

BEFORE THE
DEPARTMENT OF CORPORATIONS
STATE OF CALIFORNIA

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

CHRISTOPHER P. EPSHA,
STEVEN G. THOMPSON, and
INVESTCO MANAGEMENT &
DEVELOPMENT LLC,

Respondents.

Case No. 8171

OAH No.: 2009061109

DECISION

The attached Proposed Decision of the Administrative Law Judge of the Office of Administrative Hearings, dated March 8, 2010, is hereby adopted by the Department of Corporations as its Decision in the above-entitled matter.

This Decision shall become effective on April 7, 2010.

IT IS SO ORDERED this 6th day of April 2010.

CALIFORNIA CORPORATIONS COMMISSIONER

Preston DuFauchard

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PROPOSED DECISION

Administrative Law Judge Nancy L. Rasmussen, Office of Administrative Hearings, State of California, heard this matter on September 29 and 30, and November 4, 2009, in Oakland, California.

Corporations Counsel Edward Kelly Shinnick represented California Corporations Commissioner Preston DuFauchard.

Ronald S. Galasi, Attorney at Law, represented respondents Christopher P. Epsha, Steven G. Thompson, and Investco Management & Development LLC. Respondents Epsha and Thompson were present.

The record was closed and the matter was submitted for decision on November 4, 2009. Following the administrative law judge's request for additional evidence, the record was reopened on January 7, 2010, to receive a stipulation by the parties that the Brentwood Corn Fest was held on July 13, 14 and 15, 2007. The record was then closed and the matter was resubmitted for decision on January 7, 2010.

FACTUAL FINDINGS

Desist and Refrain Order

1. On February 18, 2009, California Corporations Commissioner Preston DuFauchard issued a Desist and Refrain Order to respondents Christopher P. Epsha, Steven G. Thompson, and Investco Management & Development LLC (IM&D). This order stated, in relevant part:

. . . [T]he California Corporations Commissioner is of the opinion that the investments offered and sold by Christopher Epsha, Steven Thompson, and IM&D constitute securities, which are subject to qualification under the California Corporate Securities Law of 1968, and that these securities have been and are being offered and sold, without an exemption, and without being qualified in violation of Corporations Code section 25110.

Pursuant to Corporations Code section 25532, Christopher P. Epsha, Steven G. Thompson, and Investco Management & Development LLC, are hereby ordered to desist and refrain from the further offer or sale of securities in the State of California, including but not limited to interests in a limited liability company, unless and until qualification has been made under the law or unless exempt.

. . . [T]he California Corporations Commissioner is of the further opinion that securities were offered and sold by means of written or oral communications that failed to disclose material facts in violation of 25401 of the Corporations Code.

Pursuant to Corporations Code section 25532, Christopher P. Epsha, Steven G. Thompson, and Investco Management & Development LLC, are hereby ordered to desist and refrain from offering or selling or buying or offering to buy securities in this state, including but not limited to interests in a limited liability company, 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 light of the circumstances under which they are made, not misleading.

2. Respondents filed a timely request for hearing on the Desist and Refrain Order and waived their right to have the hearing commence within 15 business days.

Relevant Law

3. Under Corporations Code section 25110, it is unlawful to “offer or sell” any security unless the sale has been qualified or unless the security or transaction is exempt from qualification.¹ Corporations Code section 25102, subdivision (f), provides, in relevant part, that the following transactions (known as “limited offerings”) are exempt from

¹ “Offer” is broadly defined and includes every attempt to dispose of a security. (Corp. Code, § 25017, subd. (b).)

qualification:

Any offer or sale of any security in a transaction . . . that meets each of the following criteria:

(1) Sales of the security are not made to more than 35 persons, including persons not in this state.

(2) *All purchasers either have a preexisting personal or business relationship with the offeror or any of its partners, officers, directors or controlling persons, or managers (as appointed or elected by the members) if the offeror is a limited liability company, or by reason of their business or financial experience or the business or financial experience of their professional advisers who are unaffiliated with and who are not compensated by the issuer or any affiliate or selling agent of the issuer, directly or indirectly, could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction.*

(3) Each purchaser represents that the purchaser is purchasing for the purchaser's own account (or a trust account if the purchaser is a trustee) and not with a view to or for sale in connection with any distribution of the security.

(4) *The offer and sale of the security is not accomplished by the publication of any advertisement. . . .*

[Emphasis added.]

California Code of Regulations, title 10, section 260.102.12, provides further guidance regarding the limited offering exemption. Subdivision (j) addresses what is meant by publication of advertising, as follows:

Section 25102(f)(4) of the Code is to be interpreted so as to facilitate the circulation of disclosure materials to offerees and purchasers, so long as such materials are not disseminated to the public (see Sections 25002 and 25014 of the Code). *Private placement memoranda, offering circulars and similar disclosure documents are not "disseminated to the public" for the purposes of Section 25102(f) of the Code if the issuer limits such circulation*

(1) to persons reasonably believed to be interested in purchasing the securities or

(2) *to persons whom the issuer believes may meet the qualifications required of purchasers pursuant to such section and the rules thereunder, provided with respect to clause (1) and clause (2) that neither the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general solicitation or general advertising, including, but not limited to,*

the following:

- (A) Any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio; and
 - (B) Any seminar or meeting whose attendees have been invited by any general solicitation or general advertising. . . .
- [Emphasis added.]

Subdivision (d)(1) of California Code of Regulations, title 10, section 260.102.12, addresses what is meant by preexisting personal or business relationship. That provision states, in relevant part:

The term “preexisting personal or business relationship” includes *any relationship consisting of personal or business contacts of a nature and duration 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 such relationship exists.* . . . [Emphasis added.]

4. The limited offering exemption under Corporations Code section 25102, subdivision (f), parallels the exemption from registration under the federal Securities Act of 1933 (15 U.S.C. § 77a et seq.). Section 18(b)(4)(D)² of the act, as it relates to section 4(2),³ exempts “transactions by an issuer not involving any public offering.” An issuer claims this limited offering exemption by filing a Form D with the United States Securities and Exchange Commission. (17 C.F.R. § 239.503.)

The Securities and Exchange Commission has adopted regulations, commonly referred to as Regulation D, that govern this exemption. (17 C.F.R. §§ 230.501-230.506.) Regulation D establishes the terms and conditions under which exempt offerings can be made. These include the following prohibition against “general solicitation”:

. . . [N]either the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general solicitation or general advertising, including, but not limited to, the following:
[¶] . . . [¶] (2) Any seminar or meeting whose attendees have been invited by any general solicitation or general advertising.
. . . (17 C.F.R. § 230.502(c).)

Under Regulation D, a purchaser must be either an “accredited investor” or a person who

² 15 U.S.C. § 77r(b)(4)(D).

³ 15 U.S.C. § 77d(2).

