

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA**

CASE NO. 01-7874-CIV-HURLEY

SECURITIES & EXCHANGE COMMISSION
plaintiff

vs

PAUL R. JOHNSON,
defendant

**ORDER REJECTING MAGISTRATE'S REPORT & RECOMMENDATION
ON PLAINTIFF'S MOTION TO SET NEW DISGORGEMENT AMOUNT,
GRANTING PLAINTIFF'S REVISED MOTION TO SET DISGORGEMENT
AMOUNT & ENTERING FINAL JUDGMENT OF DISGORGEMENT AS TO
DEFENDANT PAUL R. JOHNSON**

THIS CAUSE is before the court upon the plaintiff Securities & Exchange Commission ("the Commission")'s motion to set new disgorgement amount against defendant Paul R. Johnson filed November 30, 2006 [DE 301]. For reasons discussed below, the motion shall be granted and final judgment of disgorgement shall be entered against defendant Paul R. Johnson in the requested revised amount.

Procedural History

1. On August 23, 2006, this court entered final partial summary judgment in favor of the Commission and adjudicated the defendant Paul Johnson civilly liable for those investor losses corresponding to the fourteen substantive securities fraud counts on which he was previously criminally convicted. [DE# 293] Applying collateral estoppel principles, the court concluded that the factual determinations necessarily made by the jury which convicted Johnson on the criminal securities fraud charges necessarily established Johnson's civil liability for the similar, discrete

category of securities law violations encompassed in the charges set forth in the Commission's civil complaint, and that Johnson is appropriately required to disgorge all profits which he gained from those transactions.

The final judgment specifically rejected the contention that Johnson's criminal conviction translates into exposure for *all* investor losses associated with the underlying fraudulent scheme, however, and held that Johnson's financial responsibility for any investor losses beyond those determined by his conviction on the fourteen substantive securities fraud counts must be predicated on evidence which first establishes his culpability for the conduct precipitating the loss.

Since the SEC's original motion to set disgorgement amount did not establish such a predicate, this court declined to fix the amount of loss by way of summary judgment, and reserved ruling on this issue pending submission of further motion and evidentiary predicate by the Commission.

2. On November 30, 2006, the SEC sought to amend the amount of the requested disgorgement [DE#301], agreeing to limit the amount to the total value of investor losses alleged in the substantive counts of the criminal indictment on which he was convicted, to wit, \$1,505,850.00. [DE# 301] .

3. On December 4, 2006, the court granted the SEC's revised disgorgement request and entered final total disgorgement judgment of \$1,862,675.59 (\$1,505,850.00 in principal plus \$356,825.59 in prejudgment interest) [DE# 303].

4. On December 28, 2006, Johnson moved to set aside and vacate the final judgment of disgorgement, correctly pointing out that the judgment was entered just four days after the SEC filed its motion to amend its complaint, and before Johnson had an opportunity to respond with his

objections to the revised disgorgement request. [DE# 304]. In this motion, Johnson represented that he wished to file a response contesting the veracity of the SEC's underpinning representations, and specifically wished to contest whether the full amount of the \$1,505,850.00 in investor losses recited in the indictment in fact represented "ill gotten" gains to him.

5 In order to provide Johnson with a full and fair opportunity to refute the SEC's motion with appropriate evidence or argument bearing on the the issue of "ill gotten gains," on January 30, 2007, this court granted Johnson's motion, vacated the December 5, 2006 judgment of disgorgement [DE# 313], and referred the SEC's revised motion to set disgorgement to Magistrate Judge Frank J. Lynch for a report and recommendation [DE#312]. At the same time, the court granted the SEC's motion to amend the disgorgement amount sought by way of its Amended Complaint, and directed Johnson to serve his response in opposition within ten days. [DE# 313].

6. Johnson filed his response in opposition to the motion on March 23, 2007 [DE# 319], and on April 17, 2007, the SEC filed its reply [DE# 323].

7. On April 19, 2007, Magistrate Judge Lynch filed his report and recommendation upon the SEC's motion, concluding that the "state of the pleadings remain insufficient to permit this Court to enter a disgorgement assessment," and recommending that the SEC's motion be denied without prejudice for the Commission to re-file a motion that better explains the factual and legal predicate for the requested revised disgorgement. [DE # 324].

8. The SEC filed its objections to the Magistrate Judge's report on May 14, 2007 [DE# 328].

Discussion

Pursuant to 28 U.S.C. § 636(b)(1)(c) the court has made a *de novo* determination with respect to those portions of the report with respect to which formal written objection has been filed. Having done so, and having carefully reviewed the briefs submitted by both parties in support and opposition to the underlying motion, the court concludes that the SEC is entitled to entry of a disgorgement judgment in the requested revised amount, and that the Magistrate Judge misinterpreted the import of this court's prior order vacating the earlier disgorgement judgment.

