UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,
Plaintiff,

v. **Case No. 09-cv-3333 (MJD/FLN)**

TREVOR G. COOK, et al.,
Defendants,

R.J. ZAYED,
Receiver.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,
Plaintiff,

v. **Case No. 11-cv-574 (MJD/FLN)**

JASON BO-ALAN BECKMAN, et al.,
Defendants,

R.J. ZAYED,
Receiver.

PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S MEMORANDUM OF LAW IN SUPPORT OF ITS MOTION FOR SUMMARY JUDGMENT AGAINST DEFENDANTS KILEY AND BECKMAN

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Pursuant to Federal Rule of Civil Procedure 56(a), plaintiff Securities and Exchange Commission ("SEC") respectfully submits this memorandum of law in support of its motion for summary judgment against defendants Jason Bo-Allen Beckman ("Beckman") and Patrick Joseph Kiley ("Kiley") (together, "Defendants") in these two companion cases.

I. RELEVANT PROCEDURAL HISTORY

On November 23, 2009 and March 7, 2011, the SEC filed its Complaints in these two actions. The SEC charged Kiley and Beckman with conducting a massive, fraudulent securities offering. Specifically, the SEC alleged that Kiley and Beckman, together with others acting in concert with them, raised over $190 million from more than 1,000 victims by selling interests in a purported foreign currency trading venture. (Declaration of John E. Birkenheier ("Birkenheier Dec."), Ex. 1, Complaint, *SEC v. Trevor G. Cook, Patrick J. Kiley, et al.*, 09-cv-0333, Doc. # 1; Ex. 2, Complaint, *SEC v. Jason Bo-Alan Beckman, et al.*, 11-cv-574, Doc. # 1.)

In a subsequent, parallel criminal action, Kiley and Beckman were charged, *inter alia*, with mail fraud and wire fraud based on the same facts that underlay the SEC's civil actions. (Birkenheier Dec., Ex. 3, Second Superseding Indictment, *United States v. Beckman, et al.*, 11-cr-228, Doc. #162.) After trial, a jury found Kiley and Beckman guilty on all Counts. (*Id.*, Ex. 4 and 5, Verdict Forms, *United States v. Beckman, et al.*, Doc. ## 303 and 307.) Kiley and Beckman were subsequently sentenced to lengthy prison terms and ordered to pay more than $155 million of restitution. (*Id.*, Ex. 6 and 7, Judgments, *United States v. Beckman, et al.*, 11-cr-228, Doc. ## 397 and 438.)

II. STATEMENT OF UNDISPUTED FACTS

A. THE SEC'S COMPLAINTS

The SEC's Complaints against Kiley and Beckman allege that:

- Kiley and Beckman committed fraud in violation of Section 17(a) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. § 77q(a)], Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5],
- Beckman committed fraud in violation of Sections 206(1) and 206(2) of the Investment Advisers Act of 1940 ("Advisers Act") [15 U.S.C. §§ 80b-6(1) and 80b-6(2)], and
- Kiley and Beckman offered and sold securities without registration, in violation of Sections 5(a) and 5(c) of the Securities Act [15 U.S.C. §§ 77e(a) and 77e(c)].

(*Id*., Ex. 1 and 2.)

Specifically, the SEC alleges that from at least July 2006 through July 2009 the Defendants and several associates took in a total of at least $190 million from at least 1,000 victims. (*Id*., Ex. 1, ¶ 3; Ex. 2, ¶ 3.) The Defendants perpetrated their fraud through the fraudulent sale of investments in a purported foreign currency trading venture. (*Id*., Ex. 1, ¶¶ 3-6; Ex. 2, ¶¶ 3-4.) Beckman acted through The Oxford Private Client Group, LLC, a registered investment adviser of which he was the managing member. (*Id*., Ex. 2, ¶¶ 25 and 26; Ex. 8, Registration Status Report for The Oxford Private Client Group, LLC (*SEC v. Beckman*, Doc. # 4.5, pp. 20-21).) Therefore,

Beckman's alleged fraud violated the Advisers Act as well as the Securities Act and Exchange Act. (*Id*., Ex. 2, Counts V and VI.)

Among other things, the SEC alleges the Defendants falsely represented that the investors' money would be deposited into segregated accounts held in the investors' respective names, could be withdrawn at any time, would be used to finance trading by the Defendants and their associates in foreign currencies, and would generate annual returns of 10% to 12% with little or no risk. (*Id*., Ex. 1, ¶¶ 4-5; Ex. 2, ¶ 8.)

