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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH
CENTRAL DIVISION

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. NATIONAL NOTE OF UTAH, LC, a Utah Limited Liability Company and Wayne LaMar Palmer, an individual, Defendants.	**MOTION FOR SUMMARY JUDGMENT AGAINST DEFENDANT WAYNE LaMAR PALMER AND MEMORANDUM IN SUPPORT THEREOF** **CIVIL NO: 2:12 CV 00591** **Judge Bruce S. Jenkins**

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Plaintiff, Securities and Exchange Commission (the "Commission"), by and through its counsel of record, hereby moves the Court for the entry of an Order of Summary Judgment as to Defendant Wayne LaMar Palmer ("Palmer"). As set forth in the accompanying Memorandum, the undisputed facts prove that Palmer violated the registration, antifraud provisions and the broker registration requirements of the federal securities laws. Consequently, the Commission is entitled to a judgment as a matter of law.

I. Introduction

Since at least 2004, Palmer operated a classic Ponzi scheme, offering unregistered National Note of Utah, LC ("National Note") securities to investors and using funds from new investors to pay bogus returns to earlier investors. Palmer raised more than $100 million from over 600 investors in National Note through the fraudulent offer and sale of securities in the form of promissory notes. Palmer represented to investors that 1) investors' funds would be used for hard money loans, the purchase of notes, and the acquisition of real estate; 2) his and National Note's expertise in this area caused National Note to generate returns of 15 to 20% annually, allowing a guaranteed 12% annual return to investors; and, 3) the 12% return would be derived from National Note's investment prospects. Palmer further touted National Note as having "a perfect record" in that it never missed a payment of principal or interest to an investor.

Palmer omitted to disclose to investors, however, that 1) National Note was exclusively conducting business with related entities; 2) that National Note itself was insolvent and unable to make investor interest payments according to its terms; and, 3) that investor returns were being paid from the funds of new investors in a classic Ponzi scheme.

II. STATEMENT OF ELEMENTS AND UNDISPUTED MATERIAL FACTS

A. The Defendants

1. **National Note of Utah, LC** was a Utah Limited Liability Company organized on December 30, 1992. National Note's principal place of business was in West Jordan, Utah. It was owned and controlled by Palmer.[1]

2. **Wayne L. Palmer**, 57, was the sole owner and managing member of National Note. Palmer resides in West Jordan, Utah.[2]

B. Background

3. Palmer had been in the real estate and real estate financing business since 1976. In 1992, Palmer formed National Note.[3]

4. Palmer made all business decisions for National Note, including all decisions regarding the use of investor funds.[4]

5. Palmer solicited investors to purchase National Note promissory notes, which pay interest at a fixed annual rate of 12% with a minimum investment of $25,000. The notes carried a term between two and five years.[5]

6. Palmer signed each investor promissory note on behalf of National Note.[6]

7. The promissory notes issued by National Note are securities.

8. Palmer located new investors primarily by word of mouth and referrals. In addition, he taught real estate seminars across the country, and also made contact with potential investors at these speaking engagements.[7]

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[1] National Note of Utah, LC Private Placement Memorandum, attached hereto as Exhibit 1 ("Ex. 1") at pp. 45-46.
[2] Id. at p. 49; Declaration of Scott Frost ("Frost Decl."), attached hereto as Exhibit 2 ("Ex. 2"), at Ex. "A," p. 48.
[3] Ex. 2 at Ex. "D," p. 14.
[4] Ex. 2 at Ex. "A," pp. 48, 115.
[5] Ex. 1 at p. 21.
[6] Promissory Notes, attached hereto as Exhibit 3 ("Ex. 3").

9. Palmer told investors that National Note would use their funds to buy and sell mortgage notes, underwrite and make loans, or buy and sell real estate assets.[8]

10. Palmer assured investors that National Note was able to pay the promised returns of 12% annually because National Note was successfully investing the funds in projects and assets that were earning annual returns of 15-20%.[9]

11. Palmer represented to investors that both their 12% return and the safety of their principal were guaranteed and risk free. He claimed that National Note "ha[d] a perfect record," in that it never failed to make a principal or interest payment.[10]

12. The promissory notes issued to investors stated that they were secured by National Note's interest in "notes, trust deeds, and security agreements secured by real estate, mobile homes, and vehicles." This too gave investors confidence that their funds were at little risk.[11]

13. National Note raised approximately $50,000,000 in an unregistered offering of notes prior to September 2007.[12]

14. In September 2007, National Note carried out a private placement of notes under Rule 506 of Regulation D and provided offerees with a private placement memorandum ("PPM") that included unaudited financial statements for the prior year.[13]

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[7] Ex. 2 at Ex. "A," pp. 76-77; Testimony of Richard Park Arnold ("Arnold Test."), attached hereto as Exhibit 4 ("Ex. 4"), at p. 10; Testimony of Mary Varley ("Varley Test."), attached hereto as Exhibit 5 ("Ex. 5"), at pp. 9-12; Testimony of Gerald E. Wallin ("Wallin Test."), attached hereto as Exhibit 6 ("Ex. 6"), at p. 10
[8] Ex. 2 at Ex. "A," p. 93; Ex. 1 at p. 16.
[9] Ex. 2 at Ex. "A," pp. 55, 129; Testimony of Linda Tuxon ("Tuxon Test."), attached hereto as Exhibit 7 ("Ex. 7"), at pp. 12-13, 25; Ex. 4 at pp. 18, 42; Ex. 6 at p. 14; Testimony of John Spinola ("Spinola Test."), attached hereto as Exhibit 8 ("Ex. 8"), at p. 15.
[10] Ex. 2 at Ex. "D," pp. 4, 7.
[11] Ex. 3.
[12] Ex. 2 at ¶ 11.
[13] National Note raised approximately $50,000,000 in this Rule 506 offering, which ended with the filing of this action on June 25, 2012. Ex. 1; Ex. 2 at Ex. "A," p. 183.

15. Some of the investors in the September 2007 notes were accredited investors. Palmer provided these accredited investors with the PPM.[14]

16. Other investors were unaccredited, and these individuals did not receive the PPM. Instead, Palmer purports to have granted these unaccredited investors a direct security interest in a specific mortgage asset of National Note.[15] These security interests were called "Assignments of Beneficial Interest," and Palmer viewed the holders as direct investors in a National Note real estate asset.[16]

17. No registration statement was filed as to any offering of notes by National Note.

18. Palmer mailed the PPM and a subscription agreement to potential investors through the mail.[17]

19. Through at least February 2008, Palmer provided prospective investors with a glossy marketing brochure touting the National Note program. He also made this brochure available to attendees at the real estate seminars he conducted, on a table near the door.[18]

20. Among other things, the brochure features a chart showing that National Note paid a 12% return, without any variation whatsoever, from 1994 through 2003. It states that National Note's program provides double digit returns, monthly payments and safety of principal, all "Guaranteed."[19]

21. According to the brochure, "National Note pays the interest payments to its clients even when the property owner fails to pay on the loan."[20]

22. Some prospective investors received both the brochure and the PPM.[21]

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[14] Ex. 2 at Ex. "A," pp. 83, 87-88.
[15] Id. at p. 120.
[16] Id. at pp. 89; 121-2; Testimony of Julieann Palmer Martin ("Martin Test."), attached hereto as Exhibit 9 ("Ex. 9") at p. 28.
[17] Id. at pp. 34-35.
[18] Ex. 4 at pp. 11, 31-32.
[19] Ex. 2 at Ex. "D," pp. 3, 7.
[20] Id. at p. 8.

