

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

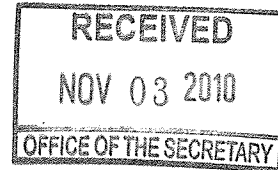
ADMINISTRATIVE PROCEEDING
FILE NO. 3-13871

In the Matter of

RONALD S. BLOOMFIELD
ROBERT GORGIA
VICTOR LABI
JOHN EARL MARTIN, SR., and
EUGENE MILLER

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CHIEF JUDGE
BRENDA P. MURRAY



POST-HEARING BRIEF OF DIVISION OF ENFORCEMENT

November 1, 2010

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The Division of Enforcement respectfully submits this Post-Hearing Brief.

PRELIMINARY STATEMENT

From the beginning of 2005 through mid-2007, Robert Bloomfield, John Martin and Victor Labi, registered representatives at Leeb Brokerage Services, Inc., allowed their customers to transfer in millions of shares of unregistered securities with no questions asked about how the customers obtained the shares. More than 4 billion shares were transferred into various Leeb accounts during this period, and they were issued by shadowy companies with scant operating record, minimal trading history, and unaudited financial statements. Bloomfield, Martin and Labi nevertheless did no inquiry into the source of these shares and allowed these penny stocks to be sold to an unsuspecting public. Robert Gorgia, Leeb's Chief Compliance Officer who exercised supervisory authority over Bloomfield, Martin and Labi, knew that no reasonable inquiry was being performed but did nothing to correct these egregious violations. Instead, Gorgia failed to act despite the steady stream of inquiries and concerns about Leeb's penny stock business from Leeb's clearing firms and law enforcement authorities.

The evidentiary record convincingly proves the egregious violations of the securities laws by the respondents:

First, Bloomfield, Labi and Martin willfully violated the registration provisions, Sections 5(a) and (c) of the Securities Act of 1933 ("Securities Act"). No dispute exists that the penny stocks at issue were unregistered and that these stocks were sold through Leeb accounts. Moreover, as registered representatives, Bloomfield, Labi and Martin are liable for violating Section 5 if they fail to conduct a reasonable inquiry. The evidence

demonstrates that they failed to conduct any inquiry, even though the circumstances called for the highest degree of scrutiny.

Leeb customers repeatedly received in large blocks of shares of various penny stocks, which the customers had obtained privately and not through any registered offering. The customers then sold the shares to the public, often during spam or other promotional activity, and wired the proceeds out of their Leeb accounts. As described more fully below, the Leeb customers engaging in this conduct included an individual with a prior pump-and-dump related consent judgment; persons known to be engaged in promotional activity in the very stocks they were selling; persons who controlled more than one brokerage account under different names and engaged in questionable trading behavior; and an offshore corporation controlled by persons who wired millions of dollars to a bank secrecy jurisdiction.

Second, Gorgia failed reasonably to supervise Bloomfield, Labi and Martin regarding these egregious Section 5 violations. Gorgia was at the head of Leeb's Supervisory Control System and was responsible for insuring that appropriate supervisory procedures were in place. Gorgia also had specific responsibility and authority to take remedial steps when deficiencies were identified in procedures or in compliance by individuals at the firm. The written supervisory procedures ("WSP") also made Gorgia responsible for reviews of customer account activity. In addition, the WSP provided for the Compliance Department to supervise OSJ branch manager Bloomfield. Gorgia represented to FINRA, in conjunction with obtaining approval for the OSJ, and acknowledged in testimony that he was responsible for supervising Bloomfield and the OSJ. Under the firm's procedures, supervision of the OSJ encompassed RR oversight,

reviews of business activity, and customer account reviews. Additionally, Gorgia was the designated AML Compliance Officer from March 2005 through June 2006, giving him direct responsibility for anti-money laundering (“AML”) compliance. The WSPs, the AML policy, and the firm’s division of responsibilities during Gorgia’s tenure also made Gorgia responsible for email review and wire transfer review, with a particular focus on transfers to third party accounts and to locations other than the customer’s primary address.

Third, Bloomfield, Gorgia, Labi, and Martin willfully aided and abetted and caused violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder by Leeb. Broker-dealers are required to have written AML programs in place that include policies and procedures that are reasonably designed to achieve and monitor compliance with the Bank Secrecy Act (“BSA”) and its implementing regulations. The BSA requires, among other things, that a suspicious activity report (“SAR”) be filed if a transaction or activity comes within the reporting requirement of 31 CFR 103.19. Section 17(a) of the Exchange Act and Rule 17a-8 thereunder require broker-dealers to abide by the BSA’s recordkeeping, retention and reporting requirements. The trading activities engaged in by Leeb’s penny stock customers raised numerous red flags that were listed in the firm’s AML program as activities that may require the filing of a SAR.

Leeb customer activity was indicative of market manipulation, prearranged trading, insider trading and other illicit conduct. Leeb failed to file a SAR on any of these activities, thereby preventing regulatory authorities and/or law enforcement from receiving useful information. Indeed, Leeb had a significant financial incentive to turn a blind eye to its customers’ conduct. During 2006 alone, Leeb’s customers’ penny stock

trading earned Leeb substantial commissions, representing almost half of the firm's commission income for the year.

Finally, the Respondents' conduct, which was knowing, flagrant and recurring, merits strong sanctions, including permanent industry bars, disgorgement, prejudgment interest and civil penalties.

STATEMENT OF FACTS

The Division relies on and incorporates herein its Proposed Findings of Fact ("FOF"), filed herewith, as its statement of facts that support the allegations against the Respondents.

Factual citations in this memorandum of law are to the FOF, the transcript of the hearing conducted on September 13, 14, 15, 16, 21 and 22, 2010 ("Tr."), or to the exhibits received into evidence during the hearing ("Div. Ex.", "Gorgia Ex.", "Labi Ex.", "Martin Ex.").

ARGUMENT

As shown below, the Division has met its burden of proving by a preponderance of the evidence that: (1) Bloomfield, Martin and Labi willfully violated Sections 5(a) and 5(c) of the Securities Act of 1933 ("Securities Act"); (2) Gorgia failed reasonably to supervise Bloomfield, Martin and Labi with a view to preventing and detecting their violations of Section 5; and (3) Bloomfield, Martin, Labi and Gorgia willfully aided and abetted and caused violations of Section 17(a) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 17a-8 thereunder.

