State of Tennessee
Department of State
Administrative Procedures Division
312 Rosa L. Parks Avenue
8th Floor, William R. Snodgrass Tower
Nashville, Tennessee 37243-1102
Phone: (615) 741-7008/Fax: (615) 741-4472

October 19, 2017

Commissioner Julie Mix McPeak
Tennessee Department of Commerce & Insurance
Office of Legal Counsel
12th Floor, Davy Crockett Tower
500 James Robertson Parkway
Nashville, Tennessee 37243-5065

Andrew J. Ermenc
114 Jefferson Drive
Hendersonville, TN 37075

Jesse D. Joseph, Esq.
Assistant General Counsel-Litigation
Tennessee Department of Commerce and Insurance
Office of Legal Counsel
8th Floor, Davy Crockett Tower
500 James Robertson Parkway
Nashville, TN 37243-0569

RE: In the Matter of: Andrew J. Ermenc Docket No. 12.06-142449J

Enclosed is an Initial Order rendered in connection with the above-styled case.

Administrative Procedures Division
Tennessee Department of State

/aem
Enclosure

BEFORE THE COMMISSIONER OF THE TENNESSEE DEPARTMENT OF COMMERCE AND INSURANCE

IN THE MATTER OF:

ANDREW J. ERMENC **DOCKET NO. 12.06-142449J**

NOTICE

ATTACHED IS AN INITIAL ORDER RENDERED BY AN ADMINISTRATIVE JUDGE WITH THE ADMINISTRATIVE PROCEDURES DIVISION.

THE INITIAL ORDER IS NOT A FINAL ORDER BUT SHALL BECOME A FINAL ORDER UNLESS:

1. THE ENROLLEE FILES A WRITTEN APPEAL, OR EITHER PARTY FILES A PETITION FOR RECONSIDERATION WITH THE ADMINISTRATIVE PROCEDURES DIVISION NO LATER THAN **November 3, 2017.**

YOU MUST FILE THE APPEAL, PETITION FOR RECONSIDERATION WITH THE ADMINISTRATIVE PROCEDURES DIVISION. THE ADDRESS OF THE ADMINISTRATIVE PROCEDURES DIVISION IS:

SECRETARY OF STATE
ADMINISTRATIVE PROCEDURES DIVISION
WILLIAM R. SNODGRASS TOWER
312 ROSA PARKS AVENUE, 8th FLOOR
NASHVILLE, TENNESSEE 37243-1102

IF YOU HAVE ANY FURTHER QUESTIONS, PLEASE CALL THE ADMINISTRATIVE PROCEDURES DIVISION, **615/741-7008 OR 741-5042, FAX 615/741-4472.** PLEASE CONSULT APPENDIX A AFFIXED TO THE INITIAL ORDER FOR NOTICE OF APPEAL PROCEDURES.

BEFORE THE COMMISSIONER OF THE TENNESSEE DEPARTMENT OF COMMERCE AND INSURANCE

IN THE MATTER OF: **TENNESSEE SECURITIES DIVISION,** **Petitioner,** **v.** **ANDREW J. ERMENC,** **Respondent.**	**DOCKET NO. 12.06-142449J** **TSD No. 16-010**

INITIAL ORDER

This matter was heard *de novo* on April 6, 2017, in Nashville, Tennessee, before Administrative Judge Phillip R. Hilliard, assigned by the Secretary of State, Administrative Procedures Division (APD), to sit for the Commissioner of the Tennessee Department of Commerce and Insurance (Commissioner). The April 6, 2017, hearing addressed the allegations contained in the NOTICE OF HEARING AND CHARGES filed on February 10, 2017. Jesse D. Joseph, Assistant General Counsel, represented the Petitioner, the Tennessee Securities Division (TSD) of the Tennessee Department of Commerce and Insurance. The Respondent proceeded *pro se*, waiving the right to legal counsel.

On May 1, 2017, a transcript of the proceedings was filed. On May 12, 2017, the Respondent filed DEFENDANT'S PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW. On May 15, 2017, TSD filed TENNESSEE SECURITIES DIVISION'S PROPOSED FINDINGS OF FACT, PROPOSED CONCLUSIONS OF LAW, AND PROPOSED JUDGMENT. On July 7, 2017, Petitioner filed TENNESSEE SECURITIES DIVISION'S MEMORANDUM OF LAW IN RESPONSE TO THE COURT'S ORDER ENTERED ON JUNE 26, 2017; and on July 10, 2017, the Petitioner filed TENNESSEE SECURITIES

DIVISION'S NOTICE OF ERRATA CONTAINED IN MEMORANDUM OF LAW FILED ON JULY 7, 2017.[1] On July 18, 2017, the Respondent filed a MOTION OF DISMISSAL[2] and RESPONSE[3] TO TENNESSEE SECURITIES DIVISION'S MEMORANDUM OF LAW IN RESPONSE TO THE COURT'S ORDER ENTERED ON JUNE 26, 2017. On July 21, 2017, the Respondent filed a letter, which requested certain information from the TSD.[4]

After consideration of the entire RECORD in this matter, it is **ORDERED** that, in accordance with TENN. CODE ANN. § 48–1–121 and/or TENN. CODE ANN. § 48–1–112 the Respondent is assessed **CIVIL PENALTIES** in the total amount of ONE HUNDRED THREE THOUSAND DOLLARS ($103,000) for violations of TENN. CODE ANN. § 48–1–121. This decision is based upon the following.

MOTION TO DISMISS

The NOTICE OF HEARING AND CHARGES in this matter was filed on February 10, 2017. In filings made on March 14 and 21, 2017, the Respondent requested that this matter be dismissed.

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[1] These pleadings were filed in response to an ORDER requesting briefs on the applicability of civil penalty statutes. The Petitioner's brief was to be filed on or before July 7, 2017. The Respondent's brief was due on or before July 17, 2017.

[2] Respondent's MOTION OF DISMISSAL is based on his assertion that the limitations periods in TENN. CODE ANN. § 48–1–122 operate as a time bar to the charges brought by Petitioner. However, the Petitioner's case is not brought under TENN. CODE ANN. § 48–1–122, which establishes a private right of action against the seller of securities, under certain circumstances, but instead under TENN. CODE ANN. § 48–1–121, which allows for an action to be brought by the Commissioner. Accordingly, the Respondent's MOTION FOR DISMISSAL is denied.

[3] Because Respondent's pleading largely fails to cite to the record, it is somewhat difficult to follow. Some of the Respondent's claims appear to constitute facts not in the record. In spite of these issues, the Respondent's pleading was considered for purposes of this INITIAL ORDER.

[4] The Respondent's letter requests a copy of the "Order of Investigation that was initiated in January of 2013." It is presumed the Respondent is referring to an Order of Investigation, as contemplated by TENN. CODE ANN. § 48–1–118. To the extent the Respondent's letter represents a discovery request, it is untimely. To the extent the request is intended to further an argument that the Petitioner's case is time-barred by TENN. CODE ANN. § 48–1–122, that argument is unavailing, as addressed *supra,* ftnt. 2.