23. Both the brochure and PPM were prepared at Palmer's direction and under his supervision. The PPM was prepared by a law firm hired by Palmer.[22]

24. Palmer acted as an unregistered broker in connection with the offers and sales of notes, by actively and continuously soliciting investors and handling investor funds, and by paying commissions to third parties who solicited investors on behalf of National Note.[23]

25. In total, since at least 2004, Palmer, through National Note, raised approximately $100 million from more than 600 investors.[24]

C. Related Entities

26. In addition to National Note, Palmer formed and controlled at least 15 related entities. Many of these entities (the "Related Entities" or the "Palmer Entities") are formed under the umbrella of a holding company, Homeland Holding Corporation.[25]

27. Since approximately 2010, National Note transacted business exclusively with the Related Entities.[26]

28. Palmer represented to investors that the Related Entities were active in the real estate development business. He stated that they were funded by loans from National Note, and that National Note held mortgages from the Related Entities to secure its loans.[27]

29. Palmer told investors that the assets of the Related Entities would secure their promissory notes, and that these assets produced revenues sufficient to pay the 12% returns.[28]

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[21] Ex. 4 at pp. 30-31.
[22] Ex. 2 at Ex. "A," pp. 116, 118.
[23] Testimony of Richard Hicks ("Hicks Test."), attached hereto as Exhibit 10 ("Ex. 10") at p. 50; Ex. 2 at ¶¶ 9, 45.
[24] Id. at ¶ 11.
[25] Id. at Ex. "A," pp. 13, 16-17.
[26] Id. at ¶ 39.
[27] Ex. 1.
[28] Ex. 7 at pp. 25-26; Testimony of Fred R. Myer, Jr. ("Myer Test."), attached hereto as Exhibit 11 ("Ex. 11"), at p. 42; Testimony of Jacob Thomas Racki ("Racki Test."), attached hereto as Exhibit 12 ("Ex. 12"), at p. 13.

30. In fact, since 2009 the Related Entities generated little revenue, and were not able to pay the debt service on their mortgages in favor of National Note.[29]

31. In 2010, the Related Entities collectively generated revenue of only approximately $300,000. By contrast, National Note's monthly obligation for investor returns equaled approximately $1 million.[30]

32. Palmer caused journal entries to be made in National Note's internal accounting system that allocated investor funds to the Related Entities, as if National Note had made a loan advance to them. He then made an entry in which the investor funds were redirected to National Note as if the Related Entity had made an interest payment on its "loan" from National Note. Subsequently, the investor funds were paid out as returns to existing investors.[31]

33. These internal accounting entries purport to represent revenue from the Related Entities; however, no funds were physically transferred between National Note and its Related Entities.[32]

34. By conducting business exclusively with Related Entities, Palmer was able to advance funds to them on paper, giving the appearance that National Note's investments were successful, even though the entities had little or no revenue.[33]

D. Ponzi Payments

35. National Note investors initially deposited their funds into an account at JP Morgan Chase Bank titled "investor trust account." National Note immediately wired nearly all these investor funds to an account at Wells Fargo titled "investor interest account."

[29] Ex. 2 at ¶¶ 18, 23, 43 and at Ex. "A," p. 213.
[30] Ex. 2 at ¶ 30.
[31] Ex. 2 at Ex. "A," pp. 195-224, and at Ex. "Q".
[32] Id.
[33] Ex. 2 at ¶ 43.

National Note's internal accounting classified the investor funds as income upon transfer to the Wells Fargo investor interest account.[34]

36. From the Wells Fargo investor interest account, Palmer used the funds to pay returns to earlier investors.[35]

37. Palmer was a signatory on all the bank accounts of National Note and authorized all transfers.[36]

38. In 2009, National Note received approximately $18.6 million from new investors and used approximately $14 million (75%) of these new investor funds to make principal and interest payments to earlier investors.[37]

39. In 2010, National Note received approximately $22 million from new investors and used approximately $18 million (81%) of these new investor funds to make principal and interest payments to earlier investors.[38]

40. In 2011, National Note took in more than $14.6 million from new investors and used approximately $12.7 million (79%) of these new investor funds to make interest and principal payments to earlier investors.[39]

41. For the period January 1, 2012 to March 31, 2012, National Note received approximately $913,958 from new investors and used approximately $740,105 (81%) of these new investor funds to make interest and principal payments to earlier investors.[40]

42. Since at least 2009, National Note would not have been able to survive without an influx of new investor funds.[41]

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[34] Id. at Ex. "A," pp. 164-165, 167, 173.
[35] Testimony of Victor Wagner ("Wagner Test."), attached hereto as Exhibit 13 ("Ex. 13") at pp. 73-74.
[36] Ex. 2 at ¶¶ 15, 17 and at Ex. "A," p. 48.
[37] Id. at ¶ 19.
[38] Id. at ¶ 20.
[39] Id. at ¶ 21.
[40] Id. at ¶ 22.

43. In October 2011, National Note stopped making investor interest payments according to its terms to most investors. While some investors received sporadic payments, none received the full amount due him.[42]

44. When investors complained to Palmer about the late or missing payments, he urged them to be patient and promised that payments would resume soon.[43]

45. Although Palmer had essentially stopped making payments according to the terms of the notes by March 2012, he continued to solicit new investors. Significantly, Palmer did not disclose that National Note was delinquent in making investor payments.[44]

E. Misrepresentations and Omissions

46. In its PPM and its marketing materials, National Note claimed to use investors' funds for hard money loans, the purchase of notes, and the acquisition of real estate. Palmer told investors he deployed their funds in projects that would earn sufficient returns to pay the promised 12% annual return.[45]

47. Palmer failed to inform investors, and the National Note PPM and marketing brochure failed to disclose, that National Note simply used a majority of investors' funds to make principal and interest payments to earlier investors.[46]

48. The unaudited financial statements provided to investors in the PPM falsely indicate that National Note generated income in the form of note interest sufficient to make investor interest payments. The PPM reads, "[i]nterest and principle [sic] payments on the notes

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[41] Id. at ¶ 23 and at Ex. "A," pp. 185-86.
[42] Ex. 2 at Ex. "A," p. 113; Testimony of Tor Loring ("Loring Test."), attached hereto as Exhibit 14 ("Ex. 14"), at p. 27; Ex. 7 at p. 33; Ex. 8 at p. 26; Testimony of Chloe Dangerfield ("Dangerfield Test."), attached hereto as Exhibit 15 ("Ex. 15"), at pp. 29-30.
[43] Ex. 14 at pp. 28-29; Ex. 5 at p. 27; Ex. 6 at pp. 55-56.
[44] Ex. 2 at ¶¶ 49, 52.
[45] Id. at ¶ 10 and at Ex. "D"; Ex. 1.
[46] Ex. 1; Ex. 2 at¶ ¶ 39, 49, 53 and at Ex. "D".

offered pursuant to this Offering Memorandum are paid out of the cash flow from the loans National Note makes to others."[47]

49. National Note and Palmer never disclosed to investors that National Note's investments were not paying sufficient income. In fact, the investments were paying almost no income. Rather, Palmer reclassified investor funds as interest income as part of National Note's internal accounting procedures and then made bogus interest payments to earlier investors.[48]

50. National Note's marketing brochure falsely assured investors that they would receive double digit returns, monthly payments, and safety of principal, "Guaranteed," and that investors could expect "12% returns with complete safety of principal."[49]

51. In reality, National Note's returns were not guaranteed. In fact, returns were not being paid timely. Importantly, the investment involved significant risk.

