INITIAL DECISION RELEASE NO. 693
ADMINISTRATIVE PROCEEDING
FILE NO. 3-15255

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

In the Matter of	:	
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JOHN THOMAS CAPITAL MANAGEMENT GROUP LLC, d/b/a PATRIOT28 LLC, GEORGE R. JARKESY, JR., JOHN THOMAS FINANCIAL, INC., and ANASTASIOS "TOMMY" BELESIS	:	INITIAL DECISION AS TO JOHN THOMAS CAPITAL MANAGEMENT GROUP LLC, d/b/a PATRIOT28 LLC, and GEORGE R. JARKESY, JR[1]
	:	October 17, 2014

APPEARANCES: Todd Brody and Alix Biel for the Division of Enforcement, Securities and Exchange Commission

Karen Cook and S. Michael McColloch for Respondents John Thomas Capital Management Group LLC, d/b/a Patriot28 LLC, and George R. Jarkesy, Jr.

BEFORE: Carol Fox Foelak, Administrative Law Judge

SUMMARY

This Initial Decision (ID) concludes that George R. Jarkesy, Jr. (Jarkesy) and John Thomas Capital Management Group LLC, d/b/a Patriot28 LLC (JTCM) (collectively, JTCM/Jarkesy or Respondents) violated the antifraud provisions of the federal securities laws. The ID orders Respondents to cease and desist from further violations and, jointly and severally, to disgorge $1,278,597 plus prejudgment interest and to pay a third-tier civil penalty of $450,000.

I. INTRODUCTION

A. Procedural Background

The Securities and Exchange Commission (Commission) instituted this proceeding with an Order Instituting Proceedings (OIP) on March 22, 2013, pursuant to Section 8A of the Securities Act of 1933, Sections 15(b)(4), 15(b)(6), and 21C of the Securities Exchange Act of 1934, Sections

[1] The proceeding has ended as to Respondents John Thomas Financial, Inc., and Anastasios "Tommy" Belesis, who settled the charges against them. *John Thomas Capital Mgmt. Grp. LLC, d/b/a Patriot28 LLC*, Exchange Act Release No. 70989, 2013 SEC LEXIS 3862 (Dec. 5, 2013).

203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940, and Section 9(b) of the Investment Company Act of 1940. The undersigned held a twelve-day hearing in New York City and remotely on February 3-7 and 24-27, 2014, and March 7 and 13-14, 2014. Thirteen witnesses testified, including Jarkesy, and numerous exhibits were admitted into evidence.[2]

The findings and conclusions in this ID are based on the record. Preponderance of the evidence was applied as the standard of proof. *See Steadman v. SEC*, 450 U.S. 91, 96-104 (1981). Pursuant to the Administrative Procedure Act (APA), 5 U.S.C. § 557(c), the parties' Proposed Findings of Fact and Conclusions of Law were considered. All arguments and proposed findings and conclusions that are inconsistent with this ID were considered and rejected.

B. Allegations and Arguments of the Parties

This proceeding concerns JTCM/Jarkesy's dealings with two hedge funds then known as the John Thomas Bridge and Opportunity Fund LP I (Fund I) and John Thomas Bridge and Opportunity Fund LP II (Fund II) (collectively, the Funds).[3] The OIP alleges that JTCM/Jarkesy engaged in various material misrepresentations and omissions, including concerning John Thomas Financial, Inc. (JTF), the Funds' placement agent, and JTF's owner, Anastasios "Tommy" Belesis (Belesis) (collectively, JTF/Belesis).

The Division of Enforcement (Division) is seeking a cease-and-desist order, disgorgement, and third tier civil money penalties against Respondents; and industry and officer and director bars against Jarkesy. Respondents argue that the charges are unproven and no sanctions should be imposed.

C. Due Process and Equal Protection

As discussed below, the Respondents have not established valid claims of due process and equal protection violations to prevent the determination of this proceeding against them.

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[2] Citations to the transcript will be noted as "Tr. __." Citations to exhibits offered by the Division of Enforcement (Division) and by Respondents will be noted as "Div. Ex. __" and "Resp. Ex. __," respectively. Some documents were offered by both the Division and Respondents, for example, the February 5, 2009, Confidential Private Placement Memorandum of John Thomas Bridge and Opportunity Fund, L.P. II (Div. Ex. 210; Resp. Ex. 1).

[3] The Funds have been known as the Patriot Bridge and Opportunity Fund LP I and LP II since September 2011. Answer of JTCM/Jarkesy (Answer) at 1.

1. The Commission Has Neither Prejudged Respondents Nor Engaged in Improper *Ex Parte* Communications with the Division

Respondents argue that the Commission prejudged the proceeding as to them by making findings of fact pursuant to the settlement with JTF and Belesis.[4] Respondents contend that: the Commission's involvement in the settlement creates fundamental unfairness because, if the initial decision as to Respondents is appealed to the Commission, the Commission will have already determined the facts and concluded that there were securities violations, in violation of the APA, 5 U.S.C. § 551 *et seq*.; and because the Division has engaged in improper *ex parte* communications with the Commission in connection with the settlement. Respondents previously raised this argument in their January 3, 2014, motion to disqualify Commissioners from being involved in this proceeding going forward. *See John Thomas Capital Mgmt. Grp. LLC*, *d/b/a Patriot28 LLC*, Admin. Proc. Rulings Release No. 1148, 2014 SEC LEXIS 27 (A.L.J. Jan. 6, 2014) (denying motion for disqualification).

The Commission has considered and rejected this very argument on several occasions. *See The Stuart-James Co.*, Exchange Act Release No. 28810, 1991 SEC LEXIS 168, at *2-18 (Jan. 23, 1991), *adhered to by C. James Padgett*, Exchange Act Release No. 38423, 1997 WL 126716, at *15-16 (Mar. 20, 1997), *pet. for review denied*, *Sullivan v. SEC*, 159 F.3d 637 (table), 1998 WL 388511 (D.C. Cir. 1998) (*per curiam*); *Steadman Sec. Corp.*, Exchange Act Release No. 13695, 1977 SEC LEXIS 1388, at *56 n.82 (June 29, 1977); *Edward Sinclair*, Exchange Act Release No. 9115, 1971 SEC LEXIS 898, at *13-14 (Mar. 24, 1971), *aff'd*, 444 F.2d 399 (2d Cir. 1971); *Atlantic Equities Co.*, Exchange Act Release No. 8118, 1967 SEC LEXIS 531, at *27-29 (July 11, 1967), *aff'd on other grounds sub nom. Hansen v. SEC*, 396 F.2d 694 (D.C. Cir. 1968), *cert. denied*, 393 U.S. 847 (1968); *see also Hortonville Joint Sch. Dist. No. 1 v. Hortonville Educ. Ass'n*, 426 U.S. 482, 493 (1976) ("Mere familiarity with the facts of a case gained by an agency in the performance of its statutory role does not, however, disqualify a decisionmaker.") (citations omitted); *New York State Dep't of Law v. FCC*, 984 F.2d 1209, 1217-18 (D.C. Cir. 1993) (deferring to Federal Communications Commission rule excepting settlement discussions from bar on *ex parte* communications). In this proceeding, the Commission stated – when considering Respondents' petition for interlocutory appeal – that it "has rejected arguments similar to those raised by JTCM and Jarkesy in an unbroken line of decisions." *John Thomas Capital Mgmt. Grp. LLC, d/b/a Patriot28 LLC*, Securities Act Release No. 9519, 2014 SEC LEXIS 308, at *6 (Jan. 28, 2014).

It is well established that the Commission's combining administrative and adjudicative functions is consistent with due process, including when the Commission considers settlement as to one or more respondents, but reviews an initial decision as to another respondent based on similar facts. A policy prohibiting settlements during the pendency of a multi-party proceeding would be contrary to the APA, which requires an agency to give all interested parties the opportunity for the submission and consideration of offers of settlement, when time, the nature of the proceeding, and the public interest permit. 5 U.S.C. § 554(c)(1). Further, while agency staff are obligated under the APA to be separated according to investigative, prosecution, and adjudicative functions, 5 U.S.C. §

[4] *John Thomas Capital Mgmt. Grp. LLC, d/b/a Patriot28 LLC*, Exchange Act Release No. 70989, 2013 SEC LEXIS 3862 (Dec. 5, 2013).

554(d), the APA exempts Commission members from this separation of functions requirement. 5 U.S.C. § 554.

The precedent that Respondents cite is inapposite. In *Antoniu v. SEC*, the court nullified Commission administrative proceedings where a Commissioner made a public speech indicating prejudgment of the respondent. 877 F.2d 721 (8th Cir. 1989), *cert. denied*, 494 U.S. 1004 (1990). In the speech, the Commissioner singled out the respondent as an "indifferent violator" and announced that the bar imposed on respondent had been "made permanent," although the proceedings against the respondent had yet to become final and the Commission had yet to issue its opinion upholding the administrative law judge's initial decision. *Id.* at 723; *see Adrian Antoniu*, Exchange Act Release No. 25169, 1987 SEC LEXIS 3086 (Dec. 3, 1987) (published nearly two months after the Commissioner's speech at issue). The court explained that the Commissioner's "words describing [the respondent's] bar as permanent can only be interpreted as a prejudgment of the issue." *Antoniu*, 877 F.2d at 723.

In *Antoniu*, the Commissioner's conduct was held to – and did not comport with – the appearance of justice. *Id*. at 724. The circumstances here are entirely different, and the Commission's publication of findings of fact, agreed on in a settlement, as to JTF and Belesis does not conflict with the appearance of justice. The other cases that Respondents cite are similarly misplaced; each also involved a speech by a Commissioner criticizing a party in a pending proceeding, not a prior published settlement. *See Cinderella Career & Finishing Schs., Inc. v. Fed. Trade Comm'n*, 425 F.2d 583 (D.C. Cir. 1970); *Texaco, Inc. v. Fed. Trade Comm'n*, 336 F.2d 754 (D.C. Cir. 1964), *vacated on other grounds*, 381 U.S. 739 (1965).

Respondents also maintain, without citing any precedent, that Article III courts have held that combining administrative and adjudicative functions is not acceptable. This is not so, and Article III courts have sanctioned such practices. In *Sinclair v. SEC*, the court specifically found no merit in the argument that a Commissioner had prejudged a non-settling respondent's case by participating in the decision to accept another respondent's settlement offer that set forth the facts stipulated by the settling respondent and the Division. 444 F.2d 399, 401-02 (2d Cir. 1971). The court noted that both the settled and litigated "proceedings met the standards of due process, with each respondent . . . being represented by competent counsel." *Id.* The Supreme Court has stated:

> It is also very typical for the members of administrative agencies to receive the results of investigations, to approve the filing of charges or formal complaints instituting enforcement proceedings, and then to participate in the ensuing hearings. This mode of procedure does not violate the [APA], and it does not violate due process of law.

Withrow v. Larkin, 421 U.S. 35, 56 (1975).[5]

[5] Part of Respondents' due process complaint is that there is a separation of powers problem because the Commission can seek money penalties both in administrative proceedings and in federal court and has unbridled discretion, without any guidelines or criteria, as to the choice of forum. Respondents describe this as "dual jurisdiction." However, Respondents do not support their argument with more than generalizations based on the Constitution.

Finally, Respondents raise this argument prematurely. Courts do not normally consider assertions of administrative bias before the completion of administrative proceedings and the exhaustion of administrative remedies. *SEC v. R.A. Holman & Co.*, 323 F.2d 284, 286-88 (D.C. Cir. 1963). The court will interrupt the progress of an adjudicative hearing only in the exceptional case where it is presented with undisputed allegations of fundamental prejudice. *Amos Treat & Co. v. SEC*, 306 F.2d 260, 261-62, 265 (D.C. Cir. 1962). The appropriate time to raise the issue is when a party seeks judicial review of the Commission's action. *R.A. Holman & Co.*, 323 F.2d at 287-88; *United States v. Litton Indus.*, 462 F.2d 14, 18 (9th Cir. 1972).

2. The Division's Production of Material to Respondents Does Not Violate Due Process

Respondents additionally argue that due process has been violated by the Division's deliberate withholding of *Brady* material and "document dump" production on Respondents. These arguments are not convincing.

The Division is required by 17 C.F.R. § 201.230 (Rule 230) to make available its investigative file to a respondent and may not withhold, contrary to the doctrine of *Brady v. Maryland*, 373 U.S. 83, 87 (1963), documents that contain material exculpatory evidence. Rule 230(b)(2). The Commission previously determined in this proceeding, on Respondents' petition for the interlocutory review, that Respondents did not establish that the Division had failed to comply with Rule 230(b)(2), and stated that Respondents "take an overly broad view of what constitutes *Brady* material." *John Thomas Capital Mgmt. Grp. LLC, d/b/a Patriot28 LLC*, Securities Act Release No. 9492, 2013 SEC LEXIS 3860, at *18-19 (Dec. 6, 2013) (Denial of Petition). Respondents have since made requests for witness interview notes, which they maintain were withheld in violation of Rule 230(b)(2). Tr. 1409-13, 1677-79, 1682-83. These requests were also unfounded; the undersigned conducted *in camera* reviews of some of the notes, and they contained no material exculpatory evidence. Tr. 1415, 1730. Further, as a general matter, complying with *Brady* does not necessitate production of witness interview notes. Denial of Petition at *17; *optionsXpress, Inc.*, Securities Act Release No. 9466, 2013 SEC LEXIS 3235, at *13-14 & n.19 (Oct. 16, 2013).

Respondents make a separate but related argument that, even if the Division has not withheld materials in violation of Rule 230(b)(2), they are unaware of exculpatory evidence because of the large amount of data the Division produced to them. Specifically, Respondents complain that the Division produced "700 gigabytes" of data in a Concordance® database,[6] and that the large amount of data to review left them unprepared for hearing. The Commission, however, has made clear that the Division's production approach in this proceeding satisfies its disclosure obligations under Rule 230(b). Denial of Petition at *26 ("Nothing in either Rule 230(b)(2) or *Brady* requires the Division to go further and prepare a 'roadmap' of the documents for the respondent's benefit."). The Commission explained:

[6] Concordance® is a software package that enables users to conduct searches and identify documents that contain matches to specified search parameters. *See* Denial of Petition at *22 n.37 (citing federal court of appeals and district court opinions).