The Defendants' representations were all false and misleading. The truth was that the investors' money was commingled in accounts belonging to Defendants and their associates. (*Id*., Ex. 1, ¶¶ 7-8; Ex. 2, ¶ 12.) Tens of millions of dollars in investor funds were diverted to the benefit of the Defendants and their associates. (*Id*., Ex. 1, ¶¶ 9-12; Ex. 2, ¶¶ 5-6, 9.) Investors were not able to withdraw their money at any time. (*Id*., Ex. 1, ¶ 5-6; Ex. 2, ¶ 14.) And the foreign currency trading that did take place resulted in losses of more than $60 million. (*Id*., Ex. 1, ¶ 13; Ex. 2, ¶¶ 10, 11, 13.) To conceal their fraud while continuing to raise new money from investors, the Defendants and their associates lulled investors with false account statements and payments of purported returns that in truth were funded by newly raised investor money. (*Id*., Ex. 1, ¶¶ 14; Ex. 2, ¶¶ 97.)

B. THE PARALLEL CRIMINAL ACTION

On July, 19, 2011, Kiley and Beckman were indicted for their roles in the offering fraud that led to the SEC's two civil actions. *United States v. Beckman, et al.*, 11-cr-228. A Second Superseding Indictment was filed against them on February 2, 2012.

(Birkenheier Dec., Ex. 3.) The Second Superseding Indictment charged Kiley and Beckman with fraudulently soliciting investors for the foreign currency trading program. (*Id*., Ex. 3, ¶¶ 11, 12.) Specifically, Kiley and Beckman were alleged to have represented that their currency trading program earned double-digit returns, typically 10.5% to 12% annually (*Id*., Ex. 3, ¶ 13); the currency trading program was so safe that investors could not lose their principal and could withdraw their assets at any time (*Id.*); and individual investors' funds would not be commingled but would be held in segregated accounts. (*Id.*) The indictment also charged that Kiley and Beckman lulled investors by sending the investors false and misleading account statements which, among other things, falsely reported that the investors were receiving the returns promised by the Defendants. (*Id*., Ex. 3, ¶¶ 15-16.) According to the indictment, not all the investors' money was used to finance currency trading. (*Id*., Ex. 3, ¶ 19.) Instead, millions of dollars was diverted to pay compensation, personal expenses, and investments of the Defendants (*Id*., Ex. 3, ¶ 19), and to make lulling payments to investors. (*Id.*) The indictment also charged that the Defendants actually did use some investor money to trade foreign currency, but that trading was risky and oftentimes resulted in significant losses to investor assets. (*Id*., Ex. 3, ¶ 21.) Finally, the indictment alleged that the Defendants and their associates acted through several companies, including The Oxford Private Client Group, LLC. (*Id*., Ex. 3, ¶ 7.)

After trial, a jury returned a verdict and found Kiley and Beckman guilty on all the Counts charged against them. (*Id*., Ex. 4, 5.) This Court subsequently sentenced Kiley

and Beckman to lengthy prison terms and ordered them to pay more than $155 million of restitution. (*Id.*, Ex. 6. 7.)

III. ARGUMENT

In light of their criminal convictions, Kiley and Beckman are estopped from contesting the SEC's allegations, and thus, there is no genuine issue with respect to any aspect of the SEC's Complaints against them. Accordingly, the Commission is entitled to summary judgment on all charges against Defendants. Furthermore, based on the Defendants' egregious conduct, high degree of scienter and culpability, and continuing defiant conduct, Defendants should be enjoined from future violations of the federal securities laws.

A. THE SEC IS ENTITLED TO SUMMARY JUDGMENT AS A MATTER OF LAW

1. Legal Standards for Summary Judgment and Collateral Estoppel

A district court "shall grant summary judgment" if the movant demonstrates that there is "no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." *See* Fed. R. Civ. P. 56(a). For purposes of summary judgment, "[a] dispute is genuine if the evidence is such that it could cause a reasonable jury to return a verdict for either party, a fact is material if its resolution affects the outcome of the case." *Johnson v. St. Paul Plumbing & Heating Co., 2014 U.S. Dist. LEXIS 177714,5, 2014 WL 7399119 (D. Minn. 2014) (citing Amini v. City of Minneapolis, 643 F.3d 1068, 1074 (8th Cir. 2011) (citing Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 252, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986))* Once the movant establishes that there is no genuine

issue of material fact, the opposing party "may not rest upon mere allegations or denials, but must set forth specific facts showing that there is a genuine issue for trial." *Becker v. Int'l Bhd. of Teamsters Local 120, 2012 U.S. Dist. LEXIS 156389, 6-7 (D. Minn. 2012) (citing to Krenik v. County of Le Sueur, 47 F.3d 953, 957 (8th Cir.1995)*. The non-moving party cannot satisfy that burden by merely showing "some metaphysical doubt as to the material facts." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986).

