

**COURTESY
COPY**

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
SECURITIES AND EXCHANGE COMMISSION, :

Plaintiff, :

v. :

TECUMSEH HOLDINGS CORPORATION, :
TECUMSEH TRADEVEST LLC, :
S.B. CANTOR & CO., INC., JOHN L. MILLING, :
GERARD A. McCALLION, :
ANTHONY M. PALOVCHIK, and DALE CARONE, :

Defendants, :

- and - :

TECUMSEH ALPHA FUND LP, :
TECUMSEH ALPHA LLC, and :
STRACQ, INC., :

Relief Defendants. :
-----X

03 Civ. 5490 (SAS)

**MEMORANDUM OF LAW IN SUPPORT
OF PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S
MOTION FOR AN ORDER AUTHORIZING CREATION OF A FAIR FUND,
APPROVING PLAN OF DISTRIBUTION AFTER NOTICE
TO INVESTORS, AND FOR A SCHEDULING ORDER**

**SECURITIES AND EXCHANGE
COMMISSION
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April 29, 2011

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Plaintiff Securities and Exchange Commission (the “Commission”) respectfully submits this Memorandum of Law in support of its motion for an Order (i) authorizing the Commission to create a Fair Fund pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7246(a); and (ii) approving the Commission’s Proposed Plan of Distribution (the “Proposed Plan”) after notice to investors, submission of objections, if any, and a hearing; and an Order setting a schedule for circulation of the Proposed Plan, filing of objections, and a hearing on the Commission’s Motion for approval of the Proposed Plan.

BACKGROUND

The Commission instituted this action on July 24, 2003 against Defendants and Relief Defendants. (Docket Entry (“DE”) 1.) At the time it filed its Complaint, the Commission also sought a Temporary Restraining Order, Preliminary Injunction, Asset Freeze and other relief, including the appointment of a receiver. (DE 5.) By Order to Show Cause, entered July 25, 2003, the Court granted Plaintiff’s application for a Temporary Restraining Order, including an Asset Freeze, and appointed a Receiver. On consent of Defendants who appeared, the Court entered a Preliminary Injunction Order on September 5, 2003. (DE 26.) On Defendant Milling’s motion, the case was stayed until August 2008. (Id.)

As alleged in the Complaint, Tecumseh and Tradevest conducted a nationwide cold-calling campaign to sell unregistered securities of Tecumseh and Tradevest. (DE 1; 103 (Opinion and Order, entered December 22, 2009, granting in part, Plaintiff’s Motion for Partial Summary Judgment against Milling.) From 2000 until July 2003, Tecumseh and Tradevest raised at least \$10 million from approximately five hundred investors. (Id.) Tecumseh, Tradevest and Milling, a securities lawyer who acted as Tecumseh’s CEO and was primarily responsible for

drafting Tecumseh's fraudulent offering materials, acted with the assistance of Defendants Cantor, a New Jersey-based broker-dealer that Tecumseh controlled; McCallion, Cantor's President; Palovchik, Tecumseh's Vice President, Carone, manager of Tecumseh's California office; and others working with them. (DE 1.)

Defendants Tecumseh, Tradevest and Milling induced investors to acquire securities of Tecumseh and Tradevest by means of a host of material misrepresentations. (DE 1; DE 127 (Opinion and Order, entered January 18, 2011, granting in part Plaintiff's Motion for Summary Judgment against Milling.) Through offering memoranda and other materials, these Defendants (a) touted false and misleading profit projections; (b) promised some investors "returns on investment" or "dividends" without disclosing that Tecumseh and Cantor had no earnings to distribute and that any such payments necessarily come from capital, including funds raised from other investors; and (c) made materially misleading statements concerning NASD approval for Tecumseh's acquisition of Cantor, a registered broker-dealer and a member of NASD. Tecumseh, Tradevest and Milling knew or acted in reckless disregard of the fact that their representations to investors concerning these matters were materially false and misleading. (Id.)

