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BEFORE THE DIVISION OF SECURITIES
OF THE DEPARTMENT OF COMMERCE
OF THE STATE OF UTAH

IN THE MATTER OF: **NORTHSTAR ENERGY, INC.,** **LARRY M. KOONCE,** **PAUL M. ESPOSITO,** **Respondents.**	**MOTION FOR JUDGMENT ON THE PLEADINGS** **Docket No. SD 05-0041** **Docket No. SD 05-0042** **Docket No. SD 05-00043**

The Utah Division of Securities (Division), by and through counsel, and pursuant to Utah Code Ann. § 63-46b-1(4)(b), and Rule 56 of the Utah Rules of Civil Procedure, hereby moves for judgment on the pleadings against Respondents. The Division's motion is made and based on the accompanying memorandum of points and authorities.

Respectfully submitted this January 8, 2007.

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BEFORE THE DIVISION OF SECURITIES
OF THE DEPARTMENT OF COMMERCE
OF THE STATE OF UTAH

IN THE MATTER OF:	**MEMORANDUM OF POINTS AND AUTHORITIES IN OPPOSITION TO DISMISSAL, AND IN SUPPORT OF MOTION FOR JUDGMENT ON THE PLEADINGS**
NORTHSTAR ENERGY, INC., **LARRY M. KOONCE,** **PAUL M. ESPOSITO,** **Respondents.**	**Docket No. SD 05-0041** **Docket No. SD 05-0042** **Docket No. SD 05-00043**

STATEMENT OF RELEVANT FACTS

1. On August 15, 2005, the Utah Division of Securities (Division) initiated agency action against Northstar Energy, Inc., Larry M. Koonce, and Paul M. Esposito (collectively "Northstar"), by issuing an Order to Show Cause (OSC). *Utah R. Evid. 201 (administrative*

tribunal can take judicial notice).

2. The facts supporting the OSC were set forth in eleven separately numbered paragraphs as follows:

   a. Jurisdiction over the Respondents and the subject matter is appropriate in this matter because the Division alleges that Respondents violated § 61-1-7 (Registration before sale) of the Act, while engaged in the offer and sale of securities in Utah. *OSC ¶ 1.*

   b. Northstar Energy, Inc. (Northstar) is a Texas corporation with its principal place of business at 740 Lexington Drive in Plano, Texas. Northstar is an independent producer of oil. *OSC ¶ 2; see also Exhibit A.*

   c. Larry M. Koonce and Paul M. Esposito of Plano, Texas are the executive officers and directors of Northstar. *OSC ¶ 3; see also Exhibit A.*

   d. On July 14, 2005, the Division received a Form D from Respondents' attorney, Suzanne W. Fallon, in Dallas, Texas, in connection with Northstar's limited offering of equity for the Northstar Las Raices Multiwell Prospect Joint Venture (Las Raices offering). *OSC ¶ 4; see also Exhibit B.*

   e. According to its Form D, Respondents made a federal covered security notice filing pursuant to Regulation D, Rule 506 of the Securities Act of 1933 (the Securities Act). *OSC ¶ 5; see also Exhibit B.*

   f. According to the Form D, Respondents sold partnership interests to one non-accredited Utah investor for $14,355. *OSC ¶ 6; see also Exhibit B.*

g. According to Rule 506 of the Securities Act, to qualify for an exemption, offers and sales of a security must satisfy all the terms and conditions of Rules 501 and 502. Rule 502(c) of the Securities Act states that "neither the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general solicitation or general advertising." *OSC ¶ 7; see also Exhibit C.*

h. Gary Bowen, Securities Examiner at the Division, reviewed the contents of Northstar's website, and found the following information regarding Northstar's Las Raices offering:

i. "If you are interested in our most current offering, or future offerings, and would like to know if you qualify, you can either go to our guestbook and fill in your information or you can fill out our questionnaire and fax (972) 769-0880 or mail it to us at the address on the bottom of this page"; and