> It is settled that the government is not required to direct a defendant to specific items of potentially exculpatory evidence within a larger body of disclosed material. Indeed, the Supreme Court has made clear that the government may satisfy its *Brady* obligations through an "open file" policy, which the Court reasoned could well "increase the efficiency and the fairness of the criminal process.

Id. at *24 (quoting *Strickler v. Greene*, 527 U.S. 263, 283 n.23 (1999)); *see also Harding Advisory LLC*, Securities Act Release No. 9561, 2014 SEC LEXIS 938 (Mar. 14, 2014) (denying petition for interlocutory review where respondents complained of large amount of data produced).

Respondents allege that due process was violated because the Division did not provide them with a list of "hot documents" to help direct them to the documents containing exculpatory evidence. However, the Commission has addressed this argument: "[Respondents] assert that the Division must go further and specifically identify material exculpatory or impeaching evidence within the production or, at the very least, provide a 'roadmap' for those documents. That is not so." Denial of Petition at *23.

3. Respondents Have Not Been Deprived of Equal Protection

Respondents claim they have been deprived of equal protection because the Commission "arbitrarily chose to litigate the claims against [them] in an administrative proceeding instead of filing suit on the same claims in federal court." This argument is not unlike that made by Rajat Gupta (Gupta) who petitioned in federal district court for declaratory and injunctive relief against the Commission, which had previously commenced administrative proceedings against him. *See Gupta v. SEC*, 796 F. Supp. 2d 503, 506-07, 513-14 (S.D.N.Y.). However, unlike Gupta, Respondents do not have a cognizable equal protection claim because there are no other defendants, connected to the same allegations of wrongdoing, against whom litigation was brought in a judicial instead of administrative proceeding. *See Harding Advisory LLC*, 2014 SEC LEXIS 938, at *33 n.42 (Mar. 14, 2014) (describing *Gupta* as "declining to dismiss complaint alleging an equal protection violation where there existed 'a well-developed public record of Gupta being treated substantially disparately from *28 essentially identical* defendants'").

Respondents mean to raise a "class of one" equal protection claim, yet such a claim requires a showing of (1) intentional different treatment from others similarly situated and (2) a lack of rational basis for such different treatment. Resp. Br. at 16; *see Vill. of Willowbrook v. Olech*, 528 U.S. 562, 564 (2000) (*per curiam*); *Witt v. Vill. of Mamaroneck*, No. 12-cv-8778-ER, 2014 WL 1327502, at *7 (S.D.N.Y. Mar. 31, 2014). Respondents merely identify alleged similarly situated litigants that were prosecuted in federal court, without providing a specific argument as to how each of these litigants is so similarly situated to Respondents. *See Missere v. Gross*, 826 F. Supp. 2d 542, 561 (S.D.N.Y. 2011) (necessary to show an extremely high degree of similarity between claimants and the persons to whom claimants compare themselves). "[S]uperficial comparisons to a few other proceedings fall short of establishing a colorable equal protection violation." *Harding Advisory LLC* at *32-33. Thus, Respondents have not made out a class of one equal protection claim.

Respondents also assert that their not having an opportunity of a hearing before a jury violates the Seventh Amendment right to jury trial and denies them equal protection. Respondents' assertion has no merit; it is well established that the lack of jury trials in Commission administrative proceedings does not violate the Seventh Amendment. *See Harding Advisory LLC* at *35 n.46 ("[T]he Seventh Amendment does not prohibit Congress from assigning the factfinding function and initial adjudication to an administrative forum with which the jury would be incompatible." (citing *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 450 (1977)); *see also Curtis v. Loether*, 415 U.S. 189, 194-95 (1974) (noting that the Seventh Amendment is generally inapplicable in administrative proceedings where jury trials would be incompatible with the whole concept of administrative adjudication); *Taggart v. GMAC Mortgage, LLC*, No. 12-cv-415, 2012 WL 5929000, at *4 (E.D. Pa. Nov. 26, 2012) (observing rule from *Curtis v. Loether*); *Vladlen "Larry" Vindman*, Securities Act Release No. 8679, 2006 SEC LEXIS 862, at *44 n.60 (Apr. 14, 2006) (citing *Atlas Roofing Co.*, 430 U.S. at 450). Further, the undersigned is aware of no authority suggesting that an equal protection claim can be established based on an agency's choice to bring enforcement proceedings in an administrative forum – lacking juries, the Federal Rules of Civil Procedure, and the Federal Rules of Evidence – over a judicial forum. *See* Denial of Petition at *26.

4. Untimeliness

Respondents contend that the claims set forth in the OIP are barred by the doctrine of laches and by the applicable statute of limitations. The defense of laches is not available against a United States government agency acting in the public interest. *David Disner*, Exchange Act Release No. 38234, 1997 SEC LEXIS 258, at *18 (Feb. 4, 1997) (citing *United States v. Summerlin*, 310 U.S. 414, 416 (1940); *United States v. Alvarado*, 5 F.3d 1425, 1427 (11th Cir. 1993)). Cease-and-desist orders and disgorgement are not subject to the five year statute of limitations provided in 28 U.S.C. § 2462. *Riordan v. SEC*, 627 F.3d 1230, 1234-35 (D.C. Cir. 2010); *Johnson v. SEC*, 87 F.3d 484, 491 (D.C. Cir. 1996). As to those sanctions that are covered by the statute of limitations, acts outside the statute of limitations may be considered to establish a respondent's motive, intent, or knowledge in committing violations that are within the statute of limitations. *Sharon M. Graham*, Exchange Act Release No. 40727, 1998 SEC LEXIS 2598, at *41 n.47 (Nov. 30, 1998) (citing Fed. R. Evid. 404(b) and *Local Lodge No. 1424 v. NLRB*, 362 U.S. 411 (1960)), *aff'd*, 222 F.3d 994 (D.C. Cir. 2000); *Terry T. Steen*, Exchange Act Release No. 40055, 1998 SEC LEXIS 1033, at *14-15 (June 1, 1998) (citing *H.P. Lambert Co. v. Sec'y of the Treasury*, 354 F.2d 819, 822 (1st Cir. 1965)). Further, such acts may be considered in determining the appropriate sanction if violations are proven. *Steen*, 1998 SEC LEXIS 1033, at *14-17.

Respondents also claim that the OIP's charges are barred because they were not timely filed following the April 4, 2012, Wells notice (Div. Ex. 642). The Division's Director is authorized by Section 4E of the Exchange Act, 15 U.S.C. § 78d-5, to extend the 180-day time limit that Section 4E establishes after providing notice to the Chairman of the Commission. *See Eric David Wanger and Wanger Inv. Mgmt., Inc.*, Securities Act Release No. 9304, 2012 WL 1037682, at *1 (Mar. 29, 2012). While the Division has not provided evidence that notice was given to the Chairman extending the time limitation, it need not have done so, as Section 4E is not a statute of limitations providing any substantive rights to Respondents, or imposing any consequences on the Division, if the deadline goes unmet. *See Montford and Co., Inc., d/b/a Montford Assocs.*, Investment Advisers Act Release No. 3829, 2014 SEC LEXIS 1529, *30-50 (May 2, 2014) (citing *Brock v. Pierce Cnty.*, 476 U.S. 253, 259 (1986) and *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 63-65 (1993)); *see also SEC v. NIR Grp., LLC*, No. 11-cv-4723, 2013 U.S. Dist. LEXIS 47522 (E.D.N.Y. Mar. 24, 2013); *SEC v. Levin*, No. 12-cv-21917, 2013 U.S. Dist. LEXIS 20027, at *34-35 (S.D. Fla. Feb. 14, 2013).

II. FINDINGS OF FACT

A. Relevant Individuals and Entities

1. JTCM and Jarkesy

JTCM, based in Houston, Texas, is an unregistered investment adviser and general partner of two hedge funds, Fund I and Fund II. Answer of JTCM/Jarkesy (Answer) at 1-2. Jarkesy controls all operations and activities of JTCM as its manager. *Id*. Jarkesy created JTCM in 2007 to serve as the adviser to Fund I. *Id*. Neither JTCM, Jarkesy, nor the Funds were registered with the Commission and Jarkesy was not associated with a registrant.[7]

2. The Funds

Jarkesy and JTCM launched Fund I in 2007 and Fund II in 2009. Answer at 1. Fund II was originally intended to be a domestic feeder fund for an international fund; due to a lack of foreign interest, Fund II was launched as an independent entity, not a feeder fund. Tr. 973, 2672-73, 2759, 2850-54; Div. Ex. 210. The Funds invested in three asset classes: bridge loans to start-up companies;[8] equity investments, principally in microcap companies; and life settlement policies. *Id.* The Funds' assets under management peaked at approximately $30 million at the end of 2011. *Id.* Together, the Funds have approximately 120 investors. Answer at 3. JTCM, acting through Jarkesy, represented that it was solely responsible for managing the funds. Answer at 6.

3. JTF and Belesis

JTF was a broker-dealer based in New York City. Answer at 2. Belesis was JTF's founder and chief executive officer. *Id*. Belesis and Jarkesy became acquainted in 2003.[9] *Id.* Until late 2011, JTF was the primary placement agent for the Funds and was one of several broker-dealers that executed equity trade orders for the Funds. Answer at 2-3; Tr. 2396. JTF brokers' representations, including misrepresentations, induced some customers to invest in the Funds. Tr. 752-53, 776-77, 782-83, 788-

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[7] Official notice, pursuant to 17 C.F.R. § 201.323, is taken of the Commission's public official records.

[8] A bridge loan is made to a company as short-term financing before it raises capital from the public. Resp. Ex. 138 at 5.

[9] At the hearing Jarkesy denied that it was 2003 when he became acquainted with Belesis, but did not provide an alternate date. Tr. 2515-21. The reason for this is not apparent from the record.

90, 793-96, 826-29, 852-54, 1351-53, 1430 1443, 1488, 1491, 1826-27, 1838, 1850-51; Div. Exs. 607, 608.

Fund I's July 2007 Placement Agent Agreement provided that the Fund pay JTF 10% of the capital contributions it received (whether sold through JTF or not) plus a 0.05% trail commission each year. Div. Ex. 501 at JTBOF 1702. A similar representation was made in Fund II's Private Placement Memorandum (PPM), and Fund I's PPM disclosed that JTF would earn commissions, without specifying the amount. Div. Ex. 206 at 46, Div. Ex. 210 at 63, 67-68. JTF and Belesis occasionally introduced Jarkesy and JTCM to candidates for bridge loans. Answer at 7. JTF also served as investment banker to several of the companies that received bridge loans from the Funds, including three of the Funds' largest holdings: America West Resources, Inc., f/k/a Reddi Brake Supply Corporation (America West), Galaxy Media & Marketing Corp. f/k/a Amber Ready, Inc. (Galaxy), and Radiant Oil & Gas, Inc., f/k/a G/O Business Solutions, Inc. (Radiant). Answer at 3; Tr. 2158-59 & *passim*.

JTF's logo – "JTF" inscribed on a shield – was displayed on PPMs, monthly and quarterly reports, marketing materials, and emails and communications related to the Funds, including investor account statements.[10] *See, e.g.*, Div. Exs. 206-11, 215, 217-20, 222, 224, 229a, 237-38, 243-44, 258. However, JTCM's website made this representation about the relationship between JTF and JTCM and the Funds:

> John Thomas Bridge and Opportunity Fund is not affiliated with John Thomas Financial. John Thomas Financial is a New York Based Broker Dealer that is acting as a selling agent for the fund. No other relationship between the parties should be construed including that of owning, managing, directing or making any decisions for the fund. The fund operates pursuant to its board of directors and the fund's manager Mr. George Jarkesy.

Div. Ex. 502. America West's and Radiant's 2010 Forms 10-K – signed by Jarkesy – represented that JTF and Fund I were not affiliates. Div. Ex. 310 at 37, 39, Div. Ex. 311 at 72, 76. In his testimony, Jarkesy indicated that his selection of the John Thomas name was serendipitous. Tr. 74.

According to Financial Industry Regulatory Authority, Inc. (FINRA), records, JTF withdrew its registration as a broker-dealer on June 14, 2013. *See* John Thomas Financial BrokerCheck Report at 2 *available at* http://brokercheck.finra.org (last visited Oct. 9, 2014).[11] Additionally, FINRA cancelled JTF's membership on August 16, 2013, for failure to pay outstanding fees, and

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[10] One iteration of Fund I's PowerPoint® marketing material even included the name "John Thomas Financial" with the logo. Div. Ex. 211. The JTF logo was discontinued after the name change to Patriot 28. Div. Exs. 234, 242, 247.

[11] Official notice, pursuant to 17 C.F.R. § 201.323, is taken of these records. *See Joseph S. Amundsen*, Exchange Act Release No. 69406, 2013 SEC LEXIS 1148, at *2 n. 1 (Apr. 18, 2013), *pet. for review denied*, No. 13-1252, 2014 U.S. App. LEXIS 15559, at *1-2 (D.C. Cir. Aug. 13, 2104).

expelled it from the securities industry on October 31, 2013, for failure to pay fines or costs associated with an August 16, 2011, Letter of Acceptance, Waiver and Consent. *Id* at 15. JTF had also been sanctioned by several state regulators for various types of misconduct. *Id* at 21-22, 24-26, 29-31.

Belesis is unusually forceful and unpleasant in business dealings. Tr. 641-42, 648-51, 692, 697-98, 1556-68, 1868, 2504; Div. Exs. 514, 521, 631. He also has a disciplinary record. *See* Anastasios P. Belesis BrokerCheck Report at 8-35 *available at* http://brokercheck.finra.org (last visited Oct. 9, 2014). Jarkesy has stopped doing business with Belesis. Tr. 2369-70, 2510-12. He became unhappy with JTF and Belesis starting in 2010 due to JTF/Belesis's hardball tactics and failure to raise money for portfolio companies at that time. Tr. 2175, 2510-12.