The stated bases were as follows: 1) that Title 48 of the Tennessee Code Annotated did not apply to individuals; and 2) that the promissory notes at issue in this matter were not securities. The request appears to be one for dismissal of the NOTICE OF HEARING AND CHARGES for failure to state a claim upon which relief can be granted and is therefore governed by TENN. R. CIV. P. 12.02(6). The Petitioner filed TENNESSEE SECURITIES DIVISION'S RESPONSE TO RESPONDENT'S MOTION TO DISMISS on March 17, 2017.

TENN. R. CIV. P. 12.02(6) motions to dismiss are granted "only when it appears that the plaintiff can prove no set of facts in support of the claim that would entitle the plaintiff to relief." *Webb v. Nashville Habitat for Humanity, Inc.*, 346 S.W.3d 422, 426 (Tenn. 2011) (quoting *Crews v. Buckman Labs. Int'l, Inc.*, 78 S.W.3d 852, 857 (Tenn. 2002)). All factual allegations made by the non-movant (here, the Petitioner) are to be taken as true. *Cook By and Through Uithoven v. Spinnaker's of Rivergate, Inc.*, 878 S.W.2d 934, 938 (Tenn. 1994) (citing *Fuerst v. Methodist Hospital South*, 566 S.W.2d 847, 848-49 (Tenn. 1978) and *Holloway v. Putnam County*, 534 S.W.2d 292, 296 (Tenn. 1976)).

The NOTICE OF HEARING AND CHARGES seeks recourse against the Respondent[5] for alleged violations of the TENNESSEE SECURITIES ACT OF 1980[6], TENN. CODE ANN. §§ 48– 1–101 to 48–1–126[7] (the Act). More specifically, Petitioner alleges that Respondent violated TENN. CODE ANN. § 48–1–121.

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[5] The NOTICE OF HEARING AND CHARGES clearly alleges the Respondent to be a natural person, Andrew J. Ermenc. *See* NOTICE OF HEARING AND CHARGES, p. 2.

[6] The language of the TENNESSEE SECURITIES ACT OF 1980 largely tracks federal law – the SECURITIES EXCHANGE ACT OF 1934.

[7] While the Act was located at TENN. CODE ANN. §§ 48–2–101 to 48–2–126 during the time period concerning most of the alleged violations, the language of the relevant portions of the Act used by Petitioner remain substantively unchanged through the filing of the NOTICE OF HEARING AND CHARGES, with one exception being the civil penalty provision found at TENN. CODE ANN. § 48–1–121(d). Issues

TENN. CODE ANN. § 48–1–121(a) provides:

> It is unlawful for **any person**, in connection with the offer, sale or purchase of any security in this state, directly or indirectly, to:
>
> (1) Employ any device, scheme, or artifice to defraud;
>
> (2) Make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or
>
> (3) Engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

TENN. CODE ANN. § 48–1–102(14) (Emphasis added).

TENN. CODE ANN. § 48–1–102(14) provides, as follows:

> As used in this part, unless the context otherwise requires:
>
> (14) **"Person" means a natural person, a sole proprietorship**, a corporation, a partnership, an association, a limited liability company, a trust, a governmental entity or agency, or any other unincorporated organization.

TENN. CODE ANN. § 48–1–102(14) (Emphasis added).

TENN. CODE ANN. § 48–1–121 is plainly applicable to "any person." Therefore, Respondent's argument that only a "Corporation or Association" can be held liable under the Act is without merit.

TENN. CODE ANN. § 48–1–102(17)(A) defines a "security," as follows:

> (17)(A) "Security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, a life settlement contract, as defined in former § 56-50-102, or any fractional or pooled interest in a life insurance policy or life settlement contract, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, certificate of interest or participation in an oil, gas, or

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concerning the appropriate civil penalty provision(s) are dealt with, separately, herein. While it is noted that the 2017 legislative session brought changes to the Act, references to the Act will track the citations made by the Petitioner in the NOTICE OF HEARING AND CHARGES in order to maintain consistency and because that was the version of the statute in effect at the time this action was instituted.

> mining title or lease or in payments out of production under such a title or lease; or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

TENN. CODE ANN. § 48–1–102(17)(B)(iii) states that "'[s]ecurity' does not include a note or other evidence of indebtedness issued in a mercantile or consumer, rather than an investment, transaction." The Petitioner alleges the promissory notes at issue to be "investments," as opposed to "mercantile or consumer transactions," throughout the Notice of Hearing and Charges. Thus, the Respondent's argument that the promissory notes are not securities, by virtue of TENN. CODE ANN. § 48–1–102(17(B)(iii), fails to form a sufficient basis to dismiss for failure to state a claim upon which relief can be granted.[8]

Based on the foregoing, and as announced at the hearing, the Respondent's request that this matter be dismissed was denied.

FINDINGS OF FACT

1. Respondent Andrew J. Ermenc (Respondent) is a resident of Tennessee, with a last known residential address of 114 Jefferson Drive, Hendersonville, TN 37075. Respondent was registered with the TSD and with the Financial Industry Regulatory Agency (FINRA) as a broker-dealer agent (Individual Central Registration Depository (CRD) # 3139539) from July 5, 1999 until December 16, 2004, when his employment with Thrivent Financial Management, Inc. (Thrivent Financial)[9] was terminated due to his failure to meet minimum production requirements. Respondent also previously held a Tennessee insurance producer license

[8] As discussed, *infra*, pp. 18-21, the promissory notes are found to be securities, in accordance with the United States Supreme Court's opinion in the case of *Reves v. Ernst & Young*, 494 U.S. 56 (1990).

[9] Respondent was employed by Aid Association for Lutherans until it merged with Lutheran Brotherhood to form Thrivent Financial in 2002.

(#0800616), which was issued in 1998. Respondent requested the cancellation of his Tennessee insurance producer's license in October 2005 and said license expired in October 2005. [EX.[10] 1, ¶ 4; NOTICE OF HEARING AND CHARGES (NOHC), ¶ 4; RESPONDENT'S ANSWER[11] TO NOHC (ANSWER), ¶ 4].

2. Prior to joining Thrivent Financial, Respondent was a managing partner of an Outback Steakhouse franchise in Nashville, with his contract beginning in 1992. From 1992 to 1997, Respondent was paid a salary from Outback as a managing partner, and when he left Outback in May of 1997 he was given options on stock that were to be exercised over a 10-year period from 1997 to 2007, at various intervals. Respondent received approximately $250,000 in cash payments on options from Outback between 1997 and 2007. Respondent exercised his last Outback stock option in May of 2007, for which he received payment in July of 2007, in the approximate amount of $120,000. [NOHC, ¶ 5; ANSWER, ¶ 5; TR.[12] pp. 94-95.]

3. Michael Lee Van Maanen (Mike Van Maanen) first met Respondent in the mid to late 1990s, when Respondent was appointed as his insurance agent with the Aid Association for Lutherans (AAL). At some point in the early 2000s, Respondent was removed as Mike Van Maanen's insurance agent with Thrivent Financial. During the transition to a new agent, Mike Van Maanen asked Respondent what he was going to be doing. Respondent told Mike Van Maanen that he was going to engage in the business of trading stocks. [NOHC, ¶ 6; ANSWER, ¶ 6].

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[10] The notation "EX." represents references to the exhibits introduced at the April 6, 2017, hearing.

[11] This pleading was filed by the Respondent on March 21, 2017.

[12] The notation "TR." represents references to the transcript of the April 6, 2017, hearing.