ii. **"The Northstar Las Raices Prospect**

Located in Webb County, Texas, this oil and gas drilling program includes four wells to be drilled inside of a currently producing field, each of the four wells will be drilled to a depth of 7,300 feet during the months of June and July 2005. Contact a Northstar associate for more info." *OSC ¶ 8; see also Exhibit D.*

i. The above-mentioned information on Northstar's web site constitutes general advertising of its limited offering. *OSC ¶ 9; see also Exhibit D.*

j. On or around August 1, 2005, Mr. Bowen contacted Respondents' attorney and gave her notice of Northstar's disqualification from a Rule 506 exemption and requested that the web site be shut down. *OSC ¶ 10; see also Exhibit E.*

k. As of August 5, 2005, the web site remained accessible to the public via the Internet. *OSC ¶ 11.*

3. On September 8, 2005, Northstar served an answer to the OSC.[1] *Utah R. Evid. 201 (tribunal can take judicial notice of this fact).* In its answer, Northstar set forth its own "statement of facts" in sixteen separately numbered paragraphs, not including subparts, followed by a "statement of law" and a request for dismissal on those facts. Northstar did not admit or deny the individually numbered paragraphs of the Division's OSC as required by statute. *Id.*

4. In the answer, Northstar admitted "that a joint venture interest was sold to an investor in Utah who was not an accredited investor as that term is defined in Rule 501(a)." *See*

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[1]The answer filed on behalf of Northstar was signed by Craig Ongley and verified by Suzanne Fallon, both attorneys in the office of Vial, Hamilton, Koch & Knox, a Texas law firm. Although a verified complaint is required when seeking an injunction under Rule 65A of the Utah Rules of Civil Procedure, neither Fallon nor Ongley filed a certificate of good standing from the State Bar of Texas as required by rule, Utah Admin. Code R151-46b-6; and the Utah Administrative Procedures Act (UAPA) does not mention verified complaints or answers, and the Division is not aware of any authority allowing or requiring verified answers in any context. The signature of an attorney already constitutes certification under both Utah Admin. Code R151-46b-7(3) and Rule 11, and unless Fallon is a witness or Northstar intended its answer to be something in the nature of a verified counterclaim, the verification seems duplicative of what an attorney certifies to under the rule. *See Utah Admin. Code R151-46b-7(3); see also Utah R. Civ. P. 11(b).* UAPA does not allow parties to file counterclaims.

Northstar's Answer, Statement of Facts, ¶ 7.

5. On December 22, 2006, Northstar served a motion to dismiss. *Utah R. Evid. 201 (tribunal can take judicial notice of this fact).* As grounds for dismissal, Northstar repeats nine of the sixteen separately numbered paragraphs in Northstar's answer in substantially the same form in a subsection styled "Background." See *Background ¶¶ 1-9;* compare *Answer ¶¶ 3-6, 8-12.*[2] Northstar provides no record cite or documentary support for any of those facts.[3] Id.

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[2]Paragraphs 1 and 3 of the Background contain additional allegations. Paragraph 1 adds the statement that Northstar acts a managing venturer in certain joint ventures, while paragraph 3 adds the statement that the Las Raices JV is managed by Northstar in return for interest and a fee. Paragraphs 10-12 purport to state the claims in the OSC. Paragraph 13 states when Northstar filed its answer. In Paragraph 14, Northstar states it unsuccessfully sought guidance from the Division. In Paragraph 15, Northstar acknowledge receipt of discovery from the Division. Paragraph 16 purports to recount what was discussed at a telephonic hearing at which Mr. Ongley was not present. Paragraph 17 acknowledges receipt of a letter from the Division about its position on IPONET and Lamp Technologies. The allegations in ¶¶ 13-17 are not relevant to a determination of jurisdiction or any of the issues raised by Northstar in its motion to dismiss. Northstar's characterization of the allegations in the OSC are likewise irrelevant. The allegations in the OSC speak for themselves. Because the statements in ¶¶ 10-17 of Northstar's "Background" are irrelevant and unsupported, they should be stricken.

