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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' OPPOSITION TO THE DIVISION'S MOTION IN LIMINE TO EXCLUDE INVESTIGATION AND DUE PROCESS EVIDENCE

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TABLE OF CONTENTS

ARGUMENT 2

A. The Division's Meandering Investigation Is Relevant. 2

B. The Court Should Allow Respondents to Call SEC Attorneys as Witnesses 5

C. The Court Should Allow Respondents to Mount a Procedural Due Process Defense 5

CONCLUSION 9

TABLE OF AUTHORITIES

Cases

1 Publicly Traded Corporations Handbook § 5:72 (2016) 1

Acqua Wellington North Am. Equities Fund, Ltd., SEC No-Action Letter, 2001 WL 1230266 (Oct. 11, 2001) 1

Amos Treat & Co v. SEC, 306 F.2d 260, 264 (D.C. Cir. 1962) 7

Antoniu v. SEC, 877 F.2d 721 (8th Cir. 1989) 7

Caperton v. A.T. Massey Coal Co., Inc., 556 U.S. 868 (2009) 7

Chapel Investments, Inc. v. Cherubim Interests, Inc., 177 F. Supp. 3d 981 (N.D. Tex. 2016) 1

FCC v. Fox Television Stations, Inc., 132 S. Ct. 2307 (2012) 4

Herndon v. Johnson, No. 88-70907, 1992 WL 152713 (E.D. Mich. April 7, 1992) 8

In re Black & Co., Inc. et al., Admin. File No. 3-3460, 1984 WL 906627 (July 12, 1974) 4

In re City of Anaheim, Admin. File No. 3-9739, 1999 WL 1034489 (Nov. 16, 1999) 2

In re Matter of J.S. Oliver Capital Management, LP., Admin File No. 3-15446, 2013 WL 11234075 (Dec. 31, 2013) 2

In re Murchison, 349 U.S. 133 (1955) 7

In re Next Financial Group, Inc., Admin. File. No. 3-12738 2008 WL 2444775 (June 18, 2008) 4

In re Timbervest, LLC, Admin. File No. 3-15519, 2015 WL5472520 (June 8, 2015) 8

Jenkins v. McKeithen, 395 U.S. 411 (1969) 8

Johnson v. Shaffer, No. 12-1059, 2014 WL 6834019 (E.D. Cal. Dec. 3, 2014) 7

KPMG, LLP v. SEC, 289 F.3d 109 (D.C. Cir. 2002) 4

Mathews v. Eldridge, 424 U.S. 319 (1976) 7

Oceana Capitol Grp. Ltd. v. Red Giant Entm't, Inc., 150 F. Supp. 3d 1219 (D. Nev. 2015) 1

Rothenberg v. Daus, 481 F. App'x 667 (2d Cir. 2012) 7

Treadwell v. Schweiker, 698 F.2d 137 (2d Cir. 1983) 8

Trinity Broad. of Fla., Inc. v. FCC, 211 F.3d 618 (D.C. Cir. 2000) 4

Upton v. SEC, 75 F.3d 92 (2d Cir. 1996) 4

Withrow v. Larkin, 421 U.S. 35 (1975) 7

Statutes

15 U.S.C. § 77c(a)(10) 1, 3

15 U.S.C. § 78n(a) 1, 3

Other Authorities

Jean Eaglesham, SEC Wins With In-House Judges, WALL STREET JOURNAL (May 6, 2015) 8

In this case, the Division alleges that Ironridge Global IV, Ltd. should have registered with the Commission as a "dealer" under § 15(a) of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78n(a), for engaging in court-supervised, debt-for-equity exchanges that § 3(a)(10) of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. § 77c(a)(10), exempts from the Commission's purview. The Division relies on an entirely novel theory, which is that Global IV supposedly acted as a statutory underwriter and that being a statutory underwriter is enough, by itself, to make one a dealer. Opposition to Summary Disposition (Oct. 13, 2015) at 16, 18. The longstanding guidance is directly contrary. *E.g.*, *Acqua Wellington North Am. Equities Fund, Ltd.*, SEC No-Action Letter, 2001 WL 1230266 (Oct. 11, 2001) (granting no-action relief to a statutory underwriter that had asked whether the dealer-registratoin provision applied to it); *see also Oceana Capitol Grp. Ltd. v. Red Giant Entm't, Inc.*, 150 F. Supp. 3d 1219 (D. Nev. 2015); *Chapel Investments, Inc. v. Cherubim Interests, Inc.*, 177 F. Supp. 3d 981 (N.D. Tex. 2016);1 Publicly Traded Corporations Handbook § 5:72, n.8 (2016).