4. Mike Van Maanen is now retired but was previously self-employed, owning a flower shop in Tennessee. Mike Van Maanen also co-owned several rental properties with his son, Michael Van Maanen, Jr., from 2000 to 2006. [TR. 49, 136].

5. Michael Van Maanen, Jr. (Mick Van Maanen) was introduced to Respondent by his father at some point in or around the early 2000s, while Respondent was working with AAL or Thrivent. [NOHC, ¶ 7; ANSWER, ¶ 7].

6. Mick Van Maanen is currently employed as an Information and Technology (IT) analyst. [TR. 63].

7. Daniel DeGuira first learned about Respondent on or about 2005 or 2006, after receiving an inheritance. Mr. DeGuira didn't know anything about investments at that time. [TR. 77-78].

8. Daniel DeGuira is currently employed by a credit card processing company. [TR. 76].

9. Daniel DeGuira's aunt, for whom the Respondent set up a Roth IRA, told him about Respondent. Mr. DeGuira's cousin and uncle gave him Respondent's phone number as someone to call regarding an investment opportunity. [TR. 84].

10. Joseph Eaton was referred to Respondent by Mick Van Maanen at some point during the summer of 2008. In or about June of 2008, Mr. Eaton contacted Respondent and discussed Respondent's investment strategies. [NOHC, ¶ 9; ANSWER, ¶ 9].

11. Mr. Eaton currently resides in Knoxville, Tennessee. [Ex. 3, DEPOSITION OF JOSEPH EATON, p. 5].

MIKE VAN MAANEN'S INVESTMENTS

12. When Respondent left Thrivent Financial, he told Mike Van Maanen, in or about 2004, that he was going to go into an investment business, and that he would pay people an 18% return on their money to handle investments. With respect to discussing the risk of loss to investors, Respondent stated that his investment strategies and methods were a "piece of cake." [NOHC, ¶ 10; ANSWER, ¶ 10; TR. 50-51].

13. On December 14, 2005, Mike Van Maanen entered into his first 12 month promissory note with Respondent regarding his investment of $10,000 at 1.5% interest per month (or 18% annual interest). Respondent told Mike Van Maanen he was going to place the money invested in "good, solid" stocks, and showed Mike Van Maanen materials setting out his stock price charting and trading strategies. [NOHC, ¶ 11; ANSWER, ¶ 11; EX. 4; TR. 51-52, 58-59].

14. Respondent told Mike Van Maanen that Respondent had an account at Scottrade brokerage in which Respondent would make the stock trades. [NOHC, ¶ 12; ANSWER, ¶ 12; TR. 60].

15. On March 16, 2006, December 10, 2007, December 28, 2007, July 21, 2008, and May 19, 2009, Mike Van Maanen and his business (Van Maanen Properties, Inc.) entered into 5 additional promissory notes with Respondent on the same terms, investing $40,000, $100,000, $200,000, $200,000, and $50,000, respectively. Respondent renewed all of these notes except the note dated May 19, 2009. Respondent renewed the December 2005 and March 2006 notes several times. [Ex. 4; NOHC, ¶ 13; ANSWER, ¶ 13].

16. Respondent did make interest payments on the notes to Mike Van Maanen, with most payments to be prorated amongst the applicable notes, until August of 2009. Respondent

has not made any further interest payments, or payments on the outstanding principal, since August 1, 2009. [NOHC, ¶ 14; ANSWER, ¶ 14; EX. 4; TR. 52, 57].

17. On several occasions, between 2009 and 2012, Mike Van Maanen had conversations with Respondent, in which conversations Respondent informed Mr. Van Maanen that there was between 30 to 40 percent of Mr. Van Maanen's original principal investment remaining. [TR. 133-134].

18. On at least two occasions, the last of which occurred a month or two prior to February of 2012, Mike Van Maanen requested the Respondent liquidate Mr. Van Maanen's principal investment amount and return it to Mr. Van Maanen. Respondent informed Mr. Van Maanen that he could not liquidate Mr. Van Maanen's share because it would not be fair to everyone else. [TR. 134].

19. Mike Van Maanen's principal investment amount was never liquidated. [TR. 134].

20. On or about February 17, 2012, by letter, Mike Van Maanen and Joseph Eaton formally notified Respondent of his default, demanded an accounting of how much of their monies remained, where those funds were invested, what percentage was in each investment, and how long it would take to convert those funds to cash. The letter concluded by saying that if these demands were not met Mr. Van Maanen and Mr. Eaton would be seeking "consult to explore any and all avenues to determine the value of our assets in your possession and to recover said assets up to the full value of the original investment." [Ex. 6].

21. On June 12, 2015, a VERIFIED COMPLAINT was filed by Mike Van Maanen, Mick Van Maanen, and Joseph Eaton against Respondent in the Sumner County Chancery Court, Case No. 2015-CV-94, alleging the breach of certain promissory notes. [Ex. 18].

22. On September 29, 2015, an AGREED ORDER OF JUDGMENT was entered in the amount of $1,184,888.00[13], with such amount "representing principal and interest owed on promissory notes referenced in the [VERIFIED] COMPLAINT[14]." The amount of principal and interest for Mike Van Maanen was stated at $819,074. [Ex. 18].

23. Respondent has not paid any money owing under the AGREED ORDER OF JUDGMENT. [TR. 58].

MICK VAN MAANEN'S INVESTMENTS

24. On August 18, 2006, September 19, 2007, June 27, 2008, and September 15, 2008, Mick Van Maanen entered into 4 separate 12-month promissory notes with Respondent at 1.5% interest per month (or 18% annual interest), investing $50,000 in the August 2006 note, and $20,000 in each of the 3 later notes. Respondent renewed the August 2006 note several times with the last renewal being on August 18, 2008. Respondent renewed the June 2008 note once. [NOHC, ¶ 15; ANSWER, ¶ 15; Ex. 7; TR. 65-66).

25. Respondent did reassure Mick Van Maanen that using his charting techniques was "a safe way to invest" and that "generally there wasn't any big risk because he [Respondent] would protect himself by investing, hedging." [TR. 64-65].

26. Respondent did make interest payments on the notes to Mick Van Maanen, with most payments to be prorated amongst the applicable notes, until August of 2009. Respondent has not made any further interest payments, or payments on the outstanding principal, since August 1, 2009. [NOHC, ¶ 16; ANSWER, ¶ 16; EX. 7; TR. 66, 69].

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[13] Judgment was also agreed to be given for attorney's fees, for all Plaintiffs, in the total amount of $3,000.

[14] The VERIFIED COMPLAINT alleges the amount due and owing to Mike Van Maanen and Van Maanen Properties, collectively, to have been $1,485,270. [EX. 18].

27. The amount of principal and interest for Mick Van Maanen was stated, in the September 29, 2015, AGREED ORDER OF JUDGMENT, at $160,912.[15] [Ex. 18].

DANIEL DEGUIRA'S INVESTMENTS

28. Respondent spoke with Daniel DeGuira in or about April 2006 about the possibility of Mr. DeGuira investing in Respondent's promissory notes, claiming that he made a substantial amount monthly through trading stocks, and that he would place the investors' money into his account at Scottrade in order to engage in such trading. Respondent did not discuss with Mr. DeGuira the risk involved in Respondent's trading activities. [NOHC, ¶ 17; ANSWER, ¶ 17; TR. 79].

