

BEFORE THE
DEPARTMENT OF BUSINESS OVERSIGHT
STATE OF CALIFORNIA

In the Matter of the Desist and Refrain Order
Issued to:

MICHAEL E. PARKER; STELLAR
ENTERPRISE ASSOCIATES, INC.;
DAYSTAR INVESTMENTS, INC.,

Respondents.

Case No. 9301

OAH No. 2012110338

FINAL DECISION (AFTER
REJECTION OF PROPOSED
DECISION) AND ORDER

DECISION

This matter was heard before Michael C. Cohn, Administrative Law Judge (ALJ), State of California, Office of Administrative Hearings, in Oakland, California, on November 26, 27, 28 and 29, 2012.

Complainant Jan Lynn Owen, California Corporations Commissioner, was represented by John R. Drews and Doug Gooding, Corporations Counsel.

Respondents were represented by Michael J. Quinn and Eric A. Bevan, Attorneys at Law. Respondent Michael Parker was present.

The record was held open for briefing. The parties' closing briefs were received on December 21, 2012, and their rebuttal briefs on January 15, 2013. Complainant's briefs were marked for identification as Exhibits C-18 and C-19 and respondents' as Exhibits R-20 and R-21.

The matter was deemed submitted for decision on January 15, 2012.

The Proposed Decision was issued by the ALJ on February 15, 2013. In accordance with Government Code Section 11517(c)(2)(E), all parties were served on June 3, 2013, with an order of rejection of the Proposed Decision of the ALJ and notified that the case would be decided by the California Commissioner of Corporations, Jan Lynn Owen, upon the record, and upon any written argument offered by the parties.

The parties were permitted to submit written arguments by July 3, 2013. The Complainant and Respondents submitted timely written arguments.

The record in this case, including the transcripts of the proceedings of November 26, 27, 28 and 29, 2012 have been given careful consideration. The following shall constitute the Decision of the California Commissioner of Business Oversight in the above-entitled matter.

FACTUAL FINDINGS

Background and Parties

1. On July 11, 2011, complainant issued a Desist and Refrain Order to Michael E. Parker; Lacy Hawkins; Stellar Enterprise Associates, Inc.; and DayStar Investments, Inc., alleging violations of two provisions of the Corporate Securities Law of 1968 – Corporations Code section 25110 (sale of unqualified securities) and Corporations Code section 25401 (sale by misrepresentation or omission) – and ordering them to desist and refrain from offering or selling any securities in California unless the securities have been qualified under the law or are exempt from qualification, and to desist and refrain from offering or selling any securities in California by means of any written or oral communication that includes an untrue statement of material fact or that omits to state a material fact necessary to make the statements made not misleading.

2. Parker, Stellar and DayStar filed timely requests for hearing. Complainant determined that Hawkins did not, and that therefore the desist and refrain order was final as to him and he was not entitled to a hearing. Although Hawkins asserted in this proceeding that he should be allowed to participate in the hearing because he was neither properly served with the desist and refrain order nor provided adequate notice of his right to a hearing, his motion to be heard on those matters was denied.¹ Hawkins is not a respondent in this proceeding and no order will be made as to him.

3. Stellar Enterprise Associates, Inc., is a California corporation formed in 2001. DayStar Investments, Inc., is a California corporation formed in 2003. DayStar operated as a subsidiary of Stellar. Michael E. Parker founded and acted as chief executive officer of both corporations. Parker is also a minister of the General Assembly Church. Lacy Hawkins is the founder and pastor of the church.

Desist and Refrain Order

4. The desist and refrain order alleges that in 2002, Parker and Hawkins began offering promissory notes and loan agreements as investments in DayStar to members of the General Assembly Church's congregation; that Hawkins repeatedly urged the congregation to attend presentations in a church meeting room after services; that Parker, with the substantial assistance of Hawkins, solicited church members to invest in DayStar securities; that general congregational solicitations were made to hundreds of church members simultaneously and

¹ In order to complete the record, respondent's motion is marked as Exhibit R-22 for identification and complainant's opposition is marked as Exhibit C-20 for identification.

were repeated numerous times; that no attempt was made to pre-qualify the church members for the purchase of securities; and that when revenue from the notes and loan agreements with DayStar began to diminish, Parker and Hawkins undertook to convince the investors to either forgive the debts they were owed by DayStar or to convert their DayStar debt to Stellar shares.