I. BLOOMFIELD, MARTIN AND LABI VIOLATED SECTION 5 OF THE SECURITIES ACT

The Order Instituting Proceedings dated April 27, 2010 ("OIP") alleges that

Bloomfield, Martin and Labi willfully violated Sections 5(a) and 5(c) of the Securities Act. Bloomfield and Martin are alleged to have participated in offerings of eight specific issuers of penny stocks (OIP ¶¶ 1, 4, 19-28) and Labi is alleged to have participated in the offerings of two penny stock issuers (OIP ¶ 3, 32-34). See also Division of Enforcement's Memorandum of Law in Opposition to Motion of Respondents Ronald S. Bloomfield and John Earl Martin Sr. for a More Definite Statement dated June 2, 2010 (Attachment).

A. The Evidence Demonstrates a Prima Facie Case

Sections 5(a) and 5(c) of the Securities Act prohibit the offer and sale of securities in interstate commerce unless a registration statement is filed with the Commission or is in effect, or the securities transactions are exempt from registration or fall within a safe harbor. To establish a *prima facie* case for a violation of the registration provisions, the Division must prove that: (1) no registration statement was filed or was in effect as to the security; (2) the use of the mails or interstate transportation or communication as a means to sell or offer the security; and (3) Bloomfield, Martin and Labi offered to sell or sold an unregistered security. *See SEC v. Cavanagh*, 1 F. Supp2d. 337, 361 (S.D.N.Y. 1998), *aff'd*, 155 F.3d 129 (2d Cir. 1998).

Once the Division establishes a *prima facie* case, the burden of proof shifts to the Respondents to show that an exemption or safe-harbor from registration was available. *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953).

Scienter is not required to establish a Section 5 violation, *see SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 859-60 (S.D.N.Y. 1997), *aff'd mem.*, 159 F.3d 1348 (2d Cir. 1998), and liability extends to all necessary participants in the unregistered sale of stock.

Cavanagh, 1 F. Supp.2d at 372.

The evidence shows that the Division has proven a *prima facie* case.

First, Attestations from the SEC's Records Officer establish that no registration statements were in effect with respect to the following ten issuers whose securities were sold to the public from Leeb accounts:

- Equipment and Systems Engineering, Inc. ("EQSE"), Div. Ex. 314;
- Adrenaline Nation Entertainment, Inc. ("Adrenaline Nation"), Div. Ex. 312;
- China Gold Corp. ("China Gold"), Div. Ex. 313;
- Goldmark Industries Inc. ("Goldmark"), Div. Ex. 315;
- Golden Apple Oil and Gas Inc. (f/k/a CDI Developments, Inc.) ("Golden Apple", Div. Ex. 316;
- iPackets International, Inc. ("iPackets"), Div. Ex. 317;
- LOM Logistics, Inc. ("LOM Logistics"), Div. Ex. 319;
- Spooz, Inc. ("Spooz"), Div. Ex. 320;
- Viyya Technologies, Inc. ("Viyya"), Div. Ex. 321; and
- Lifeline Biotechnologies, Inc. ("Lifeline"), Div. Ex. 318.

Second, Bloomfield, Martin and Labi used interstate transportation or communication or the mails in connection with the offers or sales. FOF ¶ 67.

Third, Bloomfield, Martin and Labi offered to sell or sold an unregistered security. FOF ¶¶ 63-173.

The Section 5 prohibitions extend not just to issuers but to those who engage in significant steps in the distribution process, including registered representatives such as Bloomfield, Labi and Martin. "The Securities Act expressly provides that liability

extends to ‘any person, directly or indirectly’ who sells unregistered securities in violation of the Act. 15 U.S.C. § 77e(a). Thus, the provision includes brokers and dealers. *See id.* To determine whether or not a person is liable as a seller of securities, courts have assessed whether or not ‘the defendant’s actions [were] ‘a substantial factor’ in bringing about the plaintiff’s purchases.” Pharo v. Smith, 621 F.2d 656, 667 (5th Cir. 1980). Courts have also recognized that liability has extended to ‘parties who participate in the negotiations of or arrangements for the sale of unregistered securities . . . [and] parties responsible for bringing about sales of securities they themselves do not own.’ Lewis v. Walston & Co., 487 F.2d 617, 621 (5th Cir. 1973).” SEC v. Connectajet.com, 2010 U.S. Dist. LEXIS 61213, at *5 (N. D. Tex. June 17, 2010).

B. The Broker’s Exemption Does Not Apply

An exemption from the registration requirements is an affirmative defense that Bloomfield, Martin and Labi have the burden of establishing. Newbridge Securities Corp, Initial Decision, File No. 3-13099 (June 9, 2009); Engelstad, 626 F.2d at 425; Lively v. Hirschfeld, 440 F.2d 631, 632 (10th Cir. 1971). Exemptions from the registration requirements are “strictly construed against the claimants.” Newbridge, at 51. “Evidence in support of an exemption must be explicit, exact, and not built on mere conclusory statements.” Robert G. Weeks, 56 S.E.C. 1297, 1322 & n.35 (2003). No Respondent, however, pleaded any exemption as an affirmative defense in their Answers.

During the hearing, Bloomfield appeared to assert the “brokers’ exemption” when testifying that “once we made a good-faith effort to determine that the stock was in the public domain, . . . under Rule 144, . . . there is an exemption for any brokers who are basically liquidating stock on an unsolicited basis for a customer.” Tr. at 1204. The

overwhelming weight of the evidence, however, establishes that the broker's exemption cannot apply because Respondents completely failed in their obligations to conduct a reasonable inquiry. FOF ¶¶ 47-56.

The broker's exemption applies only when the broker conducts a reasonable inquiry as to the source of the stock. Matter of Carley, et al., 2008 SEC LEXIS 222 (Jan. 31, 2008) (“[brokers’] exemption -- which is designed to exempt ordinary brokerage transactions -- is not available to a registered representative if he knows or has reasonable grounds to believe that the selling customer's part of the transaction is not exempt from Section 5 of the Securities Act”). Brokers can avoid liability for participation in unregistered offerings only if they engage in “brokers’ transactions” under Section 4(4) of the Securities Act. This term “brokers’ transactions” is defined in Rule 144(g) requires that the broker (1) does no more than execute the order to sell the securities, (2) receives no more than the usual customary broker's commission, (3) does not solicit or arrange for the solicitation of customers' orders to buy the securities, and (4) complies with a “reasonable inquiry” requirement:

The term *brokers' transactions* in section 4(4) of the Act shall for the purposes of this rule be deemed to include transactions by a broker in which such broker . . . [a]fter reasonable inquiry is not aware of circumstances indicating that the person for whose account the securities are sold is an underwriter with respect to the securities or that the transaction is a part of a distribution of securities of the issuer.

