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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16649

In the Matter of:

Ironridge Global Partners, LLC,
Ironridge Global IV, Ltd.

Respondents.

RESPONDENTS' REPLY IN SUPPORT OF SUMMARY DISPOSITION

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I. INTRODUCTION

More than two years after initiating its investigation and more than a year after issuing its first Wells notice, the Division has finally articulated the real reason for this enforcement proceeding—its desire to effectively eliminate the availability of the § 3(a)(10) exemption for small businesses, the exact opposite of the legislative intent. Rather than lobbying Congress to repeal or amend the statute that the legislature chose to enact over 80 years ago, the Division seeks to legislate by rule making, in a an impermissible and unconstitutional attempt to insinuate itself into a process where Congress has determined it does not belong. *See* 78 CONG. REC. 8668 (1934) (in order to address "complaints that the present act is too drastic, and is *interfering with business*," concurrently with the very creation of the Commission, Congress amended § 3(a)(10) to "*substantially extend* the present provisions [originally enacted in § 4 of the Securities Act of 1933] in order to cover various forms of readjustments of the rights of holders of outstanding securities, claims and property interests, *where the holders will be protected by court supervision* of the conditions of the issuance of their new securities," by making "clear that the exemptions accorded [by § 3(a)(10)] extend beyond the particular transactions therein covered, *to the security itself*." *Id.* (emphasis added). The stated purpose of the § 3(a)(10) exemption was that the long-establish court system, not the newly-created Commission, would have authority to supervise the process.

Thirty-four judges reviewed and approved the fairness of the terms and conditions of the issuance of shares to Global IV, in every case finding that the terms of the exchange were fair not only to the investor, but also to the company and its stockholders. Moreover, the courts held

that the shares could be resold by Global IV without restriction.[1] The Division nevertheless now seeks to insert a *post hoc* requirement that Global IV register as a dealer under § 15, with the stated purpose of causing the terms of the § 3(a)(10) exchanges—which 34 courts have already held to be fair—to be subject to FINRA compensation review.[2] Allowing such a result would be directly contrary to the statutory scheme, the plain language of the statute, and the express legislative intent. The Commission simply does not have the authority to overturn the statute or overrule the courts.

The Division brought this case because it does not like section 3(a)(10) exchanges being done for small public companies. Instead of attempting to have Congress revise or amend the statute, the SEC wants to restrict the availability of the statutory exemption by asking its own ALJ to alter existing law and guidance, which Respondents have relied on, to find that Global IV is a "dealer" subject to SEC registration under circumstances where no investor has been previously found to be a dealer. Indeed, not one of the dozens of different judges or scores of securities attorneys that participated in, compliance reviewed, or opined on the court-approved § 3(a)(10) exchanges ever suggested the possibility that Global IV might have to register as a

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[1] In addition, when one of the issuers subsequently challenged the propriety of the exchange under federal securities laws, the United States District Court reviewed Global IV's § 3(a)(10) exchange process at length in two separate published opinions, finding it was perfectly appropriate, *ScripsAmerica, Inc. v. Ironridge Global LLC*, 56 F. Supp. 3d 1121, 1132 (C.D. Cal. 2014), *ScripsAmerica, Inc. v. Ironridge Global LLC*, ___ F. Supp. 3d ___, 2015 WL 4747807 at *2 (C.D. Cal. Aug. 11, 2015), and that "Ironridge was permitted to sell the shares however it pleased; it was not illegal to sell freely transferrable shares in a publicly traded company," 56 F. Supp. 3d at 1165, 2015 WL 4747807 at *29.

[2] Ironically, the FINRA compensation guidelines apply only to a "public offering," and the Division does not explain why Global IV's exempt exchanges could possibly be considered public offerings. *See* FINRA Rule 5110(f)(2).

dealer. The ALJ should reject this invitation to jettison the established guidance and to change the rules by using this case to make new law.

In an attempt to justify this sweeping rule change, the Division paints an inaccurate, sinister picture of Global IV, with assertions that are as false as they are irrelevant for purposes of determining whether Global IV is a dealer. For example, the Division:

- Falsely alleges that Respondents intentionally drove down issuers' stock prices and caused harmful dilution, when in fact every court to ever consider this accusation has emphatically rejected based on the real evidence. See, *e.g.*, *ScripsAmerica, Inc. v. Ironridge Global, LLC*, 2015 WL 4747807, at *16-17 (C.D. Cal. Aug. 11, 2015) ("the court's review of the transaction data ... confirms that Ironridge sold its Scrips shares within the range at which all Scrips'shares were sold" ... "the data ... belie Scrips' conclusory allegation that Ironridge continually offered to sell at the lowest bid price, i.e., that Ironridge was bid whacking"); *NewLead Holdings Ltd. v. Ironridge Global IV Ltd.*, 2014 WL 2619588, at *7-8 (S.D.N.Y. June 11, 2014) ("There is no evidence Ironridge has ever made a short sale of NewLead stock. ... And Ironridge is responsible for only a small portion of NewLead's share dilution."); *Ironridge Global IV, Ltd. v. VelaTel Communications, Inc.*, Case No. BC 486893, at 20, 66 (Mar. 26, 2014) ("THE COURT: A lot more shares are being issued to other people than to Ironridge ... One of the impressions that I'm getting is that the problems that I see with this are, at least in large measure, Velatel's making. ... And the reason for that is because the market has been flooded with shares and perhaps other management decisions.")