“either alone or with his purchaser representative(s) has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment, or the issuer reasonably believes immediately prior to making any sale that such purchaser comes within this description.” (17 C.F.R. §§ 230.506(b)(2)(ii).) To be an “accredited investor,” an individual must have a net worth that exceeds \$1,000,000, or an income over \$200,000 (or joint income with spouse over \$300,000) in each of the last two years and a reasonable expectation of reaching the same income level in the current year. (17 C.F.R. § 230.501(a)(5) & (a)(6).)

Securities offered under the federal limited offering exemption are not subject to the qualification requirement of Corporations Code section 25110. Corporations Code section 25102.1, subdivision (d), states that the following transactions are not subject to Corporations Code section 25110:

Any offer or sale of a security with respect to a transaction that is exempt from registration under the Securities Act of 1933 pursuant to Section 18(b)(4)(D) of that act, if all of the following requirements are met:

- (1) A notice in the form of a copy of the completed Form D . . . is filed with the commissioner
- (2) A consent to service of process . . . is filed
- (3) Payment of the notice filing fee . . . is made.

5. Corporations Code section 25401 makes it unlawful to offer or sell a security “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.”

6. Corporations Code section 25532 provides, in relevant part:

(a) If, in the opinion of the commissioner, (1) the sale of a security is subject to qualification under this law and it is being or has been offered or sold without first being qualified, the commissioner may order the issuer or offeror of the security to desist and refrain from the further offer or sale of the security until qualification has been made under this law

(b) [Omitted.]

(c) If, in the opinion of the commissioner, a person has violated or is violating Section 25401, the commissioner may order that person to desist and refrain from the violation.

Investco Management & Development LLC

7. Investco Management & Development LLC (IM&D) was formed as a

California limited liability company on February 17, 2006. IM&D was founded by Christopher P. Epsha, an attorney and licensed real estate broker, Steven G. Thompson, a licensed real estate broker, and Douglas R. Hanson. Epsha and Thompson are the managing members of the company. On April 1, 2007, Barry D. LeBendig came to work at IM&D. LeBendig has been Director of Sales since May 2007.

8. Beginning in June 2006, Christopher Epsha formed a series of California limited liability companies, with IM&D a managing member of each, starting with Investco AV7 LLC and numbered consecutively up through Investco AV22 LLC.⁴ IM&D offered and sold securities in the form of interests in several of these limited liability companies, including Investco AV12 LLC (Investco 12).

Similar to representations made to prospective members of the other companies, IM&D represented to prospective Investco 12 members that their investment funds would be used by IM&D to acquire vacant land suitable for residential development in the Antelope Valley (a rural part of Los Angeles County), to manage the property for approximately four years in anticipation of appreciation due to projected population growth, and then to sell the property either “as is” or with entitlements for development or improvements. IM&D disclosed that the compensation it would receive for its management responsibilities in Investco 12 would include a commission at the time the property was purchased, a commission at the time the property was eventually sold, management fees over a four-year period, and a 10 percent to 20 percent share of the profits upon the sale of the property depending on whether entitlements for development had been obtained or improvements made.

9. In connection with the offers and sales of interests in the Investco limited liability companies, IM&D did not disclose the following facts:

- A. For each Investco LLC, IM&D had formed and were managers of a corresponding consecutively numbered Landco LLC, specifically Landco AV7 LLC through Landco AV22 LLC.
- B. Except for real property purchased directly by Investco AV10 LLC and Investco AV11 LLC, for each real property purchased by an Investco LLC, a Landco LLC had first purchased the same property from one to nine months earlier at a substantially lower price.

10. Regarding Investco 12, investors were not told that the real property purchased from Landco AV12 LLC (Landco 12) for \$375,000, with an escrow closing date of September 17, 2007, had been purchased by Landco 12 for \$207,850 one month earlier, with an escrow closing date of August 14, 2007. (The previous owner’s asking price was

⁴ The number 13 was skipped in the consecutive numbering of company names, i.e., there is no Investco AV13 LLC.

\$275,000.) Investors also were not told that IM&D was to receive 81.9 percent of the net profit from the sale of the real property by Landco 12 to Investco 12 and a total of approximately \$150,000 in profit, commissions, management fees and expenses from the transaction.

11. The Landco LLC investors are a small group of accredited investors whom Steven Thompson knew before IM&D was started. These investors are willing to invest substantial sums of money on short notice, for which they receive a 36 percent annual return. Teresa Baltao was the sole investor in Landco 12, investing \$232,000 to cover the \$207,850 purchase price for the property plus acquisition expenses, which included \$11,511 paid to IM&D for “Property Analysis and LLC Organization.” At the same time IM&D was negotiating with the seller to buy the property for Landco 12, it was calculating what price Investco 12 would pay Landco 12 for the property. So when Landco 12 bought the property for \$207,850 (the seller signed the grant deed to Landco 12 on July 9, 2007), IM&D knew Landco 12 would sell the property to Investco 12 for \$375,000 as soon as Investco 12 had taken in enough investor funds to pay that price. In his testimony at the hearing, Steven Thompson explained that it would not work for an Investco LLC to purchase property directly from the original owner because of the lack of certainty regarding the price and whether the sale would go through.

Thompson asserted that the investors all knew there was an “acquisition arm” of IM&D, and some knew it was called Landco because he mentioned the name in conversations with them. The Private Placement Memorandum for Investco 12 does state:

Sponsor [IM&D] has formed other investment and sales entities that are created and or operated for the on-going acquisition and sales of investment properties. This is to ensure that an inventory of suitable properties is available prior to any offering’s presentation to a prospective investor in any of the Sponsor’s projects. Such consistent acquisition activities enable the Sponsor to act quickly to obtain properties at favorable market value so that the costs and property location benefits can be made available to the Sponsor’s clients. . . .

Thompson testified that since IM&D got better legal counsel, they now mention Landco in the Investco documents. What the documents state about Landco was not established.

12. Thompson testified that if IM&D disclosed the full information on the Landco property acquisition, including that the investor makes a 36 percent return on a very short-term investment, potential Investco members would want to invest in Landco rather than Investco. Thompson claimed the price Investco pays Landco for the property is always well below what someone would pay if they were buying the property on their own, and there is always an “excellent upside,” meaning that Investco should make money when the property

is eventually sold.⁵ IM&D is very good at buying property in the Antelope Valley, utilizing a computer program to analyze data from MLS (Multiple Listing Service) for comparable properties and working with real estate agents to find the best deals. Thompson asserted that when making land purchases for Landco, IM&D often pays 50 percent less than the asking price.

13. The securities which IM&D offered and sold in the form of interests in the Investco limited liability companies were not qualified by the Department of Corporations.

On October 9, 2007, Christopher Epsha filed with the department a Notice of Transaction Pursuant to Corporations Code Section 25102(f) (LOEN, short for “Limited Offering Exemption Notice”) for Investco 12.⁶ The LOEN stated that the securities being offered or sold in the transaction were interests in a limited liability company, the first sale had been made on July 16, 2007, and the value of the transaction was \$870,000.⁷

On November 12, 2007, a LOEN was filed for Investco AV7 LLC. On September 22, 2009, a LOEN was filed for Investco AV19 LLC, for Investco AV20 LLC, and for Investco AV21 LLC.

