leasing Program is a security actually remains undisturbed even, *assuming arguendo,* that the Court's findings on horizontal commonality are erroneous. However, in the interests of a complete record, the Court will readdress its findings on horizontal commonality in order to clarify them for appeal.

Prime argues that the Court's reliance on the following statement in the marketing materials for the Leasing Program fails to establish that there was a pooling of interests amongst the investors as required for horizontal commonality: "[Alliance] bundle[d] the leases together in packages of several million dollars each which [were] purchased by institutional investors." (Decl. McCole, Exh. 5, at 20). Prime apparently believes the Court confused the term "institutional investor" with "Principal" and cited this excerpt for the proposition that the Principals themselves purchased leases which contained pooled funds. While the language chosen by the Court may have been a bit confusing, the Court was actually observing that the sale of "bundled leases" to institutional investors

(presumably to generate the balloon payment promised at the end of the lease term) implicitly involved pooling investor funds in order to generate higher profits on the reselling of the leases since institutional investors would buy leases in bulk. This demonstrates pooling at the end, if not at the beginning, of the lease transactions. As the SEC points out, however, evidence exists to support a finding that pooling also occurred at the inception of the leases and that investor money was pooled in the leases established by Alliance. The SEC has submitted three certificates of title, addressed to three different investors, which indicate that all three investors had been assigned to Lease Number 9803006. (McCole Decl., Exh's 8-10). Accordingly, it appears that investor money was pooled together in leases assigned to only one lessor.[1] The Court therefore finds that ample evidence, including that cited in the original order, exists to support a finding of horizontal commonality.[2]

2. Prime Argues the Court Incorrectly Found that Prime "Knew" the 30% Commissions Came From Investor Funds

Prime argues that the Court improperly concluded that Prime should have known that the 30% commissions Prime was receiving came either directly from investor funds or from investor profits. In essence, Prime asserts that the declarations of Prime's principals disavowing any knowledge that the 30% commissions came directly from the Principal's funds suffice to create a triable issue of fact as to whether Prime knew or should have known that the commissions could impact the profitability of the Principals' investment. The Court is not persuaded.[3]

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[1] Whether or not investor money was actually assigned to different pieces of equipment within the lease seems irrelevant to the Court since clearly the investors were subject to the same risks by being involved with the same lessor and, presumably, the availability of pooled assets may have enabled a contract with a lessor who required a greater amount of goods than one investor could singularly finance. Moreover, the Prime Defendants have not proffered any evidence, nor do they even allege, that individualized accounts were kept as to the particular equipment within lease 9803006 or that the profits/rental revenues were actually kept separate according to the particular piece of equipment.

[2] To the extent that Prime argues that it did not "know" about the pooling of investor funds, this is irrelevant for the purposes of establishing whether or not the Leasing Program was a security. There is no scienter requirement attached to this determination. Nor is there a scienter requirement attached to finding a violation of Sections 5(a) and 5(c) of the Securities Act or Section 15(a)(1) of the Exchange Act.

[3] To the extent that this conclusion is inconsistent with the Court's findings when ordering a preliminary injunction against Prime, the Court notes that the standards for summary judgment and preliminary injunction are different. Moreover, findings made at a hearing for preliminary injunction are necessarily more hasty and incomplete in light of the urgency surrounding the

As a threshold matter, the Court need not conclusively find that Prime actually "knew" that the 30% commissions were coming from investor funds. Rather, the Court need only find that Prime should have known this fact and was reckless in not exercising more due diligence in knowing it. Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990)(en banc), cert. denied, 499 U.S. 976 (1991).

The Independent Sales Organization Agreement between Prime and Alliance contains the following provision governing the compensation Prime was to receive:

> 4. Compensation to Prime: In consideration of your services hereunder, [Alliance] covenants to pay to you a selling fee equal to 30% of the total purchase price of Units sold by the Partnership. Payment for fees is due to Prime Atlantic, Inc., within five (5) working days after bank has acknowledged deposit of funds and/or funds are indicated to be "good" and funds will be mailed in an expedient manner. This period shall apply to any and all funds that are not presented to [Alliance] in the form of money orders, certified or cashier checks that are immediately payable.

(Decl. Wilner, Exh. 7, at 2). This compensation agreement clearly ties Prime's commissions to the number of investment contracts Prime sold to the Principals. Moreover, it clearly ties the Principal's funds to Prime's commissions since the commissions are not even payable until the Principal's check has cleared and the payment is liquid. Such a connection between the Principals' funds and Prime's commissions ought to have put Prime on notice that Alliance likely tied Prime's commissions to the Principals' funds.

Prime argues, however, that this compensation arrangement does not conclusively establish that its commissions come directly from the Principals and that Alliance could still be paying Prime "advance commissions" from its profits on the leases, separate and apart from the Principals' funds and the Principals' expected profit. This reasoning is unpersuasive for three reasons. First, Alliance certainly has not had the opportunity to make a considerable profit on the Principal's money when it has just become payable. In fact, upon first receipt of the Principals' money, it is an open question whether the investor's money will be placed in a high-yield lease or in a lease with a lessor who defaults. Hence, any cut that Prime receives before the principal's money has been invested must

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"irreparable harm" associated with a preliminary injunction. A more thorough review of the documents submitted in this matter and a more detailed analysis of the Leasing Program was available at the time of summary judgment. Accordingly, with a better understanding of the mechanics of the Leasing Program, the Court is in a posture to modify its preliminary findings and draw new conclusions.

necessarily come directly from the Principal's funds.

Second, Prime has to believe that Alliance has created a leasing program with unheard of returns in order to substantiate its beliefs regarding Alliance's profits; the actual returns on each Principal's investment must far exceed the promised 28% to the Principals if Alliance is able to deduct a 10% management fee for itself and a 30% commission to Prime and *still* generate a return of 28% on the Principals' funds. This is an incredible assumption. Prime has proffered no evidence of Alliance's alleged profits to support that this is a logical, reasonable belief. In other words, absent some evidence that Alliance could reasonably pay Prime its high commissions with profits derived exclusively from this or some other venture and not from the Principal's funds, the clear inference is that Prime's commissions had to impact the profitability of the Principal's investment.[4]

Finally, and most convincingly, the Equipment Management Agreement between the Principals and Alliance put Prime on notice that its commissions impacted the profitability and riskiness of the Principals' investment. The agreement stated in no ambiguous terms that "advances of commissions" would be deducted from the rental revenue received by the Principals. (Decl. Wilner, Exh. 6 at ¶ 9). Hence, even if Prime did not believe that its commissions were coming out of the Principal's funds in the first instance, Prime knew that the profits of the investors, i.e. the rental revenue retained by the investors, was reduced by the amount of its commissions. Accordingly, the Court finds, Prime's protestations notwithstanding, that the undisputed facts support the conclusion that Prime acted recklessly in not verifying whether or not its commissions were derived from the Principals funds or profits. Certainly, the structure of the fee-splitting agreement between Alliance and Prime should have

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[4] Prime's self-serving declarations by Prime's principals Halsey and Giavanno that they believed their commissions were coming from sources other than the investor's money do not raise triable issues of fact. Halsey merely asserts that "Prime was paid *advance* commissions." (Decl. Halsey, Exh. 77 at 10:10-13) Giavanno avers that she "believed when the Alliance leasing program began that Alliance had a substantial, existing leasing business; that it generated money from buying equipment in bulk at wholesale prices and then locating lessees to pay retail rates; and that it also made money selling commercial paper." (Decl. Giavanno at ¶3). Prime proffers no evidence to support the reasonableness of these understandings and points to no evidence indicating that Alliance actually did make profits that far surpassed those required to be paid to the Principals. Accordingly, the declarations of Halsey and Giavanno are little more than summary denials and the Court need not find that they raise material issues of fact in and of themselves. Leer v. Murphy, 844 F.2d 628, 631 (9th Cir. 1988) ("The party opposing summary judgment may not rest on conclusory allegations, but must set forth specific facts showing that there is a genuine issue for trial.").

prompted Prime to investigate the nature of its commissions and it was reckless for Prime not to do so. This is especially true since Prime's own Policies & Procedures issued to the Independent Sales Contractors employed to market the Leasing Program assured the contractors that "[a]ll materials will have been the subject of a due diligence examination." (Decl. McCole, Exh. 4 at 27). The undisputed facts therefore show that Prime should have known that its commissions were taken directly from either the Principals' funds or rental revenues, thereby impacting both the potential profitability and riskiness of the Principals' investment.[5]

3. Prime Argues the Court Treated its Reliance on Counsel Argument Improperly

Prime also argues that Court misapprehended the thrust of its argument regarding Prime's lack of knowledge that the Leasing Program was a "security" under the federal securities laws. First, Prime argues that the personal opinion of its principals Halsey and Giavanno that the Leasing Program was not a "security" was discarded out-of-hand. Second, Prime argues that its "good faith reliance" on counsel argument should have been reviewed by Court as it relates to negating Prime's scienter and liability. Finally, Prime argues that the Court misunderstood the evidence on good faith reliance insomuch as it only applied the argument in its analysis whether or not to impose a permanent injunction against Prime.

As a preliminary matter, the Court does not believe it is essential to the SEC's claim for fraud and misrepresentation under Section 10 and Rule 10b-5 that the SEC prove that Prime "knew" the Leasing Program was a "security" under the federal securities laws. The scienter requirement attaches not to knowledge that the investment is a "security," but to fraudulent omission of material information. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976) (holding that scienter is "a mental state embracing the intent to deceive, manipulate, or defraud."). Certainly, under common law fraud, Prime would be just as liable for failing to disclose its high commissions whether or not the

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[5] Although not argued by the parties, the Court also observes that an alternate basis for finding liability on Prime's part is Prime's failure to disclose its conflict-of-interest when selling Alliance's program. Prime promoted the Leasing Program without telling investors that it was receiving exceedingly high commissions on the sales. Certainly any reliance on Prime's advice by the investors should have been informed by knowledge of Prime's incentives in promoting sales. The Ninth Circuit has recognized that promoters have a duty to disclose that they "expect[] to gain personally if [investors] follow[] [their] advice." Zweig v. Hearst Corp., 594 F.2d 1261, 1266-67 (1979).

