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A06-1233

State of Minnesota
In Court of Appeals

Charles Risdall, Len Dozier, and John Risdall,
in his capacity as personal representative
of the Estate of Mary Risdall,

Respondents,

v.

Christopher C. Brown and funeral.com, inc.

Appellants.

REPLY BRIEF OF APPELLANTS
CHRISTOPHER C. BROWN AND FUNERAL.COM, INC.

Kay Nord Hunt (#138289)
LOMMEN, ABDO, COLE, KING
& STAGEBERG, P.A.
2000 IDS Center
80 South Eighth Street
Minneapolis, MN 55402
(612) 339-8131

George E. Antrim, III (#120534)
201 Ridgewood Avenue
Minneapolis, MN 55403
(612) 872-1313

Attorneys for Appellants

Scott D. Hillstrom (#15524X)
GUARDIAN LAW GROUP, LLC
527 Marquette Avenue, Suite 1800
Minneapolis, MN 55402
(612) 332-8063

Peter A. Koller (#150459)
MOSS & BARNETT, P.A.
4800 Wells Fargo Center
90 South Seventh Street
Minneapolis, MN 55402
(612) 877-5000

Attorneys for Respondents

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I. RESPONSE TO RESPONDENTS/PLAINTIFFS' STATEMENT OF THE FACTS.

Respondents/Plaintiffs (hereinafter Plaintiffs) are knowledgeable and accredited investors. They were given access to full and complete information regarding funeral.com before making their investment pursuant to PPM1. They have acknowledged, in writing, that they understood that investment in funeral.com was highly speculative and involved a high degree of risk. (A. 121-23, 127-28, 133-35, 145-47, 151-52.) Plaintiffs make no allegation that there was anything wrong with PPM1, through which they invested, but Plaintiffs allege there were problems with a later offering (PPM2), which they claim allows Plaintiffs to rescind their transaction.

Before the trial court, Plaintiffs asserted the following fact was not disputed:

> That "Plaintiffs purchased their shares in an offering *made pursuant to* Rule 506 of Regulation D promulgated under the federal securities laws." (Emphasis in the original.)

(Plaintiffs' Memorandum of Law in Opposition to Defendants' Motion for Summary Judgment, p. 3, dated June 17, 2005 (emphasis in the original).) Plaintiffs concede in their brief to this Court that PPM1, when made, in fact fully complied with Regulation D. (Respondents' Brief, p. 29.) It also stands undisputed that PPM2 was withdrawn and abandoned with no sales having been made under it. (A. 63.) The SEC has taken no action against Defendants based on their inadvertent possible violation of the no solicitation rule with regard to PPM2 and the SEC has not asserted that PPM1 and PPM2 should be treated as a single transaction under the doctrine of integration. (A. 112.)

It is only Plaintiffs who have asserted lack of Regulation D compliance based solely on their contention that subsequent offerings, specifically PPM2, are to be integrated with PPM1.[1] Only by accepting Plaintiffs' integration theory can the Court find any problem with PPM1. Plaintiffs claim that PPM1 did not comply with Regulation D because of what happened later with PPM2. (Respondents' Brief, p. 29.) Plaintiffs have cited no case that provides stock purchasers with the remedy of rescission under these facts.

Plaintiffs, on appeal, have not presented the facts of record in a light most favorable to Appellants/Defendants (hereinafter Defendants). Plaintiffs state as fact that PPM2 remained available on the website when PPM3 was issued on July 20, 2000. Actually, PPM2 was issued on May 17, 2000. (A. 109.) According to Ted Risdall, he directed the removal of PPM2 from the website on May 31, 2000. (A. 165.) PPM3 was not issued until July 20, 2000. (A. 117.)