17 C.F.R. § 230.144.

Accordingly, brokers who do no more than execute orders in return for customary commissions can be held liable for participation in unregistered offerings if they fail to conduct a reasonable inquiry. When the customers of Bloomfield, Martin and Labi brought in stock that was not obtained in a registered offering and attempted to sell that stock to the

public, the broker was obligated to conduct an “adequate inquiry under the circumstances.” Wonsover v. SEC, 205 F.3d 408, 409 (D.C. Cir. 2000), quoted in Geiger v. SEC, 363 F.3d 481, 487 (D.C. Cir. 2004). “An oft-quoted paragraph of a Commission release,” Wonsover, 205 F.3d at 415, sets forth when the broker’s inquiry can be considered reasonable:

The amount of inquiry called for necessarily varies with the circumstances of particular cases. A dealer who is offered a modest amount of a widely traded security by a responsible customer, whose lack of relationship to the issuer is well known to him, may ordinarily proceed with considerable confidence. On the other hand, when a dealer is offered a substantial block of a little-known security, either by persons who appear reluctant to disclose exactly where the securities came from, or where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for controlling persons or statutory underwriters, then searching inquiry is called for.

Distribution by Broker-Dealers of Unregistered Securities, Securities Act Rel. No. 33-4445 (Feb. 2, 1962).

The broker’s duty cannot be delegated to a third party. As a result, a broker cannot rely on a transfer agent to fulfill its reasonable inquiry obligation. Wonsover, 205 F.3d at 416 (rejecting registered representative’s reliance on clearing firm, the transfer agent and counsel); see also Stead v. SEC, 444 F.2d 713, 716 (10th Cir.1971) (“The act of . . . calling the transfer agent is obviously not a sufficient inquiry.”); A.G. Becker Paribas Inc., 48 S.E.C. 118, 121 (1985) (“If a broker relies on others to make the inquiry called for in any particular circumstances, it does so at its peril.”); Geiger, 363 F.3d at 485 (registered representative willfully violated Section 5 by “abandon[ing] even the pretense of due diligence”); Graham v. SEC, 222 F.3d 994, 1005-06 (D.C. Cir. 2000) (rejecting reliance on supervisor defense to negate a registered representative’s “independent duty to use diligence”).

Nor may brokers simply rely on a customer's statements without exploring the facts, particularly where, as here, they were aware that their customers routinely obtained stock directly from issuers. See Kane v. SEC, 842 F.2d 194, 200 (8th Cir. 1988). Absent a reasonable inquiry, a broker who participates in the unregistered sale of securities violates Section 5 of the Securities Act. See Matter of Barr, Initial Dec. Rel No. 170, 2000 SEC LEXIS 1548, at 13 (July 27, 2000) ("Mr. Barr violated Section 5 . . . because he made no inquiries – absolutely none – to determine whether the ITC shares Mrs. Erdman gave him to sell were registered.").

For several reasons, the unregistered stock received into the Leeb accounts called for a "searching inquiry". Carley, at 10. First, the issuers' stock was thinly traded. FOF ¶¶ 77, 120, 162. Second, there was multiple indications that the customers had connections with the issuers. E.g., FOF ¶¶ 33-34, 45-46, 103-106. In addition, Bloomfield, Martin and Labi repeatedly allowed customers, including persons known to them as consultants and promoters did have direct ties to issuers, to deliver in large blocks of penny stocks without undertaking any critical inquiry into the source of the shares to ensure that they were not restricted or control shares. FOF ¶¶ 21-178.

Although Bloomfield, Martin and Labi knew of the "reasonable inquiry" concept (FOF ¶¶ 48-49), they did nothing whatsoever to fulfill this duty. Instead, they testified that if a certificate for an unregistered stock did not have a restrictive legend, then the stock could be sold without further inquiry. FOF ¶ 49. There is no evidence that Bloomfield, Martin or Labi even once asked a customer for specific information regarding the nature of the transactions and the reason the stock could be sold to the public. FOF ¶¶ 49-55.

Bloomfield, Martin and Labi had a duty to conduct a reasonable inquiry even if no legend appeared on a particular certificate. “The determination by a transfer agent to remove a restrictive legend does not relieve a securities professional of the duty to investigate. Nor is it a defense, if true, that others in the industry rely on transfer agents to determine whether stock is restricted[.]. . . . [I]t is well-established that a securities professional cannot rely on the ‘self-serving statements of his sellers and their counsel without reasonably exploring the possibility of contrary facts.’” Matter of Kirby, 1934 Rel. No. 47149, 2003 SEC LEXIS 46, at notes 34 and 58 (Jan. 9, 2003).

Bloomfield went through the motions of filling out a few low-priced security questionnaires if requested to do so by Pershing, but he claimed not to know why he was asked to do so. FOF ¶ 52. Both Bloomfield and Martin admitted that they never asked any customer for documentation about the transactions in which the customers obtained the stock. FOF ¶¶ 49-55. Martin – who said in his pre-hearing testimony that he never investigated the source of shares because “[t]hat would not be my purview” – improbably testified during the hearing that he did conduct an “inquiry” but that no record existed of such inquiry. FOF ¶ 278.

The Respondents’ failure to conduct any reasonable inquiry is especially egregious in view of the widespread and obvious suspicious activity in the Leeb customer accounts and the affirmative steps which Bloomfield, Martin and Labi went to facilitate the unregistered offerings. The facts concerning the suspicious activity is essentially undisputed. Darrel and Jack Uselton controlled five accounts in the name of various corporations and partnerships (“Uselton Accounts”). FOF ¶ 21. The Useltons had prior regulatory history known to Bloomfield and Martin, as did Scott Sieck, a person

affiliated with the Uselton Accounts. FOF ¶¶ 30-31. The Uselton Accounts were moved from Western to Leeb, and the activity in the Uselton Accounts at Western was sufficiently suspicious that they were closed after only a few months. FOF ¶¶ 24-25. The pattern of activity, in which millions of shares were transferred in and then promptly sold, should have merited heightened scrutiny. Bloomfield and Martin and know that the Uselton were stock promoters and had ties to issuers. FOF ¶¶ 33-34.