The Commission charged Defendants Tecumseh, Tradevest and Milling with violations of the antifraud provisions of the federal securities laws, Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 10b-5 thereunder. (DE 1.) It charged Defendants McCallion and Palovchik with aiding and abetting Tecumseh's and Milling's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and charged Defendants Tecumseh, Tradevest, Milling, Cantor and Carone with violations of the securities registration provisions, Sections 5(a) and 5(c) of the Securities Act. (Id.) Further, the Complaint charged Cantor with violations of the broker-dealer

books and records provisions, Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-4 thereunder, and Milling with aiding and abetting those violations. (Id.) The Complaint charged Carone with violations of the broker registration provisions, Section 15(a) of the Exchange Act. (Id.) Finally, the Complaint alleged that Alpha Fund (a hedge fund for which Tecumseh acted as sole Manager), Alpha LLC (the General Partner of Alpha Fund), and Stracq, Inc. (“Stracq”) (a corporation in which Tecumseh infused investor funds) were Relief Defendants which had received proceeds of the fraud in which they had no legitimate interest. (Id.)

On April 11, 2005, the Court entered a Final Judgment on consent against Relief Defendant Stracq, pursuant to which Stracq agreed to pay disgorgement of \$660,000 to the Receiver. (DE 43.) On March 9, 2009, the Court entered a Final Judgment on consent against Defendant McCallion, pursuant to which McCallion was enjoined from further violations of the antifraud provisions of the federal securities laws, was permanently barred from participation in any penny stock offering and was ordered liable for \$1 in disgorgement and \$40,000 in civil penalty, and ordered to remit \$40,001 to the Clerk of the Court for deposit in the CRIS. (DE 74.) Also on March 9, 2009, the Court entered a Final Judgment on consent of the Receiver against Defendants Tecumseh, Tradevest and Cantor, by which Defendants Tecumseh and Tradevest were enjoined from further violations of the antifraud provisions of the federal securities laws, all three Defendants were enjoined from further violations of Sections 5(a) and 5(c) of the Securities Act, and Defendant Cantor was enjoined from further violations of Section 17(a) of the Exchange Act, and Rules 17a-3 and 17a-4 thereunder. (DE 75.) All three Defendants were further permanently barred from participation in any penny stock offering. (Id.) Tecumseh was ordered liable for \$7,271,134 in disgorgement, and Cantor was ordered jointly and severally liable with Tecumseh to disgorge \$850,000 of this amount. (Id.) No payments on these

judgments have been received and the entities are defunct. (Declaration of Nancy A. Brown, executed April 29, 2011 (“Brown Decl.”), ¶ 2.) On January 26, 2011, the Court entered Final Judgment against Defendant Milling, enjoining him from further violations of the antifraud provisions of the federal securities laws, enjoined him from further violations of Section 5 of the Securities Act, and ordered him liable, jointly and severally with Tecumseh, for disgorgement of \$7,242,167, and individually for \$3,466,346.48 in prejudgment interest and \$116,500 in civil penalties. (DE 128.) To date, Milling has made no payments on this Final Judgment. (Brown Decl. ¶ 3.)

On March 6, 2009, the Commission filed a Notice of Dismissal without prejudice, pursuant to Fed. R. Civ. P. 41(a), against Relief Defendants Tecumseh Alpha Fund LP and Tecumseh Alpha LLC. (DE 73.)

On May 27, 2008, the Court entered a Partial Final Consent Judgment against Defendant Carone by which it enjoined him from further violations of Sections 5(a) and 5(c) of the Securities Act and Section 15(a) of the Exchange Act, and permanently barred him from participation in any penny stock offering. (DE 58.) The Court ordered Carone to pay disgorgement of all ill-gotten gains, prejudgment interest thereon and a civil penalty in amounts to be determined upon motion of the Commission. (Id.) The Commission’s motion for such relief is now pending before the Court. (DE 130.)