On July 11, 2008, a completed Form D for Investco 12 was filed with the department. In this Securities and Exchange Commission form, signed by Doug Hansen on June 20, 2008, Investco 12 claimed the limited offering exemption from federal securities registration under Regulation D, Rule 506 (17 C.F.R. § 230.506). The form stated that Investco 12’s offering of \$870,000 was fully subscribed, with eight accredited investors having invested a total of \$510,000 and 10 non-accredited investors having invested a total of \$360,000.

On July 11 or 22, 2008, similar completed Form D’s were filed with the department for Investco AV7 LLC, Investco AV8 LLC, Investco AV9 LLC, Investco AV10 LLC, Investco AV11 LLC, Investco AV14 LLC, Investco AV15 LLC, Investco AV16 LLC, Investco AV18 LLC, Landco AV17 LLC and Landco AV18 LLC.

14. The main way IM&D finds potential investors is by operating booths at different festivals, fairs and trade shows. Signs at the booths focus on the message

⁵ The property pro forma estimates for Investco 12 projected that the property could be sold “as is” for \$1,413,380.

⁶ On September 27, 2007, Corporations Counsel Edward Kelly Shinnick sent a letter to Epsha questioning the activities of IM&D and requesting that (among other things) he file the required LOEN for each company for which he was claiming exemption from qualification under Corporations Code section 25102, subdivision (f).

⁷ Accounting for the difference between the \$375,000 purchase price of the property and the offering amount of \$870,000 were estimated sales and marketing costs of \$110,500, management fees of \$180,000, engineering fees of \$150,000, and assorted other expenses and costs.

“Roll-Over your IRA/401k into Real Estate.” One of the IM&D flyers handed out at the booth starts out: “Your Retirement, Is it Safe/Secure? / (Have you planned for a secure future?) / Take Control of your retirement. . . Do what Millionaires do! / Roll-Over Your IRA, SEP, Roth, 401k, etc.” This flyer mentions “Prime California Real Estate (in the DIRECT PATH of Growth & Progress)” and states, in part:

The IRS has allowed you to put your retirement savings into real estate since Individual Retirement Accounts were created by law over 30 years ago. . . . [¶] . . . [¶] You will discover that many investors such as yourself are seeking alternatives to the volatile and low-yielding equities and bond markets. Use a self-directed IRA to invest in pre-developed raw land, rental income properties, industrial and commercial properties, as well as private entities that invest in real estate and many other alternatives. [¶] Diversify, Roll-Over to a self-directed IRA with Real Estate and take control of your future!

IM&D has agents and “finders” who staff the booths. In their training, they are instructed not to discuss specific investment opportunities, the location of the property, investment amounts or returns on investments. Also, they are not to say the word “offering” at a show. Steven Thompson and Barry LeBendig both testified that agents and finders are extensively trained in what the law allows and does not allow in a public forum. IM&D has developed a script that agents and finders have to learn and are supposed to follow when talking with members of the public who come to the booth. (IM&D also has a flyer which is almost the same as the script.) This script, which is designed to educate people about rolling over IRA funds into real estate and to generate leads for a follow-up visit by an agent, goes as follows:

Lost money in your IRA/401k or other investments? Rollover to Real Estate! Take Control of **your future!** **STOP** being a deer in the headlights!

Were you **aware** under **current federal law** you are **now** allowed to have alternative investments **inside** your **existing** IRA, 401-K or other type investment or retirement account.

The majority of the public does not know about it. That’s why **KGO Radio** talks about it, **the Chronicle Examiner, New York Times & Fortune Magazine (your local paper)** all recently are writing **full page articles**, to inform the public... There may be a better way.

Do you currently have these types of accounts? Which ones? (IRA, 401k...)

Do you understand what a **rollover** is? Your money is at **Bank A** earning 5 % and you see a sign on **Bank B** across the street offering 7%, by law, you are allowed to rollover your account from A to B, B to C, etc., to receive the higher interest rate, and you would certainly like to know more about Bank B, right? GREAT, *then you will understand exactly what we do.*

We perform a **simple rollover procedure** on your behalf. We rollover part or all of your existing funds, *you will determine what percentage or dollar amount that is after you review the current opportunities...* out of your existing account into a ***Pensco Trust Co. or Charles Schwab and Co. account... you pick your custodian or bank of choice.***

Then we **re-direct those funds** on your behalf to acquire **prime California** real estate, etc; You will choose the vehicle of your preference (**now please don't misunderstand... 99%** of the real estate in California today... **We won't touch with a 10 ft. pole...** but **that very special 1%**, that perfectly positioned property, we buy in **BULK** with **CASH, WAY BELOW CURRENT MARKET VALUE.**) Either the **Grant Deed with Title Insurance**, if it's Real Estate or perhaps a **UCC 1 certificate**, were it a different entity, acts as your vehicle of security.

Now the timeline starts, over the next 18 months to 48 months, (the timeline varies depending on which opportunity you choose to work with) we apply very **specific procedures to that entity** which can add **immense value** to it **on your behalf**. During those 18 months to 48 months when these specific value added procedures are accomplished, we then sell it. **ALL the profit** goes right **back into your account** as a NON-TAXABLE event...**zero capital gains/** tax deferred, if you're using Tax Qualified funds, or subject to capital gains if you are not. **Over the past 30+ years, Alternatives, such as these** have performed very well.

NOW do you see why KGO, Fortune, NY Times (local) & SF Chron/Examiner are all trying to make the public more aware of this? [Emphasis and ellipses in original.]

People who are interested in learning more about what IM&D has to offer are asked to fill out a lead sheet, titled "Retirement Planning Information," giving their name and contact information. The form has boxes for the person to check indicating whether their

current retirement plan includes stocks, mutual funds, real estate, a savings account, 401(k), IRA, SEP IRA, Roth IRA or defined benefit plan. The agent or finder is supposed to find out the best time for a one to two hour meeting, and with respect to the checked items under retirement plan to ask: “Ball park what kind of figures are we looking at here... above or below six figures?”

15. Thompson and LeBendig explained the procedure to be followed once a lead sheet is filled out. Information from the sheet is put into the computer for tracking, and a few days after the show an agent calls the person. The agent may have several telephone conversations with the person before meeting them at their home. In these conversations, the agent is answering questions, getting to know the person, finding out whether they have funds to invest, starting to ascertain whether they are an accredited or a qualified investor,⁸ and scheduling the meeting. The first meeting at the potential investor’s home usually lasts about three hours. Most of the time is spent discussing the concept of what IM&D does and who the principals are, and getting to know the person and finding out about their employment and investments. Before showing the person any documents pertaining to the Investco offering, the agent must know that the person has the net worth or income to be an accredited investor or have a strong conviction that the person meets the criteria for a qualified investor. The agent is supposed to place a call to Thompson and introduce the potential investor to him. Thompson talks to the person on the phone so he can determine whether the person is an accredited or qualified investor. For an accredited or qualified investor, the agent presents the Investco LLC Investment Property Overview book during the last half-hour of the meeting. This spiral-bound book contains an overview of the property and the investment structure, the “Pre-Developed Land Investment Overview,” “Antelope Valley Economic Data and Industrial Overview,” property pro forma estimates, data on the property and comparable properties, a Subscription Agreement, and a Suitability Questionnaire. No documents are to be filled out at this meeting, however, since it is too early in the process. The potential investor is asked to review the materials and think about whether they want to go forward with an investment. The person is given Thompson’s business card.