Leasing Program qualified as a "security" under the federal securities laws. Hence, the fraudulent omission, and not the fact that the Program is a security, is the focal inquiry for the scienter analysis.[6]

Prime's assertions that its principals did not believe that the program was security and its purported good-faith reliance on the advice of counsel to this same effect do not, therefore, insulate it from liability as to the requisite scienter. Only if counsel had specifically opined that disclosure of the 30% commissions was not required could Prime possibly assert the good faith reliance on counsel defense. However, even then, as Court previously observed, "such reliance does not operate as an automatic defense, but is only one factor to be considered in determining the propriety of injunctive relief. SEC v. Goldfield Deep Mines Co. of Nevada, 758 F.2d 459, 467 (9th Cir. 1985)(quoting SEC v. Savoy Industries, Inc., 665 F.2d 1310, 13114 n.28 (D.C. Cir. 1981)). Accordingly, the Court did not err in its failure to address Prime's "personal knowledge" regarding whether or not the program was a security. Nor did the Court err in its treatment of Prime's reliance on counsel argument. It properly considered the argument only in the context of determining the propriety of injunctive relief.

4. Prime Argues the Court's Order of Disgorgement was Unfair

In the first instance, Prime argues that the Court's order of disgorgement was improper because it was premised on flawed conclusions regarding Prime's liability for securities violations. For the reasons set forth above, the Court concludes that its findings about Prime's liability were correct and that disgorgement was therefore authorized.

Alternatively, Prime challenges the Court's disgorgement rulings as being excessive. (Prime Mot. at 15). Specifically, Prime argues (1) that the disgorgement amounts against Halsey, Giavanno and Prime reflect a double recovery for the SEC, (2) that Prime's disgorgement should be reduced by

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[6] The Court notes that Prime cites no case that supports its argument that defendants who knowingly make false and misleading statements, yet do not believe that the investment constitutes a security, have offered evidence to negate a finding of scienter under Section 10 and Rule 10b-5. This is not surprising since such a finding flies in the face of established jurisprudence on mens rea and statutory construction. In order to convict an individual for violating a statute, one must find that the individual intended to commit a crime, i.e. intended to defraud or deceive. It is not necessary to prove that the individual intended to break a specific law, i.e. a federal securities law. The old axiom, "ignorance of the law is no excuse," is clearly applicable. U.S. v. Int'l Minerals & Chemical Corp., 402 U.S. 558, 563 (9th Cir. 1971)("The principle that ignorance of the law is no defense applies whether the law be a statute or a duly promulgated and published regulation.") Moreover, the Ninth Circuit has specifically held that an individual's "claimed lack of knowledge about the provisions of the securities law provides no defense." U.S. v. Manning, 509 F.2d 1230, 1233 (9th Cir. 1975).

the amount passed on to Master contractors and sales agents, (3) that Prime should get a reduction for the $786,248 already frozen by the SEC, and (4) that the Court should consider the Principals' recovery in the bankruptcy proceedings and reduce Prime's disgorgement accordingly. The Court will address each argument in turn.

First, to the extent that the order did not contain language that made Prime's disgorgement obligation joint and several with those of Halsey and Giavanno, the Court recognizes this to be an oversight and corrects the order accordingly.[7]

Second, with regard to Prime's contention that its disgorgement be reduced such that it reflects the amount actually retained by Prime after payments of commissions to the subcontractors, the Court makes the following observations. Disgorgement is an equitable remedy and "the amount must be reasonable, i.e. approximately equal to the unjust enrichment." SEC v. Hateley, 8 F.3d 653, 656 (9th Cir. 1993). Prime argues that it cannot be unjustly enriched by the amounts that it did not retain; accordingly, commissions paid to Master Contractors and sales representatives should be subtracted from Prime's liability. The SEC argues that it is appropriate to disgorge all the gains from Prime since no double recovery will result from doing so; the SEC has not sued the individual sales agents and asked for disgorgement of the investor funds retained by those individuals.

Both the SEC and Prime rely on the Ninth Circuit's decision in Hateley with regard to their relative positions. In Hateley, the Ninth Circuit found that it was an abuse of discretion for the SEC to award a disgorgement of approximately ten times the amount of the unjust enrichment. Id. at 656-57. Similar to the facts in the instant case, Hateley involved a "finder's fee agreement" between an individual, Jay Hold, and a corporation, Cambridge, in which Hold was to receive 90% of the commissions generated by all securities transactions he solicited for the firm. During the course of the agreement, commissions totaled roughly $55,000, of which Hold received roughly $50,000 and Cambridge (and its principals) received $5000. Securities violations were later found and disgorgement was ordered to the tune of $55,000 from Cambridge, despite a similar assessment against Hold. The Ninth Circuit found that disgorging $55,000 from Cambridge "duplicate[d] the amount that Hold was required to surrender" and was excessive. Id. at 656.

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[7] The SEC does not object to this clarification.

Here, it is clear that the SEC is not seeking duplicative recovery since it is not also seeking disgorgement of the amounts received by the independent sales contractors. However, it is also clear that Prime did not actually retain the monies it disbursed to its sales force. The Ninth Circuit in Hateley appeared to premise its conclusion that the disgorgement against Cambridge was unreasonable both on the existence of duplicative recovery and on the fact that Cambridge only actually retained 10% of the commissions under the agreement. It is certainly an open question whether the Ninth Circuit would have upheld disgorgement in the full amount against Cambridge absent the recovery from Hold. It is this Court's belief, however, that the purpose of disgorgement is to avoid unjust enrichment and to disgorge "ill-gotten gains." Since it is well-established that Prime had commission-sharing agreements with its sales force, it is well-established that Prime did not retain all the monies it initially received from Alliance. Upon reconsideration, the Court therefore agrees that a reduction of $6,185,588.17, the amount of commission payments passed on to the Master Contractors, is warranted in the disgorgement ordered against Prime.[8] (Decl. Slyngstad, Exh. 210, at 185).

As a third rationale for reducing the amount ordered disgorged, Prime argues that the $786,248 in assets that were frozen by the SEC should be deducted from the disgorgement order. The Court again rejects this argument. The total amount of "unjust enrichment" that Prime received certainly includes the amount of money still remaining in its accounts at the time they were frozen by the SEC. Accordingly, Prime's liability to the investors includes this amount.

Finally, Prime argues that any disgorgement amount against it should be reduced by the at least 41.6% that will be refunded to the Principals as a result of the bankruptcy proceedings. This argument is meritless. Disgorgement deals with Prime's obligation to return its ill-gotten gains; the amount of money it received from the leasing program. It has nothing to do with the amount of compensation the investors may be receiving from the distribution of the Alliance's assets. Prime's obligation to return the commissions it received is independent of other remedies that the investors may have.

The Court therefore orders that Prime disgorge $5,997,232.13 and pay prejudgment interest

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[8] Despite Prime's assertions that the amount disbursed to the sales force totaled almost two-thirds of the commissions received, the Court is inclined to trust the information contained in Exhibit A to the First Amended Disclosure Statement filed with the Bankruptcy Court in August of 1998.

of $329, 236.26 for a total of $6,326,468.39. Halsey and Giavanno's disgorgement amounts remain the same, but to the extent that either Halsey or Giavanno disgorge their ill-gotten gains, Prime's judgment is reduced.

C. The SEC's Objections to the Court's Summary Judgment Order Dated March 20, 2000

A. The SEC's Request for Clarification Regarding Injunctive Relief Against Prime

The SEC argues that it should be allowed to proceed to trial on the issue of whether a permanent injunction should issue against Prime. The basis for the SEC's argument is that the Court identified a material dispute of fact as to whether or not Prime relied in good-faith on the advice of counsel in its discussion regarding the propriety of injunctive relief. However, this was but one fact considered by the Court when determining whether a permanent injunction against Prime was appropriate. In its analysis, the Court indicated that there was some ambiguity as to one of the factors in the calculus for determining the propriety of injunctive relief -- the severity of Prime's scienter -- in light of this defense. However, the Court concluded that there was insufficient evidence on all the other factors to warrant the extreme relief of a permanent injunction. Accordingly, any dispute that was identified on that one prong of the test was not dispositive of the entire inquiry and did not leave the Court with the firm conviction that a trial was necessary to ascertain the propriety of injunctive relief. Rather, the Court found that there was insufficient evidence to warrant such relief on that prong as well as on the others. The decision to not grant injunctive relief is therefore final.

2. The Court Should Order Prime Defendants to Pay Maximum Penalties as Amended in 17 C.F.R. § 201.1001

The SEC also requests that the Court increase the penalties assessed against Prime to comport with the newly raised maximum penalties codified in 17 C.F.R. § 201.1001. The Court finds that penalties levied are sufficient and appropriate.

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CONCLUSION

For the reasons set forth above, the Court **GRANTS** Prime's and the SEC's motion for reconsideration and **ADOPTS** the Amended Order Granting Summary Judgment attached hereto as Appendix A.

IT IS SO ORDERED.

DATED: July 26, 2000

NAPOLEON A. JONES, JR.
United States District Judge

cc: All Parties

APPENDIX A

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, vs. ALLIANCE LEASING CORPORATION, et. al., Defendant.	CASE NO. 98-CV-1810-J (CGA) **AMENDED ORDER GRANTING PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT** **AMENDED FINAL JUDGMENT**

This matter comes before the Court on Plaintiff Securities and Exchange Commission's ("SEC") motion for summary judgment against the remaining defendants in this action: Susan Browne, Charles Browne, Prime Atlantic Inc., David Halsey, and Braccus Giavanno. For the reasons set forth below, the Court GRANTS the SEC's motion for summary judgment against all of the remaining defendants and enters an order of final judgment.