- Falsely alleges that Respondents wrongfully promoted the § 3(a)(10) exemption as a cost-effective alternative to registration, when in fact the State of California itself truthfully promotes the simple reality that: "Fairness hearings provide a fast and cost-efficient alternative to federal registration, saving companies hundreds of thousands of dollars in federal registration costs. Many high-profile California companies have taken advantage of the fairness hearing process." Dep't of Bus. Oversight, *Corporations Fairness Hearings*, http://www.dbo.ca.gov/ENF/FairnessHearings/Default.asp

- Misrepresents and mischaracterizes the stock sales made by registered broker-dealers on behalf of Global IV, via an attorney-prepared chart riddled with inaccuracies. *See* Declaration of Brendan T. O'Neil ("O'Neil Decl.") submitted herewith.

The ALJ should reject the Division's inaccurate portrait of Respondents that has no basis in objective reality and, more importantly, the Division's invitation to make sweeping new law via an administrative proceeding.

II. ARGUMENT

A. Global IV Is Not a Dealer Under Existing Guidance.

The Division argues that Global IV is a dealer under the existing guidance for two reasons, but both of those reasons are incorrect. The Division also asks the Court to abandon the established guidance that whether one is a dealer turns on at least ten factors and to instead adopt *ex post facto* sweeping new rules that have never been the subject of the normal rule-making process and which no one ever anticipated.

1. Global IV Is Not a Dealer Under the Statutory Definition.

First, the Division invokes the statutory definition of a dealer, which is "any person engaged in the business of buying and selling securities . . . for such person's own account." 15 U.S.C. § 78c(a)(5). According to the Division, that definition makes a dealer out of everyone who buys and sell securities in more than a "few isolated transactions." Opp. at 9. That expansive definition would mean that every hedge fund is a dealer, as is every private equity firm, every venture capitalist, and every human being with an eTrade account. That key part of the Division's argument should be rejected as being contrary to existing SEC guidance emphasizing a critical distinction between buying and selling securities for yourself as opposed to in service of others.

As the Commission itself said in the very case the Division cites, "engag[ing] in the business" of buying and selling securities like a dealer does not mean simply "trading [that] involve[s] more than isolated transactions." *Gordon Wesley Sodorff, Jr.*, Admin. File Proc. No. 3-7390, 1992 WL 224082, at *5 (Sept. 2, 1992). To the contrary, buying and selling as a "regular business" like a dealer means buying and selling regularly in the service of *others*, rather than self-interestedly for "one's own account." *Id.*; *see also Guide to Broker-Dealer-Registration*, "Who is a Dealer?" ("Who is a Dealer") (April 2008),

http://www.sec.gov/divisions/marketreg/bdguide.htm#II ("[I]ndividuals who buy and sell securities for themselves generally are considered traders not dealers."); *Burton Securities*, SEC No-Action Letter, 1977 WL 10680, at *1 (Dec. 5, 1977) ("[A] person who buys and sells securities for his own account in the capacity of a 'trader' or individual investor is generally not considered to be 'engaged in the business' of buying and selling securities . . . .").[3]

This distinction is critical. Whether one trades self-interestedly, or instead engages in the business of trading in service of others, depends on an established list of at least ten factors. "Who is Dealer," *supra*; *Gordon*, 1992 WL 224082, at *5 (listing factors); *Definition of Terms in and Specific Exemptions for Banks, Savings Associations, and Savings Banks Under Section 3(a)(4) and 3(a)(5) of the Securities Exchange Act of 1934*, ("Proposed Dealer Exemption Rule") Release No. 46745, 2002 WL 31428622, at *5-6 (Oct. 30, 2002) (explaining the multi-factor "Engaged in the Business" test); *National Council of Savings Institutions*, SEC No-Action Letter, 1986 WL 67129, at *2 (July 27, 1986) (describing the list of factor that make someone a "trader" rather than someone "engaged in the business" of buying and selling securities as a dealer).[4]

The Division's position is not only contrary to the existing guidance, but it would also impermissibly create an "excessively broad definition of a dealer." *See SEC v. Federated Alliance Group, Inc.*, No. 93-0895, 1996 WL 484036, at *4-5 (W.D.N.Y. Aug. 21, 1996). If "dealers" include everyone who makes money through buying and selling securities in more than isolated transactions, then every hedge fund and institutional investor nationwide is a dealer.

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[3] *See also Biefedt v. CIR*, 231 F.3d 1035, 1037 (7th Cir. 2000) (Posner, J.) (noting that the "standard distinction between a dealer and a trader" is that the "dealer's income is based on the service he provides" rather than on "fluctuations in the market value" of assets).

[4] The other source the Division cites likewise recognized that there is a list of factors that determine whether one is a dealer. *Definition of Terms in and Specific Exemptions for Banks, Savings Associations, and Savings Banks Under Sections 3(a)(4) and 3(a)(5) of the Securities Exchange Act of 1934*, Release No. 47364, 2003 WL 328058, *4 (Feb. 13, 2003).