During the time at issue, Jarkesy was in frequent contact with Belesis concerning various business dealings related to the Funds. Tr. 1555-56, 1567-68, 1577-78, 1582-83 and Div. Exs. 512, 513, 514, 516, 517, 518, 518A, 520, 639 (Galaxy); Tr. 642 and Div. Ex. 511 (America West); Div. Exs. 631, 645, 646 (EnterConnect Inc.). Belesis reinforced his position in the relationship through threats to stop selling interests in Jarkesy's Funds. Div. Ex. 631 (Mar. 12, 2009, email from Belesis to Jarkesy: "our relationship based on your actions is slowly coming to an end"), Div. Ex. 643 (Aug. 21, 2010, email from JTF to JTCM: "Per Tommy . . . [t]here will no longer be any funds from John Thomas Financial clients into the bridge fund.").

B. Credibility

Jarkesy testified at the hearing. Tr. 25-274, 1183-1339, 1499-1534, 2377-2469, 2474-77, 2486-2530, 2577-2590, 2599-2640, 2658-2818, 2830-3012. He generally testified in an evasive manner that did not provide any assurances of the reliability of his testimony. Thus, no weight has been placed on his testimony as to facts that are disputed or not corroborated by credible evidence elsewhere in the record.

In the course of his testimony, Jarkesy responded, "I don't recall" or a variant of that phrase more than 800 times, including to such questions as: "what is restricted stock?"; "what is your understanding of what institutional investors are?"; "if the fund had more than 5 percent in one company, it wouldn't be diversified?"; "[d]o you think that the addition of the term restricted makes that a different company?"; and "[d]id you have discussions with John Thomas Financial about how they were going to find investors for the fund?" Tr. 87, 160, 122-23, 185, 1184. He also responded, "I don't recall" to "why did you choose John Thomas Financial to be the lead placement agent?" and "[between] 2008 and 2009, the funds also had liquidity issues. Isn't that correct?" Tr. 2788, 2799.[12]

[12] Jarkesy also repeatedly "did not recall" when asked to identify evidence, such as emails with his name in the to, from, or cc fields that JTCM had produced, as was evidenced by the Bates numbers on the documents, starting with "JTBOF," or the path information on the bottom of the documents. Tr. 75-76; Div. Ex. 501; *see, e.g.*, Tr. 1993-94, 2883-84, 2989-90; Div. Exs. 621, 652, 660. While Jarkesy might indeed not recall specific emails, his argument that numerous documents JTCM produced through its prior counsel (not Jarkesy and JTCM's hearing counsel) are unreliable or lack foundation appears to be a suggestion that prior counsel manufactured evidence that could be used

While Jarkesy evaded a large portion of the Division's questions, his recollection markedly improved when questioned by his own counsel. Jarkesy's participation in the hearing on March 7, 2014, illustrates this. For the majority of that hearing day (approximately 120 transcript pages), Jarkesy's counsel conducted direct examination of him, during which Jarkesy used the phrase "I don't recall" or something similar about twenty-five times, while otherwise providing substantive answers to his counsel's questions. *See* Tr. 2658-2779. When the Division cross-examined Jarkesy, however, he responded to questions, with "I don't recall" or something similar over forty times in a significantly shorter period (less than twenty transcript pages) of questioning. *See* Tr. 2780-2818. For example, among the Division's first questions on cross-examination was "the bridge loans, those were high risk?," to which he answered, "I don't recall all the bridge loans, how they were done." Tr. 2781. The Division's next question, "[t]he private placements, those were high risk?," was answered with "I don't recall the private placements." *Id*.

Jarkesy further undermined his credibility by disclaiming responsibility for representations about the Funds made in the PPMs, financial statements, marketing materials, and newsletters, as discussed below.

C. <u>The Funds</u>

The Funds' PPMs and marketing materials contained various representations about the Funds and JTCM/Jarkesy's plans for managing them. Some of the representations that may have been accurate when the documents were first used became inaccurate and were not corrected.[13] The PPMs were put together with the assistance of lawyers engaged by Jarkesy. Tr. 105-06, 2371-73, 2378-80. Jarkesy determined the content of marketing materials, such as PowerPoint® presentations, with review by his lawyers. Tr. 211, 572-74, 952-53, 1484, 2557, 2783-84; Div. Exs. 211, 261, 600. Jarkesy drafted quarterly reviews provided to Fund investors; legal counsel reviewed them. Tr. 35-39; Div. Exs. 214, 218.

1. Warnings

Each PPM warned that the investment was speculative, involving substantial risks and was suitable only for those who could afford the risk of loss of their investment. Div. Ex. 206 at 2, Div. Ex. 210 at 26. In addition to the general warning, each PPM contained several pages of warnings about

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against him. However, he presented no independent evidence corroborating such wrongdoing. *See* Tr. 97, 106, 1525-27, 1980, 1991-92.

[13] Respondents argue that the Division did not prove that Fund I's June 1, 2007, PPM (as amended on August 21, 2007, to remove a $10 million minimum capital commitment requirement) and Fund II's February 5, 2009, PPM were used without alteration in selling interests in the Funds throughout the time at issue. However, Respondents, who are in the best position to know of any successor PPM amendments, did not offer evidence of any changes. Accordingly, it is found that Fund I's June 1, 2007, PPM, as amended on August 21, 2007, and Fund II's February 5, 2009, PPM were used without further amendments in selling interests in the Funds during the time at issue.

specific risks. Div. Ex. 206 at 20-32, Div. Ex. 210 at 26-50. The risks included: "These [investment, management, financing and disposition] policies may be changed from time to time at the discretion of the General Partner without a vote of the Limited Partners of the Partnership, although the General Partner has no present intention to make any such changes." Div. Ex. 206 at 20, Div. Ex. 210 at 26.

The PPM for Fund I also warned, "Any representations (whether oral or written) other than those expressly set forth in this memorandum and any information (whether oral or written) other than that expressly contained in documents furnished by the Partnership must not be relied on." Div. Ex. 206 at 3. Fund II's PPM contained a similar warning: "ONLY [JTCM] HAS BEEN AUTHORIZED TO MAKE REPRESENTATIONS, OR GIVE ANY INFORMATION, IN CONNECTION TO THE PARTNERSHIP INTERESTS. ANY INFORMATION, OTHER THAN THE INFORMATION CONTAINED HEREIN OR INFORMATION PROVIDED IN WRITING BY [JTCM], MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY THE PARTNERSHIP OR THE PARTNERS." Div. Ex. 210 at 7.

The Funds were organized as Delaware limited partnerships. Div. Exs. 206, 210. The PPMs noted, "Under the Delaware law, [JTCM] owes a fiduciary responsibility to [the] Limited Partners," that is, the investors. Div. Ex. 206 at 45, Div. Ex. 210 at 62. Fund I had a lock-up period of five years, Fund II, of four years, and each was to have a duration of ten years, with extensions possible.[14] Div. Ex. 206 at 11, 20, Div. Ex. 210 at 14, 22. Investors might be able to redeem their investments, but upon potential payment of a penalty. Div. Ex. 206 at 20 ("you will not be able to withdraw your investment from [Fund I] without significant penalty, if at all. See 'Liquidity Risks.'"), 28; Div. Ex. 210 at 28 ("During [the lock-up] period, Limited Partners may not be able to make any withdrawals from their Capital Accounts. See '<u>Risk Factors – Risks Relating to Illiquidity</u>'"). Jarkesy withdrew from Fund I $100,000 less a $20,000 penalty during February 2009.[15] Tr. 1330-35; Div. Ex. 236 at 17, Div. Ex. 316 at 11, Div. Ex. 659. Jarkesy had invested $500,000 in September 2007 as the first investor in Fund I. Div. Ex. 203 at 5.

Investments in the Funds were being sold as late as 2010. Div. Ex. 315 at 11 (Fund I's financial statement showing capital contributions for the period ended December 31, 2008), Div. Ex. 316 at 11 (Fund I's financial statement showing capital contributions for the period ended December 31, 2009), Div. Ex. 317 at JTBOF 6298 (Fund I's financial statement showing capital contributions for the period ended December 31, 2010), Div. Ex. 318 at JTBOF 6311 (Fund II's financial statement showing capital contributions for the period ended December 31, 2010). Neither Fund reached its target size. The target size for Fund I was $25 million; over its life, approximately $20 million was invested. Div. Ex. 206 at 7, Div. Ex. 317 at JTBOF 06298. The target size for Fund II was $250

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[14] In March 2012, Jarkesy emailed Fund I investors, stating his intention to wrap up the Fund, and saying, "By initial design it was contemplated that the fund would wrap up its business by September 2012." Div. Ex. 234. Investor Robert Fullhardt believed that the Fund had a September 2012 maturity date. Tr. 1362. Investor Steve Benkovsky also believed that the fund had a five-year duration that would end in 2012. Tr. 710, 746.

[15] The account statements for Jarkesy's investment in Fund I (under the name "Jarkesy Merchant Capital Ltd.") contain the notation "CC: Tommy Belesis." Div. Ex. 236.

million; approximately $4 million was invested. Div. Ex. 210 at 11, Div. Ex. 261 at 9, Div. Ex. 318 at JTBOF 6311, Div. Ex. 608 at 9. Jarkesy advised investors on March 13, 2013, that Fund I was dissolved as of that date.[16] Div. Ex. 242.

2. Investments

The PPM for each Fund stated that the Fund would make two types of investments: (1) investments in in-force life insurance policies with face values totaling 117% of the aggregate capital commitments and (2) short to medium term debt and equity investments in business enterprises. Div. Ex. 206 at 7, Div. Ex. 210 at 12. The insurance component was intended to be conservative, described in marketing materials as "Return **of** Capital," and the business component was intended to be more speculative, described in marketing materials as "Return **on** Capital." *See, e.g.*, Div. Exs. 222, 224. Thus, each Fund was described as "Two Investments ... One Fund ***Hedged***." *Id.*; *see also* Div. Exs. 211-21, 248. That is, the life insurance portfolio was represented as a conservative hedge that insured return of investors' principal and the corporate portfolio, as providing for the possibility of a profitable return on the principal. *Id.*

The PPMs described JTCM's plans to invest in a "Life Settlement Portfolio" and a "Corporate Portfolio." Div. Ex. 206 at 33-39, Div. Ex. 210 at 55-62. Life settlement refers to the purchase of existing life insurance policies at a discount to their face values, maintaining them by paying the premiums, and collecting when the insured dies.[17] *Id*. The corporate portfolio was to contain various forms of debt and equity in companies.

The PPM for Fund I represented that JTCM "intends to use up to 50% of the Capital Contributions" to acquire insurance policies. Div. Ex. 206 at 34. It represented that "[t]he aggregate face value of such acquired policies is intended to amount to approximately 117% of the aggregate capital commitments." *Id*. In a podcast sent to investors on May 21, 2009 (Podcast), Jarkesy explained that 50% of capital invested would go into life settlements; of that 50%, 30% would be used to buy the policies, and the remaining 70% would be "set aside to pay premiums through the life expectancy." Div. Ex. 203 at 21-22, Div. Ex. 204. The policies were to be held by a "Master Trust." Div. Ex. 206 at 35-36. The Master Trust was to have two deposit accounts: a collection account for the proceeds of payments of death benefits or receipts from sales of the policies, and a premium financing account, which "will contain sufficient cash upon the purchase of the Life Settlement Policies to pay the

[16] Division Exhibit 242 indicates that Fund I is being dissolved on March 13, 2013 and JTCM "will use all commercially reasonable efforts to sell all of [Fund I's] assets." Div. Ex. 242. The sale of all the assets had not occurred as of the time of the hearing; both Funds hold shares of Radiant and Fund II, at least, currently has an account at Wells Fargo Bank; Fund I has one life insurance policy. Tr. 551, 1252-53, 1314-16; Div. Ex. 404.

[17] Fund I's PPM warned, "The life settlements industry has been tainted by fraud." Div. Ex. 206 at 21. Fund II's PPM warned, "The life settlements industry has been tainted by allegations of fraud and misconduct" and noted an increasing amount of litigation concerning this. Div. Ex. 210 at 34. Indeed, an insurance company sued to have two policies that Fund I bought declared void as having been procured without an insurable interest. Div. Ex. 495.

premiums of such polic[i]es for the expected life expectancy" of the insured; the cash was to be invested in "overnight government securities until needed." Div. Ex. 206 at 36. The death benefits were to be distributed to the investors after five years. Div. Ex. 206 at 36, Div. Ex. 211 at 7, Div. Ex. 217 at 1. The PPM for Fund I further represented that the remaining amount of capital commitments "anticipated to be approximately 40%" would be devoted to corporate investments. Div. Ex. 206 at 38. The PPM for Fund II did not provide such numerical details. However, marketing materials for Fund II represented that about half of Fund II's investment would be in insurance policies amounting to at least 117% of capital commitments with additional funds to secure payment of premiums, with the other half in corporate investments. Div. Exs. 224, 608.

3. Compensation and Valuation

The PPMs disclosed that JTCM would be compensated by the "two and twenty" measure (investment management fee of 2%, per annum, of the Fund's net asset value (NAV) and performance, or incentive, fee of 20% of appreciation (in excess of a minimum) of the NAV). Div. Ex. 206 at 73, 85, Div. Ex. 210 at 19-20. Thus, the higher the value of the Funds' holdings, the higher JTCM's compensation would be.

The PPM for Fund I provided, "The value of investments made by [Fund I] will be determined solely by or under the direction of [JTCM]." Div. Ex. 206 at 40. The February 5, 2009, PPM for Fund II provided that JTCM would value insurance policies as it reasonably determines. Div. Ex 210 at 46. Corporate investments would be "fair valued." Div. Ex. 210 at 38-40. The PPM warned, "The process of valuing assets for which no published market exists is based in inherent uncertainties and the resulting values may differ from values that would have been used had a ready market existed for such assets and may differ from the prices at which such assets may be sold." Div. Ex. 210 at 65. The Funds' financial statements represented that the assets were fair valued pursuant to Financial Accounting Standards Board Statement of Financial Accounting Standards No. 157 (FAS 157), effective January 1, 2008, later updated and codified as Accounting Standards Codification 820. *See* Div. Ex. 315 at 9, Div. Ex. 316 at 9, Div. Ex. 317 at JTBOF 6296, Div. Ex. 318 at JTBOF 6308. The investments in interest-bearing and equity securities were "recorded at fair value as determined in good faith by [JTCM]." Div. Ex. 315 at 8, Div. Ex. 316 at 8, Div. Ex. 317 at JTBOF 6295, Div. Ex. 318 at JTBOF 6307. The values of insurance policies were "estimated by [JTCM] using a life expectancy model." Div. Ex. 315 at 8, Div. Ex. 316 at 8, Div. Ex. 317 at JTBOF 6295.