Respondents have asserted a number of defenses to those novel charges, including two Due Process defenses: (1) to punish Respondents under such a novel theory, especially on the order of $22 million or more, would violate Due Process, and (2) that the administrative process is systemically biased against respondents. In support of the first defense, Respondents seek to introduce evidence that, when this case began, the Division itself did not believe that Respondents' business required registration under § 15(a). Specifically, Respondents seek to introduce evidence that the Division's enforcement action against Respondents began under theories that did not include § 15(a) and then lurched from one theory to another until the Division settled on the novel charges now alleged. In support of the second defense, Respondents seek to introduce evidence about how the administrative process favors the Division over respondents.

The Division argues that Respondents' evidence in support of these two defenses should be excluded because the evidence is irrelevant. The Division is incorrect, however. The Division also argues that the procedural Due Process defense is meritless and thus does not warrant further factual development. But the Division never moved for summary disposition on that defense, so the procedural Due Process defense is part of this case; it has not been stricken or removed; and Respondents should be permitted to offer relevant evidence to support that defense. Therefore, the Division's motion in limine should be denied.

ARGUMENT

"[T]he Commission has consistently made clear that administrative law judges should be inclusive in making evidentiary determinations." *In re Matter of J.S. Oliver Capital Management, LP.*, Admin File No. 3-15446, 2013 WL 11234075, at *5 (Dec. 31, 2013); *In re City of Anaheim*, Admin. File No. 3-9739, 1999 WL 1034489, at *2 & n.7 (Nov. 16, 1999). That is especially true of evidence that respondents submit. As another ALJ recently reiterated, "It is vital that Respondents have a full and fair opportunity to show that the allegations in the OIP are not true." *Oliver Capital*, 2013 WL 11234075, at *5. By that standard, the Court should admit Respondents' evidence.

A. The Division's Meandering Investigation Is Relevant.

The Division asks the Court to exclude as irrelevant evidence related to the Division's investigation, particularly the Division's various shifting theories for holding Respondents liable. That evidence includes the Formal Order of Investigation and correspondence with the Division's Staff. The Court should reject that argument. The evidence is relevant to (1) Respondents' defense that the Division seeks to punish them under a novel theory in violation of Due Process and, relatedly, (2) Respondents' argument that the Court should not sanction them if

the Court finds that they violated the Division's novel interpretation of § 15(a) of the Exchange Act.

By way of background, in October 2013 the Commission directed the Division to investigate what the SEC apparently thought was a debt-for-equity exchange between East Coast Diversified and Ironridge Global Partners, LLC, ("Partners") under Section 3(a)(10) of the Securities Act. *See* Order of Investigation. The Commission directed the Division to investigate just two issues: (1) whether there had been violations of § 17(a) of the Securities Act and § 10(b) of the Exchange Act, which generally prohibit securities fraud; and (2) whether the exchange complied with the Securities Act § 5's securities-registration requirement. *See* Order of Investigation at 2. The Commission did *not* direct the Division to investigate any alleged violation of § 15(a) of the Exchange Act.

Thereafter during the investigation, the Division repeatedly shifted theories why one or both Respondents were liable.

- In July 2014 – nine months after the investigation began – the Division issued a *Wells* notice to Partners abandoning the original fraud theory and stating that the Division had made a preliminary determination to recommend an enforcement action for violation of Section 5 of the Securities Act and also § 15(a) of the Exchange Act. *See* Motion for Summary Disposition, Exhibit R.