BACKGROUND

This is a securities fraud action arising from the sale of interests in an equipment leasing program offered by Alliance Leasing Corporation ("Alliance"), a San Diego-based business. From December of 1997 through October 1998, Alliance located and recruited over 1,500 individuals throughout the United States to invest in an enterprise which used investor money to purchase commercial office or kitchen equipment which was then leased out to third party lessees. (First

Amended Compl. at ¶2). The lease payments by the lessees were then allegedly paid to the investors on a monthly basis for two years with a "balloon payment" at the end of the two-year period. Id. at ¶ 15. Alliance represented that investors would earn a return of 14% per year and that the investment was "low risk." Id. at ¶ 16.

In its First Amended Complaint, the SEC alleges that the investment contracts offered by Alliance were unregistered securities and that Alliance and all its collaborating partners, individually and collectively, violated several federal securities laws by failing to register the investment contracts and by misrepresenting information critical to an investor's informed decision to invest. The complaint names Charles and Susan Browne ("Brownes") and Sharon Oliver ("Oliver") individually since they were principals of Alliance, owning and controlling majority stock in Alliance.

The SEC also alleges that Defendant Prime Atlantic, Inc. ("Prime") served as a broker-dealer and was chiefly responsible for marketing the Lease Program to potential investors. Additionally, the complaint names David Halsey ("Halsey") and Braccus Giavanno ("Giavanno") individually since they were co-owners of Prime and Chief Executive Officer and Director of Sales and Marketing for Prime, respectively.

On October 7, 1998, the Court entered a Temporary Restraining Order ("TRO") and an Order Freezing the Assets of Alliance and Prime. In negotiations following the imposition of the TRO, Alliance entered into a settlement agreement with the SEC in which Alliance stipulated to a permanent injunction and disgorgement of funds. On November 20, 1998, the Court imposed a preliminary injunction on Prime and restrained it from violating securities laws as set forth in the TRO. In granting the preliminary injunction, the Court made the initial determination that the investment contracts offered by Alliance were in fact securities and that the SEC had shown "probable success on the merits" of the securities claims that did not require proof of the element of scienter.

On November 30, 1998, the Court granted the SEC's application for a Chapter 11 trustee. The Court found that appointment of a trustee was warranted in light of the clear and convincing evidence of Alliance's fraudulent activity. The Court expressly noted "instances of self-dealing between the officers of Alliance [the Brownes] and the companies it funds leases with" as evidence of Alliance's fraudulent activity. (Order Appointing Trustee, dated Nov. 30, 1998, at 9).

On January 4, 2000, Defendant Oliver, one of the principals of Alliance, consented to a permanent injunction against her and was dismissed from the case. The other principals of Alliance, the Brownes, remain in the action and have repeatedly invoked the Fifth Amendment privilege against self-incrimination in response to depositions and discovery requests. On November 1, 1999, in the interests of fairness to the SEC's thwarted discovery against the Brownes, the Court ordered that the Brownes were precluded from introducing any testimony or evidence to which they had asserted their Fifth Amendment privilege.

The SEC now urges the Court to grant summary judgment against the remaining Defendants in this action: Prime and its principals, Halsey and Giavanno, and the Brownes. The SEC seeks the entry of permanent injunctions against the remaining Defendants, disgorgement of any ill-gotten gains, and assessment of civil money penalties.

The SEC argues that there is no dispute of material fact regarding the character of the investment contracts; they are securities. Additionally, the SEC argues that there is no dispute of material fact that the Prime Defendants failed to disclose their 30% commission, a disclosure material to investors and fundamental to federal securities laws. The Brownes base their opposition to the SEC's motion for summary judgment on the single argument that the investment contracts are not securities. The Prime Defendants, on the other hand, argue that disputes of material fact exist as to the adequacy of the disclosure of Prime's commission and as to whether Prime had reason to believe that it was actually selling securities.

DISCUSSION

A. Legal Standard

Summary judgment is appropriate when there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. FED. R. CIV. P. 56(c). The party seeking summary judgment always bears the initial responsibility of identifying those portions of "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, which it believes demonstrates the absence of a genuine issue of material fact." Id.; Celotex v. Catrett, 477 U.S. 317, 323 (1986). To the extent the moving party fails to satisfy this initial burden of production, summary judgment must be denied. See Henry v. Gill Industries, Inc., 983 F.2d 943,

949-50 (9th Cir. 1993).

If, however, the moving party makes the initial showing, the burden then shifts to the nonmoving party to demonstrate that summary judgment is not appropriate. Celotex, 477 U.S. at 324. To make such a showing, "the nonmoving party must go beyond the pleadings and . . . designate specific facts showing that there is a genuine issue for trial." FED. R. CIV. P. 56(e); Celotex, 477 U.S. at 324. A dispute is "genuine" only if "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986).

At the summary judgment stage, it is not the function of the judge to weigh the evidence or make credibility determinations. Anderson, 477 U.S. at 255. Rather, the judge should simply decide whether the evidence demonstrates a genuine factual dispute for trial. Id. at 250-251. When making such a determination, "the evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in [her] favor." Id. at 255.

B. Was the Alliance Leasing Program a Security?

As a threshold matter, the Court must determine whether the Alliance Leasing Program constitutes a security. Clearly, absent a determination that the Leasing Program is a security, the remaining Defendants cannot be held liable for any of the federal securities laws violations alleged in the SEC's complaint.

The characterization of a transaction as a security is a question of law provided that there exists no dispute of material fact as to the facts examined by the Court in reaching this conclusion. U.S. v. Carman, 577 F.2d 556, 562 (9th Cir. 1978) ("Although characterization of a transaction raises questions of both law and fact, the ultimate issue of whether or not a particular set of facts, as resolved by the factfinder, constitutes an investment contract is a question of law.") Therefore, the Court may, on this motion for summary judgment, conclusively determine that the Alliance Leasing Program is a security if it finds no dispute of material fact as to the nature of the leasing transactions. The parties may argue different applications of the facts to the law, but this does not constitute a material dispute of fact; rather, such arguments are clearly legal and best resolved by the Court. However, if the parties argue that the underlying facts surrounding the transactions are in dispute, the characterization of the Alliance Leasing Program is properly in the province of the jury and summary judgment on this issue

is inappropriate.

The Court preliminarily determined that the Alliance Leasing Program was a security when it granted a preliminary injunction against Prime on November 20, 1998. On the basis of the evidence presented at the preliminary injunction hearing, the Court found that the SEC had demonstrated "probable success on the merits" with regard to its contention that the Leasing Program was a security. However, because the standard for granting a preliminary injunction is different from the standard for granting summary judgment, the Court will revisit its analysis of the Lease Program. As appropriate, the Court will defer to its previous findings and incorporate reasoning from the previous order.[1]

Definition of a Security

A "security" is defined in both 15 U.S.C. § 77b(1) and 15 U.S.C. § 78c(a)(10) to include "investment contracts" and "notes." In SEC v. W.J. Howey Co., 328 U.S. 293 (1946), the Supreme Court set forth a framework for analyzing whether transactions such as those involved in the Alliance Leasing Program are investment contracts that may be characterized as securities. Under Howey, an investment contract exists if the following three part test is met: [1] there is an investment of money, [2] in a common enterprise, and [3] with an expectation of profits produced by the efforts of others. Id. at 298-299.

1. "Investment of Money"

It is undisputed that there is an investment of money. Over 1,500 investors nationwide contributed at least $54 million to the venture. (First Amended Compl. at ¶ 2). Hence, the first element of the Howey test is clearly satisfied.

2. "A Common Enterprise"

The Ninth Circuit has determined that "common enterprise" can be demonstrated by a showing of *either* horizontal or vertical commonality. SEC v. R.G. Reynolds Ent. Inc., 952 F.2d 1125, 1130 (9th Cir. 1991). Horizontal commonality is illustrated when the enterprise is common to a group of investors; this is illustrated most easily by a showing that there is a pooling of interests amongst the investors. Id. Vertical commonality, on the other hand, is defined as an enterprise common to an

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[1] Some sections from the Court's previous Order Imposing Preliminary Injunction on Prime Atlantic, dated November 20, 1998, are adopted and incorporated in full.

investor and the seller, promoter, or some third party; this is established by showing "that the fortunes of the investors are linked with those of the promoters." Id. (quoting SEC v. Goldfield Deep Mines Co. of Nevada, 758 F.2d 459, 463 (9th Cir.1985)). In further clarifying what is encompassed by vertical commonality, the Ninth Circuit has noted that "[o]ne indicator of vertical commonality, though by no means the only indicator, is an arrangement to share profits on a percentage basis between the investor and the seller or promoter." Id.

With regard to horizontal commonality, the Court finds that there is no dispute of material fact that the Alliance Leasing Program exhibited horizontal commonality. According to the terms of the Joint Venture Agreement, the investors would provide the investment capital for Alliance to purchase commercial equipment to lease to third parties.[2] (Decl. Wilner, Exh.5 at ¶ 2). Investor money was allegedly placed in special accounts at either Wells Fargo or Merrill Lynch, and Alliance would use the capital to "engage in a single or multiple transactions with a Lessee." Id. There is no indication in the Agreement that investor money was held separately or that it was used to fund a singular leasing transaction. In fact, the offering materials and other evidence suggest otherwise.[3] Alliance's promotional materials disclose that in some cases "it bundle[d] the leases together in packages of several million dollars each which [were] purchased by institutional investors." (Decl. McCole, Exh. 5, at 20). This disclosure makes it apparent that investor funds were sometimes pooled together for the purpose of selling the leases to institutional investors to generate higher profits on the resale of the bundled leases. Additionally, the SEC has submitted to the Court three certificates of title, addressed to three different investors, which indicate that all three investors were assigned to Lease Number 9803006. (McCole Decl., Exh's 8-10). Accordingly, it appears that investor money was pooled

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[2] The Equipment Management Agreement which replaced the Joint Venture Agreement contains similar terms. (Decl. Wilner, Exh. 6, at ¶ 3).