If the person wants to go forward with an investment, a second meeting is held at their home, generally 10 to 15 days after the first meeting. At this meeting, the agent has the Investment Documents book, which contains the same documents that are in the Investment Property Overview book plus an Operating Agreement, Management Agreement and Private

⁸ The Investco 12 Suitability Questionnaire sets forth these criteria for a qualified investor:

An investor who is not an Accredited Investor can still be a suitable investor if the person, together or with a professional advisor who is independent of the Sponsors, has the financial sophistication to understand the risks and merits of the investment, and who has sufficient assets to bear the risk of the capital to be invested, should unforeseen problems materialize.

Placement Memorandum. The agent answers questions and goes over the paperwork, with the investor filling out and signing the Subscription Agreement and the Suitability Questionnaire, and signing the Operating Agreement, the Management Agreement and the property pro forma estimates. The investor also completes a Charles Schwab account application and account transfer document. The agent leaves a copy of the book and the Schwab documents with the investor. The completed investment documents are delivered to Thompson. After that, Christopher Epsha calls the investor and assists in getting the funds transferred to the Investco LLC.

Investor Juan Rodriguez

16. Juan Rodriguez is an investor in Investco 12. He learned about IM&D at the Brentwood Corn Fest, which was held on July 13, 14 and 15, 2007. At that time, he was about 55 years old and earning \$70,000 to \$75,000 a year as a loss control consultant for an insurance company. Rodriguez had worked in that field since 1980, after he graduated from college with a degree in photojournalism. He and his wife had purchased a home in Brentwood in 2005 after selling the San Jose home they owned for 21 years. Rodriguez estimated that he had \$120,000 to \$130,000 in home equity, which was carried over from the proceeds of the sale of his San Jose house. He had no savings except for a self-directed IRA or 401(k) account. This account had a value of about \$140,000, comprised roughly of one-half in mutual funds, one-quarter in a money market deposit account, and one-quarter in stocks. Rodriguez has no formal training or education in finance or investing, but prior to July 2007 he had done maybe 20 to 25 stock trades for his self-directed IRA. These transactions were usually for \$5,000 to \$10,000. Rodriguez felt he had "borderline enough knowledge" to make these trades and thinks he had made money after 20 trades. A couple of years earlier, however, his CPA had looked over Rodriguez's Ameritrade statements for his IRA and told him he did not think he was doing a very good job. Rodriguez's trading style was "a little on the risky side."

Rodriguez thinks he was at the Corn Fest on a Saturday, which would have been July 14, 2007. He recalls approaching a booth with a Prudential Real Estate sign and being handed an IM&D flyer that talked about real estate investments for an IRA. This caught Rodriguez's interest because he and his wife had casually discussed investing in real estate, and Rodriguez thought real estate was still appreciating in value. At the booth, Rodriguez met IM&D agent Jeff McThorn and they talked for about 20 minutes. During their conversation McThorn mentioned that IM&D was in the process of putting together a group of investors for property in Southern California. He said it was a good opportunity and would be profitable. He explained that a person's share of the title would be based on the amount of the investment, and that the property would be held for a period of time before it was sold. McThorn described a previous project that had been profitable. Rodriguez left his name and phone number with McThorn. (He does not recall filling out a form.)

Sometime in the next three days McThorn called Rodriguez and scheduled a meeting at Rodriguez's home on Tuesday, July 17, 2007. (There was no substantive discussion

during the phone call.) The July 17 meeting was the only time McThorn met with Rodriguez in his home, and he presented all the Investco 12 investment documents to him. Rodriguez decided to invest \$35,000 in Investco 12. McThorn went over parts of the documents with him and helped him fill out the Suitability Questionnaire. Rodriguez checked “Yes” to indicate he met the criteria for a qualified investor. The next item on the questionnaire stated: “By reason of my personal business or financial experience (as described below) . . . I believe that I am capable of evaluating the merits and risks of this investment and of protecting my own interests in connection with this investment.” In the space for describing his experience, Rodriguez wrote: “Handle and manage my own self-directed IRA and make all investment decisions.” The last two items on the Suitability Questionnaire were:

8. I have not seen or received any advertisement or general solicitation with respect to the sale of these interests.
Correct_____
 9. I have a preexisting personal or business relationship with one or more of the Sponsors, more fully described as follows:_____
- (Describe relationship; if “none,” so state.)

Rodriguez initialed the space for item 8 being correct, and he wrote in item 9: “Introduced at Brentwood Corn Fest booth.” Rodriguez signed the Suitability Questionnaire and the Subscription Agreement on July 17.⁹ By signing the Subscription Agreement, Rodriguez acknowledged that he had received and reviewed the Private Placement Memorandum. McThorn explained how to have Ameritrade transfer funds to a Charles Schwab account, and Rodriguez apparently filled out the necessary documents.

On July 25, 2007, Rodriguez experienced “buyer’s remorse” and sent a fax to Ameritrade, with a copy to IM&D, canceling his request to transfer funds to a Schwab account and Investco 12. Rodriguez testified that he phoned Christopher Epsha to tell him that he had begun to cancel his investment in Investco 12, and his discussion with Epsha reassured him and caused him to go ahead with the investment after all. Steven Thompson testified that he called Rodriguez, and Rodriguez told him he was having second thoughts about the investment. According to Thompson, when Rodriguez asked if he could cancel the deal, Thompson said “certainly.” In any event, Rodriguez appears to have decided to proceed with the investment by Friday, July 27, because on that date he faxed his wife’s and daughter’s social security numbers to Epsha. On Monday, July 30, Epsha faxed Rodriguez a letter referencing their telephone conversation that day and attaching a copy of the Investco 12 property pro forma estimates to sign and return. (Epsha wrote: “The enclosed document is missing from your signed documents.”) On July 30, Rodriguez signed the property pro forma estimates and he sent a fax to Ameritrade instructing them to process the rollover

⁹ Presumably, he also signed the Operating Agreement and the Management Agreement, but these documents are not in evidence.

request from IM&D for Investco 12. Rodriguez's Schwab IRA Rollover account statement indicates that he acquired a \$35,000 interest in Investco 12 on September 4, 2007. Rodriguez remains a member of Investco 12.

At no time did anyone from IM&D tell Rodriguez that the Investco 12 property had previously been purchased (or was in the process of being purchased) by another IM&D affiliate at a substantially lower price. Rodriguez understood that Investco 12 would buy the property on the market at a very good price.