- In January 2015, the Division issued a new *Wells* notice – this time to both Partners and Global IV. *Id.*, Exhibits S and T. This time, the Division asserted that Global IV (not Partners) had violated Section 5 and Section 15(a). And the Division asserted that Partners was vicariously liable for Global IV's supposed violations, citing § 20(a) of the Exchange Act.

- In April 2015, the Division announced that it was once again amending its *Wells* notice to allege that Partners had violated Exchange Act § 20(b) (not § 20(a)) for allegedly using Global IV to violate the dealer-registration requirement.

- On June 23, 2015, the Division obtained the OIP. The OIP omitted fraud allegations, allegations under Securities Act § 5, and allegations under Exchange Act § 20(a). Instead, the OIP alleged that Global IV had acted as a dealer by engaging in § 3(a)(10) exchanges, chiefly because Global IV had supposedly engaged in "serial

underwriting activity." OIP, ¶ 1. The OIP also alleged that Partners was vicariously liable for Global IV's conduct under Exchange Act § 20(b).

That the Division shifted theories so often – and that it is relying on theories neither it nor the Commission envisioned at the outset – is evidence that the Division is relying on novel liability theories here. Had the existing guidance clearly stated that an entity like Global IV is a dealer under § 15(a), then the Division would have pursued that theory from the beginning.

Contrary to the Division's argument in its Motion in Limine, this evidence of the theories' novelty is relevant to at least two defenses Respondents have asserted.

First, the theories' novelty shows that Respondents could not have had fair warning of their conducts' alleged unlawfulness. That fact supports Respondents' defense under the Due Process Clause, which sometimes allow an agency to *announce* a new theory in an administrative proceeding but forbids the agency from then *penalizing* the respondents based on a theory about which they lacked fair warning. *Trinity Broad. of Fla., Inc. v. FCC*, 211 F.3d 618, 628 (D.C. Cir. 2000); *see also KPMG, LLP v. SEC*, 289 F.3d 109, 116-17 (D.C. Cir. 2002); *Upton v. SEC*, 75 F.3d 92, 98 (2d Cir. 1996); *FCC v. Fox Television Stations, Inc.*, 132 S. Ct. 2307, 2317-18 (2012).

Second, and relatedly, that theory's novelty supports Respondents' defense to the Division's sizeable sanctions demand. Under SEC practice, a case's novelty weighs against imposing sanctions on a respondent. *In re Next Financial Group, Inc.*, Admin. File. No. 3-12738 2008 WL 2444775, at *50 (June 18, 2008); *In re Black & Co., Inc. et al.*, Admin. File No. 3-3460, 1984 WL 906627, at *24 (July 12, 1974).

In short, Respondents' evidence about how the Division conducted its investigation here – and the Division's shifting theories – is relevant and should be admitted. The Court should deny the Division's motion in limine.[1]

B. The Court Should Allow Respondents to Call SEC Attorneys as Witnesses

Relatedly, the Division moves the Court to forbid Respondents from calling as witnesses SEC Attorneys Matthew McNamara and Kyle Bradley, who both participated in the Division's investigation here. For the reasons above, Respondents seek to call those witnesses to establish and explain the history of the Division's investigation of Respondents.

The Division contends that any such testimony would necessarily tread on confidential attorney-client communications, confidential work product, and the like. But the investigation's history is not confidential or privileged. And, as for any questions that might elicit privileged information, that Court can deal with that on a queston-by-question basis. The Court should deny the motion.

C. The Court Should Allow Respondents to Mount a Procedural Due Process Defense

The Division asks the Court to exclude all evidence that the SEC's administrative proceedings violate Respondents' procedural Due Process rights. Motion in Limine at 5-6. Although the Division did not move for summary disposition on that defense, the Division contends that the defense amounts to mere "unsupported speculation" and thus does not warrant further factual development. *Id.* at 6. The Court should reject that argument at this point in the proceedings.

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[1] Without explanation, the Division in passing asks the Court to exclude several letters from one of the Respondents to the Division, demonstrating that Respondents cooperated fully with the investigation and even asked the Division whether the Division believed any modifications to Respondents' compliance process were necessary. *See* Motion in Limine at 3 (listing Respondents' Exhibit 44-50). This evidence likewise shows that the Division's position is a novel one: Respondents' openness and cooperativeness show that Respondents believed that they had nothing to hide under the then-existing law.