52. Palmer failed to disclose to new investors that as of October 2011 he had stopped making interest payments according to the notes' terms to earlier investors.[50]

53. Palmer neglected to tell investors that, since approximately 2010, National Note had done business exclusively with the Related Entities. Through accounting entries, he created the illusion that National Note's investments in the Related Entities produced revenue, even though the Related Entities had generated little or no revenue for several years.[51]

54. Investor promissory notes falsely stated that they are secured by assets owned by National Note, leading the investors to believe that they had a lien and could foreclose on an asset in order to recover their investment. In reality, however, the accredited note holders had no

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[47] Ex. 1 at pp. 16, 42.
[48] Ex. 2 at ¶¶ 27, 28, 43 and at Ex. "A," pp. 17-171; 195-224, and Ex. "Q".
[49] Ex. 2 at Ex. "D," p. 7.
[50] Ex. 2 at ¶¶ 49, 52.
[51] Id. at ¶¶ 39, 43.

lien or security interest in any asset whatsoever and were unsecured creditors of National Note, relying only on its promise to pay.

55. The misrepresentations and omissions detailed above are material to a reasonable investor.

56. Palmer acted with scienter. He controlled National Note's bank accounts and authorized all transfers of funds. He also made all the business decisions for National Note. He was well aware of the contents of both the marketing brochure and the PPM, since they were prepared at his direction and under his supervision. He knew that the representations made to investors regarding the company's business and the use of investor funds were false.

I. ARGUMENT

A. No Material Issue of Fact Separates the Parties

Rule 56(c) of the Federal Rules of Civil Procedure provides that a party is entitled to summary judgment if the moving party demonstrates that "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). A genuine issue of material fact exists when, after viewing the record and making all reasonable inferences in a light most favorable to the non-moving party, a reasonable jury could return a verdict for the non-moving party. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986); Dreiling v. Peugeot Motors of Am., Inc., 850 F.2d 1373, 1377 (10th Cir. 1988).

Rule 56(e) further states that "[w]hen a motion for summary judgment is made and supported as provided in this rule … the adverse party's response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial." Fed. R. Civ. P. 56(e). In other words, once the moving party has demonstrated that there are no issues of material fact in dispute, the burden shifts to the opposing party "to come forward with specific facts showing that there remains a genuine factual issue for trial." SEC v. Murphy, 626 F.2d 633, 640 (9th Cir. 1980). Furthermore, the opposing party "must do more than simply show that there is some metaphysical doubt as to the material facts." Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 586 (1986). "The mere existence of a scintilla of evidence in support of the [non-moving party's] position will be insufficient." Anderson, 477 U.S. at 252 (1986). Rather, "[t]here must … be sufficient evidence for a jury to return a verdict in favor of the nonmoving party; if the evidence is merely colorable or not significantly probative, summary

judgment should be granted." Armbruster v. Unisys Corp., 32 F.3d 768, 777 (3d Cir. 1994). Accordingly, this standard provides that "the mere existence of some alleged factual dispute" between the parties will not defeat an otherwise properly supported motion for summary judgment. Anderson, 477 U.S. at 247–48.

Summary judgment is an appropriate device in actions brought by the Commission alleging securities fraud. See, e.g., SEC v. Carnicle, 216 F.3d 1088 (10th Cir. 2000); SEC v. Bonastia, 614 F.2d 908 (3d Cir. 1980); SEC v. Research Automation Corp., 585 F.2d 31, 32 (2d Cir. 1978); see also, Anderson, 477 U.S. 242; Matsushita, 475 U.S. 574. Where, as here, the government sues under a prophylactic or remedial statute for the vindication of the public interest, summary judgment is an effective tool which enables an enforcement agency with limited manpower and resources to police serious violations of the law where no contested, material evidentiary facts exist. See, e.g., SEC v. Geyser Minerals Corp., 452 F.2d 876 (10th Cir. 1971); United States v. Papercraft Corp., 393 F. Supp. 408 (W.D. Pa. 1975).

As set forth below, the undisputed evidence shows Palmer violated Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a) ("Securities Act"), Section 17(a)(2) and (3) of the Securities Act, 15 U.S.C. § 77q(a)(2) and (3), and Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) ("Exchange Act"), and Rule 10b-5 thereunder. The uncontroverted evidence shows Palmer violated Section 5(a) and (c) of the Securities Act, 15 U.S.C. §§ 77e(a), (c). Further, the uncontroverted evidence also shows Palmer violated Section 15(a) of the Exchange Act, 15 U.S.C. § 78o(a), when he acted as a broker-dealer in offering and selling National Note promissory notes and failed to register with the Commission pursuant to Section 15(b) of the Exchange Act, 15 U.S.C. § 78o(b).

Accordingly, the Commission seeks entry of a permanent injunction against Palmer,

enjoining him from future violations of the antifraud, securities registration, and broker registration provisions of the federal securities laws. Additionally, the Commission seeks disgorgement from Palmer of his ill-gotten gains consisting of the proceeds from investors' funds, prejudgment interest thereon, and a civil monetary penalty.

B. Palmer Controlled National Note

A corporation cannot act without its principal. See, e.g., SEC v. Merrill Scott & Assocs., Ltd., 505 F. Supp. 2d 1193 (D. Utah 2007); SEC v. Milan Capital Group, Inc., No. 00-CIV-108(DLC), 2000 WL 1682761 (S.D.N.Y. Nov. 9, 2000); SEC v. Am. Commodity Exch., Inc., 546 F.2d 1361, 1365 (10th Cir. 1976). In 1992, Palmer formed National Note as a limited liability company.[52] Palmer solely owned and individually managed National Note.[53] Further, Palmer made all business decisions for National Note and decisions regarding the use of investor funds.[54] Therefore, National Note's existence and operations were contingent upon Palmer, its principal.

C. Palmer Sold Securities in the Form of Promissory Notes

The National Note investors purchased securities in the form of promissory notes. In assessing whether an investment is a security, the United States Supreme Court has noted that the fundamental purpose of the Securities Act is "to eliminate serious abuses in a largely unregulated securities market." United Hous. Found., Inc. v. Forman, 421 U.S. 837, 849 (1975). In defining the scope of the products it wished to regulate, Congress painted with a broad brush. It realized the virtually unlimited scope of "human ingenuity, especially in the creation of 'countless and variable schemes devised by those who seek the use of the money of others on the promise of

[52] Ex. 2 at Ex. "A," p. 6; Ex. 2 at Ex. "D," p. 14.
[53] Ex. 2 at Ex. "A," pp. 23, 36.
[54] Ex. 2 at Ex. "A," pp. 48, 115.

profits.'" Reves v. Ernst & Young, 494 U.S. 56, 61 (1990) (quoting SEC v. W.J. Howey Co., 328 U.S. 293, 299 (1946)).

1. Promissory Notes are Securities

According to the United States Supreme Court, notes are presumed to be securities unless the notes fall into certain judicially-created categories that are plainly not securities, or, the notes bear a family resemblance to the notes in those categories. Reves, 494 U.S. at 62. The Reves Court identified four factors to consider in determining whether a particular note is a security. These four elements are:

> (1) the motivations that would prompt a reasonable seller and buyer to enter into [the transaction]. If the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the interest is likely to be a "security" . . . (2) the "plan of distribution" of the instrument . . . (3) . . . the reasonable expectations of the investing public . . . [and] (4) . . . whether some factor such as the existence of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Acts unnecessary.

Id. at 60-61. None of the four factors is crucial, and the failure of one will not automatically result in a Court's concluding that the note in question is not a security. Rather, courts take a balancing approach to determine whether, on the whole, the note looks more like a security than not. In re NBW Commercial Paper Litig., 813 F. Supp. 7, 10 n.7 (D. D.C. 1992) (holding Commercial Paper was a security).

a. The Motivation of Investors

The first factor under Reves is an objective inquiry into the "motivations that would prompt a reasonable seller and buyer to enter into [the transaction]." SEC v. J.T. Wallenbrock & Assocs., 313 F.3d 532, 538 (9th Cir. 2002). A note is more like a security "if the seller's purpose is to raise money for the general use of a business and the buyer is interested primarily in the

profit the note is expected to generate." Reves, 494 U.S. at 66; see also Pollack v. Laidlaw Holdings, Inc., 27 F.3d 808, 812 (2d Cir. 1994) ("The inquiry is whether the motivations are investment (suggesting a security) or commercial or consumer (suggesting a non-security)."). Alternatively, a promissory note that "is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties, or to advance some other commercial or consumer purpose" will "less sensibly [be] described as a security. Reves, 494 U.S. at 66.