Under the doctrine of collateral estoppel, a party is not permitted to relitigate matters that he already has litigated and lost in a prior proceeding. The Eighth Circuit holds that collateral estoppel precludes relitigation of issues in a subsequent proceeding if the following elements are met: (1) the issue sought to be precluded must be the same as that involved in the prior litigation; (2) that issue must have been actually litigated; (3) it must have been determined by a valid and final judgment; and (4) the determination must have been essential to the judgment. *Lovell v. Mixon,* 719 F.2d 1373, 1376 (8th Cir. 1983).

"It is well established that prior criminal proceedings can work as estoppel in a subsequent civil proceeding so long as the question involved was 'distinctly put in issue and directly determined' in the criminal action." *McNally v. Pulitzer Pub. Co.*, 532 F.2d 69, 76 (8th Cir. 1976) (*quoting Emich Motors Corp. v. General Motors Corp.*, 340 U.S. 558, 568-69 (1951)); *Williams v. Liberty*, 461 F.2d 325, 327 (7th Cir. 1972); *Kauffman v. Moss*, 420 F.2d 1270, 1274 (3d Cir. 1970), *cert. denied*, 400 U.S. 846 (1970). *See also Gelb v. Royal Globe Insurance Co.*, 798 F.2d 38, 43 (2d Cir. 1986), *cert denied*, 480 U.S.

948 (1987) ("The Government bears a higher burden of proof in the criminal than in the civil context and consequently may rely on the collateral estoppel effect of a criminal conviction in a subsequent civil case"); *SEC v. Blackwell*, 477 F. Supp. 2d 891, 899 (S.D. Ohio 2007) ("the prevalence of estoppel in civil cases following their criminal counterparts is due in part to the court's desire to avoid inconsistent verdicts in light of the higher burden of proof required in the prior criminal case").

Thus, courts have frequently entered summary judgment in favor of the SEC against a defendant based upon the collateral estoppel effects of the defendant's conviction in a parallel criminal case. *See, e.g.*, *SEC v. Gruenberg*, 989 F.2d 977 (8th Cir. 1993); *SEC v. O'Hagan*, 901 F. Supp. 1461, 1466 (D. Minn. 1995); *Smith v. SEC*, 129 F.3d 356, 362 (6th Cir. 1997) (noting that "in order to prevail in the civil action, the SEC now needs only to move for summary judgment on the basis of the collateral estoppel effect of [the criminal] conviction").

Courts may enter summary judgment based on the collateral estoppel effects of prior convictions even if the charges are not identical, provided the factual determinations underlying the convictions are sufficient to establish the violations at issue in the subsequent action. Collateral estoppel bars "successive litigation of an issue of *fact* or law actually litigated and resolved in a valid court determination essential to the prior judgment, *even if the issue recurs in the context of a different claim*." *Taylor v. Sturgell, 553 U.S. 880, 892, 128 S. Ct. 2161, 2170, 171 L. Ed. 2d 155 (2008)* (quoting *New Hampshire v. Maine*, 532 U.S. 742, 748, 121 S. Ct. 1808, 149 L. Ed. 2d 968 (2001)) (emphasis added). *See, e.g., SEC v. Quinlan*, 2008 U.S. Dist. LEXIS 95789 (E.D. Mich.

2008) (granting summary judgment on the basis of the commonality of underlying factual issues in parallel criminal prosecution); *SEC v. Fisher*, 2011 U.S. Dist. LEXIS 92868 (E.D. Mich. 2011) (conviction for conspiracy to commit securities registration violations was basis for collateral estoppel on claims that defendant violated the securities laws' registration provision); *SEC v. Dimensional Entertainment Corp.*, 493 F. Supp. 1270, 1273 (S.D.N.Y. 1980) (granting summary judgment on Section 5, Section 17(a), Section 10(b), and Rule 10b-5 claims based on defendant's conviction for wire fraud even though defendant was acquitted of securities fraud); *SEC v. Pace*, 173 F. Supp. 2d 30, 30-33 (D.D.C. 2001) (granting summary judgment on Section 14(a), Section 10(b), and Rule 10b-5 claims based on defendant's conviction for wire fraud and tax fraud).