As in initial matter, several of the documents the Division seeks to exclude are not related to Respondents' defense that the administrative process violates the procedural Due Process Clause. One is a June 2014 speech by SEC Chair Mary Jo White stating, "I have asked the SEC staff to prepare two recommendations to the Commission: the first, a rule to clarify the status of unregistered active proprietary traders to subject them to our rules as dealers[.]" Respondents Ex. 59 at 4. That speech shows that even the Commission itself admits that the rules about who is a dealer – especially the rules about how trading frequency affects one's dealer status – need "clarif[ication]." Hence, the documents supports Respondents defenses that they lacked fair warning of the Division's position here, which is that trading with high frequency makes one an underwriter and thus automatically a dealer. *See* Division's Opposition to Summary Disposition at 19-20. Additionally, Respondents' Exhibits 42 and 43[2] shows that SEC ALJs are not appointed by the Commissions. *E.g.* Resp. Ex. 42 at 25 and 43 at 2. Those exhibits therefore support Respondents' Appointments Clause defenses, which is that ALJs presiding over SEC proceedings have not been appointed the way the Constitution requires for such inferior officers. *See* U.S. Const., Art. II, Sec. 2, Cl. 2. The Court should disregard the Division's argument as to those exhibits.

As for the rest, the Division's argument fails for two reasons.

First, the Division has waived its objection to allowing Respondents to mount a Due Process defense. Respondents have asserted that defense from this case's start. *See, e.g.*, Answer and Affirmative Defenses of Ironridge Global IV, Ltd. at 8. So if the Division thought that Respondents' defense was so meritless that further factual development was unwarranted, the Division should have filed a motion for summary disposition on that defense. The Division

[2] Exhibits are attached to the Division's motion.

chose not to do so and must accept the consequences. Asking the Court to essentially strike the defense through a motion in limine is improper.

Second, and in any event, the Division is incorrect that Respondents' Due Process defense is mere "unsupported speculation."

Respondents' defense is that the governing SEC practices, "rules[,] and processes" are inadequate given the stakes[3] in cases like this one and also "rig proceedings" against respondents, creating a "systemic bias" in the Division's favor. *Johnson v. Shaffer*, No. 12-1059, 2014 WL 6834019, at *9 (E.D. Cal. Dec. 3, 2014); *id.* at *9-13 (holding that a parole-eligibility protocol that was allegedly designed to make it harder for parolees to prevail could violate Due Process by causing systemic bias against parolees); *Rothenberg v. Daus*, 481 F. App'x 667, 676-77 (2d Cir. 2012). For example:

- The ultimate decision maker in many SEC cases is the Commission itself – the same body that decides to charge respondents in the first place. *See* Rule of Practice 200(a)(1). Such dual roles cause the Commission to prejudge every case against respondents "in some measure"[4] – or at least "potential[ly]"[5] do so. *See, e.g.*, *Amos Treat & Co v. SEC*, 306 F.2d 260, 263, 264 (D.C. Cir. 1962) ("[T]he investigative as well as the prosecuting arm of the agency must be kept separate from the decisional function."); *id.* at 266-67; *In re Murchison*, 349 U.S. 133, 137 (1955) ("It would be very strange if our system of law permitted a judge to act as a grand jury and then try the very persons accused as a result of his investigations."); *see Withrow v. Larkin*, 421 U.S. 35, 58 (1975) (acknowledging that the "combination of investigative and adjudicative functions" could in some circumstances present a "risk of unfairness" that "is intolerably high").[6]

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[3] *Mathews v. Eldridge*, 424 U.S. 319, 341-42 (1976).

[4] *Antoniu v. SEC*, 877 F.2d 721, 726 (8th Cir. 1989).

[5] *Caperton v. A.T. Massey Coal Co., Inc.*, 556 U.S. 868, 881 (2009) (holding that Due Process forbids a judge from participating in a case where there is an unconstitutional "potential for bias").