29. Respondent told Daniel DeGuira that he made up to 33% per month through day trading, and that he almost "doubled" the amount he owed in promissory notes through day trading. Respondent also told Mr. De Guira that he was "part of the community" of Hendersonville where "city officials" in Hendersonville, Tennessee had invested with him. Therefore, Mr. DeGuira was told, Respondent had to be "careful with their money." [TR. 84-85].

30. Based on these representations, on April 10, 2006, Daniel DeGuira entered into his first 12 month promissory note with Respondent regarding his investment of $40,000 at 1.5% interest per month (or 18% annual interest). Mr. DeGuira entered into a second promissory note with Respondent dated December 15, 2006, investing $30,000 on the same terms. [NOHC, ¶ 18; ANSWER, ¶ 18; TR. 87].

31. Respondent did make interest payments on the notes to Daniel DeGuira, with most payments to be prorated amongst the applicable notes, until August of 2009. [NOHC, ¶ 19; ANSWER, ¶ 19; TR. 79].

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[15] The VERIFIED COMPLAINT alleges the amount due and owing to Mick Van Maanen to have been $316,252.77. [EX. 18].

32. Respondent made a payment to Daniel DeGuira of $15,000 toward outstanding principal sometime in the summer of 2008; another payment of $5,000 was made sometime before July 1, 2009. Two payments of $250 were made by the Respondent to Mr. DeGuria on September 1, 2009, and March 1, 2010, respectively. However, Respondent has not made any further interest payments, or payments on the outstanding principal, since August of 2009. [NOHC, ¶ 19; ANSWER, ¶ 19; EX. 11; TR. 88, 90].

33. Daniel DeGuira called the Respondent, at some point, and demanded the return of his principal amount invested. [TR. 88].

JOSEPH EATON'S INVESTMENTS

34. Respondent informed Joseph Eaton, in June 2008, that he "watched his charts" as to stock values very closely, and that he "got in and out" of certain stocks very quickly in order to try to maximize gains and minimize losses. Respondent did not have any specific discussion with Mr. Eaton prior to Mr. Eaton's initial investment regarding any risk associated with Respondent's trading strategies. [EX. 3, DEPOSITION OF JOSEPH EATON, pp. 8-10].

35. Based on Respondent's representations, on June 20, 2008, Joseph Eaton entered into his first 12 month promissory note with Respondent regarding his investment of $25,000 at 1.5% interest per month (or 18% annual interest). Mr. Eaton entered into second and third promissory notes with Respondent dated September 8, 2008, and February 9, 2009, investing $25,000 and $50,000, respectively, on the same terms. [NOHC, ¶ 21; ANSWER, ¶ 21].

36. Respondent did make some interest payments on the notes to Joseph Eaton, to be prorated amongst the 3 notes. Respondent has not made any interest payments, or payments on the outstanding principal, since August 1, 2009. [NOHC, ¶ 22; ANSWER, ¶ 22].

37. The amount of principal and interest for Joseph Eaton was stated, in the September 29, 2015, AGREED ORDER OF JUDGMENT, at $146,402.[16] [Ex. 18].

RESPONDENT'S ACTIONS AND HIS USE OF THE INVESTMENT FUNDS

38. During all relevant times, Respondent operated his investment business as a sole proprietorship, whereby he handled investments for clients by obtaining promissory notes from individuals who wanted to invest with him. Respondent told his clients he would buy and sell securities with the funds he received from the promissory notes and give his clients a return on their money. [NOHC, ¶ 23; ANSWER, ¶ 23; TR. 104-105].

39. During all relevant times, Respondent deposited all funds received from the above (and additional) promissory note investors within his First Tennessee Bank Disbursement Account, and then transferred a portion of these funds to his Scottrade Margin Account in order to engage in stock trading. Respondent has characterized his actions as swing trading, where he would hold a position in stocks at least overnight or up to several weeks. [NOHC, ¶ 24; ANSWER, ¶ 24].

40. Respondent invested in exchange traded funds ("ETFs") small cap stocks, and options. [TR. 97].

41. Respondent was never given permission by Mike Van Maanen, Mick Van Manaen, Daniel Deguira, or Joseph Eaton (Collectively, "Investors") to use or spend any monies given to the Respondent by the Investors for the Respondent's personal use; the funds were to be used solely to invest in the stock market in order to pay the Investors the stated rate of return in the promissory notes. [EX. 3, DEPOSITION OF JOSEPH EATON, pp. 22-23; TR. 56-57, 70-71, 73-74, 78].

[16] The VERIFIED COMPLAINT alleges the amount due and owing to Joseph Eaton to have been $205,000. [EX. 18].

42. All of the Investors who testified at the hearing considered the promissory note transactions to be investment transactions. [TR. 52, 56, 67, 77-79; EX. 3, pp. 8-10].

43. Between July 18, 2008, and October 9, 2009, Respondent entered into at least 5 promissory notes with investment clients, totaling $345,000. [NOHC, ¶¶ 13, 15, 21; ANSWER, ¶ 13, 15, 21].

44. Respondent did not transfer all of the Investors' funds to his Scottrade Margin Account for trading purposes. Between July 18, 2008, and October 9, 2009, Respondent deposited only $80,000 of Investors' funds from the Disbursement Account into this Scottrade account. [EX. 12, 13, 15, 17; TR. 161-164, 168-169].

45. Between July 18, 2008, and October 9, 2009, Respondent used at least $103,111, from the First Tennessee Disbursement Account, for personal expenses for the Respondent and/or his wife, as follows:

AMOUNT	NAME	NO. OF TRANSACTIONS
$53,876	Diana Ermenc (Respondent's wife)	71
$1,620	Respondent's Home Equity Line of Credit	12
$260	Lawn Ranger (Lawn care)	4
$1,950	Wayne Stoutenberg/Stout Construction (Driveway/Bathroom work)	3
$40,100	Cash/Withdrawals to Respondent	6
$5,000	Charles Schwab (Joint Acct. - Respondent and wife)	1
$105	Stanley Steamer	1
$150	Diane Black for State Senate	1
$10	American Legion	1
$25	VFW	1
$15	Robert Labrec (NCAA Tournament pool)	1

[EX. 12, 16; TR. 169-170].

46. Respondent unilaterally "closed out" promissory notes held by Mike Van Maanen and Joseph Eaton in August of 2009. [NOHC, ¶ 28; ANSWER, ¶ 28; EX. 3, DEPOSITION OF JOSEPH EATON, pp. 14-15; EX. 5].

47. There are no provisions within any of Respondent's promissory notes involved herein that grant him the right to unilaterally cancel any of these notes prior to the stated maturity dates, or to pay a reduced interest rate. [NOHC, ¶ 29; ANSWER, ¶ 29; EXS.3, 4, & 7].

48. Immediately after informing these investors that he was unable to pay further interest on the notes and that he had to close the notes out, Respondent conveyed his 50% interest in the marital residence located at 114 Jefferson Drive in Hendersonville to his wife, by quit claim deed filed on August 8, 2009. [NOHC, ¶ 30; ANSWER, ¶ 30].