When he formed the Funds, Jarkesy engaged lawyers, auditors, and a fund administrator, AlphaMetrix 360 f/k/a Spectrum Global Fund Administration (AlphaMetrix or Spectrum). Tr. 65-66, 282-86, 2378-79; Div. Ex. 230. The services AlphaMetrix provided for the Funds are listed in a Services Agreement. Tr. 285-86, 293-94, 420; Div. Ex. 230 at Schedule I. These include calculating the NAV and calculating and distributing investor statements, monthly.[18] Tr. 286-87, 290-91; Div. Ex. 230 at Schedule I. The valuation of each asset in the Funds' holdings at each month-end was shown on each Fund's holdings pages. Tr. 326-27; Div. Exs. 301, 303. Each individual investor's share was

[18] AlphaMetrix also sent communications such as a "research report" on America West, a letter from Jarkesy, and a press release concerning America West, and a Fund "Quarterly Review to investors at the request of Jarkesy. Tr. 339-44; Div. Exs. 214, 218, 239, 240, 250.

calculated from the aggregate valuation shown on the holdings pages. Tr. 326-28, 402-03. The account statement sent to an investor showed the valuation of his interest in the Fund and any performance, not the individual holdings of the Fund. Tr. 327-29; Exs. 236, 237, 238.

Contrary to the representations in the Funds' PPMs and financial statements that JTCM set the valuations for the Funds' positions, Jarkesy disclaimed responsibility for this, indicating that AlphaMetrix valued the Funds' positions. Tr. 2663 ("The valuations were provided and checked by Alpha[M]etrix."); *see also* Tr. 1144 (The auditors "considered AlphaMetrix part of the management team."), 2157 (Jarkesy describing AlphaMetrix as a valuation consultant). In reality, AlphaMetrix did not value any of the Funds' positions itself; it had no capability to do so. Tr. 289-90, 299-300. AlphaMetrix attempted to obtain valuations for the Funds' positions from independent sources, such as Bloomberg; for assets, such as the Funds' bridge loans and short-term notes, life settlement policies, and warrants, for which it could not obtain values from an independent data provider, it asked JTCM for valuations. Tr. 287-300. AlphaMetrix tried to get as much documentation as possible in support of JTCM's marks. Tr. 311-12. Questions concerning valuation were directed to Jarkesy or to his assistants Linda Ortiz and Patty Villa, who relayed Jarkesy's decisions. Tr. 295, 300-06, 428; Div. Exs. 329, 330, 333. Jarkesy had the final word, even if unreasonable, in setting valuations; for example, he insisted on valuing restricted America West stock at the same price as free-trading stock even after AlphaMetrix questioned this. Tr. 347-50. Prices on the Funds' holdings pages, which ultimately were reflected in the account values shown in investors' monthly statements, were obtained as described above. Tr. 325-29, 402-03; Div. Exs. 301-04. JTCM would approve the holdings, then approve any profit and loss, then approve financial statements, and ultimately the investor statements. Tr. 328. AlphaMetrix eventually terminated the relationship with the Funds due to nonpayment. Tr. 345, 434-37.

Management fees paid to JTCM through December 31, 2010, totaled $1,278,597. Fund I paid $337,000 during the fifteen months ended December 31, 2008 (Div. Ex. 315 at 11), $363,700 during 2009 (Div. Ex. 316 at 12), and $509,000 during 2010 (Div. Ex. 317 at JTBOF 6299). Fund II paid $68,897 during the eighteen months ended December 31, 2010 (Div. Ex. 318 at JTBOF 6311). *See also* Tr. 2710 (Jarkesy agrees that JTCM received about $1.3 million in management fees). The financial statements did not reflect any payments of incentive fees separate from management fees.[19]

4. KPMG and Deutsche Bank

Investor updates and other marketing materials created by Jarkesy and JTCM between 2008 and 2010 identified KPMG LLP (KPMG), among others, as the auditor of Fund I, and other marketing materials identified KPMG as the auditor for both Funds through 2010. Answer at 6; Div. Exs. 220-224, 248. However, KPMG never audited either Fund. Answer at 6; Tr. 565. The Funds' auditor was Mir Fox & Rodriguez (MFR), a small Houston firm. Tr. 982-97. Eventually, MFR terminated the relationship due to nonpayment. Tr. 998. Jarkesy and JTCM's marketing materials for the Funds identified Deutsche Bank, among others, as the Funds' prime broker. Answer at 6. However, Deutsche Bank never became the Funds' prime broker. Tr. 565; Div. Ex. 229A.

[19] Incentive fees are referenced in the record. Tr. 1326, 2664-65, 2710, 2730. However, there is no evidence that establishes the amount, if any, of incentive fees actually paid to JTCM.

5. America West, Galaxy, and Radiant[20]

Portfolio companies America West, Galaxy, and Radiant figure prominently in the events at issue. Tr. *passim*; Div. Exs. *passim*; Resp. Exs. *passim*.

a. America West

America West is a now-bankrupt domestic coal producer in Utah. Tr. 620-25; Form 8-K filed January 24, 2013.[21] Alexander Walker, III (Walker), a Salt Lake City lawyer whose family operated America West's mine before the Funds' investments, is now America West's sole officer and director. Tr. 620-23. Jarkesy was a director of and active in managing America West from about December 2007 to 2012. Tr. 626-28. Brian Rodriguez (Rodriguez), an associate of Jarkesy, was also a director and CFO of the company.[22] Div. Ex. 311 at 19, 64-65.

Jarkesy introduced America West to JTF, which became the company's investment banker from 2008 through June 2011. Tr. 637-38. America West paid JTF what amounted to a 13% commission on all funds raised and was also required to use JTF for insurance and other services; America West was forced to comply with these terms because it was in dire need of financing and had exhausted other alternatives. Tr. 638-42, 681, 683. In fact, it was always undercapitalized. Tr. 675. Jarkesy was the only person from America West who could talk to Belesis but was unsuccessful in persuading him to lower the fees. Tr. 642-43, 686-87. America West was also required to issue stock in addition to paying various fees; in fact, on one occasion when Walker thought America West had a binding deal for a desperately needed cash infusion from JTF, Belesis telephoned him and demanded 10 million shares of America West stock before he would wire the money. Tr. 647-49; Div. Ex. 311 at 30-31. Jarkesy told Walker he was upset but could do nothing. Tr. 649. Eventually, America West came to believe that JTF was an affiliate of the Funds. Tr. 656-65, 688-93; Div. Ex. 346 at 72. Walker was shocked in early 2012 when a JTF representative told him it was unnecessary for Jarkesy to participate in a conference call related to the Funds' investments in America West because he could speak for Jarkesy and, in fact, JTF and Jarkesy were partners in this and other investments and "are tied at the hip." Tr. 654-58.

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[20] The Division identified, at Tr. 2486-87, the companies referred to in the OIP as Companies A, B, C, and D as follows: Galaxy is Company A; B is Radiant; C is Amber Ready, Inc.; and D is America West.

[21] Official notice, pursuant to 17 C.F.R. § 201.323, is taken of the Form 8-K and of America West's and Radiant's Forms 10-K, which are in the Commission's public official records contained in EDGAR.

[22] Marathon Advisors, LLC, jointly owned by Jarkesy and Rodriguez, was designated as the successor general partner for Fund II in the event of the withdrawal of Jarkesy as a General Partner Key Man. Div. Ex. 210 at 15, 52-53. Rodriguez was also an officer and director of Radiant. Div. Ex. 310 at 32-33.

America West paid more than $3.2 million cash in fees to JTF. Tr. 644; Div. Ex. 346 at 72 ($1,767,265 in sales commissions from Q4 2010 to May 16, 2012); 2009 Form 10-K at 42 ($115,425 in sales commissions, $180,000 in consulting fees paid in 2009); 2008 Form 10-K at 26-27 ($1,226,065 in sales commissions paid in 2008). America West also issued warrants to JTF. Div. Ex. 346 at 72; 2010 Form 10-K at 31; 2009 Form 10-K at 42. As of April 14, 2010, JTF owned 4% and the Funds, Jarkesy, and affiliates owned 19.2% of America West. Div. Ex. 311 at 69.

In addition to purchasing America West stock, Fund I made loans to America West, totaling $925,000 by the end of 2008. Div. Ex. 301 at JTBOF 19211, 19235, 19247. Fund I received additional stock in connection with the loans. America West paid JTF a commission of $120,250 in connection with the $925,000 loan. 2008 Form 10-K at 26. America West paid off the loans in January 2009. Div. Ex. 203 at 13-14, Div. Ex. 301 at JTBOF 19207, 19211. Fund I made more loans in 2009, which by the end of 2009 amounted to at least $1.3 million. Div. Ex. 301 at JTBOF 19167. By then, America West had fallen behind on its payments; it was in default and the loan was due on demand. Div. Ex. 311 at 53. Jarkesy believed that the notes would be paid; either JTF or another bank would raise capital or the notes would be restructured. Tr. 2426-29. Fund I continued to lend during 2010, and, as of year-end, had twelve notes totaling $1,725,500. Div. Ex. 301 at JTBOF 19131. Fund II also made loans during 2010; as of year-end it had seventeen notes totaling nearly $1.4 million, many of which were past due. Div. Ex. 303 at JTBOF 19287. Respondents did not write down the value of the notes. Div. Ex. 301 at JTBOF 19131, Div. Ex. 303 at JTBOF 19287. Nor did they advise their auditors that any of the notes were impaired. Tr. 1047-48, 1159. The vast majority of the loans were not repaid. Tr. 633. Rather, in July 2011, much of the debt was converted into equity and America West issued nearly 13 million shares of common stock to the holders of the notes. Tr. 633-34; Div. Ex. 346 at 30. America West paid JTF approximately $580,450 in so-called "sales commissions" with respect to this conversion. Div. Ex. 312 at 3; Resp. Ex. 138 at 272.

Jarkesy spoke highly of America West in the Podcast. Tr. 208-10; Div. Ex. 203 at 13-14, 16-17, Div. Ex. 204. His optimism was inconsistent with America West's true financial condition; the unaudited financial statements included with America West's Form 10-Q for the quarter ended March 31, 2009, contained a going concern statement. Div. Ex. 348 at 11. Jarkesy also had an optimistic "Research Report" concerning America West sent to Fund investors in September 2010, and a press release concerning an interview with Jarkesy about America West. Tr. 339-41; Div. Exs. 239, 250. In August 2011 Jarkesy sent a letter to investors with optimistic predictions about America West for the following year. Div. Ex. 240. This was again inconsistent with America West's true financial condition; its 2010 Form 10-K, signed on April 15, 2011, by Jarkesy, contained a going concern statement. Div. Ex. 311 at 12, 46.

b. Galaxy

Galaxy's business plan included an infomercial for its skin care product that was ultimately not funded. Tr. 1548, 1550-51, 1556-58; Div. Ex. 314 at 6, Div. Ex. 521. Galaxy was in poor financial shape. Tr. 1587, 1598-1600, 1700; Div. Ex. 314, Div. Ex. 514 at 1. The audited financial statements for the year ended December 31, 2009, for Galaxy's two predecessor companies each contained a going concern statement. Div. Ex. 314 at 61, 126. After an appeal from then CEO Frank DelVecchio on December 17, 2009, Belesis ordered Jarkesy to provide funds "ASAP." Div. Ex. 513. The next day, December 18, 2009, Fund I bought $30,000, and Fund II, $10,000, of Galaxy stock. Div. Ex. 314

at 15. As of September 30, 2010, Galaxy had cash of $1,330, current liabilities vastly in excess of current assets, and an accumulated deficit of $42,116,148. Div. Ex. 314 at 98.

Gary Savage (Savage), who had been CEO of a predecessor company, was Galaxy's CEO from April 2010 to July 2011, when he resigned. Tr. 1550, 1560, 1638, 1645; Div. Ex. 314 at 32. In searching for funding, Savage met Belesis, who was interested and told him to meet with Jarkesy in Houston. Tr. 1554-56, 1686, 1689-90, 1694. Savage met with or spoke on the phone with Belesis many times. Tr. 1687, 1712. *See also* Tr. 1557-99 *passim*. Galaxy did receive some loans but not the amount of financing that Belesis promised. Tr. 1564, 1703, 2454. When Jarkesy did provide financing, he sent funds directly to Galaxy's creditors rather than to Galaxy. Tr. 1569-72, 2447-51. Belesis and Jarkesy installed a CFO of their choice into the company and tightened control over check-writing.[23] Tr. 1572-86; Div. Exs. 516, 517. Together, Belesis and Jarkesy exerted control over the company.[24] Tr. 1555-56, 1567-69, 1572-86, 1711. As of February 7, 2011, Fund I owned 43.18% of Galaxy. Div. Ex. 314 at 35.

Galaxy issued penalty shares, also referred to as liquidated damages shares, pursuant to a "Registration Rights Agreement" and other agreements, to the Funds due to its defaults under those agreements. Tr. 415-19, 1738-56, 2132, 2458; Resp. Exs. 4, 6, 7, 8.

AlphaMetrix relied on Jarkesy's valuations since Galaxy was not publicly traded. Tr. 308-09; Div. Exs. 324, 329, 330. On one occasion, there was a transfer of Galaxy shares from Fund I, where they were valued at $0.002, to Fund II, where Jarkesy attempted to value the same shares at $1.00; when confronted, Jarkesy backed down, and the matter was resolved satisfactorily from an accounting standpoint. Tr. 311, 323-25, 414-15; Div. Ex. 325. From the end of 2009 through the beginning of 2011, the value that Respondents assigned to Galaxy and its predecessor company varied widely from $0.10 to $3.30. Div. Exs. 301, 305. The number of shares outstanding during that time varied, due to a reverse split, issuance of penalty/liquidated damages shares, etc.; however, the changes in the valuations did not accord with these events. Tr. 307-25, 2468, 2733-35; Div. Exs. 324, 325, 329, 330, 333. In July 2011, Respondents wrote down the value of the shares to zero. Tr. 2736; Div. Ex. 301 at JTBOF 19107, Div. Ex. 303 at JTBOF 19273.