The first factor puts the National Notes' and Palmer's promissory notes, at issue here, comfortably in the category of a security. Palmer raised money by telling people that their funds would be put into his real estate investment program and would earn high annual returns.[55] Further, Palmer represented to investors that the monies they gave were an investment and that the interest guaranteed under the notes was to be paid by the profit Palmer made by investing their monies in his various real estate schemes or developments.[56] Investors were not provided any specific information regarding any assets that purportedly backed up the notes. See Wallenbrock, 313 F.3d at 538 (lack of information regarding assets backing loan indicated investment for general business purposes). However, on their face, the notes generally claimed to be "backed by the [Palmer's and/or National Note's] interest in certain notes secured by Trust Deeds and/or Security Agreement in real estate, mobile homes and/or vehicles."[57] No specific collateral is identified in National Note.

In addition, the attractive, 12%-per-annum interest rate Palmer guaranteed to investors suggests the promissory notes are securities. See Wallenbrock, 313 F.3d at 538 (a promised interest rate above market rates suggested a security). Moreover, the fact that Palmer offered a

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[55] Ex. 2 at Ex. "A," pp. 55, 129; Ex. 7 at pp. 12-13, 25; Ex. 4 at pp. 18, 42; Ex. 6 at p. 14; Ex. 8 at p. 15.
[56] Ex. 2 at Ex. "D," pp. 4, 7.
[57] Ex. 3.

fixed rather than variable rate of return does not affect the investment's status as a security. See SEC v. Edwards, 540 U.S. 389, 397 (2004) (analyzing Howey and holding "an investment scheme promising a fixed rate of return can be an 'investment contract' and thus a 'security' subject to the federal securities laws"); Stoiber v. SEC, 161 F.3d 745, 750 (D.C. Cir. 1998) (holding fixed rate notes are securities); Pollack, 27 F.3d at 813 (noting fixed rate bonds are regulated as securities). Under these facts, the first factor of Reves is met.

b. The Plan of Distribution

The second Reves factor requires an examination of the plan of distribution of the promissory notes to determine whether the instrument has "common trading for speculation or investment." Reves, 494 U.S. at 66. If the promissory notes are sold to a broad segment of the general public, then common trading has been established. Id. at 68. Here, Palmer offered and sold the notes to a large group of investors – at least several hundred – across the United States and abroad.[58] Palmer located investors through real estate seminars he gave, word of mouth, and from third-party referrals.[59] This plan of distribution supports a finding that the notes are securities.

c. Expectations of the Investing Public

The third Reves factor requires a consideration of "whether a reasonable member of the investing public would consider these notes as investments." McNabb v. SEC, 298 F.3d 1126, 1132 (9th Cir. 2002). The opinions of individual investors as to whether the notes are securities are irrelevant. Id. Such admissions add little, if anything, to the analysis. Id. (citing Stoiber, 161 F.2d at 751). The verbal and written representations Palmer made to investors indicate that a reasonable investor would view the National Note promissory notes as an investment. National

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[58] Ex. 2 at ¶ 11.
[59] Ex. 2 at Ex. "A," pp. 76-77; Ex. 4 at p. 10; Ex. 5 at pp. 9-12; Ex. 6 at p. 10.

Note filed a Form D with the Commission seeking an exemption from registration pursuant to Rule 506 for the notes. The Form D indicates that National Note is selling securities. Moreover, the Private Placement Memorandum identifies National Notes' promissory notes as securities.[60] Palmer admitted that he raised money, evidenced by the notes, by convincing investors verbally and in writing that their money would earn a guaranteed 12% annually.[61] The investors reasonably understood, based on Palmer's representations, that interest returns under the notes would be paid from the proceeds of the investment they made in Palmer's and National Note's real estate operations. Palmer told investors their funds would be used to facilitate hard money loans, to purchase trust notes, options and leases, and to acquire and manage income-producing assets, including mobile home parks, residential health care facilities, multi-family projects, office and retail properties, self-storage facilities and undeveloped lots.[62] A reasonable investor would view such a transaction as a security purchase.

d. Risk-Reducing Factors

The final factor for a court to assess is whether there are adequate risk-reducing factors such as an alternative regulatory scheme that would "significantly reduce the risk of the instrument" to the lender, "thereby rendering the application of the Securities Acts unnecessary." Reves, 494 U.S. at 67. Here, there are no risk-reducing factors or alternative regulatory schemes that would reduce the risk to Palmer's investors. National Note's promissory notes are not secured, despite the representation, on their face, to the contrary and, as such, offer no protection to investors. Where notes are uninsured and uncollateralized, courts conclude such notes are securities. See SEC v. Cross Fin. Servs., Inc., 908 F. Supp. 718 (C.D. Cal. 1995). Thus, under a Reves analysis, the promissory notes National Note and Palmer offered, sold and issued are

[60] Ex. 1.
[61] Ex. 2 at Ex. "A," pp. 55, 129; Ex. 7 at pp. 12-13, 25; Ex. 4 at pp. 18, 42; Ex. 6 at p. 14; Ex. 8 at p. 15.
[62] Ex. 2 at Ex. "A," p. 93; Ex. 1 at p. 16; Ex. 3.

securities and were required to be registered absent an exemption from registration.

D. Palmer Violated the Antifraud Provisions of Section 17(a) of the Securities Act and Section 10(b) of the Securities Exchange Act and Rule 10b-5 thereunder

In order to prove Palmer violated Sections 17(a) of the Securities Act and 10(b) of the Exchange Act, the Commission must establish that (1) in connection with the offer and sale of securities; (2) Palmer engaged in a scheme to defraud when he made untrue statements, omitted material facts, and engaged in transactions, practices or courses of business that operated as a fraud or deceit upon the investor; (3) Palmer's misrepresentations or omissions were material, such that a reasonable investor would consider the misrepresented or omitted facts to be important in making an investment decision; and (4) Palmer acted with the requisite scienter in that he intended to deceive, manipulate or defraud investors, or acted recklessly in doing so. Aaron v. SEC, 446 U.S. 680, 701 (1980); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); Basic Inc. v. Levinson, 485 U.S. 224, 231-232 (1988); SEC v. Wolfson, 539 F.3d 1249, 1256 (10th Cir. 2008); Edward J. Mawod & Co. v. SEC, 591 F.2d 588, 595-97 (10th Cir. 1979) (defining scienter as reckless conduct); see also SEC v. Curshen, No. 09-1196, 2010 U.S. App. LEXIS 7555, at *11 (10th Cir. Apr. 13, 2010).

1. Palmer Made Fraudulent Statements and Material Omissions

Section 17(a) of the Securities Act [15 U.S.C. §77q(a)] prohibits persons, in the offer or sale of a security, from employing any device, scheme or artifice to defraud; obtaining money or property through materially false or misleading statements or omitting to state material facts; or engaging in any transaction, practice, or course of business which operates as a fraud or deceit. United States v. Naftalin, 441 U.S. 768, 773 (1979). Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit similar conduct in connection with the purchase or sale of a security.

Section 10(b) was designed to prevent all manner of fraudulent practices. Chiarella v. United States, 445 U.S. 222, 226 (1980); Ernst & Ernst, 425 U.S. at 201; Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128, 153 (1972); SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963).