17. Jeff McThorn was an agent for IM&D in 2006 and 2007. In his testimony at the hearing, McThorn claimed he had two meetings with Rodriguez at his home, and that Rodriguez filled out and signed the Investco 12 Suitability Questionnaire and Subscription Agreement during the second visit. McThorn explained that he left the marketing overview book with Rodriguez on the first visit, and gave him the bigger book with the investment documents on the second visit. (This would have been in accordance with the IM&D procedures to which Steven Thompson and Barry LeBendig testified.) McThorn claimed that during his second meeting he called Thompson and put Rodriguez on the phone with him; after they talked for 10 to 15 minutes, McThorn talked to Thompson and was told that everything looked okay, i.e., Thompson believed Rodriguez was a qualified investor. Regarding the timing of the meetings, McThorn asserted that a day or two after meeting Rodriguez at the Corn Fest, he called Rodriguez to schedule the first meeting, and the second meeting was held a few days after the first. Thompson, in his testimony, alluded to there being two meetings between McThorn and Rodriguez, but contradicted McThorn about which meeting it was that he talked to Rodriguez on the phone. Thompson testified that during McThorn's first meeting with Rodriguez, McThorn called him and put Rodriguez on the phone. Thompson recounted that he talked to Rodriguez and determined he was a qualified investor (based on what Rodriguez told him about his self-directed IRA); then he recommended that Rodriguez read the Investco 12 materials and have another conversation before his second meeting with McThorn. Thompson asserted that Rodriguez did have another phone conversation with him before the second meeting.

The testimony about there being two meetings between McThorn and Rodriguez is inconsistent with Rodriguez's testimony that there was only one meeting. At the hearing, the dates of the Brentwood Corn Fest were not established, so there was no point of reference for the length of time between that event and July 17, 2007, the date Rodriguez signed the Suitability Questionnaire and Subscription Agreement. Knowing the dates of the Corn Fest and establishing that Rodriguez met McThorn there on Saturday, July 14, just three days before their Tuesday meeting, makes it clear that there was only one meeting at Rodriguez's home. McThorn's two-meeting scenario would have required more time.

McThorn's lack of credibility regarding how many meetings he had with Rodriguez raises suspicion that he was trying to cover up his non-compliance with IM&D procedures. This, in turn, undermines his credibility regarding other matters to which he testified. For example, although McThorn could not really recall his conversation with Rodriguez at the

Corn Fest, he maintained that at fair booths he never talked about Investco offering investment property in Southern California, or other details regarding Investco products, because that was against the rules. This is not credible, particularly in view of Rodriguez's clear recollection of what McThorn told him at the Corn Fest.

18. McThorn testified that he believed Rodriguez was a qualified investor because he had been making good investment decisions for a self-directed IRA of about \$150,000, his second house was in the nicer area of Brentwood,¹⁰ and he appeared intelligent. Because he asked a lot of questions McThorn could not answer, McThorn was sure Rodriguez had more investment knowledge than he did. After his telephone conversation with Rodriguez, Thompson also believed he was a qualified investor.

Thompson was present when Rodriguez testified about his financial knowledge, experience and circumstances, and he asserted that what he heard was different from the information Rodriguez imparted to him and McThorn in July 2007. Thompson would not necessarily change his opinion that Rodriguez was a qualified investor, however.

Investor Charmaine Furman

19. Charmaine Furman is an investor in Investco 12 who learned about IM&D at the Palo Alto Concours d'Elegance car show on June 24, 2007. Barry LeBendig was staffing the IM&D booth there when Furman approached, and they talked for about 10 minutes. LeBendig told her about being able to roll over IRA and 401(k) funds into real estate investments. Furman recalls him discussing that his company had real estate investments for tax-deferred retirement accounts, and these investments were like a partnership, where more than one person invested in a property. Furman filled out a Retirement Planning Information sheet for a follow-up visit, and when LeBendig asked her if her IRA and 401(k) accounts and other retirement funds were above or below six figures, she indicated that they were above.

LeBendig had two meetings with Furman in her Palo Alto home, the first around July 8, 2007, and the second on July 15, 2007. Before the first meeting, LeBendig had several telephone conversations with Furman, to schedule the meeting, discuss the investment concept, and find out whether Furman was an accredited or qualified investor and whether she had funds to invest. In one of the phone calls, Furman told LeBendig that her net worth was over \$1,000,000. At their first meeting, which lasted three and one-half hours, LeBendig made his standard presentation on IM&D, and he elicited information from Furman relevant to whether she was a qualified investor. Based on her investment history, the questions she asked, her representation of the aggregate value of her accounts, and the fact that the few account statements she was willing to show him had values in the hundreds of thousands of dollars, LeBendig was convinced that Furman was a qualified investor. She indicated she met the criteria for an accredited investor, and she insisted she was a qualified investor. (The parties stipulated that Furman is an accredited and a qualified investor.)

¹⁰ McThorn thought Rodriguez still owned a house in San Jose.

During the meeting, LeBendig got Steven Thompson on the phone to answer a question, and Furman talked to him. LeBendig presented the Investco AV11 LLC Investment Property Overview book during the last part of the meeting. He left this book with Furman and told her he would contact her after she had a chance to review the materials.

LeBendig thinks Furman initiated the call to schedule the second meeting, and indicated she was interested in investing. At that time, LeBendig told her Investco AV11 LLC had sold out but Investco 12 was available. When they met again, LeBendig made a presentation on Investco 12 and went over the Investment Documents book. Furman had decided to invest \$40,000, and she filled out and signed the Subscription Agreement and the Suitability Questionnaire, and signed the Management Agreement.¹¹ On the Suitability Questionnaire, Furman checked “Yes” to indicate she met the criteria for an accredited investor. For item 8, she checked “Correct” after “I have not seen or received any advertisement or general solicitation with respect to the sale of these interests.” For item 9 (“I have a preexisting personal or business relationship with one or more of the Sponsors, more fully described as follows:”), Furman wrote: “I met Barry at the Palo Alto Concours De Elegance.” Furman apparently filled out the documents to roll over her IRA funds into a Charles Schwab account for investment in Investco 12. This rollover was effectuated and Furman remains a member of Investco 12.

At no time did LeBendig or anyone else from IM&D tell Furman that the Investco 12 property had previously been purchased (or was in the process of being purchased) by another IM&D affiliate at a substantially lower price. Furman would have considered that to be material information relevant to her decision whether to invest in Investco 12. LeBendig testified that he had nothing to do with Landco, and when he met with prospective Investco investors he was not necessarily aware that Landco had already purchased the property Investco would buy.

California State Fair – August 2009

20. In late August 2009, Corporations Counsel Lindsay Herrick was at the California State Fair in Sacramento with her family when she saw an IM&D booth. She had no idea that IM&D was the subject of an enforcement action with her department. Herrick walked up to the booth and started to help herself to the written materials that were stacked there. A woman at the booth, Bonnie Phillips, came up and started to talk with Herrick. She gently took the documents from Herrick’s hand, eventually handing them back with her business card stapled to them. A man was sitting at the back of the booth, and a few times he “chimed in” with what Phillips said. As Herrick recalled, the conversation between her and Phillips was something like the following:

¹¹ Presumably, she also signed the Operating Agreement and the property pro forma estimates, but these documents are not in evidence.