[3] In determining whether "a scheme involves a security, the inquiry is not limited to the contract or other written instrument." Hocking v. DuBois, 885 F.2d 1449, 1457 (9th Cir. 1989). A court may consider the promotional materials and the merchandising approaches. Id. As the Supreme Court itself has held, form should be disregarded for substance when searching for the scope of the term "security" and emphasis should be on economic reality. Tcherepnin v. Knight, 389 U.S. 332, 336 (1967).

together in leases assigned to only one lessor.[4] Horizontal commonality is therefore satisfied since investor interests were pooled in the endeavor. Accordingly, the Alliance Leasing Program is an enterprise common to a group of investors as required under the second prong of Howey. Defendants have offered no facts to dispute this assessment or to indicate any other type of interpretation of the Leasing Agreements.

Although only one type of commonality is required by the 9th Circuit, the Court nevertheless also finds that the Leasing Agreements exhibited vertical commonality. As Defendants correctly argue, vertical commonality requires that the "fortunes of the investor are interwoven and dependent upon the efforts and success of those seeking the investment." (Browne's Opp. at 3 citing SEC v. Glenn W. Turner Enterprises, Inc., 474 F.2d 476, 482, n.7 (9th Cir.), cert. denied, 414 U.S. 821 (1973)). Defendants are incorrect, however, in their assertion that vertical commonality is not satisfied here. They argue that the Lease Agreements do not contemplate that investors share the rental revenue or profits with Alliance, but rather that Alliance receive a standard commission for "packaging" the leasing deals for the investors and the third parties lessees. (Browne's Opp. at 3; Prime Opp. at 8). However, according to the express terms of the Joint Venture Agreement, the investors and Defendant Alliance actually do share in the percentage of the returns from the leasing agreements. The investors were to receive "fifty (50%) percent of the net profits and losses ... after deduction from revenue received by the [joint venture] of [Alliance's] fee of 10%." (Decl. Wilner, Exh. 5 at ¶ 5). Therefore, Alliance is clearly the beneficiary of the other 50% of the profits. While the 10% fee can arguably be viewed as an administrative fee, not dependent on the success of the venture, certainly the remaining 50% profit that the Agreement contemplates is profits that go directly to Alliance.[5] Furthermore, in

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[4] Whether or not investor money was actually assigned to different pieces of equipment within the lease seems irrelevant to the Court since clearly the investors were subject to the same risks by being involved with the same lessor and, presumably, the availability of pooled assets may have enabled a contract with a lessor who required a greater amount of goods than one investor could singularly finance. Moreover, the Prime Defendants have not proffered any evidence, nor do they even allege, that individualized accounts were kept as to the particular equipment within lease 9803006 or that the profits/rental revenues were actually kept separate according to the particular piece of equipment.

[5] The Equipment Management Lease similarly contemplates profit sharing under the provisions set forth with regard to the Management Fee which provide that the Manager (Alliance) is entitled to "any amounts left after the return of Principal's purchase price and the

its promotional materials, Alliance advertised that its fortunes were tied to the success of the investors by claiming that "there is plenty of room in which to pay a purchaser a total return of 28% for 25 months, while at the same time generating a profit for Alliance Leasing." (Decl. McCole, Exh. 5, at 20). The Defendants have therefore failed to identify any material disputes of fact as to the character of the Lease Agreements. While it is true, as Defendants argue, that the management fee itself might not rise to the level of profit-sharing, the Lease Agreements clearly indicate additional forms of profit sharing. Finding no dispute of material fact, the Court holds that Lease Program exhibits vertical commonality as required under the second prong of the Howey test.

3. "Profit by Efforts of Others"

The third prong of the Howey test is met when there is an "expectation of profits produced by the efforts of others." R.G. Reynolds Ent, Inc., 952 F.2d at 1130. This expectation is created when "'the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.'" Id. (quoting SEC v. Glenn W. Turner Ent., 474 F.2d 476, 482 (9th Cir.1973)). This third factor can be shown by the following examples:

> (1) an agreement among the parties leaves so little power in the hands of the partner or venturer that the arrangement in fact distributes power as would a limited partnership; or (2) the partner or venturer is so inexperienced and unknowledgeable in business affairs that he is incapable of intelligently exercising his partnership or venture powers; or (3) the partner or venturer is so dependent on some unique entrepreneurial or managerial ability of the promoter or manager that he cannot replace the manager of the enterprise or otherwise exercise meaningful partnership or venture powers.

Hoking v. Dubois, 885 F.2d 1449, 1460-61 (9th Cir. 1989) (adopting Williamson v. Tucker, 645 F.2d 404 (5th Cir. 1981)).

Here, the terms of the Joint Venture Agreement and the Equipment Management Agreement show that the structure of the relationship between Alliance and the investors ("principals") was one in which Alliance held most of the responsibility and the principals' role was pro forma. The Equipment Management Agreement sets forth a long list of Alliance's responsibilities while the principals' duties are limited primarily to contributing capital. (Decl. Wilner; Exh. 6 ¶ 4). Among

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return stated in paragraph seven above (28% yield)." (Decl. Wilner, Exh. 6 at ¶ 8). Again, this provision clearly contemplates that Alliance receive the share of the profits, if any, that exceed 28%.

Alliance's duties is "identifying and evaluating the financial condition, creditworthiness and other aspects of prospective lessees of equipment . . ." Id. This provision of the Equipment Agreement requires Alliance to research the financial viability of the companies considered for lease agreements and then select the most promising companies. This clearly encourages principals to rely on the wisdom of Alliance's choices. The investors themselves never sought out lessees or conducted any investigation or research into the lessees. Thus, the overall structure of the relationship between the investors and Alliance, as evidenced in the Equipment Agreement, indicates that Alliance was the moving force behind the lease transactions. In addition, given the large number of investors (about 1600), any meaningful control that the investors could have exerted was diluted, making it more likely that investors saw this as a passive investment in which they could rely on Alliance to make the necessary decisions. Therefore, the Court finds that Alliance held the primary responsibility to find lessees and enter into leases, thereby providing "essential managerial efforts."

Defendant's primary argument against this determination is based on a provision in the Equipment Lease Agreement which provides that Alliance was not allowed to enter into any leasing transaction without the express written approval of the principal. (Decl. Wilner, Exh. 6, at ¶ 5). Defendants argue that this provision proves the "existence of Principals' power and control." (Prime Opp. at 10). However, the Court is not impressed that this shows any substantial control.[6] The economic reality of the situation is that the principals trusted Alliance's self-proclaimed expertise in locating profitable leases and expected to do little in managing their interests. Clearly, the Principals' alleged veto power was not really expected to be exercised.[7] Thus, this does not demonstrate that the

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[6] In Holden v. Hagopian, 978 F.2d 1115, 1119 (9th Cir. 1992), the Ninth Circuit noted that "although on the face of the partnership agreement the investor theoretically retains substantial control over the investment and an ability to protect the investment from the managing partner or hired manager, the investor nonetheless can demonstrate such dependence on the promoter or on a third party that the investor was in fact unable to exercise meaningful partnership powers."

[7] This is particularly evident in light of the language on "lease changes" in the sales materials provided to the independent sales agents: "All independent contractors should understand and make clear to clients that, on occasion, clients may be placed initially into a lease and then unexpectedly switched to another. [ ] In the event this occurs, the client will receive a letter of explanation." (McCole Decl., Exh. 5, at 8). Obviously, the Principals' veto power, if any, is retroactive in the context of lease changes. Alliance clearly was the primary manager of all the leases.

investors had significant power in the relationship and that Alliance's efforts were inconsequential. Moreover, Defendants' arguments are not raising material issues of fact with regard to this prong of the Howey test, but are urging a different characterization of the Lease Program based on the same facts. As such, the Court properly resolves the legal question in favor of the SEC and finds that the Alliance Leasing Program did indeed employ Alliance's "essential managerial efforts which affect[ed] the failure or success of the enterprise." The third prong of the Howey test is therefore met.

Having found no dispute of material fact with regard to any of the Howey factors and having held that Alliance Leasing Program meets each of the factors, the Court finds that the Alliance Leasing Program is an investment contract which falls within the definition of a security.

C. Violation of Sections 5(a) and 5(c) of the Securities Act

Sections 5(a) and 5(c) of the Securities Act require that a registration statement be filed for every security. If no registration is filed, then it is unlawful for anyone to use interstate commerce or the mail to offer or sell the security. 15 U.S.C. §§ 77e(a)(a) and (c). The provision does not require evidence of a specific intent to violate the statute. SEC v. Geotek, 1978 WL 1105 *3 (N.D. Cal., 1978)("[I]t is not necessary that a violation of the registration requirement of Section 5 be predicated on any scienter on the defendant's part."). Hence, to prove a violation under Section 5, the SEC need only prove that there is no dispute of material fact that [1] the Alliance Lease Program is a security, [2] that a registration statement was not filed for the Alliance Lease Program, and [3] Prime and the Brownes used interstate commerce or the mail to offer or sell the security.

Each of the elements for a violation under this provision are undisputed against both the Brownes and Prime. First, as discussed above, the Joint Venture Agreement/Equipment Management Agreement is an investment contract which qualifies as a security. Second, the SEC has no registration statement on file for Alliance's securities and the Defendants do not represent otherwise. (Decl. Bisaccia ¶ 12). Finally, interstate commerce and the mails were used in connection with the sale of these securities by both Alliance and Prime because Alliance sent rental checks and other communications to investors through the mail and Prime received its commission checks through the mail. (2nd Decl. Bisaccia, Exh. 1 (Decl. Cohen ¶ 23); (Decl. Noll ¶ 9)); (Decl. Halsey, Exh. 1 (agreement between Alliance and Prime Atlantic). In addition, Alliance advertised over the Internet.