The numerous red flags associated with the Thimble accounts were glaring, and included the wiring of millions of dollars in sales proceeds to an account in Liechtenstein, a known tax haven. FOF ¶ 41.

The Uselton Accounts, the Thimble account, and Labi's customers all brazenly sold millions of shares of unregistered stock through their Leeb accounts. These sales could not have occurred without the knowledge and participation of Bloomfield, Labi and Martin, who never asked a question, never asked for any back-up documents and never refused a request. In many instances, the registration violations were accompanied by suspicious market activity, or additional suspicious trading by the Leeb customer beyond the large sales of stock. The evidentiary record of these issuances is set for in the Divisions' Proposed Findings of Fact.

The record of the documents that Respondents did *not* receive or review at the time they were violating Section 5 – because they never asked the customers or the issuers for these documents – shows that no exemption exists for any of the ten issuers whose sales violated Section 5. A summary of some of the evidence follows.

EQSE (FOF ¶¶ 69-92): In October 2005, EQSE hired the Uselton entity OTC Services to provide consulting services. To compensate OTC Services, EQSE agreed to

arrange for another shareholder to transfer 700,000 shares of purportedly unrestricted stock to OTC Services. OTC Services deposited the stock at Leeb in early November, when there had only been six trading days in EQSE since January 26, 2005. Prior to delivering in the shares, a different Uselton account at Leeb (Warrior Capital) purchased and sold small amounts of EQSE stock at a price of 15 cents per share. On the day after OTC Services delivered its stock, Warrior Capital purchased additional small amounts of shares at a price of 19 cents. The market rose from there and OTC Services sold out its 700,000 shares over the next three months.

In October 2006, another Uselton entity, Valores Fund LP, received 3.75 million shares in a private transaction, giving it control of over 24.5% of the purportedly free-trading stock. It received the stock from two entities, consultants to EQSE, that had initially controlled virtually all of the EQSE stock that was not held by EQSE's president.

On October 25, 2006, Valores Fund deposited the shares into its account at Leeb. At that time, EQSE trading volumes were routinely under 10,000 shares. However, at the end of November, Valores Fund purchased and OTC Services sold 150,000 shares opposite each other at Leeb, helping to take trading volume from 1,000 shares on November 28 to 193,155 shares on November 29 and 415,000 shares on November 30. The next day, on December 1, 2006, a press release and spam email were circulated, and the Uselton accounts began selling their shares. By December 6, 2006, the trading price had risen to 17 cents per share on a daily volume of 3 million shares. In the week from December 1 through December 8, the Valores Fund and OTC Services accounts, together with an account that an Uselton associate named Scott Sieck controlled, sold over 4.5 million shares for a net profit of \$676,184.68.

Golden Apple (FOF 93-102): On February 9, 2006, Thimble deposited 1.2 million shares of Golden Apple stock into its Leeb account, based on a direct issuance from the issuer. Thus, the shares were restricted, and not freely tradable to the public. Moreover, Golden Apple papered the transaction with a convertible promissory note that had purportedly been issued in December 2004—nine months before Thimble had been incorporated.

Moreover, only four days after delivering in the initial block of shares, Thimble received in another 390,000 shares from a third party via DTC. The transferor was controlled by the person who had been Golden Apple's secretary until one month prior to transfer. (When the transferor obtained its shares from Golden Apple, that transfer was also accompanied by a sham promissory note.)

In addition, Bloomfield and Martin eventually sold a total of 1.17 million of Thimble's GAPJ shares to the public even though the issuer had only made outdated financial information available to the public; the issuer had not publicly disclosed the share issuance to Thimble; the stock was the subject of a spam campaign; and the Commission had temporarily suspended trading in the security.

Lifeline Biotechnologies, Inc. (FOF ¶¶ 165-173): In the fall of 2005, Labi customer Gerald Alexander became involved with a stock called Lifeline Biotechnologies, Inc., and messaged Labi concerning his anticipated receipt of stock certificates and commencement of an IR campaign: "cert should hit any minute in FL to sign IR for LBTN will kick off soon." Then, beginning in January 2006 and for every month of that year, Alexander delivered large blocks of Lifeline stock into the Regis Filia and CJB Consulting accounts at Leeb. Ultimately, Alexander delivered in more than 1

billion shares of Lifeline to his Leeb accounts, and sold over 850 million of those shares through Leeb.

As of January 2006, Lifeline's total outstanding share balance equaled 181.8 million shares. By the end of 2006, there were 6.7 billion shares outstanding. Through repeated offerings -- with never more than a month between offerings -- Alexander's companies obtained 2 billion shares of Lifeline representing 31.6 % of all newly-issued shares from during 2006, and 30.75% of the total outstanding share balance as of December 31, 2006. One year earlier, on December 15, 2005, Alexander had sent Labi an IM about Lifeline, saying "lots of news and IR frist[sic] quarter."

Other issuers. The evidence of other issuances also shows that these sales violated Section 5. Thimble obtained its shares of China Gold from a person affiliated with China Gold, a company with almost no operating history or revenues. FOF ¶¶ 103-111. Thimble's LOM shares were sold from its Leeb account were received from an insider and were accompanied by an opinion letter based on a number of false representations about the source of the stock. FOF ¶¶ 112-121. The Viyya (FOF ¶¶ 122-129) and Spooz (FOF ¶¶ 130-135) stock came with letters stating that the stock was purchases for investment and not for distribution. FOF ¶¶

Thimble received restricted shares of Goldmark (whose stock had been largely dormant) indirectly from the issuer with no basis for an exemption, and sold these shares during a spam campaign. FOF ¶¶ 136-134. The iPacks (FOF ¶¶ 145-149), Adrenaline Nation (FOF ¶¶ 150-155), and CDI (FOF ¶¶ 156-164) shares were acquired by customers from affiliates of the issuers. Bloomfield, Martin and Labi made no effort to determine the source of these transfers.