The Division nonetheless persists, citing *SEC v. Big Apple,* 783 F.3d 786 (11th Cir. 2015), in arguing that regularly buying and selling securities for profit makes one a dealer regardless if one does so for his own benefit, rather than for the service of others. That citation is not persuasive. To begin, the court was addressing whether the defendants there were dealers under the Securities Act (which under § 3(a) is entirely inapplicable to court-approved § 3(a)(10) exchanges), rather than the Exchange Act's § 15(a). *Id.* at 809-10. Moreover, *Big Apple* involved criminal liability for a massive fraud, whereas the Division has not even alleged any fraud here. The key point there was that the defendants had acquired and sold the stock of *their own clients* who were participants in the fraud. 783 F.3d at 809-10. The defendants were engaged in a "pump and dump" distribution scheme, disseminating false information and then distributing shares into the market based on the fraudulently-created demand. There was overwhelming evidence that defendants were underwriters aiding and abetting fraudulent issuers, engaged not only in a distribution but in a fraudulent distribution. The defendants asserted they were not dealers because they claimed to be only a public relations firm. The court gave short shrift to this contention, and as such found it unnecessary to address or even discuss the traditional factors indicating whether one is a dealer, the bulk of which defendant met in any event. In other words, *Big Apple* is unique to its particular facts and has no application at all here.

The Division also cites *SEC v. Offill,* No. 07-1643, 2012 WL 246061 (N.D. Tex. Jan. 26, 2012). That case also does not help the Division establish that regularly buying and selling securities is enough to make one a dealer, because there the person labeled a dealer had the traditional attributes of a dealer. For example, he was an underwriter partly because he engaged in "special selling efforts" by hiring others to "conduct market awareness for the Ecogate

offering" and because he sold all of the shares "immediately" after receiving them. *Id.* at *5, 8. Additionally, like a dealer he dealt directly with the public by "selling the shares to the public." *Id.* at *8; *see also id.* at *6. Finally, he was not "buying and selling securities as an individual investor," but rather acted like a service provider. *Id.* at *9. Those factors are not present here.

Thus, the Division has failed to establishing that regularly buying and selling securities is enough, alone, to make someone a dealer.

2. Global IV Is Not a Dealer Under the Traditional Factors.

Second, the Division alternatively argues that Global IV is a dealer under the traditional list of factors. The first hole in that argument is that the Division tries to abbreviate the list of factors by dismissing the list of ten on the SEC's website as a mere "Internet summary guide" and by listing four of the eight factors from a release on "OTC Derivatives Dealers." Opp. at 9, 13; *OTS Derivatives Dealers* ("OTC Derivatives Release"), Release No. 40594, 1998 WL 745950, at *15 n.61 (Oct. 23, 1998) (listing eight factors). The ten factors listed on the "Who is a Dealer" page and the remaining four in the release are well-established in SEC guidance, not mere musings the Division is free to ignore. *E.g.*, Proposed Broker Dealer Rule, 2002 WL 31428622, at *6; *National Council on Savings Institutions*, SEC No-Action Letter, 1986 WL 67129, at *2 (July 27, 1986). In any event, Global IV is not a dealer under the four factors the Division does list.

a. Global IV does not buy or sell from "customers."

The Division contends that Global IV buys "securities as a principal directly from issuers." Opp. at 10. That argument fails. To begin, the Division did not rely on this supposed factor in the OIP, so the Division may not do so now. Motion at 16.

Further, Global IV did not buy securities from issuers. Rather, free-trading shares were issued in exchange for outstanding claims, pursuant to court-approved § 3(a)(10) exchanges.

Under court supervision, Global IV's registered broker-dealers were issued shares by the issuers after compliance review by broker-dealers and others, in exchange for bona fide outstanding claims. Not one of the judges required Global IV to register as a dealer. This is not surprising, as even the SEC's own guidance on § 3(a)(10) never hints at any such possibility, and until now the SEC had never made such a claim.

More to the point, the question is whether Global IV purchased or sold "from or to *customers*," as the Division itself acknowledged elsewhere. Opp. at 9 (emphasis added). The issuers were not Global IV's customers, but adverse parties in litigation. Global IV has no "customers" within the meaning of the securities laws. Indeed, Global IV never deals with the public; registered broker-dealers sell stock (to other broker-dealers, acting on behalf of themselves or their customers) for Global IV's benefit with direction from a registered investment advisor. O'Neil Tr. at 32-33, 33-34, 37. The only customers are the customers of the registered broker-dealers who bought stock from Global IV's broker-dealers (assuming they did not buy the shares as market makers or for their own account, in which case there are no customers at all).

b. Global IV does not maintain a "dealer inventory."

The Division argues that Global IV "resell[s] the securities in the open market." Opp. at 10. As an initial matter, the claim is demonstrably false. Global IV has never sold a single share. Rather, pursuant to court order the shares are deposited into ordinary brokerage accounts at registered broker-dealers. It is those registered broker-dealers, acting for the benefit of Global IV, who sell shares into the open market.