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[23] Two persons, in addition to Savage, had been authorized to write checks and had embezzled funds from the company. Tr. 1766-85. One of the persons was a convicted felon. Tr. 1778, 1783.

[24] Savage sued, among others, Fund I, JTCM, and JTF (JT Defendants) for unpaid salary and benefits owed by Galaxy. Resp. Ex. 312. The court declined to pierce the corporate veil and dismissed the claims against the JT Defendants, noting that the allegations "pertain precisely to the type of conduct implicated in [controlling precedent]; that the JT Defendants ensured the money they lent to Galaxy was used as they saw fit is to be expected of a lender." *Savage v. Galaxy Media & Mktg. Corp.*, No. 1:11-cv-6791 (S.D.N.Y. July 5, 2012), ECF No. 26 at 18, *aff'd*, 526 Fed. App'x. 102 (2d Cir. 2013); Official notice.

c. Radiant

Radiant is an oil and gas exploration and production company. Div. Ex. 310 at 4. As of December 8, 2010, Fund I and Jarkesy owned 17% and JTF owned 23% of Radiant. Div. Ex. 310 at 35. Jarkesy was a director of Radiant during 2010 through 2013. Tr. 1318, 2476; Div. Ex. 310 at 35-36; Form 10-K for 2011 and 2012, filed Jan. 22, 2014, at 47, Official notice. Jarkesy introduced the company to JTF. Tr. 2218. As with America West, JTF was to receive payments for investment banking services totaling 13% of the proceeds of equity financings, as well as stock and warrants. Div. Ex. 310 at 36, 57. As with Galaxy, JTF promised, but did not provide, financing of Radiant. Tr. 2491, 2511.

Radiant's predecessor, G/O Business Solutions, Inc. (GOBS), was founded in 2007. Resp. Ex. 311. At the time, the company's stock was held mostly by Sand Hills General Partners and its owner, Sand Hill Partners, LLC; Jarkesy owned a one-third interest in Sand Hill General Partners. Div. Ex. 343. On December 27, 2007, Jarkesy sold the shares of GOBS that he controlled through Sand Hill to Fund I for $400,000. Div. Ex. 301 at JTBOF 19258, Resp. Ex. 311 at 34. For more than a year, Respondents valued the shares of GOBS at cost but in March 2009 increased the value from $0.02 to $0.06 per share, recognizing an unrealized gain of $746,000. Div. Ex. 301 at JTBOF 19198. Respondents maintained this valuation until April 2010. Div. Ex. 301 at JTBOF 19154. At that time, the company reorganized, effected a 5:1 reverse split, and changed its name to Radiant. Resp. Ex. 310 at 29.

Based on the 5:1 reverse split, Respondents revalued the stock from $0.06 to $0.30 per share. Div. Ex. 301 at JTBOF 19154. In August 2010, Radiant acquired an oil and gas production company; the agreement was first announced in a Form 8-K dated July 23, 2010. Resp. Ex. 310 at 5, 9, 29. There were no public transactions in the stock during July, August, or September 2010. Div. Ex. 111. Respondents sold 300,000 shares of Radiant from Fund I to Fund II in August, with a cost basis to Fund II of $0.23. Div. Ex. 303 at JTBOF 19295. Nonetheless, Respondents increased their valuation of Radiant in Fund I to $1.00 per share in August 2010, causing an increase in Fund I's unrealized profits for this holding. Div. Ex. 301 at JTBOF 19142.

A further, 2:1, reverse split occurred in September 2010. Div. Ex. 310 at 23. The $1.00 valuation was maintained. Div. Ex. 301 at JTBOF 19136. The stock traded for the first time in fifteen months during four days in December 2010, ending the year at $4 per share. Div. Ex. 111 at 4. The price spike was coincident with the promotional campaign discussed *infra*. Using the $4 price, Respondents' valuation of Fund I's Radiant position reflected an unrealized gain at year-end of nearly $7 million, more than a $5 million gain from the previous month. Div. Ex. 301 at JTBOF 19130, 19133. Fund I's financial statements for year-end 2010 represent the fair value of the equity position in Radiant as $6,936,996. Div. Ex. 317 at 4, 8. Fund II's financial statements for year-end 2010 represent the fair value of the equity position in Radiant as $1,746,320. Div. Ex. 318 at 4, 8. Fund II held Radiant warrants, and AlphaMetrix relied on Jarkesy's valuations of them since they were not publicly traded. Div. Ex. 333. He insisted on valuing them at $6.92 as of January 31, 2011, even though they had last been priced at $0.12 on August 31, 2010. Tr. 302-06; Div. Ex. 333. JTCM justified the dramatic revaluation of the warrants, on the basis that "the stock price was crazy in Jan[uary]." Div. Ex. 333. However, this justification was inconsistent with the fact the price had fallen to $2.25 by the end of January. Div. Ex. 111.

Some of the Funds' Radiant shares were distributed to Fund I and II investors in October 2013. Tr. 48-49, 744, 818-19, 1314-15, 1398; Div. Ex. 247. Jarkesy sent the investors their stock certificates with an October 23, 2013, letter in which he enclosed a Radiant press release announcing a purchase of oil and gas properties in a cash and Radiant stock transaction; Jarkesy stated that these Radiant shares were valued at $2 per share and opined that the stock could be worth substantially more. Div. Ex. 247. Yet, the closing price available from Yahoo! Finance was $1.04 from at least October 24, 2013, to January 2, 2014; there were no transactions during that period. Div. Ex. 111A.

6. Promotions

Jarkesy directed America West to hire promotional firms to promote its stock and chose the firms. Tr. 628-32. At his behest, America West engaged MEC Promotions (MEC) to conduct a promotional campaign. Tr. 629, 870-71, 883-86. MEC received $5,000 from the Funds[25] in October 2010, $50,000 in December 2010, and $30,000 in January 2011;[26] these payments were for work being done at that time.[27] Tr. 888-91; Div. Exs. 306, 306d, 307a, 308.[28] MEC sent out ten to fifteen emails to its subscriber list of about 5,000 and posted information on its website as well.[29] Tr. 886, 897. America West, at the behest of Jarkesy, also engaged Park Avenue Consulting and Uptick Capital LLC for "investor relations services," paying them in stock, the former in October 2010, and the latter in November and December 2010. Div. Ex. 311 at 31-32. The price of America West spiked: it closed at $0.075 on October 1, 2010, but at $1.95 on December 31, 2010. Tr. 667-68; Div. Ex. 110. On December 30, 2011, it was $0.21, and on December 31, 2012, $0.047. *Id*. Respondents valued America West stock at $1.95 on Fund I's holdings page as of December 31, 2010. Div. Ex. 301 at JTBOF 19130.

[25] These payments were pursuant to a flow of funds of loan[s] the Funds made to America West. Tr. 891-92, 2493-96.

[26] MEC also received, in February 2011, 150,000 shares from America West of its stock for consulting. Tr. 892-93, 906-07; Div. Ex. 311 at 32.

[27] Additionally, on September 28, 2010, Respondents, through AlphaMetrix, sent investors a research report on America West that they had commissioned. Div. Ex. 239. Additional articles by a promoter extolling America West were published in August and September 2010 on the Examiner.com website. Div. Exs. 254, 255.

[28] Division Exhibits 306, 306a, 306b, 306c, 306d, and 307, account statements for Wells Fargo Bank account number ending in 1597, are for Fund II. Tr. 586. Division Exhibits 307a and 308, account statements for Wells Fargo Bank account number ending in 2171 are, thus, for Fund I.

[29] MEC obtained the content from public sites, not from America West. Tr. 884, 886.

MEC also conducted a more limited promotion of Radiant for which it was paid $5,000 by Fund II on December 28, 2010.[30] Tr. 897-98; Div. Ex. 306c. Radiant stock, which had not traded since September 10, 2009, when it closed at $0.12, closed at $4 on December 17, 2010, and at $4 on December 31, 2010. Div. Ex. 111. Respondents used $4 for their valuation of Fund I's Radiant position, which reflected an unrealized 2010 year-end gain of over $6.5 million, a more than $5 million gain from the previous month. Div. Ex. 301 at JTBOF 19130, 19133. Fund I's financial statements for 2010 represent the fair value of its Radiant position as $6,936,996, and Fund II's, as $1,746,320. Div. Ex. 317 at JTBOF 6291, Div. Ex. 318 at JTBOF 6303.

7. Investment Limitation

Fund I's PPM provided, under the heading "**Investment Limitations**," "The total investment of [Fund I] in any one company at any one time will not exceed 5% of the aggregate Capital Commitments." Div. Ex. 206 at 12. However, elsewhere, in a discussion of risk factors, the PPM stated, "Because as much as 10% of [Fund I's] aggregate committed capital may be invested in a single Portfolio Company, a loss with respect to such a Portfolio Company could have a significant adverse impact on [Fund I's] capital." Div. Ex. 206 at 25. The 5% figure was repeated in marketing materials and newsletters. "The fund is limited to 5% in any one corporate investment." Div. Ex. 214 at 3, Div. Ex. 215 at 3, Div. Ex. 216 at 5, Div. Ex. 217 at 2. "The fund is limited to 5% in any one corporate investment at the time of investment." Div. Ex. 218 at 5. The 10% reference cannot be reconciled with the explicit 5% limitation, which is repeated in the marketing materials and newsletters. Accordingly, it is found that the limitation was 5%. Fund II's PPM did not contain a percentage limitation. Div. Ex. 210.

Respondents' investments were not consistent with the 5% limitation. As of December 1, 2007, Fund I had capital contributions of $7,231,021.92, 5% of which is $361,551. Div. Ex. 231 at JBTOF 1692. Yet, as of that date Fund I had invested $495,705 in EnterConnect Inc., $400,000 in GOBS, $425,000 in Reddi Brake Supply Corp., and $518,800 in UFood Restaurant Group. Div. Ex. 301 at JTBOF 19257-59. As of December 31, 2008, Fund I had capital contributions of $16,620,511, 5% of which is $831,025. Div. Ex. 315. Yet, as of that date Fund I had invested $1,392,000 in America West (eight notes totaling $925,000 and more than $467,000 in America West stock). Div. Ex. 301 at JTBOF 19209, 19211. As of December 31, 2009, Fund I had capital contributions of $18,358,002, of which 5% is $917,900. Div. Ex. 316 at 11. As of that date Respondents had invested $1,860,000 in America West (a $1,330,000 note and stock and royalties purchased for more than $530,000.) Div. Ex. 301 at JBTOF 19166-67. As of December 31, 2010, Fund I had capital contributions of $20,112,852, of which 5% is $1,005,623. Div. Ex. 317. As of that date Fund I had invested $2,255,500 in America West (twelve notes totaling $1,725,500 plus the stock and royalties that cost more than $530,000). Div. Ex. 301 at JTBOF 19130-31.

As described in Fund I's financial statements, the values (as opposed to purchase price) that it assigned to its holdings also showed investments inconsistent with the 5% limitation. As described in

[30] Respondents added the $5,000 to Fund II's cost basis for the Radiant stock. Div. Ex. 303 at JTBOF 19285, 19287 (holdings pages for January 31, 2011, and December 31, 2010, showing a $5,000 increase in the cost basis for the same number of shares).

its financial statements, as of December 31, 2008, America West stock (valued at $5,465,040) comprised 33% of Fund I's capital, and Sahara Media Holdings, Inc., stock (valued at $3,049,383), 18%. Div. Ex. 315 at 5. As of December 31, 2009, America West stock (valued at $4,747,302) comprised 19% of capital, and Amber Alert/Amber Ready[31] stock (valued at $9,090,654), 37%. Div. Ex. 316 at 5. As of December 31, 2010, America West stock (valued at $7,013,322) comprised 26% of capital, and Radiant stock (valued at $6,936,996), 25%. Div. Ex. 317 at JTBOF 6291.

8. Distributions to Investors

There was one distribution to Fund I investors from a life settlement policy after the insured died. Tr. 743-44, 817, 822, 1392-94. Jarkesy told investor Robert Fullhardt that the amount distributed was small because the Fund had to retain most of the proceeds to pay premiums on the remaining policies. Tr. 1393-94. At the end of 2013 there was a distribution of shares of Radiant. Tr. 744, 818-19, 1398; Div. Ex. 247. There were no other distributions. Tr. 746, 822, 1403.

Fund I's PPM represented that the Master Trust holding the insurance policies would have a separate premium financing account, which "will contain sufficient cash upon the purchase of the Life Settlement Policies to pay the premiums of such polic[i]es for the expected life expectancy" of the insured. Div. Ex. 206 at 36. The Fund's actions were not in accord with this; it did not maintain sufficient cash to pay the premiums, and most of the policies lapsed because of this. Tr. 2503-04, 2958.

9. Life Insurance Policies

Fund II did not buy any life insurance policies; neither its financial statements nor holdings pages show any indication that Fund II owned policies. Div. Exs. 303, 318. This was inconsistent with the representations in Fund II's PPM and marketing materials. Div. Ex. 210 at 12, 55-60, Div. Ex. 224. The PPM represented that Fund II would acquire policies with a face value of at least 117% of aggregate contributions and the marketing materials represented that Fund II would devote half of its investments to policies; insurance policies were half of Fund II's two-part investment strategy. Div. Ex. 210 at 12.

Between September 28, 2007, and January 25, 2008, Fund I purchased eight life insurance policies, with face values (amount to be paid on the death of the insured) totaling $13 million. Div. Ex. 405. In April and May 2009, Fund I bought five additional policies, with face values totaling $13.5 million.[32] *Id*. Respondents decided to allow one policy (Paul Evert) with a face value of $5 million to lapse during 2009. Div. Exs. 414, 418, 424. As of December 31, 2008, Fund I had capital contributions of $16,620,511. Div. Ex. 315 at 11. Thus, the $13 million total face value of the policies was less than the 117% of that sum as promised in the PPM and marketing materials. The $21.5

[31] Galaxy was formerly known as Amber Ready, Inc., which was formerly known as Amber Alert Safety Centers, Inc. Div. Ex. 314 at 6.