Plaintiffs assert that the stated purpose for raising funds was "almost identical" under PPM1, PPM2 and PPM3. They are not "almost identical." Plaintiffs downplay the undisputed fact that it is only in PPM1, which is the stock offering under which Plaintiffs purchased their shares, that the use of the proceeds was designated as follows:

> If we sell the minimum number of Shares, we intend to use \$375,000 of the proceeds to repay a promissory note held by Christopher C. Brown, evidencing costs and expenses incurred by Mr. Brown for the development of the site design,

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[1] Such a claim is not made in Plaintiffs' Complaint and was made for the first time in their motion for summary judgment. (A. 41.)

> maintenance of the site and associated costs over the past four years.

(A. 82.)

Plaintiffs would also have the Court ignore the undisputed testimony of record that at the time of PPM1, Defendants believed PPM1 would be the only stock offering. (A. 63.) Subsequent stock offerings were necessitated based on the differing needs of funeral.com at the time the decisions to make those offerings were made. (*Id.*) In May 2000, funeral.com was told that Corio, a major website developer, needed millions of dollars to develop the funeral.com site. (*Id.*) This need made PPM2 necessary. (*Id.*)

II. FEDERAL LAW PREEMPTS PLAINTIFFS' STATE LAW CLAIM.

The National Securities Market Improvement Act of 1996 (NSMIA), 15 U.S.C. § 77r, amended Section 18(a) of the 1933 Act expressly to preempt any state Blue Sky laws requiring redundant state registration and qualification of any nationally offered and traded securities, defined by NSMIA as "covered securities." Section 18(a)(1)(A) of the 1933 Act – the NSMIA express preemption provision – specifically prohibits any state from requiring any federal "covered security" to be registered in the state:

> (a) Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any state or any political subdivision thereof –
>
> (1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that –
>
> (A) is a covered security; . . . .

This preemption provision advances the primary purpose of NSMIA, to eradicate the prior system of "dual registration" under both the 1933 Act as well as state blue sky laws for nationally traded securities:

> By 1996, Congress recognized the redundancy and inefficiencies inherent in such a system and passed NSMIA to preclude states from requiring issuers to register or qualify certain securities with state authorities . . .
>
> . . .
>
> When considered in concert, SLUSA, NSMIA and PSLRA demonstrate that Congress intended to provide national, uniform standards for the securities markets and nationally marketed securities. Through these statutes, Congress erected uniform standards for registration of, and litigation concerning, a defined class of securities.

Lander v. Hartford Life & Annuity Ins. Co., 251 F.3d 101, 108-12 (2d Cir. 2001). *Lillard v. Stockton*, 267 F. Supp. 2d 1081, 1115 (N.D. Okla. 2003) ("The NSMIA drafters intended the Act to eliminate the costs and burdens of duplicative and unnecessary regulation by designating the federal government as exclusive regulator of national offerings of securities."); *Temple v. Gorman*, 201 F. Supp. 2d 1238, 1244 (S.D. Fla. 2002) ("Congress expressed its intent in NSMIA that federal regulations alone should govern the registration of national securities offerings.").

Federal district courts have therefore dismissed a plaintiff's state law unregistered securities claims, since a state's registration requirement for "covered securities" is preempted by NSMIA and unenforceable, even when a plaintiff alleges that the defendant's Rule 506 offering was defective and did not qualify for exemption. *Temple*, 201 F. Supp. 2d at 1243-44; *Lillard*, 267 F. Supp. 2d at 1115; *Pinnacle Communications Int'l, Inc. v. American Family Mortgage Corp.*, 417 F. Supp. 2d 1073, 1087 (D. Minn. 2006).

Plaintiffs' response to these holdings is that "Defendants rely on a trio of discredited federal district court cases to try to support the proposition that an issuer need only claim sales were made 'pursuant to' Regulation D to trigger preemption of any state securities law claims." (Respondents' Brief, p. 32.) In other words, Plaintiffs would have this Court discredit a case issued in 2006 by the federal district court of Minnesota in *Pinnacle*, 417 F. Supp. 2d 1073, and instead rely on a split decision by the Alabama Supreme Court in *Buist v. Time Domain Corp.*, 926 So. 2d 290 (Ala. 2005), a decision of the Arkansas federal district court, and an unpublished decision of the Colorado federal district court.[2] (Respondents' Brief, p. 29.)