Phillips: Are you interested in diversifying your investments with real estate?

Herrick: Oh, in this climate?

Phillips: Well, I know. But that's what we do; we specialize in real estate developments. We have many years of tremendous success.

Herrick: Well, who are you?

Phillips: Well, we are Investco, and as I said we specialize in real estate developments – investments. Let me ask you this. Do you have an IRA?

Herrick: I do.

Phillips: Well, the way it works is you would roll over your IRA into another account, a custodial account, with another company. [Phillips said typically they like to use a company named Pensco Trust.] From there, we would direct your money into one of our developments for an investment.

Herrick: Are the properties in California?

Phillips: Yes, they are. Are you familiar with Antelope Valley?

Herrick: I might be.

Phillips: Well, that's a southeastern mountain range in California. [Phillips said they were developing just east of that.]

Herrick: Well, is there a minimum investment?

Phillips: Well, it really depends on a particular property, but basically each development has between 12 to 15 investors, and there's somebody who purchases the property on behalf of Investco, and you would purchase the property from them. [Phillips said they do that in order to expedite purchases. She said Herrick would get paid as an investor when Investco sells the property to a developer, on average in five years. Phillips told Herrick that, basically, her investment would be relative to the amount of money she invested. She would receive a deed of trust that evidenced her percentage interest in the investment.]

Herrick: Are you developing homes?

Phillips: We do both. We do residential and we do commercial.

Herrick: Well, what's the name of one of your subdivisions?

Phillips: Well, I can't tell you the name of the subdivision.

Herrick: Why?

Phillips: Well, if you sign this piece of paper, one of us can come out to your home and we can tell you what one of the subdivisions is named.

Herrick: Is this offering qualified?

Phillips: Yes.

Herrick: By whom?

Phillips: Well, that's confidential information.

Herrick: Well, no, that's public information.

Phillips: Well, like I said, if you sign this sheet, one of us can come out to your home and we can explain to you what it's qualified under.

Herrick: That doesn't make sense. It's either qualified with, like, the SEC or the state.

Phillips: Well, these are actually private placements.

Herrick: Okay, so, what offering exemption are you offering this under?

Phillips: Well, that's confidential, too.

Herrick: Well, no, that's public, too. I could download, like, your notice filing off the Internet.

Phillips: Well, all I can tell you is if you sign this sheet I can come out to your home. I'll tell you the name of the subdivision and what exemption we're offering this investment under.

Herrick: Okay, thank you.

Phillips did not fill out the paper. She had told Phillips her name, but did not say she was an attorney. (Phillips did not ask Herrick much about herself.) Herrick took the written materials on IM&D and left the booth. Herrick later reported the activities of IM&D at the State Fair to a department attorney doing intake for the complaint team. She was directed to provide her information to Mr. Shinnick, since he was handling the case against IM&D.

21. Pursuant to an investigation request by Mr. Shinnick, Associate Corporations Investigator Chris Lewis was assigned to conduct an undercover investigation of the activities of IM&D at the California State Fair. Lewis went to the fair on August 27, 2009, and he visited two booths operated by IM&D. (On August 31, 2009, he went back to photograph the two booths.) Lewis had decided that his undercover persona would be an engineering tech with CalTrans whose job was to pick up traffic counts on the highways. (He has a family member who retired from that job, and he knew the salary was about \$40,000 to \$50,000 a year.) Lewis decided to say, if asked, that he had about \$26,000 in a 401(k) account from a prior job, he contributed about \$100 a month into CalPERS Savings Plus, and he had bought a house but had no stock trading experience.

The main sign at each IM&D booth stated "ROLL-OVER Your IRA/401k Into REAL ESTATE." Another sign, with IM&D's name and address at the bottom, read as follows:

YOUR NEST EGG

Does it have **Pneumonia** . . . or Just a Bad Cold?

We Live in a Rapidly Changing World

Look for common sense **Alternatives**

Alternative Investments – IRA, ROTH, 401k, etc.

You need to have a "Plan B"

[Emphasis and ellipses in original.]

A sign advertised "Free 3 Minute Seminar / Every Hour on the Hour."

At the first booth, Lewis had a conversation with IM&D finder Yogen Dhanik. Dhanik said Investco was in the business of offering real estate investment opportunities; they purchase bare land and either add improvements or "flip" the land to new owners. He said the company deals only in commercial properties and buys with cash to get the best deals. Dhanik mentioned several properties Investco had recently acquired, a 100-acre ranch

in the Los Angeles area bought for 28 million dollars, a property bought from the Catholic Church for \$160,000 an acre which would have sold for \$500,000 an acre a year ago, and a property bought for \$50,000 that was worth \$1,000,000 a year ago. Dhanik said that Investco was able to buy properties for pennies on the dollar. He implied that the property bought from the Catholic Church was a property investors could invest in with their 401(k) or IRA, so Lewis asked how people like him could invest using an existing IRA. Dhanik explained that Investco has investors open a self-directed IRA with Charles Schwab or Pensco Trust, and then they can invest with Investco. He stated that Investco had an LLC they managed, which purchased the properties, and the investors would be a percentage owner in the LLC depending on the amount they invested. Investco would sell the property in 32 to 48 months, and the profits would go back in the investor's IRA tax-free. Dhanik said that Investco had historically made a profit for their investors of 20 to 30 percent per year on each property, and sometimes they made a lot more. He pointed out that 30 percent per year could mean a 90 percent profit in several years, or nearly doubling the investment. Dhanik gave Lewis several flyers, including the one starting out "Your Retirement, Is it Safe/Secure?" (see Finding 14), and he had Lewis fill out an information card so Dhanik could contact him later. When Lewis asked what the minimum investment amount was, Dhanik replied that he could invest whatever he wanted, and people he had dealt with had invested between \$20,000 and \$1,000,000. At no time in their conversation did Dhanik mention having to be an accredited or a qualified investor, nor did he ask Lewis any questions relevant to whether he was in one of those categories.

Lewis visited the second booth in another building, where he had a conversation with IM&D finder Hattie Garmon. During their conversation, Garmon said that Investco was in the business of purchasing California real estate, like bare land and even residential property, providing improvements to the land in the form of utilities and selling it to developers. She explained that her company purchases land for 50 cents on the dollar, and that is how they make a profit for their investors. Garmon stated: "Investco has never earned less than a 24 percent profit for their investors, and the investment has no risk." She said there was no risk because Investco "dots all of its I's and crosses all of its T's." In response to Garmon's question whether he had a 401(k) or an IRA, Lewis told her he had a 401(k). She asked how much, and he replied that he had a little more than \$25,000. Without asking him any questions relevant to whether he was an accredited or a qualified investor, Garmon said, "We can do something for you." Garmon gave Lewis some flyers and told him that if he filled out an interest card she would call and set an appointment to show him all three current California real estate investments managed by Investco. Garmon said any investment would be for 12 to 48 months and Lewis could nearly double his money as calculated by using the interest rate of return and dividing it by 72 ("the power of 72"). Lewis declined to fill out an information card.