[3]Northstar's motion to dismiss is accompanied by an affidavit of Paul Esposito (Esposito). The affidavit contains five separately numbered paragraphs, none of which correspond to or support any of the seventeen numbered paragraphs in "Background" except ¶ 2. See "Backround"¶ 2 ("Larry M. Koonce and Paul M. Esposito, Jr. Are executive officers and directors of Northstar"); compare Esposito Affidavit ¶ 3 ("Larry Koonce and I are the executive officers and directors of Northstar Energy, Inc."). In paragraphs 4-5 of his affidavit, Esposito states Northstar is not the issuer, but is the managing venturer of Northstar Las Raices Multiwell Prospect Joint Venture (Las Raices JV). Although the Rule 506 Form D filed by Fallons says Las Raices is a partnership, it is not a legal entity and has no legal existence. Exhibit A. Joint ventures are general partnerships. Utah Code Ann. § 48-1-3.1. Under the Utah Uniform Securities Act, partners are liable. Utah Code Ann. § 61-1-22(4); see also Utah Code Ann. § 48-1-12(1)(partners jointly and severably liable). Whether Northstar is an "issuer" is a statement of

LAW AND ARGUMENT

I The Division Has Subject Matter Jurisdiction

A. The Allegations In The OSC Should Be Accepted As True, And Deemed Admitted

Because granting a motion to dismiss deprives a party of having his day in court, *Baur v. Pacific Finance Corp., 14 Utah 2d 283, 284, 383 P.2d 397 (Utah 1963)*, a motion to dismiss should not be granted unless there are no set of facts on which a plaintiff would ever be entitled to relief. *Heiner v. S. J. Groves & Sons Co., 790 P.2d 107, 109-10 (Utah App. 1990)*. In a ruling on a motion to dismiss, courts accept "as true the factual allegations of the complaint and drawing all inferences in the plaintiff's favor." *Hunter v. Sunrise Title Co., 2004 UT 1, ¶ 6, 84 P.3d 1163*. Courts also look past whatever label a party gives a motion to dismiss "to its substance and treat it accordingly." *Grossen v. DeWitt, 1999 UT App 167, ¶ 6, 982 P.2d 581; accord In re Adoption of Baby K., 967 P.2d 947, 948 n. 1 (Utah App.1998)*.

If a party presents matters outside the pleadings in its motion, as Northstar does in this case, and asks for a final judgment on the merits, the motion is treated like a motion for summary judgment, and the requirements of Rule 56 apply. *Utah R. Civ. P. 12(c)*. The rules governing summary judgment require each fact to supported by citation to relevant materials, such as affidavits or discovery. *Utah R. Civ. P. 7(c)(e)(A)*. Unsupported conclusory statements are not evidence. *Hardman v. Bennett, 362 F.3d 676, 680 (10th Cir. 2004); see also Perkins v. Freedom of Information*

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law, legal argument, but not fact. The statement should be stricken.

Commission, 228 Conn. 158, 176, 635 A.2d 783 (1993)(unsupported statements of counsel not evidence). The rules governing summary judgment do not allow a party to support or oppose summary judgment on unsupported allegations.