The Division's point is unclear, but the Division appears to imply that Global IV carries a "dealer inventory" in securities. *See* Opp. at 9, 10. That is another factor the Division did not cite in the OIP, and as such cannot be relied up here. Motion at 16.

Regardless, Global IV does not carry a dealer inventory, which is a reservoir of an issuer's securities that a dealer maintains so that others may buy and sell those securities from and to the dealer as they wish. *Cf. Biefieldt*, 231 F.3d at 1037 (noting that a dealer "maintains an inventory in a specified stock in order to maintain liquidity" and "sells from his inventory to meet [market] demand" and "buys in the open market in order to provide a market for the people who are trying to sell"); *see also id.* at 1038 (noting that maintaining an inventory helps "maintain an orderly market in" a security). There is no evidence that Global IV does this. In other words, Global IV is not a market maker. To the contrary, Global IV never buys in the open market, and never tries to make a market. It is simply an investor.

c. Global IV does not provide "investment" advice.

The Division contends that Global IV provides "incidental investment advice to the issuers involved." Opp. at 11. But providing "investment" advice to *issuers* is not a factor for identifying a dealer. The question is whether one provides "investment" advice to "investors." *See* "Who is a Dealer," *supra* ("Do you provide *services to investors*, such as . . . giving investment advice?" (emphasis added)); Proposed Dealer Exemption Rule, 2002 WL 31428622 at *6 (stating that "buying and selling directly to *securities customers* together with conducting any of an assortment of professional market activities such as providing investment advice" indicates dealer activity (emphasis added)).

In arguing otherwise, the Division does not cite a single authority stating that giving advice to issuers makes one a dealer. Instead, the Division merely notes that in the sixty-first footnote of the OTC Derivative Dealers release, the Commission wrote that a factor in identifying a dealer is whether one provides "investment advice with respect to securities." Opp. at 24. The footnote does not state that providing "investment" advice to an issuer is a factor, nor does the footnote explain how one could provide "investment" advice to anyone other than an

"investor." *See* Motion at 23-24 (explaining that advice on structuring deals is not "investment" advice). Moreover, it is clear from the release as a whole and the context of the footnote that it is, in fact, referring to giving investment advice to investors.

d. Global IV is not an underwriter.

The Division contends that Global IV is an underwriter – apparently under the Securities Act's broad definition of that term,[5] rather than the real-world sense. Opp. at 2, 18-19. According to the Division, that is supposedly enough "by itself" to make Global IV a dealer. Opp. at 10, 16, 18. But that argument fails because the Securities Act does not apply in court-approved § 3(a)(10) exchanges. Section 3(a)(10) exchanges are the purview of the courts, not the Commission. Regardless, the argument fails for several additional reasons as well.

(1) Being an underwriter does not make one a dealer.

First, the Division is incorrect that being an underwriter is enough "by itself" to make Global IV a dealer even when *nine of the ten* factors listed in the guidance undisputedly indicate otherwise.

The Division's only basis for that theory are selective quotes from two pieces of guidance: From the "Who is a Dealer" guidance, the Division notes that the document lists as a factor whether one is an underwriter and then says after a series of other questions, "A 'yes' answer to any of these questions indicates that you *may* need to register as a dealer." Opp. at 14 (emphasis added). From the Proposed Dealer Exemption Rule, the Division notes that guidance "lists in the disjunctive several activities that may qualify as a dealer, including 'underwriting'"

[5] *See In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 629 (S.D.N.Y. 2007) (noting that the Securities Act definition of "underwriter" has been interpreted "broadly" and includes some who are not traditionally "associated with an underwriter's role" (quotation marks and citation omitted)).

and says that a "person generally may" be a dealer "by conducting various activities [including] underwriting . . . ." Opp. at 12, 16 (emphasis omitted).

The Division's selective quotations misconstrue the guidance. In "Who is a Dealer," the Commission identifies just one factor from which someone can "easily tell if [he] is a dealer," *i.e.*, whether the person "advertises publicly that [he] makes a market in securities." Otherwise, the situation is "less clear," and for those unclear circumstances the Commission lists a number of questions to help decide whether a person is a dealer. Given that context, the language the Division seizes upon means only that a positive answer to any question militates in favor of the possibility that a person might be a dealer, not that a "yes" answer to one question is or could ever be dispositive.

Likewise, the Proposed Dealer Exemption Rule says that "the analysis of whether a person meets the definition of a dealer depends upon all the relevant facts and circumstances" and that a "person must evaluate the totality of its securities activities to determine if those activities may constitute engaging in dealer activities." 2002 WL 31428622, at *6. Neither would be true if (like the Division contends) every factor listed in the disjunctive sufficed, alone, to make a person a dealer. There is no support for the Division's argument.

The Division's argument also conflicts directly with existing guidance. The guidance is clear that no one factor controls in identifying a dealer – including whether a person is an underwriter. *Nat'l Council of Savings Insts.*, SEC No-Action Letter, 1986 WL 67129, at *2 (July 27, 1986) (emphasis added); *Burton*, 1977 WL 10680, at *1-2.