Meetings with Chris Lewis – September 2009

22. On September 8, 2009, after receiving some IM&D flyers in the mail from Yogen Dhanik, Chris Lewis phoned Dhanik and arranged to meet him the following day at a

restaurant in Sacramento. At no point during their telephone conversation did Dhanik attempt to determine Lewis's financial status or investing experience. At the restaurant meeting on September 9, Dhanik was accompanied by Barry LeBendig, who did all the talking. At the beginning of his presentation on Investco, LeBendig mentioned that he thought he was going to be late because of the Bay Bridge closure. When Lewis responded that he did not work for that part of CalTrans, LeBendig asked what he did for CalTrans. Lewis advised that he was an engineering tech whose job was to pick up traffic counts on the highways. LeBendig did not ask Lewis, then or later, how much he earned in his job.

LeBendig explained that there would be four parts to their "information sharing," and they would be going over part one that day. He said the last part would be going over the actual investments Investco offered. LeBendig advised that the company invested in real estate, such as land, residential and commercial, and also technology investments. He said the first part of the presentation was information about the company, and Dhanik would cover parts two through four in the future, when Lewis could bring his wife to a presentation.

LeBendig described Investco as frugal and conservative in its investments and "ruthless" in its quest to purchase property at 10 to 50 cents on the dollar. He discussed how they buy prime property for cash, make improvements, and then sell for a profit. LeBendig said each property Investco purchases is put in a new LLC, and the company has their attorneys and engineers look the property over before preparing an offering for investors. He said Investco usually has only two investment properties or "vehicles" available, but with the current real estate market, the company has four vehicles to offer investors. LeBendig gave a hypothetical example of an investment vehicle to illustrate how an investor's ownership share corresponds to how much money is invested. He said Investco does not make their profit until the vehicle is sold, taking 50 percent of the profit and leaving 50 percent to be split among the investors; an investor would make 20 percent on their investment. LeBendig added that past performance is no indication of future performance.

Engaging Lewis in a hypothetical about selling his own house, LeBendig asked him how much his home was worth. When Lewis said he was not sure if he was "upside down" on the mortgage, LeBendig asked how much he had paid for the house. Lewis replied that he had purchased the house four years ago for \$285,000, to which LeBendig stated the home was now worth \$150,000. LeBendig then asked Lewis about his investment experience. Lewis advised that he had a 401(k) from a previous employer and he contributed \$100 per month to Savings Plus at work. LeBendig asked about the 401(k), and Lewis said he had about \$26,000 in the account. LeBendig then explained how Investco could help roll over that money into a self-directed IRA and Lewis could invest those funds in their vehicle. LeBendig proceeded to explain that only accredited or qualified investors could invest in a private placement memorandum, the vehicle Investco offered. He asked Lewis questions as he went over the criteria for being accredited or qualified, including the requirement of having enough investment experience to weigh the merits of the investment. Lewis advised LeBendig that he, or he and his wife, were not qualified investors based on the questions he had asked. As Lewis recalls, LeBendig glossed over this statement and advised him that

Dhanik would be working with him to go over parts two through four of the presentation. (LeBendig denies that Lewis ever said he and his wife were not qualified investors.)

LeBendig mentioned that the Department of Corporations had issued desist and refrain orders to a number of companies advising them that if they were violating the law in providing actual percentages of return on investment they needed to stop. He said that Investco had not violated the law in offering securities, and they retained a law firm when they received a desist and refrain order. LeBendig explained that he wanted to share this information with Lewis in case he found it out when doing due diligence on Investco.

During the last 15 minutes of the meeting, LeBendig asked Lewis if anyone from Investco had provided him actual percentages of investment returns. Lewis replied that the lady at the fair had told him the company has never provided less than a 24 percent return on investor money. LeBendig appeared to be upset about this, and said it was illegal to provide actual investment returns on a private placement memorandum. When he asked if any other person had provided investment returns, Lewis said he did not think so. (He did not disclose that Dhanik had done so.) LeBendig asked Lewis if anyone had told him where the investment property is located, and Lewis advised that the lady had told him the property was in the Los Angeles area. LeBendig said he was going to have that lady's "head" today. (LeBendig apparently knew who the lady was after he asked if the lady was black or white and Lewis told him she was black.)

When Lewis asked if Investco had a Sacramento office, LeBendig stated they did not, but they have Wednesday night meetings at the Hilton Hotel near Cal Expo where they discuss company business with investors. LeBendig said Lewis should go home and talk his wife into coming to a meeting, and by the end of the fourth meeting they would give him documents for everything they had talked about.

23. After exchanging voice mail messages with Yogen Dhanik, Chris Lewis arranged for another meeting and follow-up presentation at the same restaurant on September 21, 2009. (Lewis told Dhanik his wife would not be coming.) When Lewis arrived at the restaurant, he found that IM&D agent Dareld Phillips was there to make the presentation instead of Dhanik. Phillips explained that he was the Sacramento representative for Investco, and Dhanik was not yet a full agent.

Phillips made a presentation on real estate, describing the growth of San Jose and the factors that make a city successful, and moving on to discuss the Antelope Valley area of Los Angeles County. He showed Lewis maps and pictures of the Palmdale and Lancaster area and explained why that was such a good place to invest in land. Phillips provided Lewis with Investment Property Overview books for Investco AV21 LLC and Investco AV20 LLC, pointing out the pages with information they had already discussed. He did not point out or discuss the Suitability Questionnaire or Subscription Agreement contained in both books, nor did he ask Lewis about his qualifications to invest.

Phillips told Lewis he would invest in Investco himself except that would be considered insider trading. He said he invests in Landco, the company that initially purchases the property for Investco investors. Phillips explained that Landco did not receive its profits until Investco sold the property to builders. He did not mention how much Landco paid for property compared to what it sold the property for to Investco.¹² Phillips told Lewis that the risk factor for Investco investments is zero percent whereas the risk factor for banks is .01 percent, implying that Investco is safer than a bank. Phillips asked Lewis how much money he had to invest, and Lewis said he had \$26,000. Phillips recommended that Lewis invest in Investco AV20 LLC as that had a six to nine month turnaround because the property would be at the tentative map stage in six to eight months. He then said he could not legally tell Lewis this, but there were six to eight contractors already bidding on the property because they know Investco has a “cookie cutter” formula and will get the property to tentative map stage faster than any other company out there. Phillips said both the AV20 and AV21 investments were designed for investors with less than \$200,000 to invest. He added that 12 Investco agents were out selling these two investments, so Lewis should act fast to reserve his investment. After this meeting, Lewis had no further contact with anyone from IM&D. He was at the hearing eight days later to testify as a witness.

24. According to Steve Thompson and Barry LeBendig, Yogen Dhanik and Hattie Garmon have been suspended from working at shows because they did not follow the IM&D script in talking to Chris Lewis. They were to undergo more training before the suspensions would be lifted.