Palmer made numerous misrepresentations and omissions to investors. Through National Note, Palmer guaranteed investors a fixed, 12%-per-annum return based on the profits generated though his investing strategies.[63] Palmer told investors that he would use their funds to further invest in hard money loans, to purchase notes, or acquire real estate.[64] Contrary to his representations to investors, Palmer did not use the majority of investors' funds to finance hard money loans, to purchase trust notes, options and leases or to acquire and manage income-producing assets in which National Note's Private Placement Memorandum claims to invest, such as mobile home parks, residential health care facilities, multi-family projects, office and retail properties, self-storage facilities and undeveloped lots. Instead, Palmer used investors' money almost exclusively to pay back earlier investors in a classic Ponzi scheme.[65] Palmer failed to inform investors that their quarterly payments did not come from investment activity but instead came from newly invested funds. Palmer's scienter can be imputed to National Note, because he was its managing member. SEC v. Manor Nursing Ctrs., Inc., 458 F.2d 1082, 1089 n.3 (2d Cir. 1972).

2. Palmer's Fraud Occurred in Connection with the Purchase or Sale of Securities

Palmer made misrepresentations "in connection with" the purchase or sale of securities, in the form of promissory notes. As the Supreme Court has reaffirmed, the "in connection with"

[63] Ex. 2 at Ex. "D," pp. 4, 7.
[64] Id.
[65] Ex. 13 at pp. 73-74; Ex. 2 at ¶¶ 19-22.

requirement is to be construed broadly and flexibly to effectuate its remedial purposes. SEC v. Zandford, 535 U.S. 813, 819 (2002). Thus, the "in connection with" requirement is satisfied when someone utilizes a device "that would cause reasonable investors to rely thereon" and "so relying, cause them to purchase or sell a corporation's securities." Carter-Wallace, Inc. v. Hoyt, 150 F.3d 153, 156 (2d Cir. 1998) (citing SEC v. Tex. Gulf Sulphur Co., 401 F.2d 833, 860-62 (2d Cir. 1968) (Section 10(b) applies "whenever assertions are made … in a manner reasonably calculated to influence the investing public."); SEC v. Savoy Indus., Inc., 587 F.2d 1149, 1171 (D.C. Cir. 1978) (The "in connection with" requirement is satisfied when it can reasonably be expected that a publicly disseminated document will cause reasonable investors to buy or sell securities "regardless of the motive or existence of contemporaneous transactions by or on behalf of the violator."); see also In re Ames Dep't Stores, Inc. Stock Litig., 991 F.2d 953, 966 (2d Cir. 1993) ("[S]tatements which manipulate the market are connected to resultant stock trading."); SEC v. Rana Research, Inc., 8 F.3d 1358, 1362 (9th Cir. 1993).

The "device" used to deceive can take many forms. See, e.g., Geman v. SEC, 334 F.3d 1183, 1185-91 (10th Cir. 2003) (misrepresentations contained in a firm's brochure and customer agreements); CFTC v. Vartuli, 228 F.3d 94, 101 (2d Cir. 2000) (holding the "in connection with" requirement is met when an advertisement makes false representations regarding securities transactions); Carter-Wallace, 150 F.3d at 156 (concluding false statements appearing drug advertisements in a medical journal could meet the "in connection with" requirement). It has been held that "[t]he intended and direct link between the advertisements and the [transaction] rendered any misrepresentations in the advertising 'in connection with' the suggested . . . transactions." Vartuli, 228 F.3d at 101 (discussing the "in connection with" requirement of analogous provision of the Commodity Exchange Act); see also R&W Technical Servs. Ltd. v.

CFTC, 205 F.3d 165, 172-73 (5th Cir. 2000) (the "in connection with" requirement of the CEA is met when defendants misrepresented the performance of its commodities trading program in advertisements).

Here, Palmer utilized several "devices," including National Note promotional and sales brochures, speaking arrangements, and seminars.[66] There was a direct and intended link between these devices and the purchase and sale of securities by National Note investors. See Zandford, 535 U.S. at 819. Palmer's misrepresentations regarding the use of funds occurred in the course of the sale of those securities.

3. Palmer's Misrepresentations and Omissions Were Material

Palmer's misrepresentations and omissions regarding the use of investors' funds are material. See SEC v. Cochran, 214 F.3d 1261, 1268 (10th Cir. 2000) ("information implicating the fair market value would be material to a reasonable investor"); Everest Sec., Inc. v. SEC, 116 F.3d 1235, 1239 (8th Cir. 1997) ("It would be material to an investor to know that the offering company's existing project had been abandoned, that none of its asset value was to be recouped."). Information is material if a substantial likelihood exists that the facts would have assumed actual significance in the investment deliberations of a reasonable investor. Basic, Inc., 485 U.S. at 224. Similarly, investors would consider it important to know their funds were being misappropriated by Palmer to operate a Ponzi scheme. SEC v. TLC Invs. & Trade Co., 179 F. Supp. 2d 1149, 1153 (C.D. Cal. 2001); see also SEC v. Smith, 2005 U.S. Dist. LEXIS 21427, at *15 (S.D. Ohio Sept. 27, 2005) ("it is obvious that a reasonable investor would consider it important to know that his money would not be invested in bank stock but would instead be used for other purposes, such as to pay for [Defendant's] American Express bill, car washes, dating services, and the expenses of [Defendant's] other companies").

[66] Ex. 2 at Ex. "A," pp. 76-77; Ex. 4 at p. 10; Ex. 5 at pp. 9-12; Ex. 6 at p. 10.

Here, Palmer failed to invest the funds as he represented. In fact, Palmer used nearly all newly-invested funds to make the promised interest payments to earlier investors.[67] Palmer did not tell any investors that he would use their funds to make payments to other investors.[68] A reasonable investor would consider these facts important in making an investment decision. See, e.g., SEC v. Mantria Corp., No. 09 Civ. 02676, 2011 WL 3439348, at *3 (D. Colo. Aug. 5, 2011) (holding that it is a material omission when a company fails to disclose that newly invested money is used to pay off old investors); United States v. Bremers, 54 F. App'x 591 (5th Cir. 2002). Consequently, Palmer's misrepresentations and omissions relating to the use of investors' funds are material.

4. Palmer Acted with Scienter

Palmer acted with scienter when he misrepresented and omitted material facts that caused investors to invest in National Note. Scienter is an element of violations of Section 17(a)(1) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder but is not a required element of a violation of Sections 17(a)(2) or 17(a)(3) of the Securities Act. Aaron, 446 U.S. at 696-97. The Supreme Court has defined scienter as "a mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst, 425 U.S. at 193. Reckless conduct has been held to satisfy the scienter requirement. Edward J. Mawood & Co., 591 F.2d at 595-597. In fact, the Tenth Circuit ruled that the threshold mental state for specific "intent to deceive" is merely "recklessness." Anixter v. Home-Stake Prod. Co., 77 F.3d 1215, 1232 (10th Cir. 1996) (noting that all circuits deciding the question have settled on "reckless" scienter). Reckless conduct itself is defined as behavior that is "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

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[67] Ex. 13 at pp. 73-74; Ex. 2 at ¶¶ 19-22.
[68] Ex. 1; Ex. 2 at¶ ¶ 39, 49, 53 and at Ex. "D".

or is so obvious that the actor must have been aware of it." SEC v. Pros Int'l, Inc., 994 F.2d 767, 772 (10th Cir. 1993) (citing Hackbart v. Holmes, 675 F.2d 114, 1118 (10th Cir. 1982) (citations omitted)).

Here, Palmer acted with the requisite scienter. Palmer knew how investor funds were used, because he controlled the accounts into which investors transferred funds.[69] Additionally, almost immediately after investors deposited funds into a National Note account, Palmer personally transferred the newly-invested monies into an account he created specifically to make interest payments to earlier investors[70]. As such, Palmer knew that he used money from new investors rather than legitimately-generated profits from his purported real estate ventures to pay investors' returns.