More importantly, the Staff issued a No-Action letter to a self-described underwriter that had not registered as a dealer under § 15(a). *Acqua Wellington North American Equities Fund, Ltd.*, SEC No-Action Letter, 2001 WL 1230266 (Oct. 11, 2001). In that letter, the underwriter

based its No-Action request largely on the point that "a person's status as an underwriter, standing by itself, should not result in that person being deemed a dealer." *Id.* at *5.

The Division insists that *Acqua Wellington* is distinguishable. Opp. at 17. But its purported reasons are distinctions without a difference. Six are not established factors for distinguishing a dealer from a trader—marking yet another attempt by the Division to make new law here. The seventh is that Acqua Wellington promised not to provide "investment advice," which Global IV does not do either. Moreover, the Division omits a long list of indisputable similarities (some relevant to identifying a dealer and some not) between Acqua Wellington and Global IV. For example, Aqua Wellington did not:

- "[H]old itself out as a dealer." Neither does Global IV.
- Engage in short selling except in limited circumstances. Global IV never engages in short selling. Kirkland Tr. at 123.
- Indemnify issuers except in limited circumstances. Global IV never indemnifies issuers.
- Carry a dealer inventory. Neither does Global IV.
- Quote a market in securities. Neither does Global IV.
- Extend credit to investors. Neither does Global IV.
- Lend securities, though it appears to have had margin accounts. Global IV does not lend securities or have margin accounts.
- Use an interdealer broker for securities transactions. Neither does Global IV.
- Run a book of repurchase and reverse repurchase agreements. Neither does Global IV.
- Complete transactions without broker-dealers. Neither does Global IV.[6]

[6] Registered broker-dealers are always the ones to sell Global IV's stock (with direction from a registered investment advisor) and, in addition, most of the time issuers often have their own registered broker-dealers who introduced them to Global IV and represented them in the

See Acqua Wellington, 2001 WL 1230266, at *1, 4, 7-8.

One final example of the similarities: Acqua Wellington "face[d] risk more akin to an investor than . . . a dealer." *Acqua Wellington*, 2001 WL 1230266, at *5. Global IV does too, and in fact faces even greater risk than Acqua Wellington. Acqua Wellington was an equity-line investor, *id.* at *2, which meant that Acqua Wellington could "turn a quick profit by selling the stock [it received from issuers] immediately, often before even taking possession of the new shares." *See* Luisa Kroll, *Toxic Stock*, FORBES (March 4, 2002) http://www.forbes.com/forbes/2002/0304/040a.html. By doing so, Acqua Wellington avoided "capital risk." *Id.* Acqua Wellington was also able to hedge through short selling in some circumstances. 2001 WL 1230266, at *6.

Global IV enjoys no such advantages. In court-approved § 3(a)(10) exchanges, Global IV had a binding obligation to pay issuers' creditors in return for the stock, and that binding obligation activated as soon as the court approved the exchange (if not earlier). *See* Kirkland Tr. at 52-53; *see also id.* at 105 (stating that Global IV has always paid the creditors); Schissler Tr. at 24. Global IV then relied on the issuers' stock to potentially recoup those payments, which means that Global IV was always at risk of losing money, and sometimes did. An array of factors might increase Global IV's risk, including a decline in trading volume, the stock being halted, the company refusing to issue shares, going out of business, or filing for bankruptcy—all of which have happened to Global IV. *See* Kirkland Tr. at 186; Schissler Tr. at 23-24; Kreger Tr. at 79. Moreover, Global IV does not engage in any hedging activities. Thus, Global IV

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exchanges. O'Neil Tr. at 12, 27, 32-33, 33-34, 40; Kirkland Tr. at 118-19; *see* Sbarra Tr. at 15, 36-41; OIP, ¶ 12.

bears risk akin to a trader even more than Acqua Wellington did. If Acqua Wellington was not a dealer, Global IV is not either.

(2) Global IV is not a statutory underwriter.

Even if underwriters were automatically dealers, Global IV lacks the attributes of a statutory underwriter. As Respondents explained in the motion for summary disposition, Motion at 17, whether one is a statutory underwriter depends on whether he is involved in the "distribution" of securities, which in turn means making "special selling efforts" regarding those securities. 17 C.F.R. § 242.100(b). Global IV engages in no special selling efforts. Shares are sold only in the open market through ordinary trades from standard brokerage accounts with registered broker-dealers. Motion at 18, 20.

The Division nonetheless contends that Global IV is an underwriter for unpersuasive reasons. First, the Division argues that "distributing" securities like an underwriter does not entail making special selling efforts. According to the Division, Regulation M (which says the opposite) does not control here, so the Court should disregard the definition of "distribution" in that Exchange Act regulation, even though the Division is seeking to hold Respondents liable under §§ 15 and 20 of the Exchange Act. Instead, the Division proposes relying on three cases interpreting that term primarily under the Securities Act. *E.g. Big Apple*, 783 F.3d at 807; *Berckeley Inv. Group, Ltd. v. Colkitt*, 455 F.3d 195, 213 (3d Cir. 2006); *Ackerberg v. Johnson*, 892 F.2d 1328, 1334-36 (8th Cir. 1989).