[6] The Commission apparently does not accept this view, but Respondents respectfully request the opportunity to make their record so that they can urge the Commission to change its mind or seek relief from the Court of Appeals.

- The Division enjoys near limitless power and time to conduct discovery and develop its case against respondents. Yet respondents have few discovery tools, which are the "traditional safeguards" of Due Process. *Herndon v. Johnson*, No. 88-70907, 1992 WL 152713, at *24 (E.D. Mich. April 7, 1992) (holding that "discovery" is one of the "traditional safeguards of the adequacy [of] process" under the Due Process Clause). Without such tools, respondents have little ability to marshal evidence in their defense. *Jenkins v. McKeithen*, 395 U.S. 411, 429 (1969) ("The right to present evidence is, of course, essential to the fair hearing required by the Due Process Clause."); *Treadwell v. Schweiker*, 698 F.2d 137, 144 (2d Cir. 1983) (holding that ALJ violated Due Process by failing to enforce a subpoena to obtain evidence a party to the proceeding had sought).

- The Federal Rules of Evidence are inapplicable. The Commission may find against respondents based on hearsay. *Treadwell*, 698 F.2d at 143-44 (holding that ALJ's reliance on hearsay was one reason a proceeding violated Due Process).

- SEC ALJs are pressured to decide against respondents. One former ALJ recently reported that Chief ALJ Brenda Murray had pressured her to find against respondents and that she was expected to work on the assumption that the "burden was on the people who were accused to show that they didn't do what the agency said they did." Jean Eaglesham, SEC Wins With In-House Judges, WALL STREET JOURNAL (May 6, 2015).

- Respondents are deprived of their Constitutional right to a jury trial.

The contention that such structural defects bias the system against respondents is more than "unsupported speculation." Between October 2010 and March 2015, the Division won 90% of cases before SEC ALJs, compared with a 69% success rate in federal court. Eaglesham, *supra*. And from January 2010 through March 2015, the Commission decided in favor of the Division 95% of the time. *Id.* Thus, the Division's argument for exclusion here fails.

The Division argues that the Commission already rejected such a Due Process defense and that the Commission, and this Court, also held that such a defense does not warrant factual development. *In re Timbervest, LLC,* Admin. File No. 3-15519, 2015 WL5472520 (June 8, 2015) (Commission opinion). The Division's argument fails for two reasons. First, the Commission did not reject a structural-bias argument that agency's rules, procedures, and practices all tilt against respondents. Rather, the Commission rejected an argument that a

particular ALJ was biased against the respondents in that proceeding. *Id.* at *21-22. Second, and in any event, both the Commission's opinion and this Court's October 15, 2015 held merely that respondents were not entitled to *discovery* for evidence related to a bias defense. *Id.* at 22 (denying "discovery requests"). Neither held that respondents were barred from introducing evidence that they already had regarding bias. Quite the contrary, in *Timbervest* the Commission accepted such evidence "for inclusion in the record." *Id.*

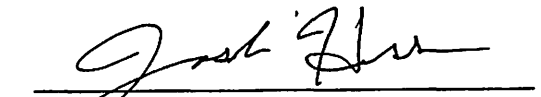
In short, the Court should deny the Division's motion to exclude evidence related to Respondents' systemic-bias defense.

CONCLUSION

Respondents respectfully request that the Court deny the Division's motions in limine.

Dated: November 10, 2016.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I hereby certify that on November 10, 2016, I filed an original and three copies of the foregoing 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, by Federal Express overnight delivery and filed a copy by facsimile transmission to (202) 772-9324, and served a true and correct copy upon counsel of record by electronic mail (and also by Fedex delivery to Division counsel), as follows:

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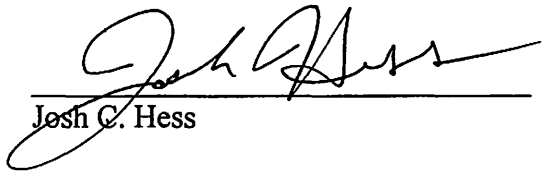

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