(Decl. Bisaccia, Exh. 3). Therefore, the SEC has demonstrated that there is no dispute of material fact with regard to any of the elements required to prove its claim that Prime and the Brownes violated 15 U.S.C. § 77e(a) and 77e(c) by offering or selling unregistered securities. Accordingly, summary judgment is GRANTED against Prime, Halsey, and Giavanno and the Brownes on this violation.[8]

D. Violation of Section 15(a)(1) of the Exchange Act

Under Section 15(a)(1) of the Exchange Act, a broker or dealer must register with the SEC before it can use the mails or any instrumentality of interstate commerce to effect any transaction in the purchase or sale of a security. 15 U.S.C. § 78o. A broker is "any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C. §78c(a)(4). Scienter, or proof of any intent to defraud, is not required under Section 15(a)(1). SEC v. Interlink Data Network of Los Angeles, Inc., 1993 WL 603274 (C.D. Cal. 1993)("The Commission need not prove scienter when alleging a violation of Section 15(a)(1)."). SEC alleges that Prime violated Section 15(a)(1) of the Exchange Act by brokering sales in a security, namely the Alliance Lease Program.

The Court finds that there is no dispute of material fact that Prime acted as a broker when it effected transactions pursuant to the joint venture/equipment management agreement. (Decl. Wilner, Exh. 7, ¶ 2 (letter from Alliance to Prime stating that Prime is "appointed as the exclusive agent of the [joint venture] in connection with the private offering of the [sale of] Units. You covenant to offer and sell Units on behalf of the [joint venture] . . ."). As stated above, the Alliance investment program was a security. Additionally, Prime utilized interstate commerce in its marketing of the Alliance Program; the initial "Independent Sales Organization Agreement" which established Prime as an agent responsible for carrying out the joint venture agreement between Alliance and its investors was sent

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[8] It is undisputed that the Brownes owned and controlled Alliance. All promotional materials indicate that the Brownes were the Chief Executive Officer and Vice President of Alliance. (Decl. Wilner, Exh. 16, at 2-3). Additionally, the Brownes themselves asserted that they were "executive employees" of Alliance in declarations before the Bankruptcy Court. (Decl. Wilner, Exh's 12-13, at 1). Finally, the Brownes are precluded from testifying otherwise pursuant to this Court's order precluding introduction of testimony on issues on which the Browne's have pled the Fifth Amendment privilege against self-incrimination. Therefore, it is clear that the Brownes may be held liable for actions taken by their company, Alliance Leasing.

Likewise, Defendants Halsey and Giavanno owned and controlled Prime and are therefore liable for the actions of Prime. Halsey admits that he was Chief Executive Officer (Decl. Wilner, Exh. 20, at 28:12-13) and Giavanno admits that he and Halsey each owned 50% of Prime Atlantic. (Decl. Wilner, Exh. 21, at 3:9-13).

through the mail, as subsequent promotional and legal materials were. Finally, the SEC has searched its files and has not found a registration statement for Prime Atlantic as a broker-dealer and Prime does not represent otherwise. (Decl. Bisaccia ¶ 12). Therefore, the SEC has shown that there is no dispute of material fact as to Prime's violation of Section 15(a)(1) of the Exchange Act. Accordingly, summary judgement is GRANTED against Prime and its owners, Halsey and Giavanno on this claim.

E. Violation of Section 10(b) of the Exchange Act and Rule 10b-5

The elements of a violation of Section 10(b) of the Exchange Act and Rule 10b-5 are as follows: (1) purchased or sold securities; (2) by use of interstate commerce or by use of the mails; and (3) either (a) employed a device, scheme or artifice to defraud; (b) made untrue statements of material fact or omitted to state material facts necessary; or (c) engaged in acts, practices, or course of business which operated or would operate as a fraud or deceit upon persons. 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5. Unlike the registration provisions, a violation under Section 10(b) requires that the SEC demonstrate scienter, "a mental state embracing the intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976). The Ninth Circuit has determined that deliberate or reckless conduct will satisfy the scienter requirement. Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990)(en banc), cert. denied, 499 U.S. 976 (1991). The Ninth Circuit has adopted the following definition of reckless conduct for 10(b) purposes:

> a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.

Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1569 (9th Cir. 1990) (quoting Sundstrand Corp. v. Sun Chem. Corp., 553 F.2d 1033, 1045 (7th Cir. 1977)). The plaintiff may rely on direct or circumstantial evidence to prove scienter. Provenz v. Miller, 102 F.3d 1478, 1490 (9th Cir. 1996).

As has been previously established, the first two elements of a Section 10b violation are clearly met: Prime Defendants and the Brownes sold the Lease Program, a security, utilizing the mail. However, the Court will examine whether there exists a dispute of material fact with regard to whether any of the Defendants had the requisite scienter and whether any of the Defendants actually engaged in actionable misrepresentations. The Court will first evaluate the evidence with regard to the Brownes and it will then evaluate the evidence against the Prime Defendants.

1. The Brownes

The Court finds the Browne's liability for fraudulent misrepresentation clear. The Brownes owned and controlled Alliance and are therefore liable for all the misrepresentations in the Leasing Program. First, it is undisputed that the Alliance Leasing Program's promotional materials emphasized the integrity and experience of Brownes while failing to disclose their previous securities violations and Charles Browne's previous bankruptcy. In relevant part, the promotional materials touted Charles Browne's "leadership track record" and "prestigious [previous] positions" while calling Susan Browne a "seasoned business professional." (Decl. Wilner, Exh. 16, at 4-5). Glaringly absent from the materials were relevant disclosures regarding Charles Browne's prior bankruptcy in 1994 (Decl. Wilner, Exh.18, at 4, 6) and the Browne's previous cease-and-desist orders related to the fraudulent sale of unregistered securities in California, Wisconsin, and Mississippi. (Decl. McCole, Exh. 6, at 1-12); (Decl. Bisaccia, Exh. 1, 1-9).

Additionally, the Brownes failed to disclose to investors that the majority of the "safe" companies that they selected to participate in the equipment leasing agreements were companies which were not at arm's-length. Specifically, Sovereign Financial Corporation (Sovereign) was formed by the Brownes and was one of the main lessees of equipment from Alliance. (Decl. Wilner, Exh's 25, 26 (Jeske Depo. at 41-42, 62, 69, 78-80, 107-8, 174-75; Lopez Depo. at 6, 10, 47-49)). The Brownes have presented no evidence disputing these characterizations of the relationships between Alliance and several of the companies it engaged in lessee relationships.[9] Self-dealing between Alliance and its lessees clearly presents conflicts of interest which are material and should have been disclosed to potential investors.

Finally, the Brownes failed to disclose that Alliance actually used 30% of all investor money to pay a sales commission to Prime. The Leasing Agreements were either silent on this point or provided generally that "advances of commissions" would be deducted from the investors' return. (Decl. Wilner, Exh. 5, Exh. 6 at 3). However, thirty percent is a significant figure and one that most reasonable investors would deem material in determining whether to invest. Hence, failure to disclose

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[9] Furthermore, the Brownes may not rest behind their assertions of the Fifth Amendment right to avoid self-incrimination, since the Court has held that so doing unduly prejudices the SEC's civil action. Hence, at this juncture, any response by the Brownes would be precluded.

this sum misrepresents the investor's potential profit.

It is apparent to the Court that there is no dispute of material fact as to the incomplete disclosures made by the Brownes with regard to their business experience, the nature of the lessees, and the commissions paid to Prime. Each factor independently likely rises to an untrue statement of fact and/or an omission of fact, but jointly there is no doubt that they rise to material misrepresentations. As such, the Court finds that the Brownes deliberately misled investors as required under the third element of Section 10(b). Accordingly, summary judgment is GRANTED against the Brownes on the Section 10(b) claim.

2. Prime Defendants

The only fraud-based allegation against the Prime Defendants is that they failed to disclose the 30% commission that they received from Alliance. SEC argues that Prime Defendants knew or were reckless in not knowing that they that they were required to disclose this crucial information to investors. (SEC Motion at 18). In response, the Prime Defendants argue that there was a general disclosure that commissions were being charged and that therefore the real issue is the materiality of the misrepresentation and whether investors relied on the misrepresentation -- triable issues of fact. (Prime Opp. at 12). Additionally, Prime argues that there is a triable issue of fact with regard to whether the Prime Defendant's good faith reliance on the advice of attorneys that the program was not a security negates the scienter required by law. (Prime Opp. at 11).

As a threshold matter, the Court observes that the disclosure of commissions and other compensation is fundamental to securities laws. Ettinger v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 835 F.2d 1031, 1033 (3rd Cir. 1987) ("The SEC has established through its enforcement actions the principle that charging undisclosed excessive commissions constitutes fraud."). In fact, in unregistered securities offerings, it is industry practice to disclose the amount of commissions paid as part of the sales effort. (Decl. Wilner, Exh. 19, Excerpts from Unregistered Securities).

a. Did Prime Know that 30% Commissions Impacted Investor Profits?

At the outset, it is important to note that the Court need not conclusively find that Prime actually "knew" that the 30% commissions were coming from investor funds. Rather, the Court need only find that Prime should have known this fact and was reckless in not exercising more due diligence

in knowing it. Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990)(en banc), cert. denied. 499 U.S. 976 (1991).

The Independent Sales Organization Agreement between Prime and Alliance contains the following provision governing the compensation Prime was to receive:

> 4. Compensation to Prime: In consideration of your services hereunder, [Alliance] covenants to pay to you a selling fee equal to 30% of the total purchase price of Units sold by the Partnership. Payment for fees is due to Prime Atlantic, Inc., within five (5) working days after bank has acknowledged deposit of funds and/or funds are indicated to be "good" and funds will be mailed in an expedient manner. This period shall apply to any and all funds that are not presented to [Alliance] in the form of money orders, certified or cashier checks that are immediately payable.

(Decl. Wilner, Exh. 7, at 2). This compensation agreement clearly ties Prime's commissions to the number of investment contracts Prime sold to the Principals. Moreover, it clearly ties the Principal's funds to Prime's commissions since the commissions are not even payable until the Principal's check has cleared and the payment is liquid. Such a connection between the Principals' funds and Prime's commissions ought to have put Prime on notice that Alliance likely tied Prime's commissions to the Principals' funds.