The majority in *Buist* rejected the reasoning of *Temple* and its progeny, claiming it to be ipse dixit despite the *Temple* court's analysis and reliance on the legislative history of the NSMIA. *Buist*, 926 So. 2d at 297.[3] Instead, the majority in *Buist* relied on a one-

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[2] While Plaintiffs assert that the federal district court decision out of Minnesota can serve only as persuasive authority, the Court must acknowledge that an Alabama state court case or unpublished decision of a federal district court should certainly not be given any more weight in this instance, considering the fact that a federal district court in Minnesota considering this issue very recently has come to an entirely different conclusion.

[3] Ipse dixit, literally, "he himself said it," means "something asserted but not proved," as in the case of a bare statement that a witness is a liar without any proof. Black's Law Dictionary 833 (7th ed. 1999). Ipse dixit is thus a critique on the quality of the evidence, rather than a court's legal skills of statutory construction.

page ruling by the Alabama Securities Commission, *In re Cherokee Energy Co.*, which, without analysis or citation to legal authority, opined that cold calls to Alabama residents nullified any exemption under Regulation D. *Id.* at 296.

Contrary to the Alabama Supreme Court's statements, the *Temple* court recited and relied specifically upon the legislative history and congressional intent of NSMIA, and *Lillard* cited federal court authorities as additional support for *Temple*'s statutory intent foundation. *Lillard*, 267 F. Supp. 2d at 115-16; *Temple*, 201 F. Supp. 2d at 1242-44. The Minnesota federal district court followed *Temple* and *Lillard* and adopted their analysis. *Pinnacle*, 417 F. Supp. 2d at 1087. Moreover, *Buist*'s concern focused more on the law of evidence and the shifting burdens of proof on summary judgment than on the law of securities regulation for its basic proposition that the burden is on the party asserting the registration exemption to prove it. *Buist*, 926 So. 2d at 298.

Here, Plaintiffs admit "as of the date [their sales to Plaintiffs] were made, the sales to Plaintiffs were made pursuant to Regulation D." (Respondents' Brief, p. 29.) There is no question that when Plaintiffs purchased the stock in question, they appreciated and understood that PPM1 was made pursuant to Regulation D. (A. 121-22, 127-28, 133-34, 145-46, 151-52.) Plaintiffs concede that if there had been no PPM2, they would agree that Regulation D would be available to Defendants. (Respondents' Brief, p. 29.)

As the record reflects, this case does not concern a sham Rule 506/Regulation D offering. There is no question that Defendants complied with Regulation D at the time of PPM1 and this is not a case where a party is merely asserting form over content. In *Buist*, the Alabama Supreme Court denied the exemption to the defendant because it submitted no evidence indicating the sale of securities was actually made in conformity with Regulation D. *Buist*, 926 So. 2d at 297-98.

The same analysis was conducted in *Hamby v. Clearwater Consulting Concepts, LLLP*, 428 F. Supp. 2d 915 (E.D. Ark. 2006). Specifically, in *Hamby*, the defendants contended the security at issue was a "covered security" even though no Form D was ever filed and argued that a mere statement in the Partnership Agreement was enough to provide an exemption. *Id.* at 919-20. The federal court in *Hamby* concluded that the defendants had not met their burden of proof. *Id.*

In *Grubka v. WebAccess Int'l, Inc.*, 2006 U.S. Dist. Lexis 44721 (Colo. Dist. Ct. 2006) (R.A. 6), another case cited by Plaintiffs, the court rejected *Temple* and asserted that a defendant cannot avoid liability under state law by declaring its alleged compliance with Regulation D. (R.A. 13.) According to this unpublished decision, "that a defendant could avoid liability under state law by declaring its alleged compliance with Regulation D is an unsavory proposition and could eviscerate the statute." *Id.* But what the federal district court ignores is that NSMIA expressly permits states to retain jurisdiction over fraudulent conduct. 15 U.S.C. § 77r(c)(1). *See also Faye L. Roth Revoc. Trust v. UBS Painewebbher, Inc*., 323 F. Supp. 2d 1279, 1299 (S.D. Fla. 2004). Accordingly, state law is not voided as the federal district court incorrectly suggests.[4]

[4] No allegation of fraudulent conduct remains in this case.