5. The desist and refrain order alleges that the interests offered in the form of promissory notes and loan agreements were securities subject to qualification under the Corporate Securities Law of 1968; that the offering and sale of securities by way of general solicitation to the congregation precludes Parker and Hawkins from availing themselves of the exemptions provided by Corporations Code sections 25102.1 or 25102, subdivision (f); and that as a result, the securities were unqualified and non-exempt and were sold in violation of Corporations Code section 25110.

6. The desist and refrain order further alleges that, in violation of Corporations Code section 25401, the securities in DayStar and Stellar were offered by means of oral or written communications that included an untrue statement of material fact or that omitted 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.

7. Finally, the desist and refrain order alleges that many of the investors never received a return of their principal or any interest; that when investors requested a return of their funds after six months to a year their requests were denied; and that investors who were promised a 35 percent return on their investments over \$250,000 received no return.

Chronology and History of the Investments

8. Lacy Hawkins founded the General Assembly Church in 1974. The General Assembly has four churches in California – Berkeley, Vallejo, Union City and Moreno Valley – and three in other states. The church has roughly 2,500 to 3,000 members.

9. Michael Parker has grown up in the church; his parents joined when he was two years old. He was ordained as a minister in the church about a decade ago. He obtained a bachelor's degree in business in 1997 and an MBA in 2001.

10. Parker founded Stellar in November 2001. Parker's "second in command" was Christopher Pratt, the corporation's secretary and only other officer. While not formally affiliated with the General Assembly Church, Stellar was intended to be a "consultant management company" that would help build businesses for church members. Over the next few years, Stellar created or acquired from church members a number of subsidiary businesses. Stellar's subsidiaries included a clothing store, a salon/spa, a health and fitness company, a cabinet shop, a construction company, and several real estate-related businesses, all of which employed church members. At their peak, the various companies employed nearly 200 church members.

11. When Stellar was unsuccessful in obtaining bank loans, Parker and Pratt decided to raise capital by investing in real estate and other projects. The goal was to provide both a nice return to investors and funds for Stellar to operate its businesses. On September 25, 2002, Parker and Pratt held a meeting at the Berkeley church with a group of invited church members to discuss pooling their money in real estate investments. As a result, in October 2002, at least 18 individuals or couples invested a total of at least \$281,650 in amounts ranging from \$150 to \$90,000. Each of these 18 investors received an "Investment Receipt" acknowledging that Stellar had received their investment "for the purpose of real estate investment services."

12. It was after receiving these investments that Parker and Pratt created DayStar as a Stellar subsidiary to serve as an investment vehicle. They sought the advice of attorney Steven Lopez who advised them how to proceed with a "debenture offering." Lopez drafted loan agreements, promissory notes and other documents to be used in the offering. DayStar was formally incorporated sometime in 2003. The documents prepared by Lopez were not put into use until sometime in 2003. Before that time, in calendar year 2002, church members had made investments totaling \$2.274 million. None of these investors received loan agreements or promissory notes at the time they made their investments; those documents were not yet in existence.

13. Parker and Pratt made their first DayStar investment presentation at the Berkeley church in March 2003. Similar presentations were subsequently held at the other three California churches as well. These presentations were open to all church members; announcements were made following church services inviting members to attend. No attempts were made to pre-qualify any investors. In these initial presentations, investors were promised returns of 10 to 15 percent during each six-month investment cycle. Respondents fully expected they would be able to pay these returns. In a presentation made a year later, in March 2004, DayStar offered somewhat smaller returns, from five to 10 percent per cycle. But investments of \$250,000 or more were offered returns of 30 percent (apparently on an annual basis).

14. DayStar continued to solicit investments from church members until the middle of 2006. From 2002 to 2006, church members invested more than \$17 million in the DayStar program. According to Parker, during the first couple of years, operations went well; the real estate market was booming and their investments had good returns. All requests for payments by investors were honored. But the overall climate began to change in 2004-2005 when the company began investing in larger projects, which "tied up" larger sums of money. As a result, DayStar was no longer able to pay all its investors.

On June 14, 2006, DayStar sent its investors a letter advising them that the then-current investment cycle was ending on June 30, 2006. Investors were given the option of rolling over all or a portion of their principal and interest or requesting withdrawal. Janet Haywood's letter showed that her principal and projected interest on June 30, 2006, was \$241,741.78. When she asked for a return of her investment she was told by Parker "there was no money." Julio and Camille Ramirez were advised that their principal and projected

interest was \$500,500. They opted to withdraw \$250,000 and roll over the rest. However, they received a letter dated August 8, 2006, stating that "[d]ue to the high amount of withdrawal requests at one time, and operating capital tied up in existing projects," their payout would be "delayed until further notice." They never received the requested withdrawal.