LEGAL CONCLUSIONS

1. The first issue in this case is whether the securities offered and sold by IM&D in the form of interests in the Investco limited liability companies were exempt from qualification, under Corporations Code section 25102, subdivision (f). To be eligible for this exemption, IM&D may not have offered or sold the securities by any form of general solicitation.¹³ All purchasers must either have a preexisting relationship with an IM&D principal or have sufficient business or financial experience that they “could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction.”¹⁴ Offering documents may have been circulated only to persons whom IM&D believed may meet these qualifications for purchasers.¹⁵

¹² There is also no mention in the Investment Property Overview books for Investco AV21 LLC and Investco AV20 LLC of the property being previously purchased by Landco for a lower price.

¹³ Corp. Code, § 25102, subd. (f)(4); Cal. Code Regs., tit. 10, § 260.102.12, subd. (j).

¹⁴ Corp. Code, § 25102, subd. (f)(2).

¹⁵ Corp. Code, § 25102, subd. (f)(4); Cal. Code Regs., tit. 10, § 260.102.12, subd. (j).

Respondents contend that what IM&D is doing at festival booths is simply educating the public about alternative investments for retirement accounts and letting people know they can invest IRA or 401(k) funds in real estate. They deny giving out any specific information about an Investco offering in this public forum, and claim that any agent or finder who did so acted outside the scope of their authority. Respondents maintain that specific information about an Investco offering was given only to potential investors whom IM&D believed were accredited or qualified investors. It is unclear whether respondents are claiming that purchasers, by reason of having met the IM&D agent at the fair or festival, have a preexisting relationship with IM&D, within the meaning of Corporations Code section 25102, subdivision (f)(2).

The IM&D flyers and signs at festival booths, and the script which is supposed to be followed by agents and finders, conveys the general information (directly or by implication) that IM&D offers investment opportunities where money from more than one investor is pooled to acquire prime California real estate which is held for a period of time before being sold for a profit, and that IRA and 401(k) funds can be used for the investment. The booth materials do not give specific information about particular Investco offerings, however. Whether this absence of specifics means that IM&D is not engaging in a form of general solicitation is a theoretical question that need not be addressed, because the reality was shown to be different from the IM&D model. At the 2007 Brentwood Corn Fest, IM&D agent Jeff McThorn gave out more specific information about IM&D's investment opportunities to Juan Rodriguez. At the 2009 California State Fair, IM&D agent/finders Bonnie Phillips, Yogen Dhanik and Hattie Garmon gave out more specific information about IM&D's investment opportunities to Lindsay Herrick and Chris Lewis. By giving out this information to members of the public who have not been screened for their investor qualifications, IM&D was engaging in a form of general solicitation.

In addition to investor Rodriguez being the subject of a general solicitation at the Corn Fest, the evidence established that IM&D had no reason to believe he was a qualified investor before McThorn came to Rodriguez's home and presented the Investco 12 offering documents to him. (McThorn knew nothing about Rodriguez's financial circumstances or experience before coming to his home.) Whether, in fact, Rodriguez was a qualified investor seems highly doubtful. He had no business experience, and his financial experience was limited to making small trades for a self-directed IRA with about \$35,000 in stocks (one-quarter of the total value of the account). He did not have sufficient income or assets to bear the risk of losing his investment capital. It would not seem reasonable to assume Rodriguez's limited financial experience gave him the capacity to protect his own interests in connection with the Investco 12 transaction, notwithstanding his representation in the Suitability Questionnaire that he met the criteria for a qualified investor. In any event, IM&D should have screened Rodriguez for his investment qualifications before coming to his home with the investment documents.

The evidence also established that IM&D agent Dareld Phillips presented specific investment documents to Chris Lewis when IM&D had no reason to believe he was a

qualified investor. What Lewis communicated to Barry LeBendig and Yogen Dhanik was that he worked for CalTrans as an engineering tech, he was not sure if he was “upside down” on his home mortgage, he had about \$26,000 in a 401(k) account, and he contributed \$100 a month to Savings Plus. And after LeBendig went over the criteria for accredited and qualified investors, Lewis told him that he, or he and his wife, were not qualified investors.

Although the evidence established that Barry LeBendig followed IM&D procedures in his dealings with investor Charmaine Furman (giving her specific information about investment opportunities only after he reasonably believed she was an accredited and/or qualified investor), the temptation to deviate from those procedures has clearly proved irresistible for other IM&D agents and finders. This is probably inevitable, given human nature and the motivation to sell the investment products.

The acquaintance Furman had with LeBendig and Rodriguez had with McThorn before they purchased their interests in Investco 12 was not a preexisting personal or business relationship within the meaning of Corporations Code section 25102, subdivision (f)(2). Aside from the fact that McThorn was not a partner, officer, director, controlling person or manager of IM&D, neither he nor LeBendig had personal or business contacts with the investor “of a nature and duration 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 such relationship exists.”¹⁶

The Investco LLC securities offered and sold by IM&D did not meet the requirements of Corporations Code section 25102, subdivision (f), for exemption from qualification.

2. The second issue in this case is whether IM&D violated Corporations Code section 25401 by failing to disclose to potential Investco LLC investors the prior purchase of the property by a Landco LLC at a substantially lower price. Determination of this issue turns on whether this information constituted a material fact. Respondents argue that because Investco was paying Landco less for the property than what someone could buy it for on their own, the fact that Landco had recently paid even less was not material. This argument is not persuasive. Investing in an Investco LLC is a good deal only if the real property can be sold at a profit after a few years. In the case of Investco 12, the property will have to be sold for more than the \$870,000 offering amount for there to be any profit, since \$495,000 in costs and fees were added to the \$375,000 purchase price. The property pro forma estimates project that if after four years the property is sold “as is” for \$1,413,380, the investors will realize an average annual return of 15.2 percent. Reaching that target price will require greater appreciation in property values if the starting point is \$207,850, the price Landco 12 paid in August 2007 (or \$275,000, the previous owner’s asking price), rather than \$375,000, the price Investco paid in September 2007. And the fact that IM&D was to receive 81.9 percent of the net profit from the sale of the real property by Landco 12 to Investco 12 and a total of approximately \$150,000 in profit, commissions, management fees

¹⁶ Cal. Code Regs., tit. 10, § 260.102.12, sub. (d)(1).

and expenses from the transaction would be material to a potential investor considering the likelihood that investors will realize a profit at the end of four years.

IM&D violated Corporations Code section 25401 by failing to disclose to potential Investco LLC investors the prior purchase of the property by a Landco LLC at a substantially lower price.

3. Corporations Code section 25532 authorizes the Corporations Commissioner to issue the Desist and Refrain Order against respondents.

ORDER

The Desist and Refrain Order issued on February 18, 2009, to respondents Christopher P. Epsha, Steven G. Thompson, and Investco Management & Development LLC is upheld.

DATED: _____

NANCY L. RASMUSSEN
Administrative Law Judge
Office of Administrative Hearings