To accept Plaintiffs' unreasonably restrictive interpretation of NSMIA's express preemption of "covered securities" would defeat the entire purpose of NSMIA "that federal regulations alone should govern the registration of national securities offerings." *Temple*, 201 F. Supp. 2d at 1244. This case illustrates the need for preemption. Plaintiffs would have this Court void their purchase on the basis of a little understood integration doctrine which depends on the application of a multifaceted subjective test the precise parameters of which are uncertain. The integration doctrine's availability is essentially dependent on questions of fact varying with the facts of each situation with little precedent to guide the courts. Any issuer of a national securities offering, knowing that despite NSMIA it will be subject to liability under state unregistered securities laws for any violation of the myriad technicalities of Regulation D, would be well-advised to ignore NSMIA and do precisely that which Congress sought to avoid with the NSMIA preemption – file duplicate, costly and redundant registrations in every state in which its shares might be offered or sold, thereby placing an undue and unnecessary burden on capital formation and markets.

Plaintiffs' assertion runs contrary to the very purpose of NSMIA. The point is, PPM1 cannot be attacked. Plaintiffs made their purchase pursuant to it. Although Plaintiffs attack Defendants' activities after PPM2 was issued, no sales were made pursuant to PPM2. Plaintiffs' whole case is premised on a technical objection which had nothing whatsoever to do with Plaintiffs' investment. Plaintiffs' claim is preempted.

III. THERE CAN BE NO INTEGRATION BECAUSE THERE WERE NO SALES AS A RESULT OF PPM2.

Plaintiffs would have this Court ignore that in order to have integration there must be sales in the offerings sought to be integrated. (*See* Appellants' Brief, pp. 27-29.) Rule 502 of Regulation D of the securities laws clearly states that "All <u>sales</u> that are part of the same Regulation D offering must meet all of the terms and conditions of Regulation D." It further states that the determination as to "whether separate <u>sales</u> of securities are part of the same offering (i.e., are considered "integrated") depends on the particular facts and circumstances."

As stated in Respondents' Brief at page 19, the five-factor test created in SEC Rel. No. 33-4552 (November 6, 1962) is the sole method for evaluating whether individual offers and sales should be "integrated" for purposes of applying Regulation D and the related state exemption provisions. The factors to be considered in determining whether offers and sales should be integrated for purposes of the Regulation D exemptions all focus on actual <u>sales</u>. That test looks at the following factors:

(a) Whether the <u>sales</u> are part of a single plan of financing;

(b) Whether the <u>sales</u> involve issuance of the same class of securities;

(c) Whether the <u>sales</u> have been made at or about the same time;

(d) Whether the same type of consideration is being received; and

(e) Whether the <u>sales</u> are made for the same general purpose.

17 C.F.R. § 230.502(a); Securities Act Rel. No. 33-4552, 27 Fed. Reg. 11316 (Nov. 6, 1962) (emphasis supplied).

As also acknowledged in Respondents' Brief at page 19 n. 8, this five-factor test originally used the word "offerings" rather than "sales." Securities Act Rel. No. 33-4552. In response, Plaintiffs in a footnote merely cite two cases and one commentator who, without discussion, continue to use the term offering instead of sales. These citations did not address, nor was it relevant to their discussion, that the use of the word sales is now contained in 17 C.F.R. § 230.502(a).

Just because certain courts have continued to use the word "offerings" in discussing the current test does not make the change from "offerings" to "sales" of "no significance," as Plaintiffs assert. The fact is that the test uses the term "sales" – a term clearly defined in the Securities Act of 1933, and a term that is consistent with the wording of Rule 502. As set forth in Section 2(a)(3) of the Act:

> The term "sale" or "sell" shall include every contract of sale or disposition of a security or interest in a security, for value.