15. In every year between 2002 and 2006, DayStar's liabilities exceeded its assets. And in each of those years, DayStar's expenses exceeded its income. The company's profit and loss statements showed net losses of \$67,071.41 in 2002, \$984,567.33 in 2003, \$1,751,826 in 2004, \$965,409.94 in 2005, and \$1,837,021.45 in 2006. The company's balance sheets showed that its liabilities exceeded its assets by \$64,568.84 in 2002, \$1,031,667.74 in 2003, \$2,783,493.74 in 2004, \$3,748,904.68 in 2005, and \$5,585,926.13 in 2006. And the company was cash poor. Although DayStar had taken in \$5.5 million in investments in 2002 and 2003, by the end of that latter year it had cash on hand of only \$128,465. This increased to \$318,449 at the end of 2004 but DayStar's cash position was in the red by half a million dollars at the end of 2005 and by over one million dollars at the end of 2006. None of this was disclosed to any prospective investors. Investors and prospective investors were always told the company was doing well. None were ever provided accountings showing DayStar's financial situation. Parker testified that Lopez had advised that the church members participating in DayStar were "lenders, not investors" and that therefore DayStar was not to provide them any documents beyond the promissory notes and loan agreements he had prepared.

16. In late 2005 or early 2006, Parker learned from new corporate counsel Steven R. Bangerter that DayStar's method of raising money was not in conformity with security regulations. Bangerter advised Parker to stop taking money through DayStar and to suspend all operations. After Stellar's chief financial officer prepared a "Financial Recovery Plan" showing how much the company and its subsidiaries, including DayStar, were losing, it was decided to raise additional capital by selling Stellar shares. Bangerter's office provided legal advice and prepared a Private Placement Memorandum (essentially a prospectus) for the offering.

17. In the summer of 2006, Parker made the first presentation for the sale of Stellar stock at a meeting in the Vallejo church's dining hall. In December 2006, DayStar sent a letter to all investors advising them of an "opportunity to take advantage of some tax savings options that may be available to you." Investors were advised that one of these options was forgiving all or a portion of the debt owed them by DayStar, which, the letter said, could be used to offset capital gains and/or ordinary income. A second option was using the funds in their DayStar account to purchase Stellar shares, which would "help reduce the debt of DayStar" while at the same time providing the investors with equity in Stellar.

18. Stellar stock was sold from July through December 2006. The sale raised approximately \$3.1 million, about half of which came through investors' conversion of DayStar debt.

19. In May 2009, the Securities and Exchange Commission notified Parker and Stellar that it was conducting an investigation concerning DayStar Investments. Parker provided requested documents to the SEC and was deposed during the investigation. The investigation focused primarily on the DayStar loan offering, though some questions were also asked about the Stellar equity offering. On July 10, 2010, the SEC notified Parker that the "inquiry has been terminated, and no enforcement action has been recommended to the Commission."

Findings on the Allegations of the Desist and Refrain Order

20. The desist and refrain order alleges violation of two provisions of the Corporate Securities Law of 1968 (Corp. Code, §§ 25000-25707): sections 25110 and 25401. Those alleged violations are addressed below in Factual Findings 26 through 40. As background to those allegations, the order makes a number of general factual allegations, some of which were proven, some of which were not. Those general allegations, as set forth above in Factual Findings 4 and 7, are addressed first.

GENERAL ALLEGATIONS

21. It is true that in 2002, Parker began offering promissory notes and loan agreements as investments in DayStar to members of the General Assembly Church's congregation, that he solicited church members to invest in these securities, that general solicitations were made to many church members simultaneously and were repeated numerous times, and that no attempt was made to pre-qualify church members for the purchase of DayStar securities.

22. It was not established that when revenue from the DayStar notes and loan agreements began to diminish that Parker "undertook to convince" church members to forgive the debts they were owed by DayStar or to convert their DayStar debt to Stellar shares. As set forth in Finding 17, in December 2006, DayStar investors were offered the opportunity to either forgive the debts owed by DayStar or to convert that debt to Stellar shares. But there is no evidence of more than this. The allegation that Parker "undertook to convince" investors implies an effort to importune or pressure investors. The forgiveness/conversion offer did not rise to this level.

23. While no attempt was made to pre-qualify church members for the purchase of the DayStar loan program, it was not established that no attempt was made to pre-qualify members for the purchase of the Stellar equity offering. The Stellar offering's private placement memorandum provides that, "The shares are being offered only to 'accredited investors' (as defined by Regulation D of the Securities Act of 1933)[.]" The letter sent to DayStar investors advising them of the opportunity to purchase Stellar stock stated that, "In order to determine that you meet the standards to participate as an accredited investor, a subscription agreement must be completed." The subscription agreement included with the

private placement memorandum required potential investors to certify that they met the net worth or income limits set forth in Regulation D for qualification as accredited investors. This was an attempt at pre-qualification.