The first problem with the Division's argument is that Regulation M is a better source for the definition of "distribution" in this Exchange Act case than the Securities Act. Regulation M was promulgated under the Exchange Act and is dedicated largely to *regulating distributions*. *See Anti-manipulation Rules Concerning Securities Offerings*, 62 F.R. 520-01, 520 (Jan. 3, 1997) (noting that Regulation M replaced other rules promulgated under the Exchange Act); *id.* at 521.

Moreover, the Division may not rely on the Securities Act here, because under § 3(a) the Securities Act does not apply to securities issued in § 3(a)(10) exchanges.

The Division's argument for relying on the Securities Act cases interpreting the word "distribution" is that Congress adopted the Securities Act definition of "underwriter" for purposes of the Exchange Act. Opp. at 19. But "distribution" and "underwriter" are two different things. That Congress adopted one definition from the Securities Act for use in the Exchange Act does not mean that it adopted all definitions from the Securities Act for use in the Exchange Act. Quite the opposite, what it shows is that Congress knew exactly how to adopt the Securities Act definition of "distribution" for purposes of the Exchange Act, if that is what it had wanted to do. It did not.

In addition, relying on the Securities Act definition makes no difference, because distribution entails special selling efforts under the Securities Act, too. *New Jersey Carpenters Vacation Fund v. Royal Bank of Scot. Grp., PLC*, 720 F. Supp. 2d 254, 263 (S.D.N.Y. 2010) (holding that an entity was not an underwriter even under the Securities Act partly because it did not "directly participate[] in the sale or distribution of . . . securities . . . by, for instance, marketing the securities to the public, [or] assisting in investor 'road shows'").

The Division nonetheless reads cases under the Securities Act to make an underwriter out of everyone who sells stock within *two years* of buying that stock – regardless of selling efforts. Opp. at 20. *Big Apple*, 783 F.3d at 807; *Ackerberg*, 892 F.2d at 1336. Such an overly expansive definition would encompass investors in virtually every private investment in public equity (PIPE) transaction ever done, and certainly every registered direct (RD) offering, virtually none of which ever register as dealers.

How quickly one sells stock is indeed relevant to deciding whether a person acquired stock with a view to immediate resale or instead for investment and sale over time. *E.g.*, 17 C.F.R. § 230.144(d)(1). But that is only one criteria for identifying an underwriter. *See* THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES LITIG., 2 L. Sec. Reg. § 4.27[3] (July 2015) ("[T]he holding period for securities acquired in a private placement or other nonpublic offerings is merely a very rough guideline and is thus not the be-all and end-all of the 'underwriter' issues.").

But a second, independent requirement is that the entity be involved in a "distribution." *See* Hazen, *supra*, § 4.27[1] ("Underwriter status also depends upon the resell or selling efforts being part of a distribution."); *Ackerberg*, 892 F.2d at 1336 ("The term 'underwriter' thus focuses on 'distribution.'"). To reiterate, "distribution" entails making special selling efforts even under the Securities Act. A distribution also entails selling stock in a "public offering," which is when stock is sold in circumstances where the buyers need extra protection. *Ackerberg*, 892 F.2d at 1336-37. Here, the buyers need no extra protection, because the sales are made by registered broker-dealers on Global IV's behalf with directions from a registered investment advisor, O'Neil Tr. at 32-33, 33-34, 37, and because Global IV obtained the shares through a § 3(a)(10) exchange under a court's supervision and approval. *See Gilbert v. Bagley*, 492 F. Supp. 714, 731 (M.D.N.C. 1980) ("supervision of the court afforded an extra measure of shareholder protection"). Thus, Global IV is not an underwriter under either the Securities Act or the Exchange Act.

(3) Global IV is not an ordinary underwriter.

The Division also seems to argue that Global IV is an underwriter in the ordinary, non-statutory sense. But see Motion at 21. For that purpose, the Division seizes on four of Global IV's supposed attributes. Opp. at 10. But Respondents are not aware of, and the Division fails

to cite, anything to support its contention that the four attributes listed are actually attributes of an underwriter.

For these reasons, Global IV is neither an underwriter nor a dealer under the Division's novel interpretation of those terms.

3. The Division May Not Rely on New Theories.

The Division attempts to avoid all of the above shortcomings by asking the ALJ to adopt new criteria for identifying a dealer. For support, the Division cites cases holding that "the Commission as an administrative agency may properly proceed by adjudication, rather than by further rule-making, *to apply a rule* to particular factual situations, whether or not such situations have previously been held to be within the rule." *J.H. Goddard*, File No. 8-3091, 801-310, 1964 WL 67878, at *4 (May 22, 1964) (emphasis added). But the Division is not seeking to apply existing rules, it is seeking to write new ones.

"Justice dictates" that the Division may not apply new rules retroactively. *Pfaff v. HUD*, 88 F.3d 739, 748 (9th Cir. 1996). At the very least, an agency may not adopt a "new standard" by "adjudication" that "departs radically from the agency's previously interpretation of the law, where the public has relied substantially and in good faith on the previous interpretation, where fines or damages are involved, and where the new standard is very broad and general in scope and prospective in application." *Id.*; *Upton v. SEC*, 75 F.3d 92, 98 (2d Cir. 1996) ("The Commission may not sanction Upton pursuant to a substantial change in its enforcement policy that was not reasonably communicated to the public."); *Epilepsy Found. of Northeast Ohio v. NLRB*, 268 F.3d 1095, 1102-03 (D.C. Cir. 2001). That is precisely what the Division proposes to do here.