2. Violations of the Antifraud Provisions of the Securities Act, The Exchange Act, and the Advisers Act

Counts II, III and IV of the Complaint against Kiley charge him with violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]. Counts II through VI of the Complaint against Beckman charge him with violating the foregoing anti-fraud provisions as well as Sections 206(1) and 206(2) of the Advisers Act [15 U.S.C. §§ 80b-6(1) an 80b-6(2)].[1]

[1] Section 10(b) and Rule 10b-5 make it illegal for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

To establish a violation under these anti-fraud provisions, the SEC must prove that a defendant: (1) engaged in prohibited conduct (i.e., employed a fraudulent scheme, made a material misstatement or omission, or engaged in a fraudulent business practice); (2) in connection with the offer, sale, or purchase of a security; (3) by means of interstate commerce. *See SEC v. Quan*, 2014 U.S. Dist. LEXIS 131618 at *11 (D. Minn. 2014) (interpreting Section 17(a), Section 10(b) and Rule 10b-5); *SEC v. Shanahan*, 646 F.3d 536,541 (8th Cir. 2011) (involving misstatements and omissions); *SEC v. Lucent Techs., Inc.*, 610 F. Supp.2d 342, 350 (D.N.J. 2009) (involving deceptive conduct).

> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security. (15 U.S.C. § 78j(b) and 17 C.F.R. § 240.10b-5.)
>
> Section 17(a) makes it illegal for any person in the offer or sale of any securities . . . by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly
>
> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.
>
> (15 U.S.C. § 77q(a)(1)-(3).)
>
> Sections 206(1) and 206(2) of the Advisers Act make it illegal for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly,
>
> (1) to employ any device, scheme, or artifice to defraud any client or prospective client, or
>
> (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.
>
> (15 U.S.C. §§ 80b-6(1) and 80b-6(2).)

A violation of Advisers Act Sections 206(1) and 206(2) requires, additionally, that the defendant was acting as an investment adviser and perpetrated his fraud on clients or prospective clients. 15 U.S.C. §§ 80b-6(1) and 80b-6(2). An individual who controls the actions of a registered investment adviser can be charged directly under Section 206 of the Advisers Act. *See Abrahamson v. Fleshner*, 568 F.2d 862, 871 (2d Cir. 1977), *cert. denied*, 436 U.S. 913 (1978) (finding individuals who were general partners of an investment partnership could be held liable under Section 206 of the Advisers Act).

The Supreme Court has held that the Advisers Act establishes a statutory fiduciary duty for investment advisers to act for the benefit of their clients. *Transamerica Mortgage Adviser, Inc. v. Lewis*, 444 U.S. 11, 17 (1979). An adviser's fiduciary duties include "an affirmative duty of utmost good faith, and full and fair disclosure of all material facts." *SEC v. Capital Gains Research, Inc.*, 375 U.S. 180, 191, 194 (1963). As such, they must act in "utmost good faith," use reasonable care to avoid misleading clients, and fully and fairly disclose conflicts of interest. *Id*. at 194, 201.

Scienter is required to prove a violation of Section 10(b), Rule 10b-5, Section 17(a)(1) and Section 206(1), while Sections 17(a)(2), 17(a)(3), and 206(2) are proven by showing a defendant acted at least negligently. *Shanahan*, 646 F.3d at 541; *SEC v. True North Fin. Corp.*, 909 F.Supp.2d 1073, 1122 (D. Minn. 2012); *Capital Gains Research Bureau, Inc.*, 375 U.S. at 195 (holding scienter not an element of Section 206(2)); *SEC v. Steadman*, 967 F.2d 636, 641 n.3 (D.C. Cir. 1992) (predicting that the Supreme Court would deem scienter an element of Section 206(1)).

Scienter requires proof of intent to deceive or severe recklessness. *Shanahan*, 646 F.3d at 543. A false or misleading statement is "material" if there is a substantial likelihood that a reasonable investor would have considered the facts stated or omitted as having "significantly altered the 'total mix' of information available." *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988).