5. Palmer Used the Means and Instrumentalities of Interstate Commerce

Palmer used the requisite jurisdictional means to affect the fraud. In Pereira v. United States, 347 U.S. 1, 8-9 (1954), the United States Supreme Court found that, when a defendant knows the use of mail or of wire services is a reasonably foreseeable consequence of their operations, that knowledge is sufficient to satisfy the "jurisdictional means" element. "All that is required to establish a violation of [Section 17(a), Section 10(b) or Rule 10b-5] is a showing that a means, instrumentality or facility of a kind described in the introductory language of th[e] section was used, and that in connection with that use an act of a kind described . . . occurred." Matheson v. Armbrust, 284 F.2d 670, 673 (9th Cir. 1960); accord, United States v. Tallant, 547 F.2d 1291, 1297 (5th Cir. 1977).

Here, Palmer made use of the mails, of the Internet, and of the telephone to solicit

[69] Ex. 2 at Ex. "A," pp. 48, 115.
[70] Ex. 13 at pp. 73-74.

investments.[71] Investors wired funds to National Notes accounts at Palmer's and/or National Notes' direction.[72] Thereafter, Palmer transferred most funds to a separate account that he used to make interest payments to earlier investors.[73] Palmer also used the telephone and email to communicate with investors.[74] That is all that is required.

E. Palmer Violated the Registration Provisions of Sections 5(a) and (c) of the Securities Act

In order to establish a violation of the registration requirements of the Securities Act, the Commission must demonstrate that defendant Palmer, directly or indirectly, offered or sold securities without a registration statement having been filed or in effect. See SEC v. Int'l Chem. Dev. Corp., 469 F.2d 20, 27 (10th Cir. 1972). "The elements of [an] action for violation of Section 5 are (1) lack of a registration statement as to the subject securities; (2) the offer or sale of the securities; and (3) the use of interstate transportation or communication and the mails in connection with the offer or sale." Europe & Overseas Commodity Traders, S.A. v. Banque Paribas London, 147 F.3d 118, 124 (2d Cir. 1998) (quoting In re Command Credit Corp, No. 3-8674, 1995 WL 279776, at *2 (SEC Apr. 19, 1995)); see also SEC v. Novus Techs., LLC, Case No. 2:07-CV-235-TC, 2010 U.S. Dist. LEXIS 111851, at *38 (D. Utah Oct. 20, 2010); SEC v. Autocorp Equities, Inc., 292 F. Supp. 2d 1310, 1327 (D. Utah 2003).

Scienter is not an element of a Section 5 violation. See Aaron, 446 U.S. at 714 n.5; SEC v. Johnston, No. 90-4189, 1992 U.S. App. LEXIS 17626, at **2-5 (10th Cir. July 28, 1992); SEC v. Universal Major Indus. Corp., 546 F.2d 1044, 1046-47 (2d Cir. 1976); SEC v. Lybrand, 200 F. Supp. 2d 384, 392 (S.D.N.Y. 2002). See also Novus Techs., 2010 U.S. Dist. LEXIS 111851 at *38. In fact, Section 5 imposes strict liability on anyone who directly or indirectly violates its

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[71] Ex. 2 at Ex. "A," pp. 76-77; Ex. 4 at p. 10; Ex. 5 at pp. 9-12; Ex. 6 at p. 10.
[72] Ex. 2 at Ex. "A," pp. 164-165, 167, 173.
[73] Id.
[74] Ex. 9 at pp. 34-35.

plain terms. See SEC v. Friendly Power Co. LLC, 49 F. Supp. 2d 1363, 1367-68 (S.D. Fla. 1999) (concluding that a Section 5 violation does not require evidence of a specific intent to violate the statute) (citing SEC v. Tuchinsky, No. 89-6488-Civ-Ryskamp, 1992 U.S. Dist. LEXIS 13650, at *6 (S.D. Fla. June 29, 1992)); SEC v. DCI Telecomms., Inc., 122 F. Supp. 2d 495, 501 (S.D.N.Y. 2000) (regardless of intent defendants violated Section 5); SEC v. Current Fin. Servs., Inc., 100 F. Supp. 2d 1, 5 (D.D.C. 2000) (Section 5 of the Securities Act imposes strict liability).

More importantly, Palmer cannot avoid Section 5 liability based on a good faith belief that the offer or sale was legal. Id.; Friendly Power Co., 49 F. Supp. 2d at 1368 (citation omitted). Nor can Palmer rely on the advice of counsel to defend against a Section 5 claim. Id. Indeed, any claim that Palmer was an unwitting participant in the scheme is of no moment. See SEC v. Parkersburg Wireless LLC, 991 F. Supp. 6, 9 (D.D.C. 1997). Moreover, Palmer's knowledge regarding the applicability of the registration requirement of Section 5 is immaterial. See SEC v. U.N. Dollars Corp., No. 01 Civ. 9059 (AGS), 2003 U.S. Dist. LEXIS 1099, at *6 (S.D.N.Y. Jan. 28, 2003), aff'd sub nom SEC v. Harris, No. 03-6109, 2004 U.S. App. LEXIS 9370 (2d Cir. May 13, 2004). "Accordingly, defendants' lack of knowledge regarding the registration requirement does not provide them with a meritorious defense." Id.

The first element of a Section 5 violation is that Palmer and National Note lacked a valid registration statement as to the subject securities. See Int'l Chem., 469 F.2d at 27. Here, Palmer sold securities in the form of promissory notes. National Note never filed a registration statement with the Commission as to those securities. "Once the SEC introduces evidence that a defendant has violated the registration provisions, the defendant then has the burden of proof in showing entitlement to exemption." SEC v. Ralston Purina Co., 346 U.S. 119, 126 (1953). These exemptions are construed narrowly to promote the general purpose of the Securities Act,

"to protect investors by promoting full disclosure of information thought necessary to informed investment decisions." Id. at 124; see SEC v. Blazon Corp., 609 F.2d 960, 968 (9th Cir. 1979). There are three main exemptions to filing a registration statement that defendants in such actions may claim: the intrastate, the private placement, and the limited offering exemptions. However, in this case, there are no applicable exemptions from the registration requirements of the Securities Act for the offer and sale of National Note securities. Therefore, the first element of a Section 5 violation – failure to register securities – is satisfied.

The Section 3(a)(11) of the Securities Act exempts securities which are sold only intrastate. To qualify for the exemption, an individual or business must offer or sell "only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within or, if a corporation, incorporated by and doing business within, such State or Territory." 15 U.S.C.A. § 77c(a)(11). This exemption does not apply, because Palmer offered and sold securities to residents of several states. The second potential exemption is the private placement exemption found in Section 4(2) of the Securities Act and the safe harbors of Rules 505 and Rule 506 of Regulation D. As a threshold, both Rules 505 and 506 require that (1) there be no general solicitation, (2) the company inform purchasers that the securities are "restricted" for resale purposes, (3) there are no more (or the company reasonably believes that there are not more) than 35 non-accredited investors, and (4) non-accredited investors receive the same documents as accredited investors as well as financial and non-financial information generally given by a reporting company, like audited financial statements. 17 C.F.R. 230.505-506. National Note does not qualify for either exemption because Palmer engaged in general solicitation through his brochure distribution and when he conducted seminars. He also did not make any reasonable investigation to assure investors were accredited.