[32] Jarkesy mistakenly said there were fourteen (rather than thirteen) policies in the Podcast that was sent to Fund I investors. Div. Ex. 203 at 20, Div. Ex. 204.

million total face value of policies held on December 31, 2009, was more than 117% of the capital contributions as of that date, $18,358,002. Div. Ex. 316 at 11. The $21.5 million face value was less than 117% of capital contributions, $20,112,852, as of December 31, 2010. Div. Ex. 317 at 11. Further, Respondents spent only $3,865,309 (including paying premiums) on life insurance policies through December 31, 2010. Div. Ex. 317 at 10. This fact, together with the fact that Respondents did not set aside funds sufficient to pay premiums shows that Respondents did not invest in insurance policies as promised in the PPM and marketing materials. Nor did they timely put all policies in the Master Trust. Div. Exs. 401, 402, 405.

Respondents retained Steve Boger, an actuary, to assist in valuing the insurance policies. Tr. 247-48, 459-60, 462, 2707; Div. Ex. 601. Boger valued the eight policies that Fund I owned at the time of his valuation in January 2009. Tr. 495-97; Div. Ex. 425. Boger testified that the underwriters from which Jarkesy had obtained life expectancy estimates (LEs) had changed their LE process such that they were providing longer LEs starting in the second half of 2008.[33] Tr. 499-500. Also, the Society of Actuaries released new valuation tables, essentially extending LEs, and Boger sent information concerning this to his clients, including Jarkesy, in March 2008. Tr. 530-33; Div. Ex. 499. Jarkesy refers to the LE increase in the Podcast and notes that JTCM wrote down Fund I's policies by almost $1.2 million as a result in the financial statements for the period ended December 31, 2008, issued March 27, 2009, and in the Fund's holdings pages as of March 31, 2009. Div. Ex. 203 at 25, Div. Ex. 301 at JTBOF 19199, 19203 (68, 72 of 167), Div. Ex. 315 at 3-5.

To reach a present value for each policy, Boger provided a range of discount rates (14%, 15%, and 16%). Tr. 502-06; Div. Ex. 425. The choice of discount rates is a matter of judgment; in Boger's words, the numbers are "a little soft." Tr. 504. Applying 14%, 15%, or 16% resulted in a negative value for the portfolio of policies. Tr. 506-07; Div. Ex. 425. At Jarkesy's request, Boger produced a second iteration, applying 12%, 14%, and 16% discount rates. Tr. 508-09; Div. Ex. 426. The portfolio had a positive value at 12%.[34] Tr. 509; Div. Ex. 426. Jarkesy chose to use the positive value at the 12% discount rate for the financial statements for the period ended December 31, 2008. Div. Ex. 315. The statements reported the value for the five policies that had positive values without netting them with the negative values of the remaining three policies. Div. Exs. 315, 426. This was apparently on the assumption that a policy could not be worth less than zero since it could be allowed to lapse,[35] as was subsequently done with the Evert policy, which had a negative value ($310,165), even at 12%, as of December 2008. Div. Ex. 426 at 2.

[33] Indeed, Fund II's PPM acknowledged the revised mortality tables. Div. Ex. 210 at 30-31.

[34] At Jarkesy's request, Boger also provided a table valuing the policies on dates in the future using 12%, 14%, and 16% discount rates. Tr. 511-15; Div. Exs. 419, 421. As Boger noted, variables, such as the discount rate, that might be accurate at the starting point could change over a period in the future. Tr. 513-15; Div. Ex. 421 at 1.

[35] Respondents make this argument in their Response to the Division's Proposed Findings of Fact and Conclusions of Law at 53-54. However, the policies had not lapsed as of December 31, 2008, and Respondents do not point to any accounting principle that allows a reporting entity to disregard an asset that it actually holds.

Respondents subsequently used different actuaries to value the five policies purchased in 2009, again requesting a 12% discount rate. Div. Exs. 432, 433, 436, 440, 442. Yet at the same time, Jarkesy knew he was currently purchasing policies at a 15% or better (that is, more inexpensively than 12%) discount. Div. Ex. 203 at 23, Div. Ex. 204, Div. Ex. 619 at 1. Respondents continued using the 12% discount rate for Fund I's 2010 financial statements. Div. Ex. 623.

Pursuant to Financial Accounting Standards Board (FASB) Staff Position 85-4-1, investors who use fair value must initially value a life insurance policy at the purchase price and remeasure it at fair value at each subsequent reporting period. Div. Ex. 119 at 2. However, Respondents immediately fair valued the new policies. Thus, as compared with the total purchase price of $1,195,000, the five policies (purchased between April 7 and May 1) were valued at $2,307,567 as of May 31, 2009, a write-up of $1,112,567. Div. Ex. 498B at AM_SEC 285200 (lines 379-93), 285203 (lines 491-92), Div. Ex. 647. While Respondents point to their reliance on attorneys, AlphaMetrix, etc., it is not clear how they could believe that life insurance policies would almost double their value a few weeks after purchase. It is noted that this revaluation offset most of the $1.2 million write-down of the first eight policies as of March 31, 2009. Jarkesy's August 2010 letter to investors stated that "we are adding more policies to the portfolio," which was untrue since Fund I purchased no policies after 2009. Div. Ex. 240.

In 2010, the Ohio National Life Assurance Corporation filed suit to have the Shirlee Davis and Joesph Griffin policies voided. *Ohio Nat'l Life Assurance Corp. v. Davis*, No. 10-cv-2386 (N.D. Ill. Apr. 16, 2010); *Ohio Nat'l Life Assurance Corp. v. Davis*, No. 10-cv-4241 (C.D. Cal. June 9, 1010). Official notice. In August 2010, Respondents wrote the policies down from $194,633 and $137,562, respectively, to $100,000 each. Div. Ex. 404 at JTBOF 10643, 10471. MFR challenged the write-down amounts as not being specifically supported in the court documents or any third-party valuation and recommended writing them back up to the amortization schedule. Div. Ex. 487 at 5. Respondents did so for the 2010 financial statements. Div. Ex. 404 at JTBOF 6453.

Although representing the insurance component as a conservative hedge, Respondents took no steps to reduce risk. Investing in a large number of policies reduces risk, known as mortality risk, as Jarkesy knew and Fund I's PPM represented; if there are only a few policies, the insureds might all live much longer than actuarially expected, thus postponing the payout and extending the time during which premiums must be paid. Tr. 465-66; Div. Ex. 206 at 36-37, Div. Ex. 600. Yet Respondents only acquired thirteen policies.

III. CONCLUSIONS OF LAW

The OIP charges that JTCM and Jarkesy willfully violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder and willfully aided and abetted and caused violations by the Funds of those provisions. Additionally, the OIP charges that JTCM and Jarkesy willfully violated Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. As discussed below, it is concluded that these charges were proved.

A. <u>Antifraud Provisions</u>

Respondents are charged with willful violations of the antifraud provisions of the Securities, Exchange, and Advisers Acts – Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder – which prohibit essentially the same type of conduct. *United States v. Naftalin*, 441 U.S. 768, 773 n.4, 778 (1979); *SEC v. Pimco Advisors Fund Mgmt. LLC,* 341 F. Supp. 2d 454, 469 (S.D.N.Y. 2004). They are also charged with willfully aiding and abetting and causing violations by the Funds of Securities Act Section 17(a) and Exchange Act Section 10(b) and Rule 10b-5.

Securities Act Section 17(a) makes it unlawful "in the offer or sale of" securities, by jurisdictional means, to:

> 1) employ any device, scheme, or artifice to defraud;
>
> 2) obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary to make the statement made not misleading; or
>
> 3) engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Similar proscriptions are contained in Exchange Act Section 10(b) and Rule 10b-5 and in Advisers Act Sections 206(1), 206(2), and 206(4), as well as in Advisers Act Rule 206(4)-8, which applies specifically to "any investment adviser to a pooled investment vehicle." 15 U.S.C § 80b-6(4); 17 C.F.R. § 275.206(4)-8.

Scienter is required to establish violations of Securities Act Section 17(a)(1), Exchange Act Section 10(b) and Rule 10b-5, and Advisers Act Section 206(1). *Aaron v. SEC*, 446 U.S. 680, 690-91, 695-97 (1980); *SEC v. Steadman*, 967 F.2d 636, 641 & n.3 (D.C. Cir. 1992). It is "a mental state embracing intent to deceive, manipulate, or defraud." *Aaron*, 446 U.S. at 686 n.5; *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 & n.12 (1976); *SEC v. Steadman*, 967 F.2d at 641. Recklessness can satisfy the scienter requirement. *See David Disner*, Exchange Act Release No. 38234, 1997 SEC LEXIS 258, at *15 & n.20 (Feb. 4, 1997); *SEC v. Steadman*, 967 F.2d at 641-42; *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1568-69 (9th Cir. 1990). Reckless conduct is "conduct which is 'highly unreasonable' and which represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it.'" *Rolf v. Blyth, Eastman Dillon & Co., Inc.*, 570 F.2d 38, 47 (2d Cir. 1978) (quoting *Sanders v. John Nuveen & Co.*, 554 F.2d 790, 793 (7th Cir. 1977)).

Scienter is not required to establish a violation of Securities Act Sections 17(a)(2) and 17(a)(3), and Advisers Act Sections 206(2) and 206(4) and Rule 206(4)-8; a showing of negligence is adequate. *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963); *SEC v. Steadman*, 967 F.2d at 643 & n.5; *SEC v. Yorkville Advisors, LLC*, No. 12-cv-7728, 2013 WL

3989054, at *3 (S.D.N.Y Aug. 2, 2013); *SEC v. Quan*, No. 11-cv-723, 2013 WL 5566252, at *16 (D. Minn. Oct. 8, 2013); *Fundamental Portfolio Advisors, Inc.*, Securities Act Release No. 8251, 2003 SEC LEXIS 1654, at *29 (July 15, 2003), *recons. denied*, Securities Act Release No. 8574, 2005 SEC LEXIS 1192 (May 23, 2005); *Byron G. Borgardt*, Exchange Act Release No. 8274, 2003 SEC LEXIS 2048, at *37-38 (Aug. 25, 2003). Negligence is the failure to exercise reasonable care. *IFG Network Sec., Inc.*, Exchange Act Release No. 54127, 2006 SEC LEXIS 1600, at *37 (July 11, 2006).

Material misrepresentations and omissions violate Securities Act Section 17(a), Exchange Act Section 10(b) and Rule 10b-5, and Advisers Act Sections 206(1), 206(2), and 206(4) and Rule 206(4)-8. The standard of materiality is whether or not a reasonable investor or prospective investor would have considered the information important in deciding whether or not to invest. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231-32, 240 (1988); *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *SEC v. Steadman*, 967 F.2d at 643.

1. Respondents Are Fiduciaries

JTCM was the general partner of the Funds and received fees for managing the Funds. Thus it was an investment adviser within the meaning of the Advisers Act. *See* Section 202(a)(11) of the Advisers Act.[36] *See also Goldstein v. SEC*, 451 F.3d 873, 876 (D.C. Cir. 2006) (holding that the general partner of a hedge fund is an investment adviser within the meaning of the Advisers Act).

Jarkesy, as owner and principal of JTCM, was an associated person of an investment adviser. *See* Advisers Act Sections 202(a)(17), 203(f). Investment advisers and their associated persons are fiduciaries. *Fundamental Portfolio Advisors, Inc.*, 2003 SEC LEXIS 1654, at *54; *see Capital Gains Research Bureau, Inc.*, 375 U.S. at 191-92, 194, 201; *see also Transamerica Mortg. Advisors, Inc. v. Lewis*, 444 U.S. 11, 17 (1979). As fiduciaries, they are required "to act for the benefit of their clients, . . . to exercise the utmost good faith in dealing with clients, to disclose all material facts, and to employ reasonable care to avoid misleading clients." *SEC v. DiBella*, No. 3:04-cv-1342, 2007 WL 2904211, at *12 (D. Conn. Oct. 3, 2007) (quoting *SEC v. Moran*, 922 F. Supp. 867, 895-96 (S.D.N.Y. 1996)), *aff'd*, 587 F.3d 553 (2d Cir. 2009); *see also Capital Gains Research Bureau, Inc.*, 375 U.S. at 194 ("Courts have imposed on a fiduciary an affirmative duty of 'utmost good faith, and full and fair disclosure of all material facts,' as well as an affirmative obligation 'to employ reasonable care to avoid misleading' his clients." (footnotes omitted)). "[W]hat is required is '. . . not simply truth in the statements volunteered, but disclosure' [of material facts]." *Capital Gains Research Bureau, Inc.*, 375 U.S. at 201. "The law is well settled . . . that so-called 'half-truths' – literally true statements that create a materially misleading impression

[36] Section 202(a)(11) provides:

> "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities . . . .

– will support claims for securities fraud." *SEC v. Gabelli*, 653 F.3d 49, 57 (2d Cir. 2011), *rev'd on other grounds*, 133 S. Ct. 1216 (2013).

JTCM is accountable for the actions of its responsible officers, including Jarkesy. *See C.E. Carlson, Inc. v. SEC*, 859 F.2d 1429, 1435 (10th Cir. 1988) (citing *A.J. White & Co. v. SEC*, 556 F.2d 619, 624 (1st Cir. 1977)). A company's scienter is imputed from that of the individuals controlling it. *See SEC v. Blinder, Robinson & Co., Inc.*, 542 F. Supp. 468, 476 n.3 (D. Colo. 1982) (citing *SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1096-97 nn.16-18 (2d Cir. 1972)). As an associated person of JTCM, Jarkesy's conduct and scienter are also attributed to the firm. *See* Section 203(e) of the Advisers Act.