49. Despite "closing out" promissory notes held by Mike Van Maanen and Joseph Easton in August of 2009, Respondent continued to correspond with Mr. Van Maanen through 2012, and with Mr. Eaton through mid-2013. These communications indicated the Respondent was still investing money on behalf of Mr. Van Maanen and Mr. Eaton. Respondent stated that out of $100,000 invested by Mr. Eaton, $30,000 remained by the end of the first of April, 2012. [NOHC, ¶ 32; ANSWER, ¶ 32; EX. 3, DEPOSITION OF JOSEPH EATON, pp. 15-20, and EX. 5 thereto]. Respondent stated, in April of 2012, that anywhere between $200,000 and $250,000 of Mr. Van Maanen's money remained. [TR. 133-136].

50. The Respondent testified, at the hearing, that as of April 2012 he had a total of $30,000 remaining of the Investors' principal.[17] [TR. 112-113].

51. All of the promissory notes were made for more than 9 months. [NOHC, ¶ 11, 13, 15, 18, 21; ANSWER, ¶ 11, 13, 15, 18, 21; EX. 4, 7; TR. 143].

52. The promissory notes did not involve any type of consumer financing.

53. The promissory notes were not secured in any way.

[17] It is not clear whether this amount represents monies from those who testified at the hearing (including Mr. Joseph Eaton, whose testimony was entered through a previous deposition), alone.

54. The promissory notes were not notes that formalized an open account debt incurred in the ordinary course of business.

ANALYSIS AND CONCLUSIONS OF LAW

1. The Petitioner's NOTICE OF HEARING AND CHARGES is amended, pursuant to TENN. COMP. R. & REGS, 1360–04–01–.05(8), to conform to the issues tried by implied consent and the evidence introduced at hearing, so as to ensure that the NOTICE OF HEARING AND CHARGES is consistent with this INITIAL ORDER and the evidence introduced at the April 7, 2017 hearing.

2. TENN. CODE ANN. § 48–1–121(a) provides:

> It is unlawful for any person, in connection with the offer, sale or purchase of any security in this state, directly or indirectly, to:
>
> (1) Employ any device, scheme, or artifice to defraud;
>
> (2) Make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or
>
> (3) Engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

3. Petitioner alleges five causes of action under this section of the Act, as follows:

> I. Respondent, in connection with the offer and sale of securities to the above investors on more than fourteen (14) occasions, omitted material facts necessary to make the statements made, in the light of the circumstances under which they were made, not misleading by failing to disclose to the above investors that his methods of stock trading could result in substantial losses of principal. These omissions on Respondent's part have violated Tenn. Code Ann. § 48-1-121(a)(2).
>
> II. Respondent, in connection with the offer and sale of securities to the above investors, engaged in acts which operated to defraud or deceive said investors by misappropriating or converting at least $103,111 of investors' funds within the Disbursement Account to

his own use between July 18, 2008 and October 9, 2009 (102 transactions), given that Respondent funneled this amount of these investors' funds from his Disbursement Account directly to his wife and to himself for his individual expenses or personal use. Respondent's fraudulent actions in this regard have violated Tenn. Code Ann. § 48-1-121(a)(3).

III. Respondent, in connection with the offer and sale of securities to the these investors on more than fourteen (14) occasions, employed devices, schemes, or artifices to defraud by promising an unusually high rate of return and full repayment of principal in writing to these investors over a very short term. In truth, Respondent was not able to pay the promised 18% annual return to earlier investors with profit earned from his trading operations, but was able to perpetuate this Ponzi scheme through mid-2009, only by obtaining new capital from new promissory note investors. Respondent's actions in this regard have violated Tenn. Code Ann. § 48-1-121(a)(1).

IV. Respondent also committed acts which deceived and operated as a fraud upon the above four (4) investors by choosing not to return to these investors at least a portion of their principal to reduce their losses when he had money available to do so by April 2012, given his acknowledgement that he had account balances amounting to approximately 25-30% of these investors' principal balances on hand by that month, nearly 3 years after he closed out his promissory note program. Respondent's actions in this regard have violated Tenn. Code Ann. § 48-1-121(a)(3).

V. Respondent further defrauded all four (4) investors by conveying to his wife his interest in real estate (a possible asset which could be used to pay creditors) 1 month after he informed these investors that he could no longer pay ongoing interest or principal according to the notes. These actions on Respondent's part have violated Tenn. Code Ann. § 48-1-121(a)(3).

[NOHC, ¶¶ 42-45].

4. In accordance with TENN. COMP. R. & REGS. 1360–04–01–02(7) and 1360–04–01–.15(3), the Petitioner must prove the alleged violations of law by a preponderance of evidence.

5. The Supreme Court of the United States, in *Reves v. Ernst & Young*, 494 U.S. 56 (1990), addressed many questions relevant to the instant matter, including what constitutes a security[18]. Therein, the Court stated that the purpose of securities law is "to eliminate serious abuses in a largely unregulated securities market" and "to regulate *investments* in whatever form they are made and by whatever name they are called." *Reves*, 494 U.S. 56, 60-61(citing *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 849 (1975)). In furtherance of that purpose, Congress recognized "the virtually limitless scope of human ingenuity, especially in the creation of 'countless and variable schemes devised by those who seek the use of money of others on the promise of profits.'" *Id.* (citing *SEC v. Howey Co.*, 328 U.S. 293, 299 (1946)). Thus, Congress intentionally "painted with a broad brush" when it defined the term security. *Id.* at 60.

6. The Supreme Court of Tennessee has specifically stated the purpose of the Act to be the prevention of frauds and impositions upon the public and that the Act should be liberally construed to effectuate its purpose. *DeWees v. State*, 390 S.W.2d 241, 242 (Tenn. 1965).

7. The Petitioner must show that the promissory notes are securities, within the meaning provided by TENN. CODE ANN. §§ 48–1–102(17)(A) and (B)(iii), in order to prove that the Respondent's conduct is governed by the Act and its implementing regulations.[19] Petitioner contends, pursuant to TENN. CODE ANN. §§ 48–1–102(17)(B)(iii), that the promissory notes at issue were "indebtedness issued in a mercantile or consumer, rather than an investment, transaction." However, there was no evidence proffered to support this position, and neither does the record support such a notion. *See State v. Brewer*, 932 S.W.2d 1, 15 (Tenn. Crim. App.

[18] The definitional language of "security" under federal law is found to be sufficiently analogous to Tennessee's provision to render case law from federal courts persuasive.

[19] The relevant language of these provisions is quoted, *supra*, pp. 4-5.

1996)("This exclusion is simply the codification of a long recognized distinction between notes issued in the context of an investment and those issued to finance the purchase of mercantile or consumer goods.")

8. Beyond the specific exemption in TENN. CODE ANN. § 48–1–102(17)(B)(iii), the language in TENN. CODE ANN. § 48–1–102(17)(A) gives rise to a rebuttable presumption that "any note" constitutes a security. *See Reves*, 494 U.S. at 67; *U.S. S.E.C. v. Zada*, 787 F.3d 375, 380 (6th Cir. 2015). In order to rebut the presumption, one "must show that the note bears a 'family resemblance' to a list of instruments that are not securities," using four factors set forth in *Reves*. *Reves*, 494 U.S. at 65. This list of instruments includes "consumer debt, home-mortgage loans, character loans to bank customers, and short-term commercial debt." *Id.* The four *Reves* factors are 1) the motivation prompting the transaction; 2) the plan of distribution; 3) the reasonable expectations of the investing public; and 4) whether a risk-reducing factor makes application of Securities laws unnecessary. *Id.* at 66-67.