The Defendants' convictions on multiple counts of wire fraud and mail fraud (together with the SEC's evidence from its emergency motion as to Beckman's control of The Oxford Private Client Group, LLC and its status as an investment adviser) satisfy all of the requirements for collateral estoppel on the securities fraud charges in these cases. *See SEC v. C.J.'s Fin.*, 2012 U.S. Dist. LEXIS 117934*10-18 (E.D. Mich. 2012) (criminal conviction for wire fraud warranted collateral estoppel on SEC's securities fraud claims); *SEC v. Shehyn*, 2010 U.S. Dist. LEXIS 84882, *7-13 (S.D.N.Y. 2010) (same).

The wire fraud and mail fraud counts involved fraud that Kiley and Beckman perpetrated against investors in the same offering and currency trading venture at issue in the SEC's two cases. In order to convict, the jury had to find that the Defendants devised a scheme and artifice to defraud and to obtain money and property by means of materially false and fraudulent pretenses, representations, and promises and concealment of material facts. (Birkenheier Dec., Ex. 3, ¶ 11.) The jury was also required to find that the Defendants acted knowingly and with intent, *i.e.*, acted with scienter. (*Id.*)

When assessing the collateral estoppel effect of a prior criminal conviction on a related civil action, the "primary inquiry is whether the factual bases for the criminal

conviction are the same factual bases which the civil suit relies upon." *C.J.'s Fin.*, 2012 U.S. Dist. LEXIS 11734, *9-10. Here, the answer to that inquiry is, "yes."

In the criminal prosecution and in the SEC's two civil actions, Kiley and Beckman were alleged to have

- Obtained millions of dollars from investors,
- For the purported purpose of investing in a foreign currency trading venture,
- By means of false and misleading statements, that
- Investors' money would be held in segregated accounts,
- Investors could withdraw their assets at any time,
- The currency trading posed little risk and
- Was sure to generate double-digit returns.

The jury in the criminal trial necessarily found the foregoing statements to have been materially false and misleading and the Defendants' conduct to have been part of a fraudulent scheme. The jury's verdict leaves no genuine dispute. The truth was that:

- Investor money was commingled in accounts held in the names of companies controlled by the Defendants and their associates,
- Investors could not withdraw their money whenever they chose to do so,
- Millions of dollars in investor money was diverted to the personal benefit of the Defendants and their associates,
- The Defendants and their associates did employ some investor money in foreign currency trading, but that trading resulted in catastrophic losses for the investors,

- The Defendants lulled their victims into believing that everything was fine, and
- The Defendants acted through various companies, including The Oxford Private Client Group, LLC.

These are the very same facts that form the core of the SEC's securities fraud allegations against Kiley and Beckman. *Compare* Birkenheier Dec., Ex. 1, ¶¶ 3-11; Ex. 2, ¶¶ 3-16; Ex. 3, ¶¶ 12-21. The additional facts that The Oxford Private Client Group, LLC was an investment adviser and that Beckman controlled the firm are established by uncontroverted evidence already in the record of the SEC's case against Beckman. (*Id.*, Ex. 8.)

Moreover, there is no dispute that the Defendants' criminal trial resulted in a final judgment on the merits and that they had a full and fair opportunity to litigate the criminal charges against them. Accordingly, the SEC has met the requirements for collateral estoppel to apply, and for summary judgment to be granted on its securities fraud charges against Kiley and Beckman.

3. Violation of the Securities Transaction Registration Provision

Count I of each of the SEC's Complaints charge the Defendants with violating Sections 5(a) and 5(c) of the Securities Act [15 U.S.C. §§ 77e(a) and 77e(c)]. A violation of Sections 5(a) and 5(c) is established by showing that: (1) no registration statement was filed or in effect for the offering of the securities; (2) the defendant, directly or indirectly, sold or offered to sell the securities; and (3) the sale was made through the use of interstate facilities or the mails. *SEC v. Great Lakes Equities Co.***,** 1990 WL 260587, *16 (E.D. Mich. 1990), *quoting SEC v. Cont'l Tobacco Co.*, 463 F.2d 137, 155 (5th Cir. 1972). Scienter is not

required to prove a violation of Section 5. *SEC v. Calvo*, 378 F.3d 1211, 1214-15 (11th Cir. 2004); *SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 859-60 (S.D.N.Y. 1997), *aff'd*, 159 F.3d 1348 (2d Cir. 1998). Once the Commission establishes a prima facie violation, the defendant assumes the burden of proving that the securities offering qualified for a registration exemption. *SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953).