On November 7, 2008, the Court entered a Consent Judgment against Defendant Palovchik by which it enjoined him from further violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, barred him from participation in any penny stock offering and ordered him to pay disgorgement of ill-gotten gains, prejudgment interest thereon, and a civil

penalty in amounts to be determined upon motion of the Commission. (DE 68.) The Commission's motion for such relief is now pending before the Court. (DE 130.)

By Order entered March 30, 2009, the Court appointed Damasco & Associates LLP, a certified public accounting firm located in Half Moon Bay, California, as tax administrator to execute all income tax reporting requirements, including the preparation and filing of tax returns, with respect to the funds under the Court's jurisdiction in this case. (DE 77.) As of February 28, 2011, there was more than \$700,000 in the CRIS account for this case.

THE PROPOSED PLAN OF DISTRIBUTION

The Commission's Proposed Plan is designed to distribute the amounts Defendants and Relief Defendants have paid under the Judgments as a Fair Fund to Tecumseh investors. The Proposed Plan aims to return to them as much of their principal investment as possible, given the disgorgement, prejudgment interest and penalty payments received from Defendants and Relief Defendants, as well as a measure of interest for the period of investment.

The Commission believes that it is appropriate and in the best interests of the investors to make a distribution of the Fair Fund on a *pro rata* basis as set out in the accompanying Proposed Plan.

A. Creation of a Fair Fund

The Commission seeks to create a Fair Fund under the Sarbanes-Oxley Act with the disgorgement, prejudgment interest and penalty amounts paid by Defendants under the terms of the Judgments. If authorized, the creation of a Fair Fund will allow the Commission to contribute the \$40,000 received in penalties from Defendant McCallion to the sums available for distribution to investors, rather than paying those amounts to the Treasury.

B. The Proposed Plan

The Proposed Plan (submitted herewith as Brown Decl., Ex. A) provides for the distribution of the Fair Fund to all eligible investors in Tecumseh and Tradevest (collectively “Tecumseh”) securities, as described in the Complaint and the Proposed Plan. The Proposed Plan contemplates that all of the Fair Fund, minus the costs of the distribution will be distributed to Tecumseh investors.¹ The Proposed Plan provides for a *pro rata* General Distribution to the Eligible Claimants in proportion to the amount each Eligible Claimant invested, minus any distributions received by such Eligible Claimant to date. No distributions will be made to claimants whose loss was less than the De Minimis amount of \$25.

The Proposed Plan also provides for the possibility of a Supplemental Distribution if sufficient monies remain in the Fair Fund after the General Distribution, either because some investors are not located after diligent efforts, or Distribution Checks are not negotiated by the Stale Date.

C. The Proposed Scheduling Order

The Commission also seeks an Order setting a schedule for the circulation of the Proposed Plan to investors, a date by which objections, if any, must be submitted, and a hearing on any objections. The proposed Scheduling Order contemplates that the Proposed Plan will be sent to Tecumseh investors within 30 days after the Court has appointed a Fund Administrator. The Commission is currently seeking proposals from Fund Administrator candidates and will propose a Fund Administrator for the Court’s approval within 45 days.

¹ The Commission is seeking proposals from candidates for appointment as Fund Administrator. The Commission plans to propose a Fund Administrator for the Court’s approval within 45 days. The proposed Scheduling Order submitted herewith contemplates that the Proposed Plan be circulated to investors for their consideration and objection within 30 days following the entry of an Order appointing a Fund Administrator.

ARGUMENT

A. The Court Should Authorize the Creation of a Fair Fund

The Sarbanes-Oxley Act allows the Commission to seek a court order that adds the penalty payments of Defendant McCallion to the amounts to be distributed to investors through the creation of a Fair Fund. 15 U.S.C. § 7246(a).¹ The Fair Fund will allow the Commission to distribute the penalties to injured investors instead of paying them to the United States Treasury.² Distributing penalties to investors comports with the Congressional intent embodied in Section 308(a) of the Sarbanes-Oxley Act. Official Committee of Unsecured Creditors of WorldCom, Inc. v. SEC, 467 F.3d 73, 82 (2d Cir. 2006). Accordingly, the Commission requests that the Court authorize the Commission to create a Fair Fund consisting of all disgorgement, prejudgment interest and penalties paid and to be paid by Defendants for distribution to Tecumseh investors.