In contrast, the term "offering" is not defined in the Securities Act or Regulation D. By using the word "sales" it is clear when the integration test applies. The Court is not free to disregard the term "sales" in determining whether the integration doctrine applies to this case. The court cannot rewrite this test under the auspices of interpretation or construction. *McNeice v. City of Minneapolis*, 250 Minn. 142, 84 N.W.2d 232, 237 (1957); *Mattice v. Minnesota Property Ins. Placement*, 655 N.W.2d 336, 341 (Minn. Ct. App. 2002). Since there were no sales under Defendants' second offering, PPM2, the integration rules do not and cannot apply.

Contrary to Plaintiffs' insinuation, Rule 155, 17 C.F.R. § 230.155, supports this holding. Rule 155 was adopted January 26, 2001 and addresses a registered offering (where public solicitation is allowed) that follows an abandoned private offering, and a private offering that follows a withdrawn or abandoned registered offering. As noted, in both situations addressed by Rule 155, an abandoned offering is involved. A Rule 506 offering is included with the definition of a "private offering."

Rule 155 provides that a private offering of securities will not be considered part of an offering for which the issuer later files a registration statement if, among other things, no securities were sold in the private offering. Rule 155 further provides that an offering for which the issuer filed a registration statement will not be considered part of a later commenced private offering if, among other things, no securities were sold in the registered offering. It is clear that it is the "sales" and not "offers" that are important in determining whether two offerings should be integrated and treated as one.

Plaintiffs correctly note that the Commission explicitly stated that the adoption of Rule 155 was not intended to "affect traditional integration analyses." The five-factor test used in determining whether integration should apply refers to "sales" in the various factors. Rule 155 would not have an adverse impact on traditional integration analyses because it, too, focuses on "sales."

Plaintiffs have provided the Court with no case, and Defendants assert there is none, where the doctrine of integration has been applied to an offering where there were no sales. Since this case involves an abandoned offering in which no sales were made, integration should not apply.

IV. EVEN IF THE COURT DETERMINES ALL DEFENDANTS' OFFERINGS MAY BE INTEGRATED REGARDLESS OF WHETHER SALES WERE MADE, THE FACTS DO NOT SUPPORT INTEGRATION.

A. The Basic Premise Is That Financial Offerings Are Separable, Not Integrated.

Plaintiffs' claim for lack of compliance with Regulation D can be made only if the Court accepts Plaintiffs' theory that the doctrine of integration applies and PPM1's Regulation D status can be voided nunc pro tunc.

In presenting their argument to this Court, Plaintiffs ignore that a basic concept running throughout the Securities Act of 1933 is that the financial dealings of an issuer are separable. 15 U.S.C. § 77a, *et seq.* Plaintiffs instead leave the Court with the incorrect impression that financial dealings of an issuer are generally to be viewed as integrated rather than separable. That financial dealings of an issuer are separable is reflected in the provisions of Section 4 of the 1933 Act, which exempts certain transactions from the registration requirements of the 1933 Act. In addition, certain of the securities exemptions contained in Sections 3 and 4 of the 1933 Act are in fact administered by the SEC as transactional exemptions. For example, Section 4(2) of the 1933 Act exempts from the registration and prospectus delivery requirements of the 1933 Act "transactions by an issuer not involving any public offering." Section 3(a)(11) of the 1933 Act exempts from the registration and prospectus delivery requirements of the 1933 Act "any security which is part of an issue offered and sold only to persons resident in a single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business in such state or territory." Section 3(b) of the 1933 Act uses the word "issue" and "small amount involved or the limited character of the public offering."

The integration doctrine is simply a logical development of the notion that an issuer should not be allowed to circumvent the registration requirements of the 1933 Act by resorting to a claim of a combination of exemptions for a series of transactions that would otherwise appear to comprise a single offering requiring registration.