In this case, none of the seventeen individually numbered paragraphs in the subsection of Northstar's memorandum styled "Background" are supported by any relevant material. They are completely unsupported. The administrative tribunal cannot consider any of them. In ruling on Northstar's motion to dismiss, the administrative tribunal must accept, as true, the allegations in the Division's OSC for the additional reason that Northstar has not claimed there are no set of facts on which the Division could ever prevail. Finally, because Northstar never denied the allegations in the Division's OSC, they are deemed admitted. *Utah R. Civ. P. 8(d).*

B. Federal Preemption Does Not Deprive The Agency of Subject Matter Jurisdiction.

Subject matter jurisdiction goes to the power of a court to hear a case or controversy. See In re Compl. of Pelland, 658 N.W.2d 849, 854 (Mich App. 2003)(subject matter jurisdiction concerns a body's abstract power to hear a case of the kind or character of the one pending, and is not dependent on the particular facts of the case). Because subject matter jurisdiction is a prerequisite to a court's power to consider the substantive issues, issues relating to subject matter jurisdiction are a threshold consideration that need to be addressed before resolving other claims. *Housing Authority of Salt Lake County v. Snyder, 2002 UT 28, ¶ 11, 44 P.3d 724; see also Chen v. Stewart, 2004 UT 82, ¶ 34, 100 P.3d 1177; Barnard v. Wassermann, 855 P.2d 243, 248 (Utah 1993).*

Subject matter jurisdiction is determined, under the well-pleaded complaint rule, by examining the allegations as they appear on the face of the complaint filed in state court, *Franchise Tax Bd. v. Constr. Laborers Vacation Trust, 463 U. S. 1, 9-10, 103 S. Ct. 2841, 77 L.Ed.2d 420 (1983)*; "unaided by anything alleged in anticipation or avoidance of defenses." *Taylor v. Anderson, 234 U. S. 74, 75-76, 34 S. Ct. 724, 58 L.Ed. 1218 (1914); Caterpillar, Inc. v. Williams, 482 U.S. 386, 392, 398-99, 107 S.Ct. 2425, 2430, 2433, 96 L.Ed.2d 318 (1987)(explaining "well-pleaded" complaint rule).*

In this case, the basis for jurisdiction can easily be determined on the face of the OSC. The Division alleged a violation of the Utah Uniform Securities Act under Utah Code Ann. § 61-1-7, not federal law. Section 61-1-7 of the Act states

> It is unlawful for any person to offer or sell any security in this state unless it is registered under this chapter, the security or transaction is exempted under Section 61-1-14, or the security is a federal covered security for which a notice filing has been made pursuant to the provisions of Section 61-1-15.5.

Utah Code Ann. § 61-1-7.

Except in the case of complete preemption, preemption is not a jurisdictional issue, and preemption does not deprive the agency of subject matter jurisdiction.[4] Because the Division alleges

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[4]The only time where federal preemption deprives a state court of subject matter jurisdiction is in the case of field or complete preemption. Zuri-Invest AG v. Natwest Finance Inc., 177 F. Supp.2d 189, 191-92, 195 (S. D. N. Y. 2001). NSMIA does not completely preempt state law.

> Few statutes possess the 'extraordinary pre-emptive power' required to occupy a field of law so entirely as to characterize any

a violation of state law and the Utah legislature gave the agency subject matter jurisdiction to determine violations of state securities laws, Northstar's motion to dismiss on jurisdictional grounds should be denied. Northstar cites no authority that holds federal preemption is a jurisdictional issue, and cites no authority that NSMIA completely preempts state law.

C. Northstar Does Not Qualify For An Exemption Because Its Website Constitutes A General Solicitation And/Or Advertisement.

Northstar contends that the National Securities Markets Improvements Act (NSMIA) prohibits the States from requiring Regulation 506, Form D notice filings, and thus, from any regulation of federal covered securities. Northstar relies on Temple v. Gorman, 201 F. Supp.2d 1238 (S. D. Fla. 2002) and its progeny Lillard v. Stockton, 267 F. Supp.2d 1081 (N. D. Ok. 2003), Pinnacle Comm'ns Internat'l., Inc. v. American Family Mtg. Corp., 417 F.Supp.2d 1073 (D. Minn.