First, the Division is proposing a radical departure from existing law. The Division would jettison the long-established rule that whether one is a dealer turns on a long list of factors,

not just one. *See Nat'l Council of Savings Insts.*, 1986 WL 67129, at *2 (whether one is a dealer may not be determined on "just one portion of [one's] activities"); *Burton*, 1977 WL 10680, at *1-2 (same). In that rule's place, the Division would hold that either of the following is enough, *alone*, to make one a dealer: (1) selling stock within two years of acquiring the stock; (2) buying and selling securities in more than isolated transactions. Such a rule would sweep in virtually every hedge fund and other institutional investor nationwide.

Second, Respondents and the public have substantially relied on the long-established guidance like *Acqua Wellington* and the other sources listed above. Indeed, there are a number of unregistered institutional investors who sell stock quickly like a statutory underwriter and also buy and sell stock regularly. Hedge funds are an obvious example. *See generally Risks of Hedge Fund Operations, Hearing on Hedge Fund Operations Before H. Comm. on Banking*, 105th Cong. (1998) (testimony of Richard R. Lindsey, Dir., Div. of Mkt. Regulation, U.S. SEC), http://www.sec.gov/news/testimony/testarchive/1998/tsty1498.htm ("Lindsey Testimony") (noting that hedge funds "typically" do not register as dealers); *see also id.* ("[T]he Commission does not regulate the activities of hedge funds[.]").

Third, the Division seeks a monetary penalty here. *See* OIP § III.C.

Fourth, the Division's proposed rule is sweeping and would envelope a number of heretofore unregistered investors, as explained above. *Ford Motor v. FTC*, 673 F.2d 1008, 1009 (9th Cir. 1981) ("[A]n agency must proceed by rulemaking if it seeks to change the law and establish rules of widespread application."). In short, the Division's proposal goes too far.

The Division argues that its position was foreseeable to Global IV, and thus not the sweeping and novel position Respondents contend, because Partner's "set[] up Global IV" in order to "qualify for the foreign broker-dealer exemption" to § 15(a). Opp. at 5. The Division

misstates the record. In the examination transcripts cited, the witnesses stated that Global IV was established in the British Virgin Islands "primarily to take advantage of the administrative capability" of the offshore funds administrator, as well as to take advantage of tax benefits. Kirkland Tr. at 24-25; Kreger Tr. at 48-49.

In addition, structuring Global IV offshore qualified it as "a non U.S. person." (Kirkland Tr. at 24.) But this is relevant only for purposes of Regulation S, and has nothing whatsoever to do with § 3(a)(10) exchanges. *See* 17 C.F.R. § 230.902(k) (definition of "U.S. person" under Regulation S). Similarly, being in the BVI qualified Global IV as a foreign broker-dealer. (Kirkland Tr. at 24; Kreger Tr. at 49:2-4 ("Q. So is Ironridge Global IV a broker/dealer? A. I don't know, it's not my area.").) *See* 17 C.F.R. § 240.15a-1. As a foreign broker-dealer Global IV was "exempt from the registration requirements of sections 15(a)(1) or 15B(a)(1) of the [Exchange] Act to the extent that" it might engage in various activities and transactions. *See* 17 C.F.R. § 240.15a-6. "Since inception [Global IV] has made investments in a number of different structures" including "public offering." O'Neil Tr. at 53-54. Qualifying Global IV as a foreign broker-dealer was potentially beneficial for any number of potential transaction structures.

There is no evidence that Respondents (or anyone else on the planet) ever thought that Global IV might be deemed a dealer with regard to court-approved § 3(a)(10) exchanges.

4. Global IV Is a Foreign Broker-Dealer and Thus Exempt.

The Division makes two arguments for why Global IV is not exempt as a foreign broker-dealer, but its arguments are unpersuasive. First, the Division denies that Global IV "[e]ffects [§ 3(a)(10)] transactions in securities with or for . . . [a] registered broker dealer." 17 C.F.R. § 240.15a-6(a)(4). But there is no dispute that registered broker-dealers are the ones who receive and sell the shares issued in exchange for claims purchased by Global IV pursuant to court-approved agreements in the court-approved § 3(a)(10) exchanges.

In addition, in most cases the issuers themselves are represented by registered broker-dealers. *See* Sbarra Tr. at 15, 36-41.

The Division wants to treat each § 3(a)(10) exchange as multiple separate transactions—i.e., an exchange and a sale on the open market. But the Divisions entire theory of why Global IV is a dealer is that it was an underwriter selling shares in a distribution, which would mean that the entire deal was part of one transaction. The Division cannot have it both ways. Moreover, the exchange was exempt "to the extent that" shares were sold by registered broker-dealers, 17 C.F.R. § 240.15a-6, and every single one was.

Second, the Division also argues that Global IV solicits the issuers in § 3(a)(10) exchanges, despite explicit record evidence to the contrary. Motion at 26. The Division fails to point to a single completed exchange in which Global IV had solicited the issuer, so the Court should reject that argument.