Plaintiffs cite *Donohoe v. Consolidated Operating Products Corp.*, 982 F.2d 1130 (7th Cir. 1992). *Donohoe* acknowledges this purpose of the integration doctrine, which was premised on the concern that exemptions not be misused. The integration doctrine was developed to address the situation where a seller breaks an offering into small pieces in order to avoid the requirements of Section 5. The doctrine of integration allows a court to decide whether the offerings and sales constitute a single transaction and to test the entire plan of financing against the conditions of an exemption.

Factually, in *Donohoe*, CPOCO offered limited partnership shares in CPOCO 1-4 pursuant to SEC Rule 505, 17 C.F.R. § 230.505, which permits relatively small offerings (of less than $5 million) to be made to 35 or fewer investors. Each of the four offerings satisfied the requirement of Rule 505 individually. The question before the court was whether the issuers of securities had done so to avoid the requirement of Section 5 by breaking offerings into small pieces. *Id.* at 1140.

In *Johnston v. Bumba*, 764 F. Supp. 1263 (N.D. Ill. 1991), another case cited by Plaintiffs, the factual situation was quite different than that before this Court. In that case, the plaintiffs brought suit seeking to collect on a promissory note which they alleged was executed and delivered by the defendant, Lincoln J. Bumba, in connection with Bumba's acquisition of an interest in a limited partnership known as Aqua Solar Associates, Ltd. This case was identical to 17 other suits brought by the plaintiffs against individuals who executed promissory notes in the venture. *Id.* at 1268. The court was considering a plaintiff's right to recover on the note in light of Bumba's contention that two violations of the securities laws occurred: the securities should have been registered but were not, and the securities were sold through the use of false statements and omissions of material facts. *Id.* at 1271. It was in that context that the court concluded the offerings should be considered a single integrated offering. It should be noted that the court also stated that "our disposition of this case would nevertheless be the same even if the Aqua Solar offering is considered alone." *Id.* at 1272, n. 7.

B. If the Same Facts Support Integration and Nonintegration, the Court Is Not Free on Summary Judgment to Find Integration.

1. Only five factors may be considered.

Before the trial court, Plaintiffs asserted integration depended on the application of the five-factor test contained in 17 C.F.R. § 230.502(a). (Plaintiffs' Memorandum of Law in Opposition to Defendants' Motion for Summary Judgment, p. 11, dated June 17, 2005.) Now, on appeal, Plaintiffs contend there are "additional factors" beyond the five-factor test which the Court should consider. (Respondents' Brief, pp. 27-28.) In addition to that assertion having not been raised below and therefore not properly before the Court, the only factors the Court may consider are contained in § 230.502(a). Applying the five factors to the facts of record, Plaintiffs are not entitled to summary judgment.

2. Court must view facts most favorable to Defendants.

If the same facts can support integration or nonintegration, the court is not free on summary judgment to find integration and grant summary judgment against Defendants. For example, one of the factors is whether the offerings proposed to be integrated are made for the same general purpose. If the general purpose is viewed as the enrichment of a common sponsor, then any offering of securities will be deemed to have been made for the same general purpose. On the other hand, if the proceeds for one offering are to be used for a distinct purpose such as to repay a promissory note, the offerings should not be viewed as being made for the same general purpose.

The same is true in considering whether the differing offerings are part of a single plan of financing. This can be viewed as a restatement of the question whether the offerings are being made for the same general purpose. If this factor is interpreted as being whether the offerings have as their common plan the furtherance of the sponsor's financial well-being, then any offering of securities will meet this test. To adopt Plaintiffs' theory of integration would result in all offerings being integrated, which is contrary to the general principle that financial dealings of an issuer are separable.

Another example is the factor of whether "the same type of consideration is to be received" from the different security sales. This will nearly always be answered in the affirmative in most contexts since most are sold, at least in part, for cash. Plaintiffs disagree with this contention, but Loss and Seligman, *Fundamentals of Securities Regulation*, Ch. 3.C.1., p. 362 (2004), a treatise which Plaintiffs cite, agrees with Defendants' analysis:

> The final factor, "same types of consideration," has rarely been of much significance in resolving whether two or more issues should be integrated for the simple reason that cash is the normal consideration in both integrable and nonintegrable offers.