9. As to the first factor, there is considerable unrebutted testimony from the Investors that they were interested primarily in the profit (18% annual interest) they would receive from the Respondent. It is also undisputed that the Respondent's purpose was to finance substantial investments for his clients and to make money for his investment business at the time. It is clear that the motivation was for the Investors (payees of the notes) to make money by virtue of the Respondent's ability to invest these monies into the stock market for a substantial profit – the notes, in this context, were quintessential investments. *See Zada*, 787 F.3d at 380 (citing *Pollack v. Laidlaw Holdings, Inc.*, 27 F.3d. 808, 812 (2nd Cir. 1994) (inquiry turns on whether the buyers purpose was investment versus a commercial or consumer transaction). They were not designed to "facilitate the purchase of a minor asset or consumer goods, to correct for the

seller's cash-flow difficulties, or to advance some other commercial or consumer purpose." *See Reves*, 494 U.S. at 66. Therefore, the application of this factor leads to the conclusion that the notes are securities.

10. As to the second factor, the maker of the notes (the Respondent) offered them to a variety of different people. The payees were not sophisticated "institutional investors," but instead laypersons whom securities laws are squarely intended to protect. *Id.* at 381 (citing *Pollack v. Laidlaw Holdings, Inc.*, 27 F.3d. 808, 813-814 (2nd Cir. 1994)). Thus, the application of this factor weighs in favor of the finding that the notes are securities.

11. The third factor asks whether a reasonable person would expect securities laws to apply to the transaction. In the analogous case[20] of *U.S. S.E.C. v. Zada*, 787 F.3d 375 (6th Cir. 2015), the defendant offered promissory notes to payees in exchange for a return on their monies. While the face of the notes said nothing about what the maker would be doing with monies, the payees all were told that the monies would be invested in the oil industry. Because the monies were purportedly to be invested in a commodity that is traded on global markets, the Sixth Circuit Court of Appeals found that a reasonable person would have expected securities laws to apply to the promissory note transactions. *U.S. S.E.C. v. Zada*, 787 F.3d 375, 381 (6th Cir. 2015). Here, similarly, while the notes were silent about what the maker (the Respondent) would be doing with the monies, the parties all understood that the Respondent would be investing the monies in the stock market[21] – transactions which are typically subject to securities laws when made between stockbrokers, or financial advisors, and clients. While the *Reves*

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[20] The *Reeves* case also involved the question of whether promissory notes were securities.

[21] The proof showed that the Respondent had conversations, to varying degrees, with the different payees about what types of stocks he intended to invest in.

decision makes plain that this factor is not determinative no matter which way the evidence points, *Reves*, 494 U.S. at 66, it is concluded that a reasonable person would expect securities laws to apply to these promissory notes.

12. The fourth and final consideration is whether there are risk-reducing factors that would make the application of securities laws unnecessary. As in *Reves*, the notes, here, are uncollateralized and uninsured. *Reves*, 494 U.S. at 69. And as in *Reves* and *Zada*, if securities laws do not apply, then the notes in question would entirely escape governmental regulation. *Reves*, 494 U.S. 56, 69; *Zada*, 787 F.3d 375, 381. In short, there were no protections, whatsoever, afforded to the subject Investors.[22]

13. Based on the foregoing, it is concluded that the promissory notes are securities, as contemplated by TENN. CODE ANN. §§ 48–1–102(17)(A).

14. Respondent appears to have asserted an affirmative defense under TENN. R. CIV. P. 8.03 by contending that some or all of the $120,000 he spent on personal items from the Disbursement Account was his own money. Essentially, Respondent is asserting a new allegation (commingling) that seeks to avoid liability as to the misappropriation charge because of a legally sufficient excuse. *See Thompson, Breeding, Dunn, Creswell & Sparks v. Bowlin*, 765 S.W.2d 743, 744 (Tenn. Ct. App. 1987) (citing Pivnik, Tenn. Circuit Court Prac. (2nd Ed.), § 12-4) ("[a]n affirmative defense is one that wholly or partly avoids the cause of action asserted by the preceding pleading by new allegations that admit part or all of the cause of action, but

[22] Several of the Investors sued the Respondent in State court for breach of contract and were awarded an agreed judgment in excess of $1,000,000. However, this "post-injury opportunity" is not the type of risk-reducing factor contemplated by the Court in *Reeves*, which examples operate to prevent investors from harm in the first place. *See Stoiber v. S.E.C.*, 161 F.3d 745, 752 (D.C. Cir. 1998). The rationale for front-end risk reduction is made plain, here, as it would appear the Investor-plaintiffs in the aforementioned lawsuit have little more than a paper judgment to show for their efforts, the Respondent-defendant not having paid any monies to satisfy the judgment.

avoids liability because of a legally sufficient excuse, justification, or other matter negating the alleged breach or wrong.").

15. To the extent that Respondent is asserting an affirmative defense, his argument fails because he failed to meet his burden of proof. The appellate courts of Tennessee are clear in holding that "the burden of proving an affirmative defense is on the party asserting it." *Tennessee Farmers Mut. Ins. Co. v. Farrar*, 337 S.W.3d 829, 837 (Tenn. Ct. App. 2009). Here, the burden of proving that the funds used for his own personal purposes between July 2008 and October 2009, were in fact his own personal monies, shifts to Respondent. However, Respondent was unable to prove that he placed his own funds in the Disbursement Account, and testified inconsistently on this point at his May 16, 2016, deposition in the Sumner County Chancery Court matter. As the First Tennessee Bank account holder, Respondent was in a better position than anyone else to have maintained and produced copies of any deposits of this approximate $120,000 amount, which allegedly came from his Outback Steakhouse stock options, into his First Tennessee Bank Disbursement Account. No such documentary evidence was proffered by the Respondent. [TR. 125-126].

Failure to Disclose Risks of Investment

16. As a former registered broker-dealer agent for AAL and Thrivent, and in his capacity as a sole proprietor receiving funds from investors to make stock trades, where the client has "requested the broker or advisor to provide investment advice or has given the broker discretion to select his or her investments, the broker or advisor assumes ***broad fiduciary obligations that extend beyond the individual transactions***." *See Johnson v. John Hancock Funds*, 217 S.W.3d 414, 428 (Tenn. Ct. App. 2006). (Emphasis added). It is undisputed on this

record that all of the Investors gave Respondent very broad discretion to select particular investments; therefore Respondent assumed such broad fiduciary responsibilities.

17. In *French v. First Union Securities, Inc.*, 209 F. Supp.2d 818, 824-25 (M.D. Tenn. 2002), the court cited the general rule that an agent generally has a fiduciary relationship with his or her principal, and that a stockbroker is generally deemed to be the agent of his or her client. Respondent has testified that he ran an investment business as a sole proprietor where he handled investments (stock trades) for his clients. [TR. 104-105].

18. The proof shows that the Respondent minimized, at best, the risks associated with his investment strategies in his discussions with the Investors. The results of his efforts belie any contention that the risk was anything other than extremely high. While risk is inherent in any investment venture, it was incumbent upon the Respondent to explain the specific risks associated with the type of trading activities in which he involved the Investors' money. *See Winslow v. BancorpSouth*, No. 3:10-00463, 2011 WL 7090820, at *17 (M.D. Tenn. April 26, 2011). The proof shows the Respondent fell short in this regard.

