Kline, Scot

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From: Alexander, Jon
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Here are some pertinent case excerpts on the 'in connection with' requirement of the antifraud provisions of the federal securities laws (Section 1o of the Securities Exchange Act, SEC Rule 10b-5, and Section 17 of the Securities Act).

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Courts construe broadly the "in connection with" element of Section 10(b), Rule 10b–5, and Section 17(a). *SEC v. Credit Bancorp, Ltd.*, 195 F.Supp.2d 475, 491 (S.D.N.Y.2002); *SEC v. Hasho*, 784 F.Supp. 1059, 1106 (S.D.N.Y.1992). To establish that fraudulent conduct satisfies the "in connection with" requirement, "[i]t is enough that the scheme to defraud and the sale of securities coincide." *SEC v. Zandford*, 535 U.S. 813, 822, 122 S.Ct. 1899, 1904, 153 L.Ed.2d 1 (2002). The "in connection with" requirement is satisfied whenever "assertions are made ... in a manner reasonably calculated to influence the investing public, e.g., by means of the financial media...." *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 862 (2d Cir.1968). Applying this standard, courts have concluded that publicly-disseminated press releases, research reports, and website representations that contain materially false and misleading statements regarding an issuer of securities satisfies the "in connection with" requirement. *See, e.g., SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1362 (9th Cir.1993); *see also Rowinski v. Salomon Smith Barney Inc.*, 398 F.3d 294 (3d Cir.2005) (statements made in a research report satisfied the "in connection with" requirement under Section 10(b)); *SEC v. DCI Telecomm., Inc.*, 122 F.Supp.2d 495, 499–500 (S.D.N.Y.2000) *259 (statements in press releases and website content satisfy the "in connection with" requirement).

S.E.C. v. StratoComm Corp., 2 F. Supp. 3d 240, 258-59 (N.D.N.Y. 2014), appeal dismissed (Aug. 18, 2014)

The Defendants challenge the application of the Exchange Act to their conduct because they contend that the alleged fraud was not in connection with the purchase or sale of a security. They claim that they sell information, not securities.
7 In order to prove that the Defendants violated Section 10(b) of the Exchange Act, the SEC must establish that they (1) made a material misrepresentation or a material omission, or used a fraudulent device; (2) with scienter; (3) in connection with the purchase or sale of securities. *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir.1999). The Defendants' motion to dismiss challenges the third element.
89 **The "in connection with" element is satisfied when the misrepresentation or omission or use of a device would be the sort of conduct on which a reasonable investor would rely, and, so relying, would purchase or sell securities. *In re Carter–Wallace, Inc. Sec. Litig.*, 150 F.3d 153, 156 (2d Cir.1998). The "in connection with" requirement is construed broadly and flexibly to effectuate the remedial purposes of the federal securities laws. *SEC v. Zandford*, 535 U.S. 813, 819, 122 S.Ct. 1899, 153 L.Ed.2d 1 (2002).**
Paragraph 47 of the complaint has alleged facts that if proven could show that the Defendants provided false or misleading information to their auto-trading subscribers upon which reasonable investors would rely in the purchase or sale of securities. Because the complaint has alleged facts that would support the "in connection with" element of Section 10(b) of the Exchange Act, the Defendants are not entitled to dismissal of Count One.

S.E.C. v. Terry's Tips, Inc., 409 F. Supp. 2d 526, 533 (D. Vt. 2006)

MLSMK argues for the first time in its supplemental brief that the defendants' conduct is not "actionable securities fraud" because the "the predicate acts alleged in this case could not possibly have induced MLSMK to purchase or sell securities." It contends that the claim therefore does not satisfy the requirements of section 10(b) of the Securities Exchange Act.

Compare Appellant's Supp. Br. 6, *with* Appellees' Supp. Br. 7–8. Even were we not to consider this argument waived because of the lateness of the hour in which it was asserted, we would nonetheless decline to address it because we conclude that the effect of the RICO Amendment does not turn on whether MLSMK would be able to state a valid claim against JPMC and Chase Bank under section 10(b).

To the extent that MLSMK argues that the defendants' alleged conduct does not qualify as securities fraud because it was not "integrally related to the purchase and sale of securities," Appellant's Supp. Br. 6, we conclude that the contention is without merit. In *Bald Eagle Area School District,* the Third Circuit considered a plaintiff's allegation that a defendant bank had assisted in "a massive Ponzi scheme ... perpetrated through the purchase and sale of [securities] in violation of securities laws including § 10(b) of the Securities Exchange Act of 1934," and determined that the alleged scheme was "at the heart of th[e plaintiff's] RICO action." *Id.,* 189 F.3d at 328. The court concluded that **"[a] Ponzi scheme ... continues only so long as new investors can be lured into it so that the early investors can be paid a return on their 'investment.' Consequently, conduct undertaken to keep a securities fraud Ponzi scheme alive is conduct undertaken in connection with the purchase and sale of securities."** *Id.* at 330; *cf. Sell v. Zions First Nation Bank,* No. CV–05–0684, 2006 WL 322469, at *10, 2006 U.S. Dist. LEXIS 6558, at *33–*34 (D.Ariz. Feb. 9, 2006) (stating that "the question is not whether a plaintiff can state a claim under a non-securities-related predicate act, but whether the allegations that form the basis of that predicate act occur 'in connection with' securities fraud," and concluding that, **in a Ponzi scheme, a bank's "disbursement[s] of money from more recent investors to older investors" are actions "in connection with" securities fraud**).