24. It is true that many of the investors never received a return of their principal or any interest; that when investors requested a return of their funds after six months to a year, some of their requests were denied, at least in 2005 and 2006; and that at least one investor who was promised a 30 percent return on his investment over \$250,000 received no return.

ALLEGED VIOLATION OF CORPORATIONS CODE SECTION 25110

25. Corporations Code section 25110 provides that "It is unlawful for any person to offer or sell in this state any security in an issuer transaction...unless such sale has been qualified ...or unless such security or transaction is exempted ..."

26. There are two offerings at issue here: the DayStar Joan offering and the Stellar equity offering. Both were securities under Corporations Code section 25019. Respondents did not seek to qualify either security under the Corporate Securities Law of 1968. They did file exemption notices for both offerings under Corporations Code section 25102, subdivision (f). That subdivision generally provides that offerings are exempt from qualification if they are sold to not more than 35 persons, all of whom either have a preexisting personal or business relationship with the offeror or its officers, directors and managers or by reason of their business or financial experience could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction.

27. The DayStar loan offering and the Stellar equity offering were each sold to far more than 35 persons. Therefore, regardless of whether the purchasers had the necessary personal or business relationship with DayStar and Stellar's directors (and it is likely many did not – Parker's relationship to them as a minister in the church would not seem to meet the test required by the statute),² respondents are precluded from availing themselves of the exemption in section 25102, subdivision (f).

28. Corporations Code section 25102.1 also exempts from qualification any sale of a security to a "qualified purchaser" as defined by federal securities law and regulations. While the Stellar equity offering was limited to "accredited investors" as defined by federal law and regulation, that term is not equivalent to "qualified purchaser." An accredited investor is one with a net worth in excess of \$1,000,000. (17 C.F.R. § 230.501(a).) A qualified purchaser is an individual with at least \$5,000,000 in investments. (15 U.S.C. § 80a-2(a)(51)). There was no showing that any of the investors in either the DayStar offering or the Stellar offering were qualified purchasers.

² See California Code of Regulations, title 10, section 260.102.12, subd. (d). A "preexisting personal or business relationship" must be of the type "such as would enable a reasonably prudent purchaser to be aware of the character, business acumen and general business and financial circumstances of the person with whom the relationship exists."

29. Since the DayStar offering and the Stellar offering were not qualified under the Corporate Securities Law of 1968 and were not entitled to exemption from qualification under either Corporations Code section 25102, subdivision (f), or section 25102.1, both offerings were sold in violation of Corporations Code section 25110.

ALLEGED VIOLATION OF CORPORATIONS CODE SECTION 25401

30. Corporations Code section 25401 provides that “It is unlawful for any person to offer or sell a security in this state...by means of any written or oral communication which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.”

31. The desist and refrain order alleges that in the process of offering securities Parker, with the substantial assistance of Hawkins, made the following five misrepresentations to investors:

- a) Investors would receive a 10 percent to 20 percent return on their funds every six months to one year.
- b) The investment contained no risk since the money invested would be secured by real property.
- c) Investors would be free to withdraw all their funds at six month or one year intervals, and would receive a payment of interest as well as a return of their principal.
- d) Investors who invested more than \$250,000 would receive a 35 percent return on their money.
- e) If members of the church did not invest with DayStar or Stellar they would no longer be members of the church and would not have eternal life.

And the desist and refrain order alleges that respondents made the following four omissions:

- f) Failed to emphasize to investors that the loan agreement and promissory note contained language that allowed DayStar and Stellar to extend repayment dates to infinity by asking for unlimited extensions of repayment dates.
- g) Failed to provide accurate accounting to investors in DayStar and Stellar and failed to disclose significant losses while claiming the businesses were continuing to be profitable.
- h) Continued to sell investments in DayStar from 2002 to 2006 and failed to disclose to investors that DayStar operated at a loss every year.

i) Failed to inform investors that “a large part of their funds would be paid to subsidiaries of DayStar and in turn this money would be used to pay inflated management fees to Stellar, both of which were controlled by Parker with the substantial assistance from Hawkins.”