The investments offered and sold by Kiley and Beckman were investment contracts and therefore securities under Section 2(a)(1) of the Securities Act [15 U.S.C. § 77b(a)(1)], Section 3(a)(10) of the Exchange Act [15 U.S.C. § 78c(a)(10)], and Section 202(a)(18) [15 U.S.C. § 80b-b-2(a)(18). An investment contract exists where (1) a person invests his or her money, (2) in a common enterprise, and (3) is led to expect profits from the efforts of the promoter or a third party. *SEC v. Edwards*, 540 U.S. 389, 394 (2004); *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99 (1946).

The first *Howey* prong is satisfied, because investors gave money to the Defendants for the purpose of investing in the Defendants' foreign currency trading venture. The third prong is also satisfied, because the Defendants led investors to expect profits to be derived from trading in foreign currencies by the Defendants and their associates. The Eighth Circuit has not definitively ruled on whether the second prong, the "common enterprise" element, is satisfied by vertical commonality, horizontal commonality, or both. *See Sias v. Herzog*, 2006 WL 2418950 at *8 (D. Minn. 2006). But the facts necessarily found in the criminal case satisfy both the vertical commonality and the horizontal commonality tests.

"As a general guide, 'vertical commonality' requires only a pooling of the interests of the developer or promoter and each individual investor . . ." *Top of Iowa Co-op. v. Schewe*,

6 F.Supp.2d 851 (N.D. Iowa 1998). Two types of vertical commonality have been identified: "broad" and "strict." *Sias*, 2006 WL 2418950 at *8. To establish broad vertical commonality, the fortunes of the investors need only be linked to the efforts of the promoter. To establish strict vertical commonality, the fortunes of the investors need to be tied to the fortunes of the promoters. *Top of Iowa Co-op.*, 6 F.Supp.2d at 852. Here, broad vertical commonality is established because the investors' fortunes were dependent on the Defendants' fund raising and foreign currency trading. Strict vertical commonality is also present because both the investors' returns and the Defendants' income hinged upon the success of the foreign currency trading, such that both the Defendants' and investors' profits were linked.

Horizontal commonality exists if the "funds of two or more investors . . . go into a 'common pool from which all may benefit.'" *Stone v. Kirk*, 8 F.3d 1079, 1085 (6th Cir. 1993) (*quoting Newmyer v. Philatelic Leasing, Ltd.*, 888 F.2d 385, 394 (6th Cir. 1989)); *see also Top of Iowa Co-op.*, 6 F.Supp.2d 851. In this case, despite their promises to the contrary, the Defendants commingled the investors' money in pooled accounts and used some of those commingled funds to finance their currency trading. Thus, horizontal commonality existed.

The criminal jury necessarily found that the Defendants acted in interstate commerce. And no registration statement was ever filed with the SEC for the interests offered and sold by the Defendants. (Birkenheier Dec., Ex. 9, Attestations of SEC Records Officer, *SEC v. Beckman*, Doc. # 4.6, pp. 6, 8.) Thus, all the elements of the unregistered offer and sale of securities have been satisfied.

B. THE COURT SHOULD IMPOSE PERMANENT INJUNCTIONS

Based on the undisputed facts, the Court should impose the injunctive relief sought by the Commission.

The SEC is authorized to seek a permanent injunction upon a proper showing that a person has violated the federal securities laws. 15 U.S.C. §§ 77t(b), 78u(d), 80b-9(d). To obtain injunctive relief, the SEC must establish that a violation has occurred and that there is a reasonable likelihood of future violations. *SEC v. Comserv Corp.*, 908 F.2d 1407, 1412 (8th Cir. 1990) (citing *SEC v. Commonwealth Chem. Sec., Inc.*, 574 F.2d 90, 99 (2d Cir. 1978)). Because SEC injunctive actions are created by statute, there is no need to find irreparable injury. *SEC v. Management Dynamics, Inc.*, 515 F.2d 801, 808 (2d Cir. 1975).

In these cases, it is conclusively established that Kiley and Beckman violated Sections 5(a), 5(c), and 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. It is likewise conclusively established that Beckman also violated Sections 206(1) and 206(2) of the Advisers Act. In assessing whether there is a likelihood of future violations, courts consider: "the degree of the defendant's scienter, the isolated or recurrent nature of the violation, the defendant's recognition that his conduct was wrongful, the likelihood that the defendant's professional occupation will allow for future violations, and the defendant's sincerity in assuring against future violations." *Quan*, 2014 U.S. Dist. LEXIS 131618 at *30-31.