MLSMK Inv. Co. v. JP Morgan Chase & Co., 651 F.3d 268, 277 n.11 (2d Cir. 2011)

The "in connection with the purchase or sale" requirement must be construed "not technically and restrictively, but flexibly to effectuate its remedial purpose." *SEC v. Zandford,* 535 U.S. 813, 820–21, 122 S.Ct. 1899, 153 L.Ed.2d 1 (2002). In *SEC v. Zandford,* 535 U.S. 813, 122 S.Ct. 1899, 153 L.Ed.2d 1 (2002), the Supreme Court gave deference to the SEC's interpretation of the "in connection with the purchase or sale" requirement, explaining that

[T]he SEC has consistently adopted a broad reading of the phrase "in connection with the purchase or sale of any security." It has maintained that a broker who accepts payment for securities that he never intends to deliver ... violates § 10(b) and Rule 10b–5. This interpretation of the ambiguous text of § 10(b), in the context of formal adjudication, is entitled to deference if it is reasonable.

Id. at 819–20, 122 S.Ct. 1899 (internal citations omitted). Pursuant to a broad interpretation of **"in connection with,"** the Supreme Court held that the **requirement was satisfied where a broker who had investment authority over a client's account sold the securities in the account and pocketed the sales proceeds.** *Id.* **While the fraudulent conduct alleged—misappropriation of the proceeds of securities sales—was not the direct result of a purchase or sale, the broker's scheme to defraud "coincided" sufficiently with the actual (and completely legitimate) sale of those securities to satisfy the "in connection with" requirement.** *Zandford, supra.,* 535 U.S. at 820, 122 S.Ct. 1899.

In re J.P. Jeanneret Associates, Inc., 769 F. Supp. 2d 340, 361 (S.D.N.Y. 2011)

In order to make out a Section 10(b) and Rule 10b–5 claim, the Plaintiffs "must establish that 'the defendant, in connection with the purchase or sale of securities, made a materially false statement of a material fact, with scienter, and that the plaintiff's reliance on the defendant's action caused injury to the plaintiff.' " *Lawrence v. Cohn*, 325 F.3d 141, 147 (2d Cir.2003) (quoting *Ganino v. Citizens Utils. Co.*, 228 F.3d 154, 161 (2d Cir.2000)). **Because certain alleged misrepresentations were made after the purchase of securities, and therefore not "in connection with the purchase or sale of securities," the Court concludes that those misrepresentations are not actionable.**

Ashland Inc. v. Morgan Stanley & Co., 700 F. Supp. 2d 453, 463 (S.D.N.Y. 2010) aff'd, 652 F.3d 333 (2d Cir. 2011)

Kline, Scot

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2015 WL 4067095
United States District Court,
D. New Hampshire.

SECURITIES AND EXCHANGE COMMISSION
v.
Allen R. SMITH.

Civil No. 14-cv-192-PB.
|
Signed July 2, 2015.

Attorneys and Law Firms

Stephen W. Simpson, Us Securities & Exchange Commission, Washington, DC, for Plaintiff.

Allen Ross Smith, Winter Haven, FL, pro se.

MEMORANDUM AND ORDER

PAUL BARBADORO, District Judge.

*1 The Securities and Exchange Commission (the "SEC") claims in this securities fraud action that Allen Smith participated in an advance-fee investment fraud scheme in his capacity as an attorney and fiduciary. The SEC now moves for summary judgment and asks the court to impose injunctive relief, disgorgement, and a monetary civil penalty against Smith. Most of the SEC's claims require proof of scienter, which ordinarily must be resolved during a trial. Here, however, the SEC has produced compelling evidence of Smith's involvement in the fraud, and Smith's meager opposition to the SEC's motion neither identifies a genuine dispute of material fact nor explains why the SEC's motion should be denied. Accordingly, I determine that the SEC is entitled to summary judgment on both its substantive claims and its requests for disgorgement and permanent injunctive relief. But because the SEC's claim for a monetary penalty requires further factual and legal development, I deny the SEC's request for a civil monetary penalty without prejudice to its right to renew its request in a properly supported motion.

I. *BACKGROUND*

The SEC alleges that Smith participated in an investment fraud scheme in his capacity as an attorney and fiduciary. I first summarize the scheme itself and then describe Smith's involvement.

A. *The Fraudulent Scheme*

Between 2009 and 2011, Martin Schläpfer, James Warras, and Hans-Jurg Lips (the "Principals") conducted an advance-fee investment scam that defrauded more than 30 investors out of over $10.8 million. The Principals conducted their fraud through a number of business entities, including:

- Malom Group AG (with "Malom" being an acronym for "make a lot of money"), a Swiss business organization run by Schläpfer and Lips.
- Northamerican Sureties (Europe) AG ("NAS Europe"), another Swiss business organization where both Schläpfer and Warras served as executives.
- Northamerican Sureties Ltd. ("NAS Ltd."), a Utah organization that specialized in issuing surety bonds guaranteeing loan performance. Although Schläpfer was a board member of both NAS Europe and NAS Ltd., the two firms were separate entities.
- M.Y. Consultants, Inc., a Nevada firm with few, if any, regular employees that facilitated Malom's transactions with investors.
- Maxmore Corporation Ltd., a Hong Kong business organization of which both Schläpfer and Warras were principals.

The Principals devised two separate investment scams. The first, which the SEC calls the "joint venture offering," lasted from August 2009 until August 2011. For an advance fee of between $150,000 and $200,000, this scam invited investors to enter into joint venture arrangements with several of the business entities controlled by the Principals, most frequently Maxmore. Those entities, the Principals claimed, would then use their capital to purchase U.S. treasury securities at a discount, resell them for a 100 percent profit, and repeat the cycle, generating a significant yield on the investors' original contribution. In fact, the entire arrangement was fraudulent; no such trades ever took place. The Principals