32. While the desist and refrain order relates to two distinct investment offerings - the DayStar loan program and the Stellar equity offering – it does not specify which alleged misrepresentation or omission refers to which offering. Respondents assert that the order is thus impermissibly vague and should be rescinded. But it is clear from the content and context of each allegation to which offering each applies, and even though there was some ambiguity in the structure of the order, respondents' defense to the allegations was not hampered. Allegations a), b), c), and d) can apply only to the DayStar investments since they were the only ones that were to pay specified returns, were to run for six- or 12-month investment periods, and were real estate-based. Allegation f) clearly applies only to DayStar since it references loan agreements and promissory notes. Allegations h) and i) specifically refer only to DayStar. The only allegations that could apply to both offerings are e) and g).

33. Taking the five alleged misrepresentations first, the evidence failed to establish that two of them were made at all.

ALLEGATION b): It was not established that respondents represented the investment contained no risk since the money invested would be secured by real property. By its terms, this allegation can refer only to the DayStar investment since it was the only one secured by real property.

Complainant presented five investor witnesses. Kathleen Haywood testified that at a DayStar presentation she attended with 40 or 50 others, Parker said the investment contained "no risk." Haywood's mother-in-law, Alvanelle Haywood, attended the same presentation. Although she "felt" the investment had no risk, and would not have invested if anyone had told her there was a risk, she conceded that no one from DayStar said the investment had no risk. Similarly, Betty Jo Thomas testified that she was never told the investment was without risk, although she did not understand there was a risk. Neither Julio Ramirez nor Stanley White testified they were told the DayStar investment had no risk. Parker denied telling potential investors there was no risk, and asserted he told them to seek outside advice before investing. Christopher Pratt, the No. 2 man at DayStar and Stellar from 2002 to 2006, made investor presentations with Parker. Pratt left the companies in February 2007. Although he testified as a witness for complainant and his testimony was clearly at odds with Parker on financial issues, he concurred that no one was ever told the DayStar investment had no risk. In sum, despite the testimony of Kathleen Haywood, it was not shown by a preponderance of the evidence that respondents represented the DayStar investment contained no risk.

ALLEGATION e): It was not established that respondents represented that if members of the church did not invest with DayStar or Stellar they would no longer be members of the church and would not have eternal life. Kathleen Haywood, Alvanelle Haywood and

Betty Jo Thomas all denied being told that they could not be members of the church and would not have eternal life if they did not invest in DayStar. When asked if she had been told this, Thomas laughed as if to signify the question was ridiculous. The only one to testify that these statements were made was Julio Ramirez. He was "absolutely" certain that Hawkins said if you did not get behind the DayStar investment you were not really a member of the church and risked eternal life. Testifying as a witness for respondents, however, Camille Ramirez, Julio's wife at the time of the investments, testified she never heard Hawkins make such a statement. Stanley White provided some marginal support for the allegation, testifying that on several occasions he heard Hawkins say that Stellar and the church were "one," and "If you're not with Stellar, you're not with the General Assembly." But this is a far cry from the allegation that members were told they would not have eternal life and would not be members of the church if they did not invest. It was not shown by a preponderance of the evidence that respondents made these representations.

34. Respondents do not deny that they made the representations set forth in allegations a), c) and d) of Finding 31, above, i.e., that investors would receive a 10 to 20 percent return on their funds every six months to one year; that investors would be free to withdraw all their funds at six-month to one-year intervals and receive both interest and return of principal; and that investors who invested more than \$250,000 would receive as much as a 30 percent³ return on their money. They deny, however, that these were misrepresentations. Parker and Pratt both credibly testified that when they made these representations, they fully intended to pay the promised rates of return. They also credibly testified that during the first couple of years, DayStar's real estate investments did well and they were able to fully pay off all investors who requested return of their principal and interest at the end of a six- or 12-month investment cycle. They do not deny that in subsequent years DayStar was unable to honor all investors' requests for the return of their investments.

35. Turning to the alleged omissions, respondents admit portions of the allegations, deny others, and contend they were not required to provide some of the items listed.

ALLEGATION f): Respondents deny they failed to "emphasize to investors" that the DayStar loan agreement and promissory note allowed for unlimited extensions of repayment dates. They point out that the "Extension of Loan Due Dates" clause of the loan agreement contains this final sentence: "This extension of the due date may be requested up to **UNLIMITED** times on the above terms and conditions." That the word "unlimited" is in bold, underlined, all capitals text, they contend, is proof of their efforts to emphasize the term.