Finally, he did not provide non-accredited investors – or any investors for that matter – with the required financial information. See Western Federal Corp. v. Erickson, 739 F.2d 1439, 1442 (9th Cir. 1984) (private placement exemption not available where no access to the kind of information registration would disclose). In sum, Palmer cannot claim the private placement exemption, because he failed to follow even the most basic requirements of the exemption. The third exemption Palmer could claim is the limited offering exemption, found in Rule 504 of Regulation D. The limited offering exemption requires that a company raise less than $1,000,000 and not engage in any general solicitation. 17 C.F.R. § 230.504. This exemption is not available, because National Note raised more than $1,000,000, and National Note engaged in a prohibited general solicitation. Id. Therefore, Palmer sold securities without filing a registration statement or qualifying for an exemption.

The second and third elements of a Section 5 violation are also easily proved. The second element requires the absence of a registration statement when Palmer offered or sold securities. See Europe & Overseas Commodity Traders, 147 F.3d at 124. Palmer sold National Note securities in the form of promissory notes but failed to file a registration statement as to those securities. Thus, the second element is satisfied. The third element requires the use of interstate communications. Id. Palmer utilized the mail system, email, fax and the Internet to solicit investments in National Note, satisfying the intrastate communications requirement.[75] See SEC v. Solucorp Indus., Ltd., 274 F. Supp. 2d 379, 419 (S.D.N.Y. 2003). Consequently, Palmer violated Section 5 of the Securities Act when he failed to file a registration statement for National Note securities.

F. Palmer Violated Section 15(a) of the Exchange Act

Section 15(a)(1) of the Exchange Act prohibits a broker or dealer from making use of the

[75] Ex. 9 at pp. 34-35.

mails or any means or instrumentality of interstate commerce to effect or attempt to induce transactions in securities unless registered with the Commission in accordance with Section 15(b). 15 U.S.C. § 78o(a)(1). SEC v. United Monetary Servs., Inc., [1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,284 at 96,302 (S.D. Fla. 1990). Section 3(a)(4) of the Exchange Act defines "broker" as "any person engaged in the business of effecting transactions in securities for the account of others." The phrase "engaged in the business" connotes regular participation in securities transactions. Among the activities that indicate a person may be a broker are: solicitation of investors to purchase securities, involvement in negotiations between the issuer and the investor, and receipt of transaction-related compensation. See e.g. SEC v. Hansen, No. 83 CIV 3692, 1984 WL 2413 (S.D.N.Y. Apr. 6, 1984). Actions indicating that a person is "effecting" securities transactions include: soliciting investors; handling customer funds and securities; participating in the order-taking or order-routing process; and, extending or arranging for the extension of credit in connection with a securities transaction. See, e.g., Massachusetts Fin. Servs., Inc. v. Sec. Investor Prot. Corp., 411 F. Supp. 411, 415 (D. Mass. 1976), aff'd, 545 F.2d 754 (1st Cir. 1976); Hansen, 1984 WL 2413, at *10; SEC v. Nat'l Exec. Planners, Ltd., 503 F. Supp. 1066, 1073 (M.D.N.C. 1980); SEC v. Century Inv. Transfer Corp., Fed. Sec. L. Rep. (CCH) ¶ 93,232 (S.D.N.Y. Oct. 5, 1971). Scienter is not required in order to prove a violation of Section 15(a). See Merrill Scott, 505 F. Supp. 2d at 1216 (citing SEC v. Martino, 255 F. Supp. 2d 268, 283 (S.D.N.Y. 2003)); see also SEC v. Interlink Data Network of Los Angeles, Inc., No. 93-3073 R, 1993 WL 603274 (C.D. Cal. Nov. 15, 1993), rev'd on other grounds, 77 F.3d 1201 (9th Cir. 1996). Therefore, the Commission need only establish that Palmer acted as a broker-dealer in offering and selling National Note securities and that he failed to register with the Commission under Section 15(b). 15 U.S.C. § 78o(b).

Palmer was in the business of selling securities in the form of promissory notes. He engaged in the repeated sale of securities since at least 2004.[76] Palmer paid transaction-based commissions to third party individuals who referred investors to National Note without disclosing the payment of commissions to the investors.[77] Palmer therefore was a "broker" as defined under the Exchange Act. Palmer was not registered with the Commission in accordance with Section 15(b) nor was he associated with a registered broker or dealer. Palmer used the mails or instrumentalities of interstate commerce to induce investors to purchase National Note securities.[78] Consequently, Palmer violated Section 15(a) of the Exchange Act.

II. THE COMMISSION IS ENTITLED TO THE INJUNCTIVE AND MONETARY RELIEF IT SEEKS

"Once a violation of the federal securities laws has been found, a district court 'has broad equitable power to fashion appropriate remedies.'" Milan Capital, 2000 WL 1682761, at *9 (quoting SEC v. First Jersey Sec., Inc., 101 F.3d 1450, 1474 (2d Cir. 1996)). The Commission seeks an Order permanently enjoining Palmer from future violations of the federal securities laws, disgorgement together with prejudgment interest thereon and a civil monetary penalty.

A. The Court should Permanently Enjoin Palmer

The Court may grant permanent injunctions against future violations of the federal securities laws on a motion for summary judgment. Murphy, 626 F.2d at 655; Am. Commodity Exch., 546 F.2d at 1365; Geyser Minerals, 452 F.2d 876 (10th Cir. 1971). Section 20(b) of the Securities Act and Section 21(d)(1) of the Exchange Act grant the Commission authority to seek injunctive relief when it appears, upon proper showing, "that any person is engaged or is about to engage in acts or practices constituting a violation of any provision [of the Acts]." 15 U.S.C. §

[76] Ex. 2 at ¶ 11.
[77] Ex. 2 at ¶¶ 9, 45.
[78] Ex. 9 at pp. 34-35.

77t(b); 15 U.S.C. § 78u(d)(1). Here, Palmer will continue to violate the federal securities laws if not enjoined. His conduct meets the statutory requirement of "proper showing" to establish the likelihood that he will violate securities laws in the future, demonstrating the need for a permanent injunction.

In remedial enforcement actions, the Commission appears "not as an ordinary litigant, but as a statutory guardian charged with safeguarding the public interest in enforcing the securities laws." SEC v. Mgmt. Dynamics, Inc., 515 F.2d 801, 808 (2d Cir. 1975). The Commission, unlike private litigants, is not required to show risk of irreparable injury or balance of the equities in its favor to make the statutory "proper showing" for an injunction. SEC v. Unifund SAL, 910 F.2d 1028, 1036 (2d Cir. 1990). In order to make the "proper showing" required by statute, the Commission must establish that there is a substantial likelihood of future violations. Pros Int'l, 994 F.2d at 769; Murphy, 626 F.2d at 655.

When determining the likelihood of future violations, courts should consider and evaluate the totality of the circumstances. Pros Int'l, 994 F.2d at 769; Murphy, 626 F.2d at 655. Foremost among these circumstances is the past illegal conduct of the defendant, from which a court may infer the likelihood of future violations. Mgmt. Dynamics, 515 F.2d at 808. Past conduct amounting to "systematic wrong doing rather than an isolated occurrence" may be "particularly appropriate" for a permanent injunction. Milan Capital, 2000 WL 1682761, at *9 (citing First Jersey, 101 F.3d at 1477 (internal citations omitted)). Several factors courts use to determine the likelihood of future violations include "the seriousness of the violation, the degree of scienter, whether the defendant's occupation will present opportunities for future violations and whether defendant has recognized his wrongful conduct and gives sincere assurances against future violations." Pros Int'l, 994 F.2d at 769. No single factor is considered dispositive when