Prime argues, however, that this compensation arrangement does not conclusively establish that its commissions come directly from the Principals and that Alliance could still be paying Prime "advance commissions" from its profits on the leases, separate and apart from the Principals' funds and the Principals' expected profit. This reasoning is unpersuasive for three reasons. First, Alliance certainly has not had an opportunity to make a considerable profit on the Principal's money when it has just become payable. In fact, upon first receipt of the Principals' money, it is an open question whether the investor's money will be placed in a high-yield lease or in a lease with a lessor who defaults. Hence, any cut that Prime receives before the principal's money has been invested must necessarily come directly from the Principal's funds.

Second, Prime has to believe that Alliance has created a leasing program with unheard of returns in order to substantiate its beliefs regarding Alliance's profits; the actual returns on each Principal's investment must far exceed the promised 28% to the Principals if Alliance is able to deduct a 10% management fee for itself and a 30% commission to Prime and *still* generate a return of 28% on the Principals' funds. This is an incredible assumption. Prime has proffered no evidence of

Alliance's alleged profits to support that this is a logical, reasonable belief. In other words, absent some evidence that Alliance could reasonably pay Prime its high commissions with profits derived exclusively from this or some other venture and not from the Principal's funds, the clear inference is that Prime's commissions had to impact the profitability of the Principal's investment.[10]

Finally, and most convincingly, the Equipment Management Agreement between the Principals and Alliance put Prime on notice that its commissions impacted the profitability and riskiness of the Principals' investment. The agreement stated in no ambiguous terms that "advances of commissions" would be deducted from the rental revenue received by the Principals. (Decl. Wilner, Exh. 6 at ¶ 9). Hence, even if Prime did not believe that its commissions were coming out of the Principal's funds in the first instance, Prime knew that the profits of the investors, i.e. the rental revenue retained by the investors, was reduced by the amount of its commissions. Accordingly, the Court finds, Prime's protestations notwithstanding, that the undisputed facts support the conclusion that Prime acted recklessly in not verifying whether or not its commissions were derived from the Principals funds or profits. Certainly, the structure of the fee-splitting agreement between Alliance and Prime should have prompted Prime to investigate the nature of its commissions and it was reckless for Prime not to do so. This is especially true since Prime's own Policies & Procedures issued to the Independent Sales Contractors employed to market the Leasing Program assured the contractors that "[a]ll materials will have been the subject of a due diligence examination." (Decl. McCole, Exh. 4 at 27). The undisputed facts therefore show that Prime should have known that its commissions were taken directly from either the Principals' funds or rental revenues, thereby impacting both the potential profitability and

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[10] Prime's self-serving declarations by Prime's principals Halsey and Giavanno that they believed their commissions were coming from sources other than the investor's money do not raise triable issues of fact. Halsey merely asserts that "Prime was paid *advance* commissions." (Decl. Halsey, Exh. 77 at 10:10-13) Giavanno avers that she "believed when the Alliance leasing program began that Alliance had a substantial, existing leasing business; that it generated money from buying equipment in bulk at wholesale prices and then locating lessees to pay retail rates; and that it also made money selling commercial paper." (Decl. Giavanno at ¶3). Prime proffers no evidence to support the reasonableness of these understandings and points to no evidence indicating that Alliance actually did make profits that far surpassed those required to be paid to the Principals. Accordingly, the declarations of Halsey and Giavanno are little more than summary denials and the Court need not find that they raise material issues of fact in and of themselves. Leer v. Murphy, 844 F.2d 628, 631 (9th Cir. 1988) ("The party opposing summary judgment may not rest on conclusory allegations, but must set forth specific facts showing that there is a genuine issue for trial.").

riskiness of the Principals' investment.[11]

b. Was Omission of Prime's 30% Commissions Material?

In their argument against a finding of scienter on summary judgment, the Prime Defendants properly note that materiality is a mixed issue of fact and law and therefore can raise triable questions of fact. TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 450 (1976)(finding that issue of materiality of fact omitted from proxy statement is mixed question of law and fact). In fact, "only if established omissions are 'so obviously important to an investor that reasonable minds cannot differ on the question of materiality' is the ultimate issue of materiality appropriately resolved 'as a matter of law' by summary judgment." Id. at 450 (citing Johns Hopkins University v. Hutton, 422 F.2d 1124, 1229 (C.A. 4 1970.). Here, Prime Defendants argue that a question of materiality is raised because the Equipment Management Lease makes reference generally to the fact that "advances of commissions" would be deducted from investors' returns. (Decl. Wilner, Exh. 6 at ¶ 9). While it does not specify the exact amount, Prime Defendants argue that the reference at least takes the question out of the realm of omissions and moves it into the realm of misrepresentations and therefore requires that reliance be demonstrated on the part of the investors. The Court finds this semantic distinction disingenuous. The disclosure could equally well be viewed as an omission of the exact amount of commission paid as it could a misrepresentation.[12] Therefore, the adequacy of the disclosure is the issue to be resolved for the purposes of the materiality analysis.

The Court holds that exorbitant commission fees of 30 cents on every dollar invested are clearly material to an investor's assessment of the strength of a potential investment. As previously established, Prime knew that its fees were either coming directly from investor funds or profits.

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[11] Although not argued by the parties, the Court also observes that an alternate basis for finding liability on Prime's part is Prime's failure to disclose its conflict-of-interest when selling Alliance's program. Prime promoted the Leasing Program without telling investors that it was receiving exceedingly high commissions on the sales. Certainly any reliance on Prime's advice by the investors should have been informed by knowledge of Prime's incentives in promoting sales. The Ninth Circuit has recognized that promoters have a duty to disclose that they "expect[] to gain personally if [investors] follow[] [their] advice." Zweig v. Hearst Corp., 594 F.2d 1261, 1266-67 (1979).

[12] Even if the failure to reveal the 30% commission was viewed as a mere misrepresentation, SEC is not required to demonstrate reliance in a Commission enforcement action for injunctive relief. SEC v. Rana Research, Inc., 8 F.3d 1358, 1359 & 1363 n.4 (9th Cir. 1993).

Reasonable minds could not differ that a general disclosure of "commissions" is not the equivalent of a disclosure of 30% commissions. Furthermore, reasonable minds could not differ that large commissions amounting to 30 cents on every dollar invested are patently material. The Ninth Circuit has held that the "materiality of information relating to financial condition, solvency, and profitability is not subject to serious challenge." SEC v. Murphy, 626 F.2d 633, 653 (9th Cir. 1980). Clearly, large commissions impact the profitability of an investment and as such are material to an investor's informed decision. Therefore, the Court finds that there is no triable issue of fact that the disclosure was material. By failing to disclose their 30% commission as a reasonable person dealing in securities should have done, Prime Defendants recklessly omitted material information from the securities offering.

c. Did Prime Rely in Good Faith on Legal Counsel?

Alternatively, Prime Defendants assert the affirmative defense that they believed in good faith that the Alliance Leasing Program was not a security in light of the legal advice they received. Hence, they argue that they had no intent to defraud or mislead since they were unaware that the Alliance Leasing Program was a security which required certain disclosures. Additionally, they argue that they were not reckless in their belief that the Leasing Program was not a security. The Court must therefore ascertain whether the Prime Defendants raise a triable defense as to their good faith reliance on legal advice.

As a preliminary matter, the Court does not believe it is essential to the SEC's claim for fraud and misrepresentation under Section 10 and Rule 10b-5 that the SEC prove that Prime "knew" the Leasing Program was a "security" under the federal securities laws. The scienter requirement attaches not to knowledge that the investment is a "security," but to fraudulent omission of material information. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976) (holding that scienter is "a mental state embracing the intent to deceive, manipulate, or defraud."). Certainly, under common law fraud, Prime would be just as liable for failing to disclose its high commissions whether or not the Leasing Program qualified as a "security" under the federal securities laws. Hence, the fraudulent

omission, and not the fact that the Program is a security, is the focal inquiry for the scienter analysis.[13]

Prime's assertions that its principals did not believe that the program was security and its purported good-faith reliance on the advice of counsel to this same effect do not, therefore, insulate it from liability as to the requisite scienter. Only if counsel had specifically opined that disclosure of the 30% commissions was not required could Prime possibly assert the good faith reliance on counsel defense. However, even then, "such reliance does not operate as an automatic defense, but is only one factor to be considered in determining the propriety of injunctive relief." SEC v. Goldfield Deep Mines Co. of Nevada, 758 F.2d 459, 467 (9th Cir. 1985)(quoting SEC v. Savoy Industries, Inc., 665 F.2d 1310, 13114 n.28 (D.C. Cir. 1981)). Hence, the Court will consider this argument only in determining the appropriateness of injunctive relief in this case and not for purposes of liability.[14]

Prime Defendants have therefore failed to raise any material disputes of fact to preclude summary judgment. It is established that the Alliance Leasing Program was a security and that failure to disclose the 30% commissions rises to the level of an actionable misrepresentation under the third prong of Section 10(b). The Prime Defendants clearly should have known that they were receiving the 30% commissions directly from investor funds or profits and that this was not being disclosed to the investors. Certainly, failing to disclose such a material fact presents a danger of misleading buyers that was obvious to Prime. Accordingly, the Court GRANTS summary judgment against the Prime Defendants on the Section 10(b) claim.

F. Violation of Section 17(a) of the Securities Act

In order to prove a violation under Section 17(a) of the Securities Act, the SEC must prove that

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[13] The Court notes that Prime cites no case that supports its argument that defendants who knowingly make false and misleading statements, yet do not believe that the investment constitutes a security, have offered evidence to negate a finding of scienter under Section 10 and Rule 10b-5. This is not surprising since such a finding flies in the face of established jurisprudence on mens rea and statutory construction. In order to convict an individual for violating a statute, one must find that the individual intended to commit the crime, i.e. intended to defraud or deceive. It is not necessary to prove that the individual intended to break a specific law, i.e. a federal securities law. The old axiom, "ignorance of the law is no excuse," is clearly applicable. U.S. v. Int'l Minerals & Chemical Corp., 402 U.S. 558, 563 (9th Cir. 1971)("The principle that ignorance of the law is no defense applies whether the law be a statute or a duly promulgated and published regulation.") Moreover, the Ninth Circuit has specifically held that an individual's "claimed lack of knowledge about the provisions of the securities law provides no defense." U.S. v. Manning, 509 F.2d 1230, 1233 (9th Cir. 1975).