Based on these factors, permanent injunctive relief is necessary and appropriate against Kiley and Beckman. Their violations were long and repeated. They acted with knowledge and intent to deceive. They caused devastating financial harm to hundreds of vulnerable victims. And to this day, they have shown neither remorse nor acceptance of responsibility for their guilt and the harm they have caused.

C. THE COURT SHOULD ORDER THE DEFENDANTS TO PAY DISGORGEMENT AND PREJUDGMENT INTEREST

Over the course of their fraud, the Defendants and their associates took in a total of $193,103,061 from their investor-victims. (Declaration of Luz M. Aguilar ("Aguilar Dec."), ¶ 11 and Ex. 3 and 4.) The Defendants and their associates returned $49,874,319 of that money back to investors, leaving the Defendants and their associates with ill-gotten gains totaling $143,228,742. (*Id.*) The SEC asks that the Court order the Defendants, jointly and severally, to disgorge those ill-gotten gains plus prejudgment interest.

Disgorgement is an equitable remedy with a dual purpose: to "deprive a wrongdoer of his unjust enrichment and to deter others from violating securities laws." *SEC v. Teo*, 746 F.3d90, 105, (3d Cir. 2014) (*quoting SEC v. First City Fin. Corp.*, 890 F.2d 1215, (D.C. Cir. 1989)); *see also, SEC v. O'Hagan*, 901 F. Supp. 1461, 1468 (D. Minn. 1995). Exactitude is not required; "disgorgement need only be a reasonable approximation of profits causally connected to the violation." *First City Fin. Corp.*, 890 F.2d at 1231. Once the SEC gives the Court a reasonable approximation of disgorgement, the burden shifts to the Defendants to show that the SEC's estimate is not

reasonable. *Teo*, 2014 WL 503455 at *11. Any risk of error or uncertainty falls on the wrongdoer. *SEC v. Patel*, 61 F.3d 137, 140 (2d Cir. 1995).

Caselaw provides five principles which should guide the determination of disgorgement against Kiley and Beckman. First, in calculating disgorgement, the SEC need not offset amounts that the Defendants expended in taxes. *See, e.g.*, *SEC v. Merchant Capital, LLC*, 486 Fed. Appx. 93, 96 (11th Cir. 2012) (holding that, in calculating Defendants' disgorgement, "[w]e reject the argument that the district court was required to take into account the amount of income taxes paid"); *SEC v. U.S. Pension Trust Corp.*, 444 Fed. Appx. 435, 437 (11thCir. 2011) ("We know of no authority, and the [Defendants]cite none, requiring the court to deduct from the disgorgement figure the amount of ill-gotten gains paid to the government in income tax"); *SEC v. Dibella*, 2008 WL 6965807, *3 (D. Conn. 2008) (income taxes not deductible from disgorgement amount); *SEC v. Svoboda*, 409 F.Supp.2d 331, 345 (S.D.N.Y. 2006) (finding no legal authority to support deducting capital gains taxes from disgorgement amount).

Second, for similar reasons, Defendants cannot offset expenses incurred in operating their business—or any other expenses for that matter. *See SEC v. Brown*, 658 F.3d 858, 861 (8th Cir. 2011)(stating that the "overwhelming weight of authority holds that securities law violators may not offset their disgorgement liability with business expenses"); *SEC v. Hughes Capital Corp.*, 917 F.Supp. 1080, 1087 (D.N.J. 1996)(same); *SEC v. Benson*, 657 F.Supp. 1122, 1134 (S.D.N.Y. 1987) ("the manner in which [defendant] chose to spend his misappropriations is irrelevant as to his objection to disgorge. Whether he chose to use this money to enhance his social standing through

charitable contributions, to travel around the world, or to keep his co-conspirators happy is his own business").

Third, the Court need not consider the Defendants' ability to pay when ordering disgorgement. To be sure, the disgorgement sought in this case is substantial. That is to be expected; there is no dispute that the Defendants were enormously successful at raising money. Their fraud lasted for years and took in $193.1 million from investors. (Aguilar Dec., ¶ 11, Ex. 3 and 4.) Kiley and Beckman may well be unable to satisfy the award sought by the SEC. But, inability to pay is not a defense. *See, e.g., SEC v. Juno Mother Earth Asset Mgmt., LLC*, 2014 WL 1325912, *3 (S.D.N.Y. 2014). Courts recognize that to hold otherwise would lead to an absurd result: defendants could escape disgorgement liability simply by spending their ill-gotten gains. *See, e.g., SEC v. Warren*, 534 F.3d 1368, 1370 n.2 (11th Cir. 2008); *SEC v. Inorganic Recycling Corp*., 2002 WL 1968341, *2 (S.D.N.Y. 2002) (*quoting SEC v. Grossman*, 1997 WL 231167, *10 (S.D.N.Y. 1997) ("The fact that swindlers have run through the proceeds of the fraud and are now insolvent should not prevent the imposition of a remedy, since defendants may 'subsequently acquire the means to satisfy the judgment'"). Moreover, the imposition of the disgorgement award sought by the SEC would serve the second purpose of disgorgement—deterring fraud by others.