19. The Petitioner has shown, by a preponderance of the evidence, that in connection with the offer of securities to the Investors on more than fifteen (15) occasions (there were 15 promissory notes sold to these investors, in total, and many more renewals of notes) the Respondent omitted material facts necessary to make the statements made, in the light of the circumstances under which they were made, not misleading by failing to disclose to the above investors that his methods of stock trading could result in substantial losses of principal. These omissions on Respondent's part violate TENN. CODE ANN. § 48–1–121(a)(2).

Misappropriation or Conversion of Investors' Monies

20. The testimony from the Investors was clear that none of them anticipated or agreed that the Respondent would or could use their monies for the Respondent's own purposes. Instead, they rightly believed, or were led to believe, that the monies would only be used to gain a return on their money. This use of the Respondent's monies constitutes a violation of TENN. CODE ANN. § 48–1–121(a). *See, e.g., Zada* 787 F.3d at 382.

21. The Petitioner has shown, by a preponderance of the evidence, that in connection with the offer of securities to the Investors, the Respondent engaged in acts which operated to defraud or deceive the Investors by misappropriating or converting at least $103,111 of investors' funds within the First Tennessee Bank Disbursement Account to his own use between July 18, 2008 and October 9, 2009 (102 transactions), given that Respondent funneled this amount of these investors' funds from his Disbursement Account to his wife and to himself for his individual expenses or personal use. Respondent's fraudulent actions in this regard have violated TENN. CODE ANN. § 48–1–121(a)(1–3).

Failure to Return Outstanding Principal

22. Petitioner asserts that the Respondent's failure to return outstanding principal owing to certain payees (Mr. Joseph Eaton and Mr. Mike Van Maanen) when he had the money to do so, some three years after the promissory notes were unilaterally closed out by the Respondent, constitutes a violation of TENN. CODE ANN. § 48–1–121(a)(3). Respondent led Mr. Joseph Eaton and Mr. Mike Van Maanen to believe that he had significant amounts of their principal remaining as late as April 2012. By the Petitioner's own admission, at the hearing, this was not true. It cannot be determined how much money the Respondent actually had at that time. However, because the Respondent's statements were deceitful, and were directly or

indirectly related to the investments made by these Investors, it constitutes a violation of TENN. CODE ANN. § 48–1–121(a)(2).

23. The Petitioner has shown, by a preponderance of the evidence, that Respondent committed acts which deceived and operated as a fraud upon two of the Investors by not being truthful about the amount of principal remaining for those two Investors. Respondent's actions in this regard have violated TENN. CODE ANN. § 48-1-121(a)(3).

Ponzi Scheme

24. In addition to the testimony from the Investors, and limited testimony from the Respondent, the State also relied on testimony from its investigator, Mr. William Sweeten. Mr. Sweeten is a securities examiner in the financial services investigative unit, having served in that capacity for just under two years, as of the time of the hearing. [TR. 138-139]. Prior thereto, Mr. Sweeten was an investigator for the Tennessee Department of Corrections (TDOC) where he prepared reports to assist in parole and probation determinations. [TR. 139]. Beyond his job title and previous experience with the TDOC, Mr. Sweeten's qualifications, training, and experience are unknown.

25. The proof regarding swing trading and the level of risk associated therewith consisted of brief testimony from Mr. Sweeten. According to Mr. Sweeten, day trading takes place in one day whereas swing trading takes two days to two weeks, which makes swing trading more risky. Mr. Sweeten's understanding of these terms and the risks of swing trading were said to have come from "Investopedia" and the "FCC." [TR. 170-171]. It is concluded that Mr. Sweeten's testimony falls short of establishing, by a preponderance of the evidence, that omissions about risks associated with swing trading, on Respondent's part, violated Tenn. Code Ann. § 48–1–121(a)(2).

26. The Petitioner's proof as to the allegation that the Respondent's activities constituted a Ponzi scheme came through the testimony of Mr. Sweeten. Mr. Sweeten considered the fact that the Respondent maintained more of the investor's funds in his First Tennessee Disbursement Account than the Respondent transferred into his trading account (the Scottrade account). According to Mr. Sweeten, this raised a concern that the monies were "possibly converted to personal use," and that there was "a deception, possibly." Mr. Sweeten also testified that the Respondent did use over $100,000 of the investor's funds for personal use. Mr. Sweeten further testified that the Respondent's promise of an 18% return, which Mr. Sweeten found to be a red flag, in and of itself, was similar to that of Charles Ponzi, who promised a 50% return. However, Mr. Sweeten was not in a position to testify about what the typical expected return would have been on the type of investing the Respondent was involved in during the time in question. [TR. 167-169; 202-204]. While the proof certainly raises the specter of impropriety, it is insufficient to show, by a preponderance of the evidence, that the Respondent's actions constituted a Ponzi scheme, resulting in a violation of TENN. CODE ANN. § 48–1–121(a)(1).

Respondent's Conveyance of Real Property to Wife

27. Petitioner asserts that the Respondent's transfer, by quitclaim deed, of the Respondent's interest in the home of the Respondent and his wife constitutes a violation of TENN. CODE ANN. § 48–1–121(a)(3). While the transfer may constitute a conveyance intended to defraud a potential creditor, such a transfer does not constitute a violation of TENN. CODE ANN. § 48–1–121(a)(3).

28. TENN. CODE ANN. § 48–1–121(d) provides:

> The commissioner may, after notice and opportunity for a hearing under the Uniform Administrative Procedures Act, compiled in title 4, chapter 5,

> impose a civil penalty against any person found to be in violation of this section, or any regulation, rule or order adopted or issued under this section, in an amount not to exceed five thousand dollars ($5,000) per violation.

29. While TENN. CODE ANN. § 48–1–121(d) was not enacted until April 23, 2010, the undersigned finds that this provision can be retroactively applied in this case. The statute in question is remedial as it provides a means by which a cause of action may be effectuated, a wrong addressed, or relief obtained. *Doe v. Sundquist*, 2 S.W.3d 919, 923 (Tenn. 1999) (citing *Dowlen v. Fitch*, 264 S.W.2d 824, 826 (Tenn. 1954)).

30. The application of the four-factor test set out in *Doe* shows there is no vested right impaired or destroyed by the statute in question. The public interest is advanced by the statute in question, which seeks to protect the public; the Respondent could have had no reasonable expectation that a monetary sanction would not follow a violation of securities law and likewise could not have been surprised by the enactment of the statute setting forth specific civil penalties; and the statute is remedial in nature. *See Id.* at 923-924.

31. The fact that the statute concerns state governance (also known as police powers) affords greater deference to the statute when determining whether it may be applied retroactively. *See, e.g., Shields v. Clifton Hill Land Co.*, 28 S.W. 668, 674 (Tenn. 1894); *Doe v. Sundquist*, 943 F.Supp. 886, 893 (M.D. Tenn. 1996); *American Traffic Solutions, Inc. v. City of Knoxville*, No. E2012-01334-COA-R3-CV, 2013 WL 5677342, at *6 (Tenn. Ct. App. 2013) (perm. app. denied, March 4, 2014).