[14] See discussion infra in Section G -- Remedies.

Defendants (1) offered or sold any security; (2) by the use of interstate commerce or by the use of the mails; and (3) either (a) employed any device, scheme, or artifice to defraud or (b) obtained money or property by means of an untrue statement of a material fact or by the omission of a material fact; or (c) engaged in a transaction which operates as fraud or deceit upon the purchaser. 15 U.S.C. § 77(q)(a). A violation under Section 17(a) requires that the SEC demonstrate scienter, "a mental state embracing the intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976).

In light of the similarity between the elements of a violation under Section 17(a) and elements under Section 10(b), the Court finds that its previous analysis of the evidence under Section 10(b) applicable. The only real distinction between the two sections is that Section 10(b) requires the "purchase or sale" of securities while Section 17(a) deals with the "offer or sale" of securities. With regard to all Defendants, the salient inquiry is whether they engaged in the "sale" of securities.[15] Therefore, based on the foregoing analysis, the Court concludes that all Defendants are liable under Section 17(a) as well. Accordingly, summary judgment is GRANTED with respect to all Defendants on this claim for the reasons set forth in the Section 10(b) analysis.

G. REMEDIES

The SEC seeks the following relief against each of the Defendants: (1) permanent injunctive relief, (2) disgorgement, and (3) civil penalties. The Court will address the appropriateness of each remedy in turn.

1. Permanent Injunctive Relief

Permanent injunctive relief is appropriate when the SEC can show a reasonable likelihood that, absent an injunction, the defendant will engage in future violations. Murphy, 626 F.2d at 655. Whether a likelihood of future violations exists depends on the "totality of the circumstances surrounding the defendant and his violations." Id. The Ninth Circuit has delineated the following factors for the Court to consider in predicting the likelihood of future violations:

(1) the degree of scienter involved; (2) the isolated or recurrent nature of the infraction; (3) the

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[15] The Defendants do not present separate arguments with regard to their liability for violations of Section 17(a) and Section 10(b). Like the Court, Defendants properly recognize that their liability for both sections hinges only on a finding of the requisite scienter.

> defendant's recognition of the wrongful nature of his conduct; (4) the likelihood, because of defendant's professional occupation, that future violations might occur; (5) and the sincerity of his assurances against future violations.

SEC v. Fehn, 97 F.3d 1276, 1295 (9th Cir. 1996).

As to the Brownes, the Court finds that the totality of circumstances dictate the imposition of a permanent injunction. First, the Court finds that the Brownes blatantly misrepresented material information to investors in the Alliance Leasing Program -- their misrepresentations were serious enough to suggest a high degree of scienter. They failed to disclose material commissions, they failed to disclose a clear conflict of interest in that many of the purported, safe lessees were in fact companies owned and operated by the Brownes or their family, and they failed to disclose their past citations for securities laws violations. Second, the Court finds that this was not an isolated infraction; the Brownes are repeat offenders in the securities fraud arena. The Brownes have been enjoined and asked to cease-and-desist from offering securities in three different states prior to their involvement with the Alliance Leasing Program. Murphy, 626 F.2d at 655 ("The existence of past violations may give rise to an inference that there will be future violations; and the fact that the defendant is currently complying with the securities laws does not preclude an injunction."). Third, the Brownes have taken no responsibility for their actions or made any assurances that future violations will not occur; in fact, they have asserted the Fifth Amendment right against self-incrimination throughout these proceedings and still maintain that their actions do not give rise to securities violations. Finally, it seems very likely that the Brownes will engage in future projects that implicate securities laws. In fact, the SEC has provided the Court with the contractual agreement for the Browne's newest venture -- raising capital for the development of the Yosemite Motor Speedway.[16] (3rd Decl. Wilner, Exh. 1, 1-4). Taking all of these factors into consideration, the Court GRANTS a permanent injunction against Charles and Susan Browne because there is more than a reasonable likelihood of future violations.

As to the Prime Defendants, the Court does not find that the factors presented herein justify the extreme relief of a permanent injunction. Unlike the Brownes, the Prime Defendants do not have

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[16] The Brownes object to the introduction of this evidence based on the SEC's lack of personal knowledge of the contractual arrangements. However, the contract is attached to the exhibit and speaks for itself. Furthermore, the Court is not agreeing to any characterization of the new venture and only notes that it falls in the same line of investment projects as the Alliance Leasing Program.

securities violations in their backgrounds. Furthermore, the Prime Defendants' scienter does not rise to the level of the Brownes. Beyond the fact that the material misrepresentations made by Prime are far less extensive than those perpetrated by the Brownes, the Court also finds that Prime's arguments regarding their good faith reliance on legal advice raises some questions about the degree of Prime's scienter which justify denying the permanent injunction. As previously noted, the Court may properly consider Prime's arguments regarding their reliance on legal advice in the context of determining the propriety of injunctive relief. SEC v. Goldfield Deep Mines Co. of Nevada, 758 F.2d 459, 467 (9th Cir. 1985).

Prime argues that it received two attorney letters which opined that the Alliance Leasing Program was not a security. (Prime Opp. at 11). Specifically, Prime received such letters from Andrew J. Yurcho, Esq. and from Laurence Leafer, Esq. (Giavanno Decl., Exh's 67, 68). Leafer was paid over $1,000,000 from the Alliance offering proceeds and Yurcho was Corporate General Counsel for Alliance. (Wilner Supp. Decl., Exh. 1, (Leafer Depo. at 12-13, 153)). The Court is not persuaded by the legal opinions sought and retained by counsel affiliated with and paid by Alliance; clearly, attorneys on the payroll of Alliance had an interest in their determination that the Leasing Program was not a security. On the other hand, the Court does feel that Halsey's and Giavanno's purported reliance on representations allegedly made by the law firm of Baker & Hostetler which drafted the Equipment Management Agreement might provide a basis for a claim of good faith reliance. Halsey and Giavanno maintain that they were initially told by Baker & Hostetler that the program was not a security.[17] (Giavanno Decl. at ¶ 7)("Frank Mock, Esq. of Baker & Hostetler, made oral statements to both David Halsey and I that he did not believe the Alliance equipment leasing program was a security with the use of this Equipment Management Agreement."). However, Baker & Hostetler sent a letter on March 27, 1998 that indicated that it thought that the Alliance Leasing Program "could be deemed by certain state regulators as being a security." (Giavanno Decl., Exh. 93, at 1). It is unclear to this Court whether or not Baker & Hostetler made the representations that Prime Defendants allege prior to March 27, 1998. Clearly, Baker & Hostetler drafted the agreement and thereby gave it some

[17] The SEC objects to this evidence as inadmissible hearsay. However, the statements are not being offered for the truth of the matter asserted. FED. R. EVID. 801(c). The statements are merely being offered for their effect on the listener.

presumption of legality; it is also apparent to the Court that Baker & Hostetler has a significant interest in denying any oral representations to the contrary at this juncture and had a similar interest at the March 27, 1998 date of the letter when several state regulators had begun to investigate Alliance. Therefore, looking at the evidence in the light most favorable to Prime, the Court is inclined to believe that prior to March 27, 1998, the Prime Defendants could have relied in good faith on Baker & Hostetler's alleged representations that the Alliance Leasing Program was not a security.[18] Accordingly, the Court finds that this evidence lends possible support to the inference that Prime's scienter did not rise to the level of the Browne's or to a level justifying a permanent injunction.

Hence, it is clear that the SEC has not presented sufficient evidence to the Court to justify the imposition of a permanent injunction against Prime, Halsey, and Giavanno. There is a paucity of evidence that Prime is likely to engage in future securities violations, there is no evidence that Prime has previously engaged in securities violations, and Prime has made assurances against future violations. Accordingly, the Court DENIES injunctive relief against Prime.

2. Disgorgement

A district court may order disgorgement of unlawful gains pursuant to its equitable powers. SEC v. Rind, 991 F.2d 1486, 1493 (9th Cir. 1993). Disgorgement prevents unjust enrichment and is not considered an award of damages. Id. A person may be held jointly and severally liable for disgorgement with an entity he or she controls. Hateley v. SEC, 8 F.3d 653, 656 (9th Cir. 1993). Courts have also found that it is appropriate to award prejudgment interest to ensure that the defendants do not profit from holding illegally obtained funds over time. SEC v. Manor Nursing Ctrs, Inc., 458 F.2d 1082, 1105 (2d Cir. 1972).

Here, the SEC has submitted evidence collected by the bankruptcy trustee that demonstrates that the Brownes paid themselves compensation above their salary and bonus payments of at least

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[18] The Court is of the firm belief, however, that any good faith reliance that could have been asserted by Prime on the basis of Baker & Hostetler's alleged representations terminated upon receipt of the March 27, 1998 letter from Baker & Hostetler. Furthermore, Prime's knowledge of investigations that several state securities regulators were initiating against Alliance in the Spring of 1998 should have given Prime actual notice that the Leasing Program was likely a security which required certain disclosures. Prime can point to no legal assurances that the Leasing Program was not a security from Baker & Hostetler or other sources after the March 27, 1998 date. Therefore, Prime's liability after the March 27, 1998 date is clear.

$477,467 in 1998 through direct payments, reimbursement of personal charge cards, and payments routed through other entities and family members. (Trustee Decl. at ¶ 4). Because the Court has determined that the Brownes violated several securities laws and are jointly and severally liable for the actions of Alliance, the Court finds it appropriate to disgorge the Browne's ill-gotten gains. Furthermore, the Court finds that the SEC has adequately established that the Browne's should disgorge $477,467 and that prejudgment interest in the sum of $26,212 is warranted.[19]

With regard to Prime Defendants, the SEC has set forth evidence that indicates that Prime received $12,182,820 from Alliance, Halsey received $1,615,999 and Giavanno received $1,691,011. (Trustee Decl. at ¶ 5). The Prime Defendants do not dispute that they received these amounts; however, they argue that any disgorgement should be offset by what the investors receive as a result of Alliance's bankruptcy proceedings. (Prime Opp. at 15). Additionally, Prime argues that it paid two-thirds of these amounts to creditors and master contractors. Id. The Court will address each of these arguments in turn.