II. GORGIA FAILED REASONABLY TO SUPERVISE BLOOMFIELD, LABI AND MARTIN WITH A VIEW TO PREVENTING AND DETECTING THEIR SECTION 5 VIOLATIONS

Under Section 15(b)(4), supervisors must respond reasonably when confronted with red flags suggesting that an registered representative may be engaging in improper activities. See George J. Kolar, Exchange Act Rel. No. 46127, 2002 SEC LEXIS 1647 (Commission Opinion, June 26, 2002). Moreover, a failure to learn of improprieties when diligent application of supervisory procedures would have uncovered them also constitutes a failure to supervise. See John A. Carley, Exchange Act Rel. No. 57246, 2008 SEC 222 at *67 and n.76 (Commission Opinion, Jan. 31, 2008) (review of paperwork that was “cursory at best” constituted a failure to supervise); Stephen J. Horning, Exchange Act Rel. No. 56886, 2007 SEC LEXIS 2796 at *27 and n.17 (Commission Opinion, Dec. 3, 2007) (supervisor failed to uncover errors because of cursory review of reports), aff’d, 570 F.3d 337 (D.C. Cir. 2009).

As Leeb’s Chief Compliance Officer and head of its Supervisory Control System Gorgia was responsible for developing and maintaining appropriate supervisory procedures. FOF ¶¶ 18, 179. In addition to Gorgia’s supervisory responsibilities, compliance officers as a general matter, whether or not they are “in line” supervisors of registered representatives, are responsible for supervisory failures if, under the particular circumstances of the case, they have “a requisite degree of responsibility, ability or authority to affect the conduct of the employee whose behavior is at issue.” Marion Bass Securities Corp., Exchange Act Rel. No. 43754, 2000 SEC LEXIS 2806 at *5-6 (Dec. 20, 2000). As with any non-line supervisors, liability turns on whether the person had responsibility for a particular area of conduct and was in a position to control that

conduct. Marshall Dornfeld, Exchange Act Rel. No. 55209, 2007 SEC LEXIS 214 at *12 (Jan. 31, 2007); Robert J. Check, Exchange Act Rel. No. 26367, 49 S.E.C. 1004 at 1008 (Dec. 16, 1988).

The Section 5 registration violations by Bloomfield, Martin and Labi occurred because Gorgia ignored red flags that they were not conducting adequate reviews, failed to conduct necessary reviews when confronted with facts calling out for them, and failed to put in place procedures that would have detected and prevented the unlawful conduct. FOF ¶¶ 179-203. Although Gorgia had overlapping supervisory responsibilities with former president Miller, that does not absolve him of his own obligation to supervise. See James J. Pasztor, Exchange Act Rel. No. 42008, 54 S.E.C. 398 at n.28 (Commission Opinion, Oct. 14, 1999) (individual not relieved of supervisory duties because supervisory authority was shared with another).

Gorgia, moreover, was a supervisor under the Gutfreund test:

[D]etermining if a particular person is a “supervisor” depends on whether, under the facts and circumstances of a particular case, that person has a requisite degree of responsibility, ability or authority to affect the conduct of the employee whose behavior is at issue. Thus, persons occupying positions in the legal or compliance departments of broker-dealers have been found by the Commission to be “supervisors” for purposes of Sections 15(b)(4)(E) and 15(b)(6) under certain circumstances.

Gutfreund, 51 S.E.C. at 113.

Gorgia had many supervisory responsibilities regarding the penny stock business. He was responsible for the firm’s written supervisory procedures, was supposed to review monthly trading activity, he represented to the NASD that he and Miller would supervise the OSJ and that he would conduct quarterly audits. FOF ¶¶ 19, 179. Indeed, when Leeb sought FINRA’s approval to open the OSJ, the firm represented to FINRA that “Mr.

Bloomfield will be supervised by Mr. Robert Gorgia, who is the Chief Compliance Officer.” FOF ¶ 19.

Gorgia was also the primary contact with Pershing. These firms on a regular basis throughout Gorgia’s tenure at Leeb brought their “reasonable inquiry” concerns to Gorgia’s attention. FOF ¶¶ 184-201. Gorgia nevertheless did nothing. FOF ¶¶ 235-237.

Gorgia never wrote, proposed, adopted or implemented written procedures for handling low-priced transactions and conducting the reasonable inquiry. FOF ¶¶ 181. Gorgia also never put in place procedures to ensure that the low-priced questionnaires, which often contained answers that were inaccurate, incomplete or nonsensical, were truthful. Under Leeb’s WSP, Gorgia had significant supervisory responsibility for key areas implicated by the conduct at issue here. FOF ¶ 179. Specifically, as head of the firm’s Supervisory Control System, he was responsible not only for insuring that appropriate supervisory procedures were in place, but was given specific responsibility for taking remedial steps when deficiencies were identified in either the procedures or in compliance by individuals at the firm. FOF ¶ 179. Finally, the WSP also made him responsible for monthly reviews of customer account activity, a responsibility he shirked by failing to review any clearing firm reports other than commission and execution-related reports. Notwithstanding his responsibility, Gorgia repeatedly failed to discover through reasonable supervisory steps the firm’s role in trading large blocks of penny stocks without registration statements being in effect, the suspicious nature of transactions in customer accounts, and the failure of the RRs to conduct a reasonable inquiry into their customers’ unregistered stock sale.

Apart from Bloomfield, Martin and Labi, Gorgia was the person at Leeb who best knew that no reasonable inquiry was being performed. Again and again during 2005 and 2006, Pershing and Legent brought concerns to Gorgia's attention that should have prompted action. FOF ¶¶ . Gorgia, however, never lifted a finger to make sure that the reasonable inquiry was done.

Gorgia's failure to exercise any degree of supervision over the penny stock business was egregious. Leeb was a relatively small firm, yet Gorgia never addressed the glaring violations of the securities laws that were taking place. The contrast with another compliance officer from Western, a much larger broker-dealer where Bloomfield and Martin worked before Leeb, is particularly instructive. Watanabe focused on the red flags as soon as Martin and Bloomfield joined Western and, following a thorough investigation, closed the Uselton accounts at Western, which led directly to martin's departure. FOF ¶¶ 24-26. Gorgia, however, failed to take even the most basic steps to rein in the penny stock business in eighteen months.