Fourth, in addition to disgorging Defendants' ill-gotten gains, the Court may also order payment of prejudgment interest on those gains to prevent the Defendants from getting what amounts to an interest-free loan due to their fraud. *SEC v. Lawton*, 2011 WL 494888, *5 (D. Minn. 2011); *SEC v. Brown*, 2010 WL 1780144, at *2 (D. Minn. 2010).

Both the SEC and District Courts routinely calculate prejudgment interest using the rate applied by the Internal Revenue Service ("IRS") for the underpayment of federal income tax. *See id.*; *SEC v. First Jersey Securities, Inc.*, 101 F. 3d 1450, 1476 (2d Cir. 1996) (noting use of IRS underpayment rate in calculating prejudgment interest). Following these principles, the SEC calculates the Defendants' prejudgment interest as $12,699,781. (Aguilar Dec. ¶13, Ex. 5.)

Fifth, Kiley and Beckman should be ordered to pay the full disgorgement and prejudgment interest amount jointly and severally, between themselves and among the other defendants. Courts have broad discretion to impose joint and several liability where—as here—"two or more individuals or entities collaborate or have a close relationship in engaging in the violations of the securities laws." *SEC v. Platforms Wireless.*, 617 F.3d 1072, 1098 (9th Cir. 2010); *see also SEC v. Hughes Cap. Corp.*, 124 F.3d 449, 455 (3d Cir. 1997); *SEC v. Calvo*, 378 F.3d 1211, 1215-16 (11th Cir. 2004). The guilty verdict in the criminal case establishes that Kiley, Beckman, and their associates conspired together in perpetrating their fraud. (Birkenheier Dec., Ex. 3, Count 13; Ex. 6, Count 13; Ex. 7, Count 13.) The SEC's proposed settlements with Trevor Cook and the defendant-entities controlled by the Receiver impose joint and several liability for the full amounts of disgorgement and prejudgment interest. Together, the judgment sought against Kiley, the judgment sought against Beckman, and the consent judgments with Cook and the defendant-entities would provide that all the defendants in the two SEC cases are held jointly and severally liable for the full amount of the ill-gotten gains derived from their fraudulent scheme plus prejudgment interest.

Based on the foregoing, the SEC asks that the Court order Kiley and Beckman to pay, jointly and severally, $143,228,742 in disgorgement and $12,699,781 in prejudgment interest, for a total liability of $155,928,523. (Aguilar Dec. ¶¶13, Ex.5.)

D. THE COURT SHOULD DISMISS THE SEC'S CLAIMS FOR CIVIL PENALTIES

In its Complaints, the SEC sought civil penalties against Kiley and Beckman. (Birkenheier Dec., Ex. 1, at 48; Ex. 2, at 42-43.) The purposes of civil penalties are to punish defendants and to achieve specific and general deterrence. In this case, however, Kiley and Beckman have been sentenced to lengthy prison sentences. As a result, no additional punitive or deterrent benefit would accrue to the public from the imposition of the civil penalties sought by the SEC. Therefore, the SEC asks that the Court dismiss its claims for civil penalties against Kiley and Beckman.

IV. CONCLUSION

For the reasons set forth above, the Commission respectfully requests that the Court grant summary judgment against Kiley and Beckman and enter final judgments against them making findings of fact, imposing permanent injunctions, and ordering disgorgement and prejudgment.

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Respectfully submitted,

s/John E. Birkenheier
John E. Birkenheier
(Bar Number 6270993)
Justin M. Delfino
U.S. Securities and Exchange Commission
175 W. Jackson Blvd., Suite 900
Chicago, Illinois 60604
Tel: (312) 886-3947 (Birkenheier)
Tel: (312) 353-1821 (Delfino)
Fax: (312) 353-7398
Email: birkenheierj@sec.gov
Email: delfinoj@sec.gov