With regard to Prime's argument that any disgorgement amount against it should be reduced by the at least 41.6% that will be refunded to the Principals as a result of the bankruptcy proceedings, the Court is not convinced. Disgorgement deals with Prime's obligation to return its ill-gotten gains; the amount of money *it* received from selling the Leasing Program. Hence, the operative inquiry is whether the Prime Defendants were unjustly enriched by the proceeds they received from Alliance -- they clearly were. It is irrelevant to the disgorgement analysis that the investors may be compensated from other sources.

Second, with regard to Prime's contention that its disgorgement should be reduced such that it reflects the amount actually retained by Prime after payments of commissions to the subcontractors, the Court makes the following observations. Disgorgement is an equitable remedy and "the amount must be reasonable, i.e. approximately equal to the unjust enrichment." SEC v. Hateley, 8 F.3d 653, 656 (9th Cir. 1993). Prime argues that it cannot be unjustly enriched by the amounts that it did not

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[19] The fact that the Brownes have failed to offer any additional information about payments received because they have asserted their Fifth Amendment privilege does not bar disgorgement. In fact, their assertion of the privilege means that the SEC need only establish that the Brownes received investor funds since adverse inferences may be drawn from the Browne's silence. SEC v. Colello, 139 F.3d 674, 678 (9th Cir. 1998).

retain; accordingly, commissions paid to Master Contractors and sales representatives should be subtracted from Prime's liability. The SEC argues that it is appropriate to disgorge all the gains from Prime since no double recovery will result from so doing; the SEC has not sued the individual sales agents and asked for disgorgement of the investor funds retained by those individuals.

Both the SEC and Prime rely on the Ninth Circuit's decision in Hateley with regard to their relative positions. In Hateley, the Ninth Circuit found that it was an abuse of discretion for the SEC to award a disgorgement of approximately ten times the amount of the unjust enrichment. Id. at 656-57. Similar to the facts in the instant case, Hateley involved a "finder's fee agreement" between an individual, Jay Hold, and a corporation, Cambridge, in which Hold was to receive 90% of the commissions generated by all securities transactions he solicited for the firm. During the course of the agreement, commissions totaled roughly $55,000, of which Hold received roughly $50,000 and Cambridge (and its principals) received $5000. Securities violations were later found and disgorgement was ordered to the tune of $55,000 from Cambridge, despite a similar assessment against Hold. The Ninth Circuit found that disgorging $55,000 from Cambridge "duplicate[d] the amount that Hold was required to surrender" and was excessive. Id. at 656.

Here, it is clear that the SEC is not seeking duplicative recovery since it is not also seeking disgorgement of the amounts received by the independent sales contractors. However, it is also clear that Prime did not actually retain the monies it disbursed to its sales force. The Ninth Circuit in Hateley appeared to premise its conclusion that the disgorgement against Cambridge was unreasonable both on the existence of duplicative recovery and on the fact that Cambridge only actually retained 10% of the commissions under the agreement. It is certainly an open question whether the Ninth Circuit would have upheld disgorgement in the full amount against Cambridge absent the recovery from Hold. It is this Court's belief, however, that the purpose of disgorgement is to avoid unjust enrichment and to disgorge "ill-gotten gains." Since it is well-established that Prime had commission-sharing agreements with its sales force, it is well-established that Prime did not actually retain all the monies it initially received from Alliance. The Court therefore agrees that a reduction of $6,185,588.17, the amount of commission payments passed on to the Master Contractors, is warranted

in the disgorgement ordered against Prime.[20] (Decl. Slyngstad, Exh. 210, at 185).

Having found that the Prime Defendants are guilty of violating several securities laws, the Court orders that Prime disgorge $5,997,232 and pay prejudgment interest of $329,236 for a total of $6,326,468. Halsey and Giavanno are individually ordered to disgorge their ill-gotten gains and pay prejudgment interest in the following amounts: Halsey: $1,704,717; Giavanno: $1,783,847. However, Prime's disgorgement obligation is joint and several with those of Halsey and Giavanno; to the extent that either Halsey or Giavanno disgorge their ill-gotten gains, Prime's judgment is reduced.

3. Civil Penalties

Section 20(d)(2) of the Securities Act and Section 21(d)(3) of the Exchange Act authorize a court to impose civil penalties against a party for violating any provision of the statute or rules enacted thereunder. 15 U.S.C. § 77t(d)(2); 15 U.S.C § 78u(d)(3). The amount of the penalty is determined by the court "in light of the facts and circumstances" and in accord with a three-tier system for evaluating the severity of the infractions. Here, the third tier is clearly triggered since the violations "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement" and "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons." As has been previously established, both the Brownes and Prime Defendants recklessly disregarded securities requirements by marketing the Alliance Lease Program as they did; this caused substantial losses to befall the Alliance investors. Accordingly, the Court orders civil penalties as follows: the Brownes shall each pay $477,467, the gross amount of their pecuniary gain;[21] Prime shall pay $500,000; Halsey and Giavanno shall each pay $100,000.

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[20] Despite Prime's assertions that the amount disbursed to the sales force totaled almost two-thirds of the commissions received, the Court is inclined to trust the information contained in Exhibit A to the First Amended Disclosure Statement filed with the Bankruptcy Court in August of 1998.

[21] Under Section 20(d)(2), the Court may, in its discretion, impose the greater of the statutory maximum or the gross amount of pecuniary gain. The Court finds that imposition of the gross amount of pecuniary gain is warranted against the Brownes in light of their flagrant violations of the securities laws.

CONCLUSION

For the reasons set forth above, the Court **GRANTS** the SEC's motion for summary judgment against Defendants Charles Browne, Susan Browne, Prime Atlantic, Inc., David Halsey, and Braccus Giavanno. Accordingly, **FINAL JUDGMENT** should be entered as follows to these Defendants:

I.

IT IS ORDERED that Defendants Susan Browne and Charles Browne and their officers, agents, servants, employees, attorneys, and those persons in active concert or participation with any of them who receive actual notice of this Final Judgment by personal service or otherwise, and each of them, are permanently restrained and enjoined from, directly or indirectly:

A. making use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell any security through the use or medium of any prospectus or otherwise, unless a registration statement is in effect as to such security;

B. carrying or causing to be carried any security through the mails or in interstate commerce, by any means or instruments of transportation, unless a registration statement is in effect as to such security; and

C. making use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer or sell or offer to buy any security through the use or medium of any prospectus or otherwise unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or any public proceeding of examination;

in violation of Sections 5(a) and 5(c) of the Securities Act.

II.

IT IS FURTHER ORDERED that Defendants Susan Browne and Charles Browne and their officers, agents, servants, employees, attorneys, and those persons in active concert or participation with any of them who receive actual notice of this Final Judgment by personal service or otherwise, and each of them, are permanently restrained and enjoined from, directly or indirectly, in the offer or

sale of the securities of any issuer, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails:

A. employing any device, scheme, or artifice to defraud;

B. obtaining money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

C. engaging in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser;

in violation of Section 17(a) of the Securities Act.

III.

IT IS FURTHER ORDERED that Defendants Susan Browne and Charles Browne and their officers, agents, servants, employees, attorneys, and those persons in active concert or participation with any of them who receive actual notice of this Final Judgment by personal service or otherwise, and each of them, are permanently restrained and enjoined from, directly or indirectly, in connection with the purchase or sale of securities of any issuer, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange:

A. employing any device, scheme, or artifice to defraud;

B. obtaining money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

C. engaging in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon any person;

in violation of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

IV.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Defendants Susan Browne, Charles Browne, Prime Atlantic, Inc., David Halsey, and Braccus Giavanno shall pay

disgorgement plus pre-judgment interest calculated pursuant to 28 U.S.C. § 1961 in the following amounts:

Defendant	Disgorgement	Interest	Total
Susan Browne	$477,467	$26,212	$503,679
Charles Browne	$477,467	$26,212	$503,679
Prime Atlantic, Inc.	$5,997,232	$329,236	$6,326,468
David Halsey	$1,615,999	$88,718	$1,704,717
Braccus Giavanno	$1,691,011	$92,836	$1,783,847

Defendants Susan Browne and Charles Browne are jointly and severally liable for the disgorgement and prejudgment interest ordered against them. Prime's disgorgement obligation is joint and several with those of David Halsey and Braccus Giavanno.

Each defendant shall pay the amount of disgorgement and prejudgment interest by cashier's check, certified check, or postal money order within thirty days of entry of this Final Judgment. This disgorgement payment shall be made payable to the United States Securities and Exchange Commission and shall be transmitted to the Comptroller, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312, under cover of a letter that identifies the defendant, the name, and case number of this litigation and the court. A copy of this letter shall be simultaneously transmitted to counsel for the Commission in this action at its Pacific Regional Office.

V.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that the Defendants shall be liable for civil penalties resulting from their violations as follows:

Defendant	Civil Penalty
Susan Browne	$477,467
Charles Browne	$477,467
Prime Atlantic, Inc.	$500,000
David Halsey	$100,000
Braccus Giavanno	$100,000

Each defendant shall pay the amount of civil penalties by cashier's check, certified check, or postal money order within thirty days of entry of this Final Judgment. This payment shall be made payable to the United States Treasury, and shall be transmitted to the Comptroller, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312, under cover of a letter that identifies the defendant, the name, and case number of this litigation, and the court. A copy of this letter shall be simultaneously transmitted to counsel for the Commission in this action at its Pacific Regional Office.

VI.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that this Court shall retain jurisdiction over this action for all purposes in connection with this matter, including implementation and enforcement of the terms of this Judgment and other decrees that may be entered herein and to grant such relief as the Court may deem necessary and just.

IT IS SO ORDERED.

DATED: July 26, 2000

NAPOLEON A. JONES, JR.
United States District Judge

cc: All Parties
Magistrate Judge Aaron