32. Additionally, as found, *supra*, p. 24, ¶ 21, the Petitioner has proven that certain statements made by the Respondent after the enactment of TENN. CODE ANN. § 48–1–121(d) are violative of the law.

33. In any event, TENN. CODE ANN. § 48–1–112 would authorize the imposition of up to $5,000 in civil penalties, per violation, as it was in effect during the earliest time in question.

34. The Act does not establish factors to be considered when assessing civil penalties. As stated, *supra*, ftnt.18, the federal statutes are substantially similar and, therefore, federal law is found to be persuasive authority. Thus, the following factors will be considered: 1) the egregiousness of the violations; 2) the isolated or repeated nature of the violations; 3) the degree of scienter involved; and 4) the likelihood of the defendant's occupation will present opportunities (or lack thereof) for future violations.[23] *See U.S. S.E.C. v. Zada*, No. 10-CV-14498, 2014 WL 354502, at *3, ((E.D. Mich., January 31, 2014), *aff'd* 787 F.3d 375 (6th Cir. 2015) (citing *U.S. S.E.C. v. C.J.'s Financial*, No. 10-13083, 2012 WL 3600239, at *9 (E.D. Mich., July 30, 2012)).

35. It is determined that the misappropriation of funds, or conversion of funds to personal use, was particularly egregious – it cuts to the very heart of the fiduciary duty owed by the Respondent to the Investors. The failure to advise the Investors of potential risks involved is also egregious. These particular individuals were not savvy investors. They relied on the representations of the Respondent, who had been a licensed broker-dealer agent and insurance producer. They were often told that little, if any, risk was involved. While deceitful statements about remaining amounts of principal are arguably less egregious, they were certainly not inconsequential.

36. The misappropriation of funds, or conversion of funds, persisted for more than a year, involving 102 separate transactions. The failure to advise the investors of the potential

[23] Some federal cases also consider the following: 1) the sincerity of the defendant's assurances, if any, against future violations; 2) the defendant's recognition of the wrongful nature of his conduct; and 3) the defendant's age and health. The first two factors would seem to punish the defendant for maintaining his innocence and, therefore, were not considered. *See U.S. S.E.C. v. Zada*, 787 F.3d 375, 383 (6th Cir. 2015). No proof was introduced as to the Respondent's age or health.

risks extended over several years as more notes were signed and/or renewed. Deceitful statements about remaining principal amounts, while only made to two Investors, were repeated several times.

37. It is somewhat difficult to ascertain the level of scienter. On one hand, the Respondent maintains that the promissory notes were not securities – he did not believe that he was committing any wrongdoing. On the other, there is no question that he knowingly used the investors' money for his own personal gain. There is also little doubt that the Respondent knew his methods were more risky than he made known. The statements regarding remaining principal unquestionably involved a high level of scienter – the Respondent knew full well that he did not have the amounts of principal remaining that he represented.

38. Opportunities for other similar violations appear to be limited. It is highly unlikely that the Respondent could ever obtain a license to conduct similar activities in the securities industry. The Respondent is now fully aware that his actions were indeed violative of the Act. Therefore, it is determined to be doubtful that Respondent will repeat this behavior in the future.

39. Considering all the foregoing factors, it is concluded that the amount of $103,000 is an appropriate civil penalty for these violations, this amount sufficiently serving both a punitive and deterrent (general and specific) effect.

IT IS THEREFORE ORDERED that:

The Respondent is hereby assessed and shall pay a total of one hundred three thousand, dollars ($103,000) in **CIVIL PENALTIES**, pursuant to TENN. CODE ANN. §§ 48–1–112(d) and 48–1–121(d).

This INITIAL ORDER imposing sanctions against Respondent is entered to protect the

public and investors in the State of Tennessee, consistent with the purposes fairly intended by policy and provisions of the Act.

It is so ORDERED.

Entered and effective this the 19TH day of OCTOBER, 2017.

Phillip Hilliard / by EDC

PHILLIP R. HILLIARD
ADMINISTRATIVE JUDGE
ADMINISTRATIVE PROCEDURES DIVISION
OFFICE OF THE TENNESSEE SECRETARY OF STATE

Filed in the Administrative Procedures Division, Office of the Tennessee Secretary of State, this the 19TH day of OCTOBER, 2017.

J. Richard Collier

J. RICHARD COLLIER, DIRECTOR
ADMINISTRATIVE PROCEDURES DIVISION
OFFICE OF THE TENNESSEE SECRETARY OF STATE

APPENDIX A TO INITIAL ORDER
NOTICE OF APPEAL PROCEDURES

Review of Initial Order

This Initial Order shall become a Final Order (reviewable as set forth below) fifteen (15) days after the entry date of this Initial Order, unless either or both of the following actions are taken:

(1) A party files a petition for appeal to the agency, stating the basis of the appeal, or the agency on its own motion gives written notice of its intention to review the Initial Order, within fifteen (15) days after the entry date of the Initial Order. If either of these actions occurs, there is no Final Order until review by the agency and entry of a new Final Order or adoption and entry of the Initial Order, in whole or in part, as the Final Order. A petition for appeal to the agency must be filed within the proper time period with the Administrative Procedures Division of the Office of the Secretary of State, 8th Floor, William R. Snodgrass Tower, 312 Rosa L. Parks Avenue, Nashville, Tennessee, 37243-1102. (Telephone No. (615) 741-7008). See Tennessee Code Annotated, Section (T.C.A. §) 4-5-315, on review of initial orders by the agency.

(2) A party files a petition for reconsideration of this Initial Order, stating the specific reasons why the Initial Order was in error within fifteen (15) days after the entry date of the Initial Order. This petition must be filed with the Administrative Procedures Division at the above address. A petition for reconsideration is deemed denied if no action is taken within twenty (20) days of filing. A new fifteen (15) day period for the filing of an appeal to the agency (as set forth in paragraph (1) above) starts to run from the entry date of an order disposing of a petition for reconsideration, or from the twentieth day after filing of the petition, if no order is issued. See T.C.A. §4-5-317 on petitions for reconsideration.

A party may petition the agency for a stay of the Initial Order within seven (7) days after the entry date of the order. See T.C.A. §4-5-316.

Review of Final Order

Within fifteen (15) days after the Initial Order becomes a Final Order, a party may file a petition for reconsideration of the Final Order, in which petitioner shall state the specific reasons why the Initial Order was in error. If no action is taken within twenty (20) days of filing of the petition, it is deemed denied. See T.C.A. §4-5-317 on petitions for reconsideration.

A party may petition the agency for a stay of the Final Order within seven (7) days after the entry date of the order. See T.C.A. §4-5-316.

YOU WILL NOT RECEIVE FURTHER NOTICE OF THE INITIAL ORDER BECOMING A FINAL ORDER

A person who is aggrieved by a final decision in a contested case may seek judicial review of the Final Order by filing a petition for review in a Chancery Court having jurisdiction (generally, Davidson County Chancery Court) within sixty (60) days after the entry date of a Final Order or, if a petition for reconsideration is granted, within sixty (60) days of the entry date of the Final Order disposing of the petition. (However, the filing of a petition for reconsideration does not itself act to extend the sixty day period, if the petition is not granted.) A reviewing court also may order a stay of the Final Order upon appropriate terms. See T.C.A. §4-5-322 and §4-5-317.