III. BLOOMFIELD, GORGIA, LABI AND MARTIN WILLFULLY AIDED AND ABETTED AND CAUSED VIOLATIONS OF SECTION 17(a) OF THE EXCHANGE ACT AND RULE 17(a) THEREUNDER

Section 17(a) of the Exchange Act requires broker-dealers like Leeb to make and keep certain records. In particular, Rule 17a-8 thereunder requires every registered broker-dealer to comply with the requirements of 31 CFR 103. Section 103, in a subpart entitled "Reports by brokers or dealers in securities of suspicious transactions," requires that broker-dealers file suspicious activity reports ("SARs") with U.S. Treasury Department's Financial Crimes Enforcement Network ("FinCEN"). A broker-dealer must report a transaction as suspicious if it learns of a transaction, or pattern of

transactions, involving or aggregating to at least \$5,000 that the broker-dealer knows, suspects or has reason to suspect: (1) involves funds derived from illegal activity or were conducted to disguise funds derived from illegal activities; (2) were designed to evade any requirements of the BSA; (3) had no business or apparent lawful purpose; or (4) involved use of the broker-dealer to facilitate criminal activity. 31 C.F.R. § 103.19 (“SAR Rule”).

Rule 17a-8 requires broker-dealers to comply with the recordkeeping, retention, and reporting obligations of the regulations under the BSA. The failure to file a SAR, as required by the SAR Rule, is a violation of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder, and is enforceable by the Commission. See, e.g., Park Financial Group, Inc., Exchange Act Rel. No. 56902, 2007 SEC LEXIS 2824 (Settled Order, Dec. 5, 2007); Ferris Baker Watts, Inc., Exchange Act Rel. No. 59372, 2009 SEC LEXIS 305 (Settled Order, Feb. 10, 2009).

Aiding and abetting violations of the securities laws involve three elements: (1) a primary or independent securities law violation committed by another party; (2) substantial assistance by the aider and abettor in the conduct constituting the primary violation; and (3) provision of that assistance with the requisite scienter. In the Matter of vFinance Investments, Inc., 2010 SEC LEXIS 2216 at *41 (July 2, 2010). As the Commission has recently affirmed, the scienter element is satisfied if the aider and abetter “knew of, or recklessly disregarded, the wrongdoing and [his] role in further it.” Id.

“Causing” liability also requires the establishment of three elements: (1) a primary violation; (2) an act or omission by the respondent that was the cause of the

violation; and (3) the respondent knew, or should have known, that his or her conduct would contribute to the violation. Robert M. Fuller, Exchange Act Rel. No. 48406, 2003 SEC LEXIS 2041 at *13-14 (Commission Opinion, Aug. 25, 2003), petition denied, 95 Fed. Appx. 361 (D.C. Cir. 2004). Negligence is sufficient to establish causing liability at least in cases where the primary violation does not require scienter. Joseph John Vancook, Exchange Act Rel. No. 61039A, 2009 SEC LEXIS 4040 at *57 n.65 (Commission Opinion, Nov. 20, 2009). Aiders and abettors of a violation also cause the violation. Warwick Capital Mgmt., Inc., Inv. Adv. Act Rel. No. 2694, 2008 SEC LEXIS 96 at n.21 (Commission Opinion, Jan. 16, 2008).

It is undisputed that Leeb failed to file any SARs during the Relevant Period, FOF ¶ 204, and that the SAR Rule's dollar threshold reporting requirement was exceeded. The evidence also shows repeated transaction that should have given the Respondents "reason to suspect that the transaction . . . [h]as no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage." 31 CFR 103.19(a)(2)(iii).

In particular, Bloomfield and Martin's customers, the Useltons and Thimble, each engaged in a series of penny stock transactions that should have been suspected as potential registration violations, that suspiciously coincided with price or volume spikes, or penny stock promotional campaigns, or that were indicative of market manipulation. Furthermore, the circumstances surrounding their business and/or the organization of their accounts, such as the Thimble account's jurisdiction of incorporation and international wire transfer activity, raised additional red flags. FOF ¶¶ 21-41.

Likewise, Labi's customers, including Gerald Alexander, engaged in a similar pattern of penny stock activity, delivering in and selling out large volumes of penny stock shares that should have been suspected as registration violations; engaging in conspicuous stock promotional activities; trading based on advance information about promotional activity; and organizing two corporate accounts in a manner that raised red flags requiring the filing of a SAR. FOF ¶¶ 42-46.

Leeb did not file a single SAR with FinCEN, as required by the SAR Rule, concerning any of the transactions and activities in these accounts. Div. Ex. 389. Accordingly, Leeb's failure to file a SAR is a violation of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder.¹

Gorgia, Bloomfield, Martin and Labi aided and abetted and caused Leeb's violations of Section 17(a) and Rule 17a-8. Gorgia, Bloomfield, Martin and Labi all were aware of their ongoing obligation to monitor and report suspicious activity and knew, or were reckless in not knowing, of the suspicious transactions and activities that were occurring. Bloomfield, Martin, and Labi, as the responsible RR's who managed the day-to-day activity in their respective customer accounts, were well aware of all of the details of their customers' accounts that triggered Leeb's obligation to file a SAR, including their customers' use of multiple LLCs, the location, organization and substance of their customers' business, the wire transfer activity, and suspicious trading. Yet they took no steps to initiate the filing of a SAR by Leeb.

¹ On January 4, 2010, the Commission obtained a default judgment against Gerald Alexander in an action including Section 5 claims based in part on activity conducted through Leeb. See Lit. Release No. 21363 (SEC v. Alexander, No. 1:09-cv-0805-HTW (N.D. Ga.)). On March 18, 2009, the Commission obtained a consent judgment against Darrel and Jack Uselton for spam-related activity including, in part, stocks traded through Leeb. See Lit. Release No. 20961 (SEC v. Usleton et al., No. 07-2211 (S.D. Tex.)).

Gorgia, as Compliance Officer and AML supervisor, was confronted repeatedly with problematic customer activity, yet failed to act on it. FOF ¶¶ 234-249. By failing to do so, he aided and abetted and caused Leeb's violations.