B. The Court Should Approve the Proposed Plan

After notice of the Proposed Plan and the Commission's motion for approval is sent to investors, and after investors have an opportunity to object, the Court should approve the Commission's Proposed Plan.

¹ Section 308(a) of the Sarbanes-Oxley Act, 15 U.S.C. § 7246(a), provides:

If in any judicial or administrative action brought by the Commission under the securities laws ... the Commission obtains an order requiring disgorgement against any person for a violation of such laws or the rules or regulations thereunder, or such person agrees in settlement of any such action to such disgorgement, and the Commission also obtains pursuant to such laws a civil penalty against such person, the amount of such civil penalty shall, on the motion or at the direction of the Commission, be added to and become part of the disgorgement fund for the benefit of the victims of such violation.

² Prior to the Sarbanes-Oxley Act, all civil penalties were required to be paid to the United States Treasury under Section 21(d)(3)(C) of the Exchange Act. See 15 U.S.C. § 78u(d)(3)(C).

District Courts have broad authority to approve plans of distribution proposed by the SEC in enforcement cases. SEC v. Wang, 944 F.2d 80, 85 (2d Cir. 1991).¹ In reviewing proposed plans, the Second Circuit instructs that courts should defer to the “experience and expertise” of the Commission in determining how to distribute the funds. WorldCom, 467 F.3d at 82. The Court acts within its discretion, therefore, where it determines that the plan proposed by the Commission is “fair and reasonable.” Id. (citing Wang, 944 F.2d at 85 (“once the district court satisfies itself that the distribution of proceeds in a proposed SEC disgorgement plan is fair and reasonable, its review is at an end.”))

Here, the Commission’s Proposed Plan is both fair and reasonable because it attempts to return to all Tecumseh investors some measure of their principal investment, net of distributions received by them to date, on a *pro rata* basis.

C. The Court Should Enter the Proposed Scheduling Order

The Commission proposes that the Court enter a Scheduling Order setting the dates by which the Proposed Plan should be circulated to investors, investors should submit objections and the Commission should respond, and a hearing date on the Commission’s motion for approval of its Proposed Plan.

CONCLUSION

For all the foregoing reasons, the Commission respectfully requests that the Court grant its Motion for an Order (i) authorizing the Commission to create a Fair Fund pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002; and (ii) approving, after notice to investors and an

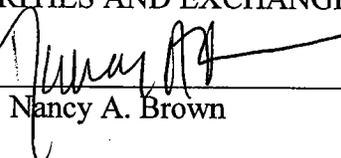
¹ Although a distribution of disgorged funds is not required by statute, where practicable, disgorged money is often distributed to victims of the violation in accordance with a plan proposed by the Commission and approved by the court. Where feasible and appropriate to effect such a distribution, the Commission has been vested with broad discretion in fashioning distribution plans for funds like the Proposed Plan in this case. See id.

opportunity for them to object, the Commission's Proposed Plan; and an Order setting a schedule for circulation of the Proposed Plan, filing of objections, and a hearing on the Commission's Motion for approval of the Proposed Plan.

Dated: New York, New York
April 29, 2011

SECURITIES AND EXCHANGE COMMISSION

By: _____



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Certificate of Service

I hereby certify that I caused the foregoing Memorandum of Law In Support of Plaintiff's Motion For an Order Authorizing Creation of a Fair Fund, Approving Plan of Distribution after Notice to Investors, and for a Scheduling Order to be served on the Receiver in this action, Robert Knuts, Esq., by emailing a copy of the same to him at rknuts@parkjenson.com this 29th day of April 2011.

A handwritten signature in black ink, appearing to read "Nancy A. Brown", is written over a horizontal line. The signature is cursive and includes a long horizontal stroke extending to the right.

Nancy A. Brown