Id. at 362.

C. Applying the Facts in a Light Most Favorable to Defendants, There Is No Integration.

1. The sales are not part of a single plan of financing and were not made for the same general purpose.

Plaintiffs would have this Court ignore the facts of record. In addressing whether the sales were made for the same general purpose and whether the sales are part of a single plan of financing, it cannot be ignored that the use of proceeds in PPM1 is different than the use of proceeds in the other PPMs. In PPM1, the offeree was informed that if the minimum number of shares were sold, $375,000 of the proceeds would be used to repay a promissory note held by Brown. (A. 82.) PPM1 raised $760,006. Accordingly, 50% of PPM1 was used for this sole purpose, which was not the purpose of any of the other offerings. $375,000 of the funds were available to funeral.com. Contrary to Plaintiffs' position, on summary judgment, the trial court is not free to infer that repaying a note to Chris Brown is for the same general purpose as providing funds to funeral.com and, therefore, integration applies. (*See* Respondents' Brief, p. 24.) If the purpose of the offerings is a factual question, it cannot be decided on summary judgment in favor of the moving party.

Plaintiffs assert that the federal district court's decision in *Livens v. William D. Witter, Inc.*, 374 F. Supp. 1104 (D. Mass. 1974), is distinguishable. It is not. In *Livens*, the plaintiff purchased securities from the defendant in unregistered transactions on five occasions between October 1967 and December 1968. To avoid the statute of limitations problems, plaintiff alleged that his purchases were part of a single integrated offering of securities of the bankruptcy company which began in October 1967 and extended until April 1970. The court stated as follows:

> Plaintiff's integration theory tracks SEC Interpretive Release No. 33-4552. Although not yet applied by a court in the context of the availability of an exemption under Section 4(2), there is no reason why it should not be if the facts warrant. In the instant case, some basis for integration appears in the facts that (a) for the most part the offerings were made for the same general purpose, and (b) the parties recognized that the first financing in October 1967 might be inadequate and additional financing might be required. On the other hand, everyone hoped and expected that the initial $630,000 would be sufficient to enable LPC [the bankruptcy company] to operate profitably . . . .
>
> Thereafter, each successive financing was expected by the defendants to be the last which would be required to make LPC self-supporting. A series of obstacles to profitability was encountered, many of them beyond the control of the company or the defendants who, incidentally, each invested $1,400,000 of their own funds . . . .

> The evidence simply did not show a single plan of financing.

Id. at 1107.

The case is noteworthy because of its emphasis on the "single plan of financing" factor, whose absence was evidenced by the fact that at the time of each offering no subsequent offering was being considered by the issuer.

In *Barrett v. Triangle Mining Corp.* [1975-76 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,438 (S.D.N.Y. 1976), the court likewise declined to integrate two separate sales of securities. The court stated:

> It does not appear that this second sale was part of the original plan of financing for the corporation. After totally unforeseen operating difficulties were encountered, six of the investors who were the most active were asked to contribute additional funds.

(A. 185.)

In direct contravention to the federal district courts' analyses in *Livens* and *Barrett*, Plaintiffs would also have this Court disregard the undisputed fact of record that at the time of PPM1, Defendants believed PPM1 was the only stock offering they would need. Like *Livens*, Defendants hoped and expected PPM1 would be the one and only offering. Subsequent stock offerings, however, were necessitated based on the differing needs of funeral.com at the time the decisions to make offerings were made. Following *Livens* and *Barrett*, there should be no integration.

Similarly, Plaintiffs would have the Court ignore that preferred shares, in addition to common shares, were sold. (Respondents' Brief, p. 25.) The Court cannot ignore that fact. As Loss and Seligman explain in their *Fundamentals of Securities Regulation*, at page 361:

> When different classes of securities, such as common stock and preferred stock, are offered, the courts and the Commission generally have not integrated.