IV. THE COURT SHOULD IMPOSE MEANINGFUL SANCTIONS AND OTHER REMEDIES AGAINST RESPONDENTS

A. Bloomfield, Martin, Labi and Gorgia Should Be Barred From Association With Any Broker or Dealer

Section 15(b) of the Exchange Act, 15 U.S.C. § 78o(b), authorizes the Commission, if it finds that it is in the public interest, to bar any person from being associated with any broker or dealer. Such actions can be taken against any person who, among other things, has willfully violated or willfully aided and abetted any other person's violation of any provision of the Securities Act, the Exchange Act, or any of the rules and regulations promulgated under those statutes.

The public interest analysis requires consideration of the following factors: (1) the egregiousness of the respondent's actions; (2) the isolated or recurrent nature of the infractions; (3) the degree of scienter involved; (4) the sincerity of the respondent's assurances against future violations; (5) the respondent's recognition of the wrongful nature of their conduct; and (6) the likelihood that their occupation will present opportunities for future violations. See, e.g., Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979); In the Matter of Weeks, Admin. Proc. File No. 3-9952, 2002 WL 169185 (Initial Decision Feb. 4, 2002). The severity of the sanction depends on the facts of each case and the value of the sanction in preventing a recurrence of the violative conduct. See Berko v. SEC, 316 F.2d 137, 141 (2d Cir. 1963).

The Steadman factors warrant the imposition of a permanent bar from association with a broker or dealer. The Respondents' conduct was particularly egregious and was not an isolated infraction but instead occurred repeatedly and regularly through the Relevant Period. The Respondents also knew what they were doing and acted deliberately and recklessly. There have been no assurances against future violations; indeed, Respondents insisted throughout the hearing that they did nothing wrong or improper. Finally, it is highly likely that the Respondents will violate the law again if not barred. Bloomfield and Martin have continued in the penny stock business throughout the past eight years, and Gorgia continues to be employed as a supervisor at a broker-dealer. Thus, permanent bars against Bloomfield, Martin, Labi and Gorgia are in the public interest and warranted in this case in light of their egregious conduct as described above.

Alternatively, should Gorgia not be barred from association with a broker or dealer, Gorgia should be barred pursuant to Section 15(b) from association with any broker or dealer in a supervisory capacity.

B. Penny Stock Bars Are Appropriate

The securities at issue come within the definition of "penny stock" because the issuers fail to qualify for any of the exceptions defined by Section 3(a)(51) of the Exchange Act and Rule 3a51-1 thereunder. The securities were sold for less than \$5 per share and were never traded on an exchange or quoted on the NASDAQ. FOF ¶ 68. In addition, the issuers do not meet the exceptions based upon financial thresholds contained in Rule 3a51-1(g). Because of their roles in the Leeb customers' penny stock sales to the public, permanent penny stock bars against Bloomfield, Martin, Labi and Gorgia are also appropriate. See Matter of Weeks, 2003 SEC LEXIS 2572; 56 S.E.C. 1297 (Oct. 23,

2003) (barring respondent from participating in any offering of penny stock, “including acting as a promoter, finder, consultant, or other person who engages 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”); Matter of Beatty, SEC Rel. No. 271, 2005 SEC LEXIS 95 (Jan. 14, 2005) (barring respondent from participating in any offering of penny stock).

**C. Cease and Desist Orders Are Warranted
Against Bloomfield, Martin, Labi and Gorgia**

Section 21C of the Exchange Act, 15 U.S.C. § 78u-3, authorizes the Commission to order a person who has been found to have violated any provision of the Exchange Act, or the rules and regulations thereunder, or caused any such violation by an act or omission the person knew or should have known would contribute to such violation, to cease and desist from committing or causing such violations, or future violations. Similarly, Section 8A of the Securities Act, 15 U.S.C. § 77h-1, and Section 9(f) of the Investment Company Act, 15 U.S.C. § 80-9(f), authorize the Commission to enter cease-and-desist orders prohibiting violations of the Securities Act and the Investment Company Act, respectively.

As described above, Bloomfield, Martin and Labi and Gorgia each willfully violated Section 5(a) and 5(c) of the Securities Act; Gorgia failed reasonably to supervise Bloomfield, Labi and Martin within the meaning of Sections 15(b)(4) and 15(b)(6) of the Exchange Act; and Bloomfield, Martin, Labi and Gorgia willfully aided and abetted and caused violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. Their actions demonstrate a conscious disregard of the federal securities laws. Accordingly,

cease-and-desist orders against Bloomfield, Martin, Labi and Gorgia are appropriate to prevent violations and future violations of the statutes and rules set forth above.

D. Bloomfield, Labi and Martin Should Be Required to Disgorge Their Ill-Gotten Gains

Bloomfield, Labi and Martin should each be ordered to pay disgorgement plus prejudgment interest. “The primary purpose of disgorgement as a remedy for violation of the securities laws is to deprive violators of their ill-gotten gains, thereby effectuating the deterrence objectives of those laws.” SEC v. First Jersey Sec., Inc., 101 F.3d 1450, 1474 (2d Cir. 1996) (citations omitted). Moreover, “effective enforcement of the federal securities laws requires that the SEC be able to make violations unprofitable.” Id. (quoting SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1104 (2d Cir. 1972)). “To the extent that compensation flows from ill-gotten gains, the offending parties should be required to disgorge such to prevent unjust enrichment.” SEC v. Rogers, 221 F.3d 1349 (Table), 2000 WL 642467, at *2 (9th Cir. May 18, 2000) (citation omitted).

When calculating disgorgement, however, “separating legal from illegal profits exactly may at times be a near-impossible task.” SEC v. First City Fin. Corp., 890 F.2d 1215, 1231 (D.C. Cir. 1989). Disgorgement, therefore, “need only be a reasonable approximation of profits causally connected to the violation.” Id. See also First Jersey Sec., Inc., 101 F.3d at 1475; SEC v. Drexel Burnham Lambert, 837 F. Supp. 587, 612 (S.D.N.Y. 1993), aff’d 16 F.3d 520 (2d Cir. 1994), cert denied 513 U.S. 1077 (1995). “[A]ny risk of uncertainty [in calculating disgorgement] should fall on the wrongdoer whose illegal conduct created that uncertainty.” First Jersey Sec., 101 F.3d at 1475 (quotation omitted). Once the Division establishes a reasonable approximation of unjust

enrichment, the burden then shifts to respondent. See SEC v. Lorin, 76 F.3d 458, 462 (2d Cir. 1996).