Thus, even if Global IV were a dealer, it would be a foreign broker-dealer and exempt from § 15(a).

B. The Division's Novel Section 20(b) Theory Fails.

In another attempt to make new law here, the Division asks the Court to reject long-standing case law holding that § 20(b) requires a respondent to have had control over the primary violator. *See* Motion at 26 (listing cases). The statutory text says otherwise, because § 20(b) is part of a provision titled in part "Liability of *controlling* persons . . ." and expressly requires that the defendant commit a violation "by means of" the primary violator. 15 U.S.C. § 78t (emphasis added). The Division's interpretation of § 20(b) is also unreasonable, because "every link in a chain of command would be personally criminally and civilly liable for the violations of inferior corporate agents." *SEC v. Coffey*, 493 F.2d 1304, 1318 (6th Cir. 1974).

The Division argues that Congress implicitly overruled *Coffey* and its progeny because in a 1975 amendment Congress amended § 20(a) without adopting *Coffey* expressly. The Division has things backwards. That Congress amended the statute in 1975 is the end of the matter: Courts must presume that Congress knew about *Coffey* and would have overruled the decisions expressly if Congress disagreed. *See, e.g., Aguirre v. Los Angeles Unified School Dist.*, 461 F.3d 1114, 1118 (9th Cir. 2006).

The Division also relies on three other unpersuasive sources to support the argument that § 20(b) does not require control. The first is *SEC v. Strebinger, et al.*, No. 14-3533, 2015 WL 4307398 (N.D. Ga. June 11, 2015). There, however, the court stretched § 20(b) because otherwise there would have been no remedy for securities fraud. *Id.* at *11-12. There is no securities fraud here or any concern that wrongdoing would go totally unpunished without § 20(b), so there is no reason to stretch § 20(b). The Division also cites the 22nd footnote of *Short Sales in Connection With a Public Offering*, which mentions briefly that § 20(b) does not require control. Rel. No. 26028, 1988 WL 1000034 (Aug. 25, 1988). Because that footnote does not address the contrary case law or Congress's decision to abide by *Coffey*, that footnote is unpersuasive. Finally, the Division cites a single-sentence dictum from *Dirks v. SEC*, 463 U.S. 646 (1983). There, the Court suggested that a corporate insider might violate 20(b) by giving inside information to an outsider for the insider's personal gain. *Id.* at 659. The Court did not say either way if that would be true even when the insider did not control the outsider, so *Dirks* does not help the Division.

Next, the Division argues that § 20(b) is a form of "primary liability." That marks yet another attempt to create new law here: the case law is clear that § 20(b) establishes secondary liability only. Motion at 29-30.

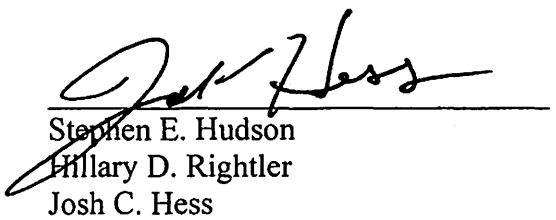
Finally, the Division argues that Partners "knowingly" caused Global IV to violate § 15(a). As explained above, nothing could be further from the truth. The Division's novel § 20(b) theory fails.

III. CONCLUSION

For these reasons, the Court should enter summary disposition for Respondents.

Dated: October 20, 2015.

Respectfully submitted,



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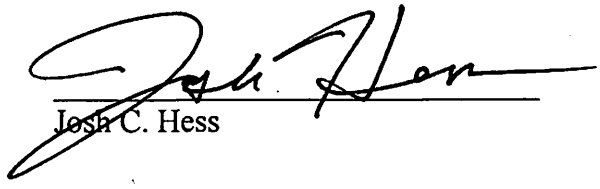
CERTIFICATE OF COMPLIANCE

I certify that the foregoing memorandum has 6,980 words starting with the Introduction and ending with the Conclusion and therefore complies with Rule of Practice 154.



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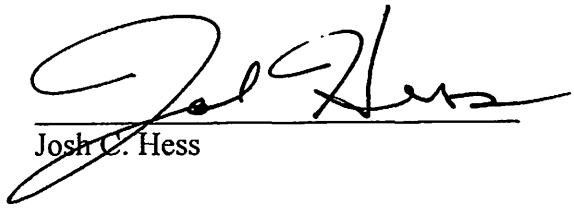
CERTIFICATE OF SERVICE

I hereby certify that on October 20, 2015, I filed and original and three copies of the foregoing by Federal Express Overnight Mail with the Office of the Secretary, Securities and Exchange Commission, Attn: Secretary of Commission Brent J. Fields, 100 F Street NE, Mail Stop 1090, Washington, DC 20549, and by facsimile transmission to (202) 772-9324, and served a true and correct copy upon counsel of record and the hearing officer by electronic mail, as follows:

Mr. Robert Gordon: gordonr@sec.gov
Securities and Exchange Commission

The Honorable James E. Grimes: alj@sec.gov
Administrative Law Judge
William Miller: millerwi@sec.gov



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