Under application of collateral estoppel doctrine, the fact of Johnson's criminal conviction upon the fifteen substantive securities fraud counts in question establishes that Johnson defrauded the investors identified in those counts of the \$1,505,850.00 in cumulative losses alleged in the indictment. This established cumulative loss of the defraud investors, in turn, represents "ill gotten gains" to Johnson which must now be disgorged. The Commission is not required to trace how Johnson used the money from the investors he defrauded, nor is Johnson entitled to claim a "credit" or offset for funds he obtained through the fraud and then spent on "overhead business expenses" incurred in carrying out the fraudulent scheme.¹

Through operation of collateral estoppel principles, the Commission thus establishes a reasonable approximation of disgorgement, and the burden accordingly shifts to Johnson to demonstrate that the Commission's estimate is not a reasonable approximation. *SEC v Calvo*, 378 F.3d 1211 (11th Cir. 2004). Johnson does not begin to meet this burden with the suggestion that he may have spent some of the investors' money on ordinary business overhead expenses. *SEC v*

¹*SEC v Svoboda*, 409 F. Supp. 2d 331 (S. D. N. Y. 2006); *SEC v TLC Investments and Tarde Co.*, 179 F. Supp. 2d 1149 (C.D. Cal. 2001); *SEC v Hughes Capital Corp.*, 917 F. Supp. 1080 (D. N.J. 1996); *SEC v Great Lakes Equities Co.*, 775 F. Supp. 211 (E.D. Mich. 1991)

United Energy Partners, 2004 WL 314185 (5th Cir. 2004)(overwhelming weight of authority recognizes that securities fraud violators may not offset their disgorgement liability with business expenses); *SEC v First Pacific Bancorp.*, 142 F.3d 1186 (9th Cir. 1998)(proceeds spent to perpetuate fraud subject to disgorgement).

Conclusion

The defendant Paul R. Johnson has now had full and fair opportunity to present all evidence and argument which he wishes to marshal in opposition to entry of the requested revised disgorgement judgment. Having carefully reviewed his submissions, the court finds no legal or factual basis which precludes entry of a disgorgement judgment that corresponds to the amount of investor losses identified in the substantive counts of the superseding criminal indictment (Counts 2 through 15) on which he was convicted, as requested by the Commission in its revised motion.

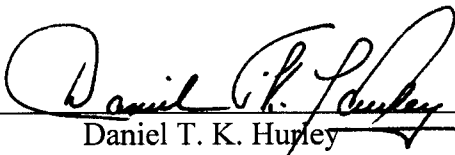
It is accordingly **ORDERED AND ADJUDGED**:

1. The Commission's objections to the Magistrate Judge's Report and Recommendation [DE# 328] are sustained, and the court respectfully declines to adopt the Report and Recommendation of Magistrate Judge Lynch on the Commission's revised disgorgement motion [DE#324].
2. The plaintiff Securities and Exchange Commission's motion to set new disgorgement amount [DE# 301] is **GRANTED**.
3. It is accordingly **ORDERED and ADJUDGED** that the Securities and Exchange Commission shall recover from the defendant **PAUL JOHNSON** the sum of \$1,505,850.00 in **DISGORGEMENT**, plus prejudgment interest in the amount of \$356,825.59, for a **TOTAL DISGORGEMENT JUDGMENT AMOUNT of \$1,862,675.59**, which sum shall bear interest at the rate prescribed by 28 U.S.C. § 1961 from the date of entry of this judgment, for which let execution issue.

4. The total payment of \$1,862,675.59 in disgorgement and prejudgment interest shall be due and payable by the defendant Johnson within **THIRTY (30) DAYS** from the date of this Final Judgment of Disgorgement. All payments shall be made by United States post money order, certified check, cashier's check or bank money order payable to the Securities and Exchange Commission. The payments shall be delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way,, Mail Stop 0-3, Alexandria, Virginia 22312 and shall be submitted under cover letter identifying Paul R. Johnson as a defendant in this action, which shall be further identified by full case style and number. A copy of the cover letter and money order or check shall be sent to Scott Masel, Senior Trial Counsel, Securities and Exchange Commission, 801 Brickell Avenue, Suite 18800, Miami, Florida 33131.
5. There being nothing further for the court to do at this juncture, the Clerk of Court is directed to mark this file as **CLOSED** and terminate any pending motions as **MOOT**.

DONE AND ORDERED in Chambers at West Palm Beach, Florida this 21st day of

June, 2007.


Daniel T. K. Hurley
United States District Judge

cc.

Scott Masel, Esq. (SEC)

Paul Johnson, *pro se*

Reg. No. 74884-004

Unit B, FCI Miami

PO 7798800, Miami, FL 33177