> claims arising there under as federal.' The NSMIA is not one of those few. It is well-settled law that federal law does not enjoy complete preemptive force in the field of securities. State securities laws exist in every state, the District of Columbia, and Puerto Rico, and, far from preempting the field, Congress has expressly preserved the role of the states in securities regulation. The states enjoy broad powers to regulate such diverse subjects as . . . fraud in the sale or purchase of securities and the rendering of investment advisory services. Given the concurrent nature of federal/state jurisdiction over securities, the NSMIA clearly lacks the complete preemptive force needed for field preemption.

Zuri-Invest AG v. Natwest Finance Inc., 177 F.Supp.2d 189, 195 (S. D. N. Y. 2001)(internal citations omitted); see also Patterman v. The Travelers, Inc., 11 F. Supp. 2d, 1382 (S. D. Ga. 1997)("Neither the text of the statute nor its legislative history manifest Congress' intent to completely pre-empt state law claims within NSMIA's scope.").

2006). Northstar also contends that the SEC's No-Action letters in IPONET and Lamp Technologies applies to issuers, offering their own securities. IPONET and Lamp Technologies applied to intermediaries, not issuers. Northstar does not claim to be an intermediary and cites no authority that extends IPONET and Lamp Technologies to issuers. Likewise, Northstar cites no authority that the opinion of a federal district court decision is controlling in this forum. *See Buist v. Time Domain, 926 So.2d 290, 297 (Ala. 2005)(criticizing Temple and Lillard for lack of analysis, failure to cite case law or other supporting authority, and announcing an ipse dixit – because we said it – ruling); see also Blue Flame Energy Corp. v. Ohio Dep't of Commerce, 2006 WL 3775856, ¶ 39, (Ohio App. 10 Dist. Dec. 26, 2006)(criticizing Temple for supplanting plain language of Section 77r)* [5].

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[5]Blue Flame also criticized Temple for trying to infer legislative intent when there was none.

> We find *Temple* and its progeny unpersuasive. In order to reach its holding, the *Temple* court supplanted the plain language of Section 77r with its own reading of the statute. As we stated above, a security is covered if it " *is exempt* from registration," not if it is sold *pursuant to* a putative exemption. Section 77r(b)(4), Title 15, U.S.Code (emphasis added). Although the *Temple* court relied upon legislative intent in crafting its alternative reading of Section 77r, intent is irrelevant if the statute is unambiguous. *Hughes Aircraft Co. v. Jacobson* (1999), 525 U.S. 432, 438, 119 S.Ct. 755 ("As in any case of statutory construction, our analysis begins with 'the language of the statute.' And where the statutory language provides a clear answer, it ends there as well."). Appellees do not point to, and we cannot find, any ambiguity in Section 77r.
>
> Further, we decline to follow *Temple* because, as other authorities have recognized, the *Temple* court's reading of Section 77r would

Nevertheless, even though preemption is not a jurisdictional issue, Northstar is partly correct about preemption: in 1996, Section 18 of the Securities Act was amended by NSMIA to do away with the need for dual registration of certain securities with both state and federal governments on certain conditions, one being that the security is a "covered security." Buist, *926 So.2d at 294 (citing 15 U.S.C. § 77r(a)(1)); Blue Flame (federal covered securities are exempt from state regulation, and state law is preempted to the extent it attempts to regulate the issuance and sale of a covered security).*

In order to be a "covered security," however, the transaction must be eligible for an exemption under SEC rules and regulations promulgated under Section 4(2) of the Securities Act. Buist, *926 P.2d at 294 (citations omitted).* Rule 506 of Regulation D is the only rule or regulation promulgated by the SEC under Section (4)(2) to date. To qualify for an exemption pursuant to Rule 506, the offer and sale cannot involve a "public offering," and "must satisfy all the terms and

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> allow an issuer to avoid any state regulation or liability under state law simply by claiming compliance with Regulation D. *Grubka v. WebAccess Internatl., Inc.* (D.Colo.2006), 445 F.Supp.2d 1259, 1270; 12 Long, Blue Sky Law (2006), Section 3:81, fn. 7 ("If all that was required for preemption was a bald-face statement that the offering was made under Rule 506, then any con artist could avoid state registration by telling the investor that the offering was a private placement under Rule 506."); Cohn, Securities Counseling for Small and Emerging Companies (2006), Section 6:24.50 ("Unless courts require at a minimum a bona fide effort to comply with [R]ule 506, the mere assertion of form would control, and sham Rule 506 offerings would be exempt from state registration or exemption laws.").