It is true that the word "unlimited" is emphasized to the greatest extent possible in the loan agreement. However, it is also true that many investors did not receive, or even see, this loan agreement until well after they had made their investments. DayStar did

³ Although the allegation referred to 35 percent, there was no evidence anyone was promised more than 30 percent. This small difference, however, in no way changes the essence of the allegation.

not begin using the loan agreement until January 1, 2003. Yet by that time, respondents had already collected \$2.274 million in investment funds, about 13 percent of the total taken during the four years the investment was offered. None of the early investors saw the loan agreement until months after they made their investments. And there was credible testimony from later investors that they did not see or receive the loan agreement until after they had made their investments. Kathleen Haywood made her first DayStar investment in January 2004. She testified she did not receive the loan agreement until four to six months later. Julio Ramirez invested \$250,000 in DayStar on July 7, 2004, and an additional \$100,000 later that month. Yet his loan agreement and \$350,000 promissory note are both dated July 31, 2004. It was not until he received the loan agreement that he learned of the unlimited extensions provision.

36. *ALLEGATION g*): This is one of the two allegations that apply to both the DayStar and the Stellar offerings. There are two aspects to this allegation: that respondents failed to provide accurate accountings to investors, and that they failed to disclose significant losses while claiming the businesses were continuing to be profitable.

As to both offerings, respondents admit that no accountings were provided to investors. Regarding DayStar, Parker testified that counsel Steven Lopez advised that the church members participating in DayStar were "lenders, not investors" and that therefore DayStar was not to provide them any documents beyond the promissory notes and loan agreements he had prepared. Regarding Stellar, Parker testified that the company relied upon the advice of attorney Steven Bangerter as to what information needed to be provided in the private placement memorandum.

Parker disputes that DayStar was operating at a loss, contending that because the company used an accrual method of accounting, the net loss of over \$980,000 reported on the company's 2003 profit and loss statement, for example, may have shown a loss "at that moment" that did not reflect a loss in reality. Nevertheless, in their DayStar presentations to church members, respondents never disclosed the negative financial information set forth above in Finding 15. To the contrary, investors credibly testified that respondents repeatedly described DayStar as profitable and successful. Parker testified he represented the company was successful because that is what he felt at the time.

As to Stellar, the evidence indicates that Stellar had significant losses at the time Stellar shares were offered and sold in 2006 and those losses were not disclosed to investors. Christopher Pratt testified that the negative financial conditions of Stellar were not disclosed in presentations by Parker about the Stellar equity offering.

Stellar's CFO, Jeff Long, prepared a "Financial Recovery Document" on December 21, 2005 outlining financial losses by Stellar and its subsidiaries. By the end of 2005 and throughout 2006, several meetings were held with Stellar executives to discuss Stellar's precarious financial situation.

At the beginning of 2006, executive staff for Stellar took reduced salaries and further agreed to forgo their salaries for six months. Stellar shares were sold to investors from July to December 2006. By December 2006, Pratt testified that they had to “shut everything down.” Michael Parker testified that by the end of 2006, Stellar staff had been significantly reduced.

While a private placement memorandum (PPM), which disclosed “risk factors”, was prepared for the Stellar offering, testimony indicated that the PPM was not provided investors prior to purchasing Stellar shares. Alvanelle Haywood testified that she was not provided documentation about Stellar prior to investing. Betty Jo Thomas also testified that she was never given any paperwork or financial documents regarding Stellar before she invested. Ms. Thomas also testified that she was told that the business was doing well. Both witnesses testified that they invested their money in Stellar because they believed the company was doing well, but would not have invested had they known Stellar’s true financial condition.

Furthermore, while Pratt testified during cross-examination that he had no reason to believe that the PPM or the individual perspective questionnaire were not provided to investors, on re-direct, Pratt clarified that he would not have known whether or not these documents were provided to investors because he was no longer an officer in August 2006 and moved to southern California.

In reviewing the record, the evidence indicates that Stellar had significant losses at the time Stellar shares were offered and sold in 2006 and those losses were not disclosed to investors. Furthermore, investors were not provided the PPM prior to investing to evaluate the risks involved. A review of the record shows that the Department established by a preponderance of the evidence that respondents failed to disclose significant losses while claiming that Stellar was continuing to be profitable. However, the Department failed to show that respondents were obligated to provide prospective investors an accounting with the PPM.

37. *ALLEGATION h*): As set forth above in Finding 36, at no time during the 2002-2006 period that DayStar investments were sold did respondents disclose the negative financial information set forth above in Finding 15. Again, respondents assert that this non-disclosure was based upon the advice of counsel Steven Lopez. They assert they made no effort to hide anything about the operation of the business.