2. Aiding and Abetting; Causing

The OIP charges that Respondents "aided and abetted" and "caused" violations by the Funds of the antifraud provisions. For "aiding and abetting" liability under the federal securities laws, three elements must be established: (1) a primary or independent securities law violation committed by another party; (2) awareness or knowledge by the aider and abettor that his or her role was part of an overall activity that was improper; and (3) that the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation. *See Graham v. SEC*, 222 F.3d 994, 1000 (D.C. Cir. 2000); *Woods v. Barnett Bank of Ft. Lauderdale*, 765 F.2d 1004, 1009 (11th Cir. 1985); *Investors Research Corp. v. SEC*, 628 F.2d 168, 178 (D.C. Cir. 1980); *IIT v. Cornfeld*, 619 F.2d 909, 922 (2d Cir. 1980); *Woodward v. Metro Bank of Dallas*, 522 F.2d 84, 94-97 (5th Cir. 1975); *SEC v. Coffey*, 493 F.2d 1304, 1316-17 (6th Cir. 1974); *Russo Sec. Inc.*, Exchange Act Release No. 39181, 1997 SEC LEXIS 2075, at *16-17 & n.16 (Oct. 1, 1997); *Donald T. Sheldon*, Exchange Act Release No. 31475, 1992 SEC LEXIS 3052, at *18 (Nov. 18, 1992), *aff'd*, 45 F.3d 1515 (11th Cir. 1995); *William R. Carter*, Exchange Act Release No. 17597, 1981 SEC LEXIS 1940, at *78 (Feb. 28, 1981). A person cannot escape aiding and abetting liability by claiming ignorance of the securities laws. *See Sharon M. Graham*, Exchange Act Release No. 40727, 1998 SEC LEXIS 2598, at *29 n.33 (Nov. 30, 1998), *aff'd*, 222 F.3d 994 (D.C. Cir. 2000). The knowledge or awareness requirement can be satisfied by recklessness when the alleged aider and abettor is a fiduciary or active participant. *See Ross v. Bolton*, 904 F.2d 819, 824 (2d Cir. 1990); *Cornfeld*, 619 F.2d at 923, 925; *Rolf*, 570 F.2d at 47-48; *Woodward*, 522 F.2d at 97. That is, it must be established that a respondent either acted with knowledge or that he "encountered 'red flags,' or 'suspicious events creating reasons for doubt' that should have alerted him to the improper conduct of the primary violator," or there was a danger so obvious that he must have been aware of it. *Howard v. SEC*, 376 F.3d 1136, 1143 (D.C. Cir. 2004).

For "causing" liability, three elements must be established: (1) a primary violation; (2) an act or omission by the respondent that was a cause of the violation; and (3) the respondent knew, or should have known, that his conduct would contribute to the violation. *Robert M. Fuller*, Exchange Act Release No. 48406, 2003 SEC LEXIS 2041, at *13-14 (Aug. 25, 2003), *pet. for review denied*, 95 F. App'x 361 (D.C. Cir. 2004). A respondent who aids and abets a violation also is a cause of the violation under the federal securities laws. *See Graham*, 1998 SEC LEXIS 2598, at *30 n.35. Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *See KPMG Peat Marwick LLP*, Exchange Act Release No. 43862, 2001 SEC LEXIS 98, at *82 (Jan. 19, 2001), *recons. denied*, Exchange Act Release No. 44050, 2001 SEC LEXIS 422 (Mar. 5, 2001), *pet. for review denied*, 289 F.3d 109 (D.C. Cir. 2002), *reh'g en banc denied*, 2002 U.S. App. Lexis 14543 (D.C. Cir. 2002).

3. Willfulness

In addition to authorizing a cease-and-desist order, pursuant to Sections 8A(a) of the Securities Act, 21C(a) of the Exchange Act, 9(f) of the Investment Company Act, and 203(k) of the Advisers Act, and disgorgement, pursuant to Sections 8A(e) of the Securities Act, 21B(e) and 21C(e) of the Exchange Act, 9(e) of the Investment Company Act, and 203(j) of the Advisers Act, the OIP authorizes sanctions pursuant to Sections 15(b) of the Exchange Act, 9(b) and 9(d) of the Investment Company Act, and 203(e), 203(f), and 203(i) of the Advisers Act. Willful violations by Respondents must be found in order to impose sanctions on them pursuant to Sections 15(b) and 21B of the Exchange Act, 9(b) and 9(d) of the Investment Company Act, and 203(e), 203(f), and 203(i) of the Advisers Act. A finding of willfulness does not require an intent to violate, but merely an intent to do the act which constitutes a violation. *See Wonsover v. SEC*, 205 F.3d 408, 413-15 (D.C. Cir. 2000); *Steadman v. SEC*, 603 F.2d at 1135; *Arthur Lipper Corp. v. SEC*, 547 F.2d 171, 180 (2d Cir. 1976); *Tager v. SEC*, 344 F.2d 5, 8 (2d Cir. 1965).

B. Antifraud Violations

The record shows that Respondents violated the antifraud provisions by making material misstatements and omissions. These include the representations in Fund I's PPM and marketing materials that the Fund would not invest more than 5% of capital in one company and that the Fund would set aside sufficient cash to pay the premiums of the policies that it purchased for the expected life expectancy of the insured.[37] Respondents argue that the representations were not false when made and that the PPM gave JTCM discretion to change the investment strategy of the Fund. Yet, Respondents never informed investors and potential investors of such changes. The marketing materials and newsletters even continued to stress that the insurance portfolio was a conservative hedge against the corporate portfolio and continued to stress the 5% limitation. These misrepresentations and omissions were clearly material; the lack of diversification of corporate investments increased the risk of loss and the lack of funds to pay insurance premiums guaranteed the loss of those assets. While the representations concerning insurance and corporate investments may have been true when originally made, they became misrepresentations thereafter. *See SEC v. Merchant Capital, LLC*, 483 F.3d 747,

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[37] Respondents appear to suggest that they are not responsible for representations in the PPMs because they were prepared by outside counsel. To the extent they raise a reliance on counsel defense, it is inapposite, as Respondents do not claim that they consulted counsel before undertaking the actions that were inconsistent with the representations. *See David Henry Disraeli*, Securities Act Release No. 8880, 2007 SEC LEXIS 3015, at *29 n.39 (Dec. 21, 2007). In considering whether to credit an advice of counsel claim, the Commission considers four elements: "that the person made complete disclosure to counsel, sought advice on the legality of the intended conduct, received advice that the intended conduct was legal, and relied in good faith on counsel's advice." *Howard Brett Berger*, Exchange Act Release No. 58950, 2008 SEC LEXIS 3141, at *38 (footnote citing precedent omitted), *pet. for review denied*, 347 F. App'x 692 (2d Cir. 2009), *cert denied*, 559 U.S. 1102 (2010).

769 (11th Cir. 2007) ("What may once have been a good faith projection became, with experience, a materially misleading omission of material fact.").

Falsely representing and omitting to disclose the true relationship between JTCM/Jarkesy and JTF/Belesis was also material. The fact of concealment of or minimizing the relationship in itself was material. In addition, Belesis's input into decisions concerning portfolio companies and receipt of fees from such companies affected the degree of profit or loss that the companies might attain, directly affecting the returns, or lack thereof, of investors. To the extent that Respondents argue that the fees JTF/Belesis received were the result of agreements between JTF/Belesis and the companies, not JTCM/Jarkesy, Jarkesy was a director of America West and of Radiant, as was his affiliate Rodriguez who was also an officer of the companies. Thus, Jarkesy was involved in those companies' decisions and cannot disclaim responsibility for the fees the companies paid to JTF/Belesis.

Further, Jarkesy's influence on valuing Fund assets (always in an upward direction) was also material. The fact that the PPM for Fund I provided that the value of investments would be determined solely by JTCM did not give Respondents unlimited discretion to set arbitrary and capricious values that were self-serving. Indeed, the Funds' financial statements represented that the assets had been fair valued. Finally, the continuing misrepresentation, never corrected, that KPMG, a "Big 4" firm was the Funds' auditor, when in reality it was a small Houston firm (however well-qualified), was also material.

The evidence shows at least a reckless degree of scienter. Jarkesy was JTCM's *alter ego* and sole decision-maker for the Funds. Thus, he had to have been aware that the Funds were heavily concentrated in a few companies, such as America West, Galaxy, and Radiant, yet he never amended Fund I's PPM and used marketing materials and newsletters that represented that the Fund was limited to 5% in any one corporate investment. Likewise, he knew the truth about the Fund's investments in life insurance policies at the time he made the Podcast in which he represented that about half of capital contributions were devoted to insurance policies and that 70% of that half was set aside to pay premiums. In reality, most of the policies eventually lapsed because of failure to pay premiums.

The fact that others, such as JTF and Belesis, may have contributed to the misrepresentations and the downfall of portfolio companies does not relieve Respondents from responsibility. *See James J. Pasztor*, Exchange Act Release No. 42008, 1999 SEC LEXIS 2193, at *16-19, 25-30 (Oct. 14, 1999) (supervisor held liable for registered representative's execution of violative directed trades; supervisor had tried to stop the trading but was overruled by broker-dealer's owner who was friendly with the customer); *Charles K. Seavey*, Advisers Act Release No. 2119, 2003 SEC LEXIS 716, at *13-14, 19-20 (Mar. 27, 2003) (associated person found liable where investment adviser required him to sign materially misleading letter), *aff'd*, 111 F. App'x. 911 (9th Cir. 2004). Respondents point to investor witnesses' having failed to read the PPM. However, investors need not have in fact relied on a false statement for an enforcement action for fraud to be made out. *See TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *Geman v. SEC*, 334 F.3d 1183, 1191 (10th Cir. 2003).

In sum, it is concluded that Respondents willfully violated the antifraud provisions of the Securities, Exchange, and Advisers Acts by their conduct described above. Additionally, by the same misconduct, the Funds violated Securities Act Section 17(a) and Exchange Act Section 10(b) and Rule 10b-5, and Respondents willfully aided and abetted and caused the Funds' violations.

IV. SANCTIONS

The Division requests a cease-and-desist order, disgorgement, a third-tier civil money penalty, an industry bar, and officer and director bars. As discussed below, Respondents will be ordered to cease and desist from violations of the antifraud provisions, to disgorge, jointly and severally, ill-gotten gains of $1,278,597 plus prejudgment interest, and to pay a third-tier penalty of $450,000; and industry and officer and director bars will be ordered against Jarkesy.[38]

A. Sanction Considerations

In determining sanctions, the Commission considers such factors as:

> the egregiousness of the defendant's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant's assurances against future violations, the defendant's recognition of the wrongful nature of his conduct, and the likelihood that the defendant's occupation will present opportunities for future violations.

Steadman, 603 F.2d at 1140 (quoting *SEC v. Blatt*, 583 F.2d 1325, 1334 n.29 (5th Cir. 1978)). The Commission also considers the age of the violation and the degree of harm to investors and the marketplace resulting from the violation. *Marshall E. Melton*, Exchange Act Release No. 48228, 2003 SEC LEXIS 1767, at *4-5 (July 25, 2003). Additionally, the Commission considers the extent to which the sanction will have a deterrent effect. *Schield Mgmt. Co.*, 2006 SEC LEXIS 195, at *35-36 & n.46. As the Commission has often emphasized, the public interest determination extends to the public-at-large, the welfare of investors as a class, and standards of conduct in the securities business generally. *See Christopher A. Lowry*, Investment Company Release No. 2052, 2002 SEC LEXIS 2346, at *20 (Aug. 30, 2002), *aff'd*, 340 F.3d 501 (8th Cir. 2003); *Arthur Lipper Corp.*, Exchange Act Release No. 11773, 1975 SEC LEXIS 527, at *52 (Oct. 24, 1975). The amount of a sanction depends on the facts of each case and the value of the sanction in preventing a recurrence. *See Berko v. SEC*, 316 F.2d 137, 141 (2d Cir. 1963); *Leo Glassman*, Exchange Act Release No. 11929, 1975 SEC LEXIS 111, at *7 (Dec. 16, 1975).

B. Sanctions

1. Cease and Desist

Securities Act Section 8A, Exchange Act Section 21C(a), and Advisers Act Section 203(k) authorize the Commission to issue a cease-and-desist order against a person who "is violating, has violated, or is about to violate" any provision of those Acts or rules thereunder. Whether there is a reasonable likelihood of such violations in the future must be considered. *KPMG Peat Marwick LLP*, 2001 SEC LEXIS 98, at *101. Such a showing is "significantly less than that required for an injunction." *Id.* at 114. In determining whether a cease-and-desist order is appropriate, the

[38] The Division also requests a censure. In view of the more severe sanctions imposed, a censure is unnecessary.

Commission considers the *Steadman* factors quoted above, as well as the recency of the violation, the degree of harm to investors or the marketplace, and the combination of sanctions against the respondent. *See WHX Corp. v. SEC*, 362 F.3d 854, 859-61 (D.C. Cir. 2004); *KPMG*, 2001 SEC LEXIS 98, at *116.

Respondents' conduct was egregious and recurrent; the various material misrepresentations and omissions continued during a period of more than two years. Up to 120 investors in the two Funds were affected. The conduct involved at least a reckless degree of scienter. The lack of assurances against future violations and recognition of the wrongful nature of the conduct goes beyond a vigorous defense of the charges. Respondents' attempt to displace all blame onto lawyers, the Funds' administrator, JTF/Belesis, and others is an aggravating factor. Jarkesy's chosen occupation in the financial industry will present opportunities for future violations. The violations were neither recent nor remote in time, but were ongoing within the past five years. The evidence of record does not quantify precisely the degree of harm to investors and the marketplace in dollars, but Fund investors, who were given inaccurate information, received very little in return out of a total investment of about $24 million. Harm to the marketplace is evident from the dishonest nature of Respondents' misconduct. In light of these considerations, a cease-and-desist order is appropriate.

Respondents' lack of a disciplinary history does not remove the need for sanctions. *Mitchell M. Maynard*, Advisers Act Release No. 2875, 2009 SEC LEXIS 1621, at *42 & n.39 (May 15, 2009) ("[T]he absence of disciplinary history is not mitigative as securities professionals should not be rewarded for complying with securities laws.").