Blue Flame, ¶¶ 43-44

conditions" of Rule 501 and 502. *17 C.F.R. § 230.506(b)(1)).* Under the plain language of Rules 501 and 502, purchasers must be "accredited investors" (or "sophisticated non-accredited investors") and the issuer cannot use any form of general solicitation or general advertisement.[6]

> [N]either the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general advertising, including, but not limited to, the following:
>
> > (1) Any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio.
> >
> > . . .

17 C.F.R. § 230.502(c).

Posting information about an offering on an unrestricted website constitutes a public offering, and general solicitation. *Blue Flame, 2006 WL 3775856, ¶¶ 50-52.* If an issuer fails to satisfy the conditions of the exemption, the stock is no longer a covered security, state regulation is not preempted, and the state may require registration. *See id. at ¶ 39, 50-56.*

In this case, Northstar made a public offering to non accredited investors by offering its own

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[6]Rule 506 also imposes two, specific conditions:

> "First, no single offering, as defined in Rule 502(a), may involve more than 35 purchasers, as 'purchaser' is defined in Rule 501(3). 17 C.F.R. § 230.506(b)(2)(i). Second, any purchase must be either an 'accredited investor' as defined by Rule 501(a), his purchase representative must so accredited, the purchase must have some sophistication in investing, or the issuer must reasonably believe that the purchaser is so knowledgeable immediately before selling the security to the purchaser. 17 C.F.R. § 230.506(b)(2)(ii).

Buist at 295.

stock on a public website. Offering the sale of securities on a website constitutes general solicitation and general advertising. Because Northstar made a general solicitation and public offering, and sold to a non accredited investor, it is ineligible for an exemption.[7]

CONCLUSION

In summary, in order to be a federal covered security under NSMIA, all conditions of the Act – general and specific – must be met. The burden of establishing an exemption rests on the party claiming it. *Buist at 296 (citations omitted).* Northstar failed to establish its eligibility for an exemption, and cannot do so because it made a public offering by general advertisement and sold to an unaccredited investor. For these reasons, the Division is entitled to judgment on the pleadings.

Respectfully submitted this January 8, 2007.

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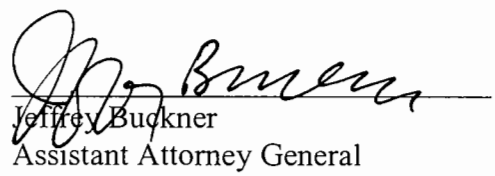
UTAH ATTORNEY GENERAL



Jeffrey Buckner
Assistant Attorney General

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[7]Likewise, Northstar's reliance on Temple is misplaced for the additional reason that there is no allegation – or proof – that it ever filed a Form D with the SEC. *Temple, 201 F. Supp. 2d at 1244.* Thus, there is conflict because there is no dual registration in this case.

CERTIFICATE OF MAILING

I, Ina Jensen, hereby certify that I have this day served a copy of the foregoing **Motion for Summary Judgment, Memorandum of Points and Authorities in Opposition to Motion to Dismiss, and in Support of Motion for Summary Judgment** to Respondents by mailing a copy, with postage prepaid, to:

Craig G. Ongley
Vial, Hamilton, Koch & Knox, LLP
1700 Pacific Avenue, Suite 2800
Dallas, TX 75201

Dated this 8th day of January 2007.

Ina Jensen