38. *ALLEGATION i*): Respondents dispute all aspects of the allegation that investors were not informed that "a large part of their funds would be paid to subsidiaries of DayStar and in turn this money would be used to pay inflated management fees to Stellar, both of which were controlled by Parker with the substantial assistance from Hawkins."

From the start, the purpose of Stellar was to be a "consultant management company" that would help build businesses for church members. DayStar was created to provide funds for Stellar and its subsidiary companies. (Contrary to the allegation, DayStar had no subsidiaries.) The initial DayStar presentation in March 2003 showed that its goals

included creating new businesses and employment opportunities for church members. The March 2004 presentation showed that DayStar had funded a number of Stellar's subsidiary companies. While the general relationship between the businesses was never withheld from investors, the fact that Stellar was to collect management fees, and the amount of those fees, was not disclosed.

DayStar's profit and loss statements show expenses for management fees of \$366,713.25 in 2003 and \$950,000 in 2004. No management fees are shown in any other years. Stellar's profit and loss statements show income from management fees of \$1,248,495.51 in 2003, \$2,934,000 in 2004, \$69,000 in 2005, and \$5,081,00.20 in 2006. Parker testified, however, that the only management fees DayStar actually paid were \$30,000 in 2002 and \$347,378 in 2003. Again, it was asserted that the companies' use of an accrual method of accounting distorted the reality of the situation.

Complainant asserts, and it is found, that the amount of management fees actually paid by DayStar is irrelevant. What is relevant is that the DayStar/Stellar business plan intended for DayStar, a company controlled by Parker, to pay significant management fees to Stellar, a company also controlled by Parker. That is a fact that should have been disclosed to investors.

MATERIALITY

39. "A fact is material if there is a substantial likelihood that, under all the circumstances, a reasonable investor would consider it important in reaching an investment decision. [Citations omitted.]" (*Insurance Underwriters Clearing House, Inc. v. Natomas Co.* (1986) 184 Cal App. 3d 1520, 1526; *Lynch v. Cook* (1983) 148 Cal.App.3d 1072, 1081-1082.)

The representations and omissions discussed above in Findings 34 through 38 – i.e., that investors would receive a 10 to 20 percent return on their funds every six months to one year (allegation (a)); that investors would be free to withdraw all their funds at six month to one year intervals and receive both interest and return of principal (allegation (b)); that investors who invested more than \$250,000 would receive as much as a 30 percent return on their money (allegation (c)); that the loan agreement permitted unlimited extensions of the loan repayment date (allegation (t)); that DayStar had significant undisclosed losses (allegations (g) and (h)); and that DayStar would use investors' funds to pay significant management fees to Stellar (allegation (i)) – were all material ones. Each of these facts is one that a reasonable investor would consider important in deciding whether or not to invest in the DayStar loan program.

LEGAL CONCLUSIONS

1. In their Notice of Defense and opening and closing arguments, respondents object that the desist and refrain order is so indefinite or uncertain that respondents cannot identify the transaction(s) or prepare a defense. This objection is

overruled. As set forth in Finding 32, while there was some ambiguity in the structure of the order, it was clear from the content and context of each allegation to which offering each applied and respondents' defense to the allegations was not hampered.

2. Respondents assert an “advice of counsel defense” to both the violation of Corporations Code section 25110 (sale of unqualified securities) and some aspects of the violation of Corporations Code section 25401 (sale by misrepresentation or omission), e.g., failure to provide an accounting, failure to disclose financial information.

Mistake of law based upon the advice of counsel is not a defense to violations that do not require specific intent. (*People v. Vineberg* (1981) 125 Cal.App.3d 127, 137.)

In a case involving a criminal prosecution for violation of Corporations Code section 25401, the Supreme Court in *People v. Simon* (1995) 9 Cal.4th 493, explained that the Corporate Securities Law of 1968 creates three levels of enforcement for violations of the act: civil (sections 25500-25510), administrative (sections 25530-25536) and criminal (sections 25540-25404). While section 25540 makes it a crime to “willfully” violate a provision of the Act, willfulness need not be shown to establish an administrative violation. The court stated, at pages 515-516:

An enforcement action by the commissioner to enjoin future sales by means of false or misleading statements is designed to protect the public. [Citations.] For that reason, it is irrelevant that the defendant knows that the statements or omissions are false or misleading. In light of the language of section 25401, it is reasonable to conclude that the Legislature did not intend to permit members of the public to be harmed by such sales simply because the offeror was unaware that his or her sales pitch was misleading. The relatively small civil penalty authorized implies that administrative enforcement of section 25401 was permissible regardless of whether a violation or threatened violation of that section was a knowing violation.