Moreover, Loss and Seligman also recognize that "slight differences between two securities have nonetheless been held to justify nonintegration." *Id.* They offer the following example:

> For example, in *SEC v. Dunfee*, the court refused to integrate 6 percent notes payable in 20 monthly installments with 7 percent notes issued eight months later and payable in 36 months.

Id.

The district court was not free to state that the difference in price is "irrelevant." (A. 12.) Nor are Plaintiffs entitled to self-servingly assert that the preferred shares are not part of the integration so as to eliminate that fact from the analysis. (A. 11-12.)

The facts of record do not support integration.

V. REGARDLESS OF WHETHER THE OFFERINGS ARE DEEMED INTEGRATED, UNDER THE FACTS OF THIS CASE, PLAINTIFFS ARE NOT ENTITLED TO RESCIND THEIR TRANSACTION.

Rescission under Minn. Stat. § 80A.23, subd. 1 is an equitable remedy. The trial court, however, refused to address the equities before granting rescission. This is error.

The fact that Plaintiffs allege securities fraud in their Complaint is irrelevant to this appeal. They have voluntarily dismissed any claim of fraud. It is Defendants' position that Plaintiffs, in fact, never had a viable claim for securities fraud. (*See* Defendants'

Memorandum of Law in Opposition to Plaintiffs' Motions for Summary Judgment, pp. 6-7, dated June 16, 2005.)

The subscription agreements signed by Plaintiffs established their status as accredited investors, and the Plaintiffs acknowledged therein that the shares being acquired by them had not been registered and were being offered pursuant to exemptions from registration under the 1933 Act. They acknowledged in writing that they were given access to full and complete information regarding funeral.com, including the opportunity to meet with funeral.com officers and review any documents they desired. They attested that they were experienced and knowledgeable in financial and business matters, capable of evaluating the merits and risks of investing in the shares, and did not need or desire the assistance of a knowledgeable representative to aid in the evaluation of such risks. They specifically attested that they understood the investment in these shares is highly speculative and involves a high degree of risk. (A. 121-22, 127-28, 133-34, 145-46, 151-52.) The simple fact is that they have no claim for fraud.

The record stands undisputed that any purported solicitation with regard to PPM2 caused no harm to Plaintiffs. This is not a case of ill-gotten gains. It is a case where Plaintiffs clearly purchased exempt securities. They then argue a subsequent inadvertent error by Defendants, which had nothing to do with their purchase and which was committed after their purchase, can be used by them to protect themselves from their business judgment. To grant Plaintiffs a remedy under the Blue Sky laws is inappropriate and Plaintiffs are certainly not entitled to recovery in "equity." The grant of rescission should be reversed.

CONCLUSION

Appellants respectfully request that the trial court be reversed and this action ordered dismissed. In the alternative, if the Court finds a material issue of fact, the judgment must be reversed and the case remanded for further proceedings.

Dated: October 6, 2006

LOMMEN, ABDO, COLE, KING & STAGEBERG, P.A.

BY________________________

Kay Nord Hunt, I.D. No. 138289
2000 IDS Center
80 South Eighth Street
Minneapolis, MN 55402
(612) 339-8131

GEORGE E. ANTRIM, III, PLLC

George E. Antrim, III, I.D. No. 120534
201 Ridgewood Avenue
Minneapolis, Minnesota 55403
(612) 872-1313

Attorneys for Appellants

CERTIFICATION OF BRIEF LENGTH

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01, subds. 1 and 3, for a brief produced with a proportional font. The length of this brief is 5,295 words. This brief was prepared using Word Perfect 10.

Dated: October 6, 2006

LOMMEN, ABDO, COLE, KING & STAGEBERG, P.A.

BY______________________________

Kay Nord Hunt, I.D. No. 138289
2000 IDS Center
80 South Eighth Street
Minneapolis, MN 55402
(612) 339-8131

GEORGE E. ANTRIM, III, PLLC
George E. Antrim, III, I.D. No. 120534
201 Ridgewood Avenue
Minneapolis, Minnesota 55403
(612) 872-1313

Attorneys for Appellants