2. Disgorgement

Sections 8A(e) of the Securities Act, 21B(e) and 21C(e) of the Exchange Act, 9(e) of the Investment Company Act, and 203(j) of the Advisers Act authorize disgorgement of ill-gotten gains from Respondents. Disgorgement is an equitable remedy that requires a violator to give up wrongfully obtained profits causally related to the proven wrongdoing. *See SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1230-32 (D.C. Cir. 1989); *see also Hateley v. SEC*, 8 F.3d 653, 655-56 (9th Cir. 1993). Disgorgement returns a violator to where it or he would have been absent the violative activity. *See First City Fin. Corp.*, 890 F.2d at 1231.

The amount of the disgorgement ordered need only be a reasonable approximation of profits causally connected to the violation. *See Laurie Jones Canady*, Exchange Act Release No. 41250, 1999 SEC LEXIS 669, at *38 n.35 (Apr. 5, 1999) (quoting *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1475 (2d Cir. 1996)), *pet. for review denied*, 230 F.3d 362 (D.C. Cir. 2000); *see also SEC v. First Pac. Bancorp*, 142 F.3d 1186, 1192 n.6 (9th Cir. 1998) (holding disgorgement amount only needs to be a reasonable approximation of ill-gotten gains); *accord First City Fin. Corp.*, 890 F.2d at 1231-32.

Management fees and incentive fees are appropriately disgorged where they constitute ill-gotten gains earned during the course of violative activities. *See SEC v. Kapur*, No. 11-cv-8094, 2012 WL 5964389, at *3-4 (S.D.N.Y. Nov. 29, 2012); *In re Parkcentral Global Litig.*, 884 F. Supp. 2d 464, 484-45 (N.D. Tex. 2012); *SEC v. Radical Bunny, LLC*, No. 09-cv-1560, 2011 WL 1458698, at *8 (D. Ariz. Apr. 12, 2011), *aff'd*, 532 Fed. App'x 775 (9th Cir. 2013); *Joseph John VanCook*, Exchange Act Release No. 61039A, 2009 SEC LEXIS 3872, at *72-73 (Nov. 20, 2009). Accordingly, Respondents will be ordered to jointly and severally disgorge $1,278,597, the fees they received from the Funds, plus prejudgment interest. Respondents will be held jointly and severally liable because JTCM was Jarkesy's *alter ego* in the violative activities. *See SEC v. Monterosso*, 756 F.3d 1326, 1337-38 (11th Cir. 2014); *Donald L. Koch*, Exchange Act Release No. 72179, 2014 SEC LEXIS 1684, at *100 n.246 (May 16, 2014), *pet. for review docketed*, No. 14-1134 (D.C. Cir. July 11, 2014); *Daniel R. Lehl*, Exchange Act Release No. 45955, 2002 SEC LEXIS 1796, at *50-53 & n.65 (May 17, 2002).[39]

3. Civil Money Penalty

Sections 8A of the Securities Act, 21B of the Exchange Act, 203(i) of the Advisers Act, and 9(d) of the Investment Company Act authorize the Commission to impose civil money penalties for willful violations of those Acts or rules thereunder. In considering whether a penalty is in the public interest, the Commission may consider six factors: (1) fraud; (2) harm to others; (3) unjust enrichment; (4) previous violations; (5) deterrence; and (6) such other matters as justice may require. *See* Sections 21B(c) of the Exchange Act, 203(i)(3) of the Advisers Act, and 9(d)(3) of the Investment Company Act; *New Allied Dev. Corp.*, Exchange Act Release No. 37990, 1996 SEC LEXIS 3262, at *30 n.33 (Nov. 26, 1996); *First Sec. Transfer Sys., Inc.*, Exchange Act Release No. 36183, 1995 SEC LEXIS 2261, at *9 (Sept. 1, 1995); *see also Jay Houston Meadows*, Exchange Act Release No. 37156, 1996 SEC LEXIS 1194, at *25-27 (May 1, 1996), *aff'd*, 119 F.3d 1219 (5th Cir. 1997); *Consol. Inv. Servs., Inc.*, Exchange Act Release No. 36687, 1996 SEC LEXIS 83, at *22-24 (Jan. 5, 1996).

As to Respondents, there are no mitigating factors, and several aggravating factors. They violated the antifraud provisions, so their violative actions "involved fraud [and] reckless disregard of a regulatory requirement" within the meaning of Sections 21B(b)(3)(A), (c)(1) of the Exchange Act, 203(i)(2)(C)(i), (3)(A) of the Advisers Act, and 9(d)(2)(C)(i), (3)(A) of the Investment Company Act. Harm to others is shown by the millions of dollars of losses incurred by the Funds' investors, who may have decided not to invest or to stay invested had they received accurate information. Deterrence also requires a substantial penalty because of the abuse of the fiduciary duty owed by investment advisers.

Penalties in addition to the other sanctions ordered are in the public interest in this case in consideration of fraud, harm to others, unjust enrichment, and the need for deterrence. *See* Sections 21B(c) of the Exchange Act, 203(i)(3) of the Advisers Act, and 9(d)(3) of the Investment Company Act; *see also* H.R. Rep. No. 101-616 (1990), *reprinted in* 1990 U.S.C.C.A.N. 1379, 1384-87. The Division requests that Respondents be ordered to pay third-tier penalties. A third-tier penalty, as the Division requests, is appropriate because Respondents' violative acts involved fraud and resulted in

[39] In addition to requesting disgorgement, the Division requests "an accounting of all JTCM operations and investments." Div. Post-Hearing Mem. at 25. The Division, however, nowhere provides any more detail about this request or any authority for imposition of an accounting. Accordingly, the undersigned declines to impose such a sanction.

substantial losses to other persons who may have decided not to invest or to stay invested in the Funds had they received accurate information. *See* Sections 8A(g)(2)(C) of the Securities Act, 21B(b)(3) of the Exchange Act, 203(i)(2)(C) of the Advisers Act, and 9(d)(2)(C) of the Investment Company Act. Under those provisions, for each violative act or omission after February 14, 2005, and before March 4, 2009, the maximum third-tier penalty is $130,000 for a natural person. 17 C.F.R. §§ 201.1003, .1004. For each violative act or omission on or after March 4, 2009, and before March 5, 2013, the maximum third-tier penalty is $150,000 for a natural person. 17 C.F.R. § 201.1004, .1005. The provisions, like most civil penalty statutes, leave the precise unit of violation undefined. *See* Colin S. Diver, *The Assessment and Mitigation of Civil Money Penalties by Federal Administrative Agencies*, 79 Colum. L. Rev. 1435, 1440-41 (1979).

The events at issue started before, and continued after, March 4, 2009. They will be considered as three courses of action – the violations arising from the material misrepresentations and omissions relating to (1) the life settlement component of the Funds' investments; (2) the corporate investment component of the Funds' investments; and (3) Respondents' relationship with JTF/Belesis – resulting in three units of violation. Since JTCM was essentially Jarkesy's *alter ego* in the violative activities, a third-tier penalty amount of $450,000 will be ordered against Respondents, jointly and severally. Combined with the other sanctions ordered, this penalty is in the public interest. Insofar as Respondents argue that the imposition of penalties would be an impermissible retroactive application of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act), the argument fails. Respondents' violative conduct continued after the July 22, 2010, effective date of the Dodd-Frank Act.

4. Industry Bar

The Division requests that Jarkesy be barred from the securities industry. Combined with other sanctions ordered, bars are in the public interest and appropriate deterrents.[40] The violations involved scienter. Jarkesy's business provides him with the opportunity to commit violations of the securities laws in the future. The record shows a lack of recognition of the wrongful nature of the violative conduct. His attempts to deflect blame onto others are aggravating factors. In short, it is necessary in the public interest and for the protection of investors that Jarkesy be barred from the industry.

5. Officer and Director Bar

Securities Act Section 8A(f) and Exchange Act Section 21C(f) authorize a bar against a respondent who has violated, respectively, Securities Act Section 17(a)(1) or Exchange Act Section 10(b), from acting as an officer or director of any issuer with a class of securities registered

[40] The fact Respondents were not registered with the Commission does not insulate Jarkesy from a bar. The Commission has authority to bar persons from association with investment advisers, whether registered or unregistered. *See Teicher v. SEC*, 177 F.3d 1016, 1017-18 (D.C. Cir. 1999). Likewise, the fact that the Funds were not registered investment companies is not a barrier to imposing an investment company bar. *See Zion Capital Mgmt. LLC*, Securities Act Release No. 8345, 2003 SEC LEXIS 2939, at *18 n.27 (Dec. 11, 2003).

pursuant to Exchange Act Section 12 or that is required to file reports pursuant to Exchange Act Section 15(d), "if the conduct of that person demonstrates unfitness to serve as an officer or director of any such issuer." In line with the reasoning in *Joseph P. Doxey*, Initial Decision Release No. 598, 2014 SEC LEXIS 1668, at *74-78 (A.L.J. May 15, 2014), the so-called *Patel* factors[41] will be applied in addition to the *Steadman* factors in evaluating the appropriateness of this sanction.

As discussed above, Jarkesy violated Securities Act Section 17(a)(1) and Exchange Act Section 10(b) while acting with scienter and awareness of the deceptive and manipulative nature of his conduct. The violations continued for several years. As managing member of JTCM and the founder and adviser of the Funds, Jarkesy was at the center of the fraud. His economic stake in the violation is shown by the nearly $1.3 million in fees that JTCM received from the Funds. Also, Jarkesy was a director of companies that were affected by the fraud. Without an officer and director bar, Jarkesy would be free to assume officer and director roles in the future.

Thus, it is appropriate and in the public interest to impose a permanent officer and director bar against Jarkesy. He will be barred from acting as an officer or director of any issuer with a class of securities registered pursuant to Exchange Act Section 12 or that is required to file reports pursuant to Exchange Act Section 15(d).

V. PROCEDURAL ORDER

IT IS ORDERED that Division Exhibit 231 (Fund I partnership book allocation for 2007-2010, JTBOF 1691-99) IS ADMITTED.[42]

VI. RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.351(b), it is certified that the record includes the items set forth in the record index issued by the Secretary of the Commission on September 23, 2014, and Division Exhibit 231.

VII. ORDER ON MOTION TO DISMISS

During the hearing the undersigned reserved ruling on Respondents' motion to dismiss. Based on the findings and conclusions set forth above:

IT IS ORDERED that Respondents' motion to dismiss IS DENIED.

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[41] The *Patel* factors are: (1) the egregiousness of the underlying securities law violation; (2) recidivism; (3) the defendant's role or position in the fraud; (4) degree of scienter; (5) the defendant's economic stake in the violation; and (6) the likelihood of recurrence. *SEC v. Bankosky*, 716 F.3d 45, 48 (2d Cir. 2013); *SEC v. Patel*, 61 F.3d 137, 141 (2d Cir. 1995).

[42] Division Exhibit 231 was offered, objected to by Respondents, and not admitted during the hearing. The Division has renewed its request that the exhibit be admitted, and both parties have cited to it in their post-hearing Proposed Findings of Fact and Conclusions of Law. *See* Division Finding of Fact No. 47 and Respondents' Counter-Statement.

VIII. ORDER

Based on the findings and conclusions set forth above:

IT IS ORDERED that, pursuant to Sections 8A of the Securities Act, 21C(a) of the Exchange Act, and 203(k) of the Advisers Act GEORGE R. JARKESY, JR., and JOHN THOMAS CAPITAL MANAGEMENT GROUP LLC, d/b/a PATRIOT28 LLC, CEASE AND DESIST from committing or causing any violations or future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder.

IT IS FURTHER ORDERED that, pursuant to Sections 8A(e) of the Securities Act, 21B(e) and 21C(e) of the Exchange Act, 203(j) of the Advisers Act, and 9(e) of the Investment Company Act, GEORGE R. JARKESY, JR., and JOHN THOMAS CAPITAL MANAGEMENT GROUP LLC, d/b/a PATRIOT28 LLC, jointly and severally, DISGORGE $1,278,597 plus prejudgment interest at the rate established under Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. § 6621(a)(2), compounded quarterly, pursuant to 17 C.F.R. § 201.600(b). Pursuant to 17 C.F.R. § 201.600(a), prejudgment interest is due from November 1, 2013, through the last day of the month preceding which payment is made.

IT IS FURTHER ORDERED that, pursuant to Sections 8A(g) of the Securities Act, 21B of the Exchange Act, 203(i) of the Advisers Act, and 9(d) of the Investment Company Act, GEORGE R. JARKESY, JR., and JOHN THOMAS CAPITAL MANAGEMENT GROUP LLC, d/b/a PATRIOT28 LLC, jointly and severally, PAY A CIVIL MONEY PENALTY of $450,000.

IT IS FURTHER ORDERED that, pursuant to Sections 15(b) of the Exchange Act, 203(f) of the Advisers Act, and 9(b) of the Investment Company Act, GEORGE R. JARKESY, JR., IS BARRED from associating with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stock[43] and is prohibited, permanently, from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter.

IT IS FURTHER ORDERED that, pursuant to Sections 8A(f) of the Securities Act and 21C(f) of the Exchange Act, GEORGE R. JARKESY, JR., IS BARRED from acting as an officer or director of any issuer that has a class of securities registered with the Commission pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act.

[43] Thus, he will be barred from acting as a promoter, finder, consultant, or agent; or otherwise engaging in activities with a broker, dealer, or issuer for purposes of the issuance or trading in any penny stock, or inducing or attempting to induce the purchase or sale of any penny stock, pursuant to Exchange Act Section 15(b)(6)(A), (C).

Payment of penalties and disgorgement plus prejudgment interest shall be made on the first day following the day this Initial Decision becomes final. Payment shall be made by certified check, United States postal money order, bank cashier's check, wire transfer, or bank money order, payable to the Securities and Exchange Commission. *See* 17 C.F.R. § 201.601(a), (c). The payment, and a cover letter identifying the Respondents and Administrative Proceeding No. 3-15255, shall be delivered to: Enterprises Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, AMZ-341, 6500 South MacArthur Blvd., Oklahoma City, Oklahoma 73169. A copy of the cover letter and instrument of payment shall be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice, 17 C.F.R. § 201.360. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111(h) of the Commission's Rules of Practice, 17 C.F.R. § 201.111(h). If a motion to correct a manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or a motion to correct a manifest error of fact or the Commission determines on its own initiative to review the Initial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

Carol Fox Foelak
Administrative Law Judge