In a case involving a criminal prosecution for violation of Corporations Code section 25401, the Supreme Court in *People v. Salas* (2006) 37 Cal.4th 967, 972, analyzed *Simon* and held, “the same principles should apply whether a defendant is charged with selling an unregistered security, as occurred here, or with making misleading statements or omissions in selling a security, as in *Simon*.” (*Id.* at p. 978.)

Because proof of a specific intent to violate Corporation Code sections 25110 and 25401 is not required in an administrative enforcement action, neither lack of knowledge nor reliance upon advice of counsel is a valid defense.

3. Respondents contend that the representations they made to investors were all made in good faith, with no intent to defraud. Complainant asserts that respondents' intent is irrelevant. The recent case of *People v. Butler* (December 21, 2012, G043100) 212 Cal.App.4th 404 [2012 Cal.App. LEXIS 1301], supports complainant's position. That case involved a criminal prosecution for violation of Corporations Code section 25401. Butler offered promissory notes to investors paying 12 percent interest without disclosing, among other things, the financial situation or viability of the business plan of the issuer of the notes. The prosecution's theory in that case was that it was irrelevant whether or not Butler believed his business venture would succeed. "Rather, the theory of the prosecution's case was [Butler's] promises to pay his investors were *misleading* in light of material omissions by [Butler] pertaining to the likelihood of repayment. Butler's subjective belief about whether he could repay his investors was irrelevant under the prosecution's theory." (Emphasis in original.) Accepting the prosecution's theory, the court held that Butler's "promises to repay principal and interest on promissory notes were misleading in the absence of disclosures about the nature of his business enterprises..." And, the court held, even if there had been insufficient evidence that Butler's promises of repayment were "false," the fact remained that he "did not make sufficient disclosures to the victims to make his statements not misleading."

Here, while in the early years of the DayStar loan program respondents made promises to repay investors interest and principal in good faith with a belief they would be able to keep those promises, continuing to make those promises in later years without disclosing the financial difficulties DayStar was undergoing made those continuing promises misleading. This failure to disclose DayStar's financial difficulties and its ongoing poor performance are at the core of the violation of Corporations Code section 25401.

4. Respondents assert that the allegation that they made a material omission by "fail[ing] to emphasize" to investors the possibility of unlimited extensions of the loan repayment dates fails as a matter of law because the law does not recognize a claim for failure to emphasize something. But this assertion overlooks the fact, as set forth in Finding 35, that while the loan agreement did emphasize the possibility of unlimited extensions, many investors did not receive that agreement until well after they had made their investment. To those investors, there was a complete nondisclosure of the term. This is an actionable omission.

5. Respondents assert that the promises that investors would receive specified interest rates on their investments and would have the ability to withdraw all funds at six-month or one-year intervals are forward looking statements of intent that cannot constitute violations of Corporations Code section 25401 unless respondents knew they would be unable to perform. The holding in *Butler, supra*, 212 Cal.App.4th 404 [2012 Cal.App. LEXIS 1301], as set forth in Legal Conclusion 3, defeats this assertion.

6. Respondents assert that they had no statutory or contractual obligation to provide an accounting to investors or to disclose losses to them, and that these allegations therefore fail as a matter of law. While the asserted lack of obligation may have been true as to the initial investors, *Butler* makes clear that at least in the later years of the DayStar program respondents had an obligation to inform potential investors of the company's precarious financial situation. As to Stellar, however, as set forth in Finding 36, it was not

established respondents were obligated to provide an accounting with the private placement memorandum.

7. The Security and Exchange Commission's decision not to pursue an enforcement action after investigating the DayStar loan program is not dispositive of the issues involved here, i.e., whether respondents violated provisions of the Corporate Securities Law of 1968.

8. As to the DayStar loan program, respondents violated Corporations Code section 25110 as set forth in Findings 27 through 29 and Corporations Code section 25401 as set forth in Findings 34 through 39.

9. As to the Stellar equity offering, respondents violated Corporations Code section 25110 as set forth in Findings 27 through 29 and Corporations Code Section 25401 as set forth in Findings 36.

10. By reason of the matters set forth in Legal Conclusions 8 and 9, cause for issuance of the desist and refrain order exists pursuant to Corporations Code section 25532.

ORDER

The desist and refrain order issued to respondents Michael E. Parker, Stellar Enterprise Associates, Inc., and DayStar Investments, Inc., is sustained.

This Decision shall become effective on October 11, 2013.

IT IS SO ORDERED.

DATED: September 11, 2013

/s/

JAN LYNN OWEN
Commissioner of Business Oversight
California Department of Business Oversight