The Division seeks disgorgement of all commissions from sales from certain penny stock accounts between October 1, 2005 and June 1, 2007 (for Bloomfield and Martin) and from April 1, 2005 through April 12, 2007. The calculations were derived from the Respondents' own testimony and documents. See Div. Exs. 361 and 362. This constitutes a "reasonable approximation" of the profits and the Respondents did not offer any evidence or testimony showing that the Division's calculation was erroneous. (Bloomfield and Martin offered argued that any disgorgement should be determined differently based on particular trades but did not argue that the Division's calculation was erroneous.)

Given the egregious nature of the conduct, it would be unjust for the Court to allow Bloomfield, Labi and Martin to retain their penny stock commissions earned during the period. See In the Matter of Trautman Wasserman & Company, Inc., Admin. Proc. File No. 3-12559, 2008 WL 149120, at *24-25 (Initial Decision Jan. 14, 2008) (Murray, ALJ) (ordering disgorgement of respondent Trautman's compensation during the relevant period); In the Matter of Kenneth R. Ward, Admin. Proc. File No. 3-9237, 2003 WL 1447865, *14 (March 19, 2003) (disgorgement of commissions earned during relevant period).

E. Respondents Should Pay Prejudgment Interest on Disgorgement

Bloomfield, Labi and Martin should be ordered to pay prejudgment interest on any disgorgement ordered through the date of entry of an order directing disgorgement. Prejudgment interest deprives a defendant of an interest-free loan in the amount of his ill-

gotten gains, thereby preventing unjust enrichment. SEC v. Grossman, No. 87 Civ. 1031, 1997 WL 231167, at *11 (S.D.N.Y. May 6, 1997), aff'd in part and vacated in part on other grounds, 173 F.3d 846 (2d Cir. 1999). In calculating prejudgment interest on disgorgement ordered for securities law violations, the Commission uses the Internal Revenue Service's "underpayment rate," which is a floating interest rate that the IRS uses to determine interest due on underpaid taxes, in administrative proceedings. *See* 17 C.F.R. § 201.600(b). The IRS rates are not punitive, but rather are set at a level to prevent unjust enrichment. *See* 26 U.S.C. § 6621(a)(2); SEC Rules & Regulations, 60 Fed. Reg. 32738, 32788 (June 23, 1995).

F. Bloomfield, Labi, Martin and Gorgia Should Be Required to Pay Substantial Penalties

Under Section 21B of the Exchange Act, 15 U.S.C. § 78u-2, the Commission may impose civil monetary penalties in proceedings instituted under Section 15(b) of the Exchange Act, against any person who is found to have willfully violated, or aided and abetted, any provision of the Exchange Act if such penalties are in the public interest. Six factors are relevant to determining whether civil monetary penalties are in the public interest: (1) deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; (2) harm to others; (3) unjust enrichment; (4) prior violations; (5) deterrence; and (6) such other matters as justice may require. *See* Section 21B(c) of the Exchange Act. "Not all factors may be relevant in a given case, and the factors need not all carry equal weight." In the Matter of Robert G. Weeks, Admin. Proc. File No. 3-9952.

Section 21B(b) of the Exchange Act specifies a three-tier system identifying the maximum amount of civil penalties, depending on the severity of the respondent's

conduct. Second tier penalties are awarded in cases involving fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement. Third-tier penalties are awarded in cases where such state of mind is present, and, in addition, where the conduct in question directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons, or resulted in substantial pecuniary gain to the person who committed the act or omission.

The Division respectfully submits that third-tier penalties are appropriate against Bloomfield, Martin, Labi and Gorgia. The Respondent's conduct was egregious and they knew what they were doing. Their Section 5 violations place millions of shares of unregistered stock of shadowy issuers in the hands of the public, thereby creating a risk of substantial loss. In addition, the conduct resulted in pecuniary gain to the Respondents, especially Bloomfield, Labi and Martin, whose income was based on commissions.

G. Inability to Pay

Bloomfield and Martin, despite having been repeatedly advised prior to and during the hearing that any claim of inability to pay must be supported by sworn financial statements, failed to submit any evidence regarding their financial condition. As a result, they have waived any claim of inability to pay. Matter of Carley, Initial Dec. Rel No. 292, 2005 SEC LEXIS 1745 (July 18, 2005) (four Respondents who failed to submit financial statements waived inability-to-pay claim).

Gorgia and Labi did make submissions in support of their inability to pay argument. Labi Ex. 1; Gorgia Ex. 400. Gorgia's documents, however, raise questions about his credibility and candor. For example, Gorgia claims that he pays 100% of the food expenses for the five adults living in his home, although three of them are adults

with jobs and income. The Division's cross-examination also revealed numerous questions and discrepancies regarding Gorgia's claimed expenses, liabilities and deductions. FOF ¶ 279.

Labi submitted evidence of his debts and sparse financial condition. Labi Ex. 1. However, as Judge Lynch observed in *SEC v. Inorganic Recycling Corp.*, "to withhold a civil penalty simply because a defendant cannot pay 'would not serve the purposes of the securities laws.'" *SEC v. Kane*, 2003 WL 1741293, *4 (S.D.N.Y. Apr. 1, 2003) (citations omitted). And the possibility does exist that one day Labi's "fortunes will improve, and that one day the SEC will be able to collect on even a severe judgment." *Id.* See also *Roor*, Fed. Sec. L. Rep. P, 92,904, *10 (ordering \$100,000 penalty despite defendant's claim that he was "financially destitute . . . [with] no assets to speak of"). In addition, Labi is not deserving of the Court's discretion because he evaded service of the OIP and because he improperly sought to stay this proceeding through a bankruptcy filing on the business day before the hearing commenced.

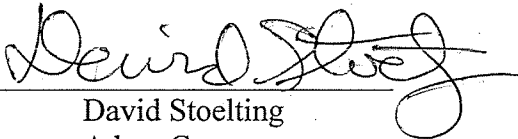
CONCLUSION

Based on the foregoing, the Division respectfully requests that this Court enter the Division's proposed findings of fact and conclusions of law and impose the requested sanctions on the Respondents.

Dated: New York, New York
November 1, 2010

Respectfully submitted,

DIVISION OF ENFORCEMENT

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