evaluating the likelihood of a future violation, but the degree of scienter does "bear heavily" on the decision. Id. (citing SEC v. Haswell, 654 F.2d 698, 699 (10th Cir. 1981)). Significantly, the Commission is not required to prove the existence of every one of these factors to establish a proper showing and obtain an injunction. Murphy, 626 F.2d at 656 (factors are not individual prerequisites to issuance of a permanent injunction by summary judgment). As discussed above, Palmer acted with a high degree of scienter. He (1) made misrepresentations to investors regarding National Note's purchasing arrangements; (2) made misrepresentations to investors concerning returns on investments; (3) made misrepresentations about the use of investors' funds; and (4) failed to disclose that National Note was operating as a classic Ponzi scheme. Simply put, Palmer was a facilitator, an active participant and beneficiary in a scheme to defraud approximately 600 investors out of over $100 million. Also, the egregious, systematic, and widespread nature of Palmer's conduct clearly demonstrates the need for a permanent injunction to deter future violations of the federal securities laws. Palmer's actions were not a single incident or one-time occurrence, but rather a systematic program of deception and fraud perpetrated over many years. From 2004 to 2012, he solicited investor funds while knowingly misusing investor funds. Consequently, given his conduct, the high degree of scienter demonstrated, and the high likelihood that Palmer will likely engage in violations of the securities laws, this Court should permanently enjoin Palmer from violating Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a); Section 10(b) of the Exchange Act, 15 U.S.C § 78j(b); and, Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5; Section 5(a) and (c) of the Securities Act, 15 U.S.C. § 77e(a), (c); and Section 15(a) of the Exchange Act, 15 U.S.C. § 78o(a).

B. The Court Should Order Palmer to Disgorge Ill-Gotten Gains

That the Commission may seek and the courts may order disgorgement of ill-gotten gains in Commission-instigated injunctive actions is well settled. Merrill Scott, 505 F. Supp. 2d at

1216 (referencing First Jersey, 101 F.3d at 1474). Actions for disgorgement of improper profits are equitable in nature. Id. The purpose of disgorgement is to prevent unjust enrichment. Id. By depriving violators of their ill-gotten gains, disgorgement effectuates the deterrence objective of the securities laws. First Jersey, 101 F.3d at 1475. Furthermore, the amount of disgorgement should include all gains flowing from illegal activities and "need only be a reasonable approximation of profits causally connected to the violation." Id. (quoting SEC v. Patel, 61 F.3d 137, 139 (2d Cir. 1995)); SEC v. First Pac. Bancorp, 142 F.3d 1186, 1192 n.6 (9th Cir. 1998). Moreover, the amount of disgorgement should not include any offset for the operating expenses of National Note. Wallenbrock, 440 F.3d at 1115 (concluding "it would be unjust to permit the defendants to offset against the investor dollars they received the expenses of running the very business they created to defraud those investors into giving the defendants the money in the first place"). "Neither the deterrent purpose of disgorgement nor the goal of depriving a wrongdoer of unjust enrichment would be served were we to allow these defendants – who defrauded investors … to 'escape disgorgement by asserting that expenses associated with this fraud were legitimate.'" Id. (quoting SEC v. Kenton Capital, Ltd., 69 F. Supp. 2d 1, 16 (D.D.C. 1998)).

The Commission is entitled to full disgorgement and prejudgment interest in order to deter Palmer, and other potential violators, from future violations of the securities laws and to make their victims whole to the fullest extent practicable. Palmer misappropriated at least $1,408,022.38 from investors. The Commission is entitled to an order requiring Palmer to disgorge his ill-gotten gains in the amount of $1,408,022.38, together with prejudgment interest thereon in the amount of $326,947.58, for a total of $1,734,969.96.[79]

C. The Court Should Impose a Civil Monetary Penalty against Palmer

Pursuant to Section 20(d)(2) of the Securities Act and Section 21(d)(3) of the Exchange

[79] Declaration of Matthew A. Himes ("Himes Decl."), attached hereto as Exhibit 16 ("Ex.16").

Act, the Commission seeks civil penalties for violations of the federal securities laws against Palmer. 15 U.S.C. § 77t(d)(2); 15 U.S.C. § 78u(d)(3). Like a permanent injunction, civil penalties are imposed to deter the wrongdoer from similar misconduct in the future. Accordingly, the factors considered to determine the likelihood of future violations for the purposes of a permanent injunction are also useful in assessing civil penalties. SEC v. Brethen, No. C-3-90-071, 1992 WL 420867, at *23 (S.D. Ohio Oct.15, 1992). When determining the appropriate civil penalty to impose, the Brethen Court recognized and examined three salient factors identified originally in SEC v. Youmans, (1) the egregiousness of the violations; (2) the isolated or repeated nature of the violations; and, (3) the degree of scienter involved. Id. (recognizing Youmans, 729 F.2d 413, 415 (6th Cir. 1984)); see also SEC v. Deyon, 977 F. Supp. 510, 519 (D. Me. 1997) (imposing $75,000 penalty against defendant based on his "fraudulent" conduct); SEC v. Custable, No. 94 C 755, 1996 WL 745372, at *5 (N.D. Ill. Dec. 26, 1996) (imposing civil penalty of $60,000, less than the maximum penalty, based in part on defendant's cooperation during the course of litigation). A third-tier penalty is appropriate where the violations (1) involve "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement" and (2) "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons." 15 U.S.C. §§ 77t(d)(2)(c); 78u(d)(3)(b)(iii). Furthermore, in determining whether to assess civil penalties, a court may consider evidence of a defendant's overall conduct, including conduct that is not directly related to the violations at issue. For example, the Moran Court considered the defendant's refusal to recognize the seriousness of his violations in deciding to impose civil penalties under the remedies act. 944 F. Supp. 286, 296 (S.D.N.Y. 1996).

The facts show that Palmer repeatedly induced investors to participate in his and National

Note's systematic program of deception and fraud. Although he knew investor money was being misappropriated, Palmer continued to solicit new investors and take their money. Palmer's high level of scienter is further evidenced by the expansive nature of the National Note scheme and by the number of investors involved. Palmer targeted investors from all over the country, giving no consideration to their level of sophistication. Palmer did not accurately represent how the money was being used or how profitable the investment was.[80] Even the filing of the Commission's enforcement action has not stopped Palmer from engaging in conduct that violates the federal securities laws.[81] As such, this Court should grant the Commission's request for third-tier civil penalties against Palmer in addition to a permanent injunction and disgorgement of misappropriated investor funds.

For violations occurring after March 3, 2009, third tier civil penalties may be imposed at a rate of up to $150,000 per violation for each natural person. See 17 C.F.R. 201.1004. Imposition of these penalties requires proof of "substantial losses or risk of losses to others." Id. Of course, the Court is empowered to set the penalty at any amount it deems appropriate under the circumstances, taking into account the public interest factors identified in Section 21(d)(2) of the Securities Act and 21(d)(3) of the Exchange Act. Those public interest factors are: (1) whether the act or omission involved fraud or deceit; (2) the harm to others resulting either directly or indirectly from such act or omission; (3) the extent to which any person was unjustly enriched; (4) whether such person has previously been found to have violated the securities laws; (5) the need to deter such person and other persons from committing such acts or omissions; and, (6) such other matters as justice may require.

[80] Ex. 2 at ¶¶ 49, 52.
[81] Ex. 2 at ¶¶ 49, 52.

III. CONCLUSION

There is no material issue of fact separating the parties in this action. Palmer's violations of the federal securities laws merit the harshest sanctions available. The record contains undisputed evidence—including Palmer's own testimony—that Palmer violated Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a); Section 10(b) of the Exchange Act, 15 U.S.C § 78j(b); in particular, Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5; Sections 5(a) and (c) of the Securities Act, 15 U.S.C. §§ 77e(a), (c); and Section 15(a) of the Exchange Act, 15 U.S.C. § 78o(a). For the reasons set forth in this memorandum, the Commission requests this Court to grant its Motion for Summary Judgment and award the relief requested.

Respectfully submitted this 19th day of July 2013.

/s/ Thomas M. Melton

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