UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-13927

In the Matter of **GORDON BRENT PIERCE, NEWPORT CAPITAL CORP., and JENIROB COMPANY LTD.,** **Respondents.**	**Administrative Law Judge** **Carol Fox Foelak**

DIVISION OF ENFORCEMENT'S REPLY ON ITS MOTION FOR SUMMARY DISPOSITION AGAINST RESPONDENT PIERCE

MARC J. FAGEL
MICHAEL S. DICKE
JOHN S. YUN
JUDITH L. ANDERSON
STEVEN D. BUCHHOLZ
44 Montgomery Street, Suite 2600
San Francisco, CA 94104
Tel: (415) 705-2500
Fax: (415) 705-2501
Attorneys for
DIVISION OF ENFORCEMENT

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES

RULES

OTHER AUTHORITIES

I. INTRODUCTION

Despite conceding that he violated Section 5 of the Securities Act of 1933 ("Securities Act") for his unregistered sales of shares of Lexington Resources, Inc. ("Lexington") through Newport Capital Corp. ("Newport") and Jenirob Company Ltd. ("Jenirob") for net proceeds of $7,247,635.75 and that he deliberately concealed evidence of these sales during the investigation conducted by the Division of Enforcement ("Division"), Respondent Gordon Brent Pierce ("Pierce") argues that no repercussions should follow. Pierce stakes his defense on the erroneous theory that the Division's present claims were adjudicated on the merits in the prior proceeding and are now barred by the doctrine of res judicata. Pierce fails to acknowledge, however, that in the Initial Decision in the prior proceeding, the Hearing Officer ruled that his unregistered sales through Newport and Jenirob were beyond the scope of the first Order Instituting Proceedings (OIP). Thus, as the Initial Decision makes clear, the only Section 5 claim within the scope of the first OIP, and the only Section 5 claim adjudicated in the first proceeding, concerned Pierce's sales of Lexington stock from his *personal* account. Based upon these sales, disgorgement was awarded only for his $2,077,969 in profits. Pierce did not appeal this ruling and cannot argue otherwise now. Pierce's res judicata defense collapses in the face of this simple truth.

Allowing Pierce to escape liability for his securities law violations would not serve the purpose of the res judicata doctrine but rather would frustrate the interest of justice. The evidence unequivocally shows that the two claims in the two successive OIPs are not identical. The Division's present Section 5 claim against Pierce for his unregistered sales of 1.6 million shares of Lexington stock through Newport and Jenirob is distinct from its Section 5 claim against Pierce in the first proceeding for his unregistered sales of 300,000 shares of Lexington stock from his personal account. Pierce's argument to the contrary confuses evidence that he was not entitled to an exemption from registration because he acted as an issuer and underwriter

with evidence supporting the Division's *prima facie* case establishing the Section 5 violation for his sales from his personal account. Additional evidence of Pierce's role in transferring Lexington stock was offered by the Division and considered by the Hearing Officer in connection with Pierce's affirmative defense, as well as Pierce's failure to file required reports in violation of Sections 13(d) and 16(a) of the Securities Exchange Act of 1934 ("Exchange Act").

In addition, the parties never had a full and fair opportunity to litigate the Division's present Section 5 claim on the merits in the prior proceeding because the Hearing Officer ruled that it was beyond the scope of the first OIP. As a result of this procedural ruling that the Hearing Officer lacked authority to adjudicate the claim, there was no final judgment on the merits. Far from preventing repetitious litigation, application of res judicata would prevent the Division's claim from ever being heard – a result at odds with the public's interest in vigorous enforcement of the federal securities laws.

Moreover, the Division could not include this claim in the first OIP because Pierce had concealed the requisite evidence and misled the Division during his investigative testimony. Pierce's concealment should not be rewarded by permanently barring adjudication of this claim through a res judicata defense. Despite this concealment and despite the clear procedural ruling in the Initial Decision, Pierce contends that the Division was obligated to pursue this claim, if at all, in the first proceeding (even though it did not even receive the requisite evidence until after the hearing). This is a stark reversal from Pierce's argument during the first proceeding that allowing the claim to be adjudicated in that proceeding would violate his due process rights to notice of the claim and would require discovery and a new hearing. Hence, Pierce's present assertion that the Division should have sought leave to amend the first OIP or appealed the Initial

Decision to the Commission is not only incorrect, but such a course would not serve the res judicata goal of promoting judicial economy.

Accordingly, Pierce's res judicata defense must fail and the Division's motion for summary disposition should be granted in its entirety.

II. LEGAL ARGUMENT

A. Summary Disposition Should Be Granted Because Pierce Does Not Contest the Division's Claims

In his Answer and by failing to oppose the Division's opening brief on its affirmative case, Pierce concedes that he made unregistered sales of Lexington stock through the Newport and Jenirob accounts at a Liechtenstein bank for net proceeds of $7,247,635.75 without an applicable exception from registration. There is thus no genuine issue with regard to any material fact as to Pierce's liability for violation of Section 5 of the Securities Act, as alleged in the present OIP. Further, Pierce's affirmative defenses to this claim must fail, as discussed below. Accordingly, under SEC Rule of Practice 250(b), the Hearing Officer should grant the Division's motion for summary disposition.

B. Summary Disposition Should Be Granted Because Pierce's Res Judicata Defense Is Inapplicable

1. The Purpose Of The Res Judicata Doctrine Is To Promote Judicial Efficiency And Protect The Interests Of Justice

As the Supreme Court has held, res judicata "encourages reliance on judicial decisions, bars vexatious litigation, and frees the courts to resolve other disputes." *Brown v. Felsen*, 442 U.S. 127, 131 (1979) (denying application of res judicata). The Court cautioned that because res judicata can "shield the fraud and the cheat as well as the honest person . . . [i]t therefore is to be invoked only after careful inquiry." *Id.* at 132. Courts have emphasized the value of res judicata in promoting judicial economy. *See, e.g., Montana v. United States*, 440 U.S. 147, 154-55

(1979) ("To preclude parties from contesting matters that they have had a full and fair opportunity to litigate protects their adversaries from the expense and vexation attending multiple lawsuits, conserves judicial resources and fosters reliance on judicial action by minimizing the possibility of inconsistent decisions"); *Tahoe Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 322 F.3d 1064, 1077 (9th Cir. 2003) (same, noting public interest in preserving judicial economy) (citations omitted). Yet, "[w]hile the doctrine of res judicata is meant to foster judicial efficiency and protect defendants from the oppression of repeated litigation, it should not be applied inflexibly to deny justice." *Smith v. Pittsburgh Gage and Supply Co.*, 464 F.2d 870 (3d Cir. 1972). Permitting Pierce to invoke a res judicata defense under the circumstances here would not serve the doctrine's policy goals or protect the interests of justice.

Pierce must establish three elements for res judicata to apply. The earlier suit must have "(1) involved the same claim or cause of action as the later suit, (2) reached a final judgment on the merits, and (3) involved identical parties or privies." *Mpoyo v. Litton Electro-Optical Sys.*, 430 F.3d 985, 987 (9th Cir. 2005). As discussed below, none of the elements of res judicata are satisfied here.[1]

---

[1] Pierce's attempt to distinguish the cases the Division cited in its opening brief on the res judicata standard is unavailing. Pierce reads *Greenberg v. Board of Governors*, 968 F.2d 164, 168 (2d Cir. 1992), far too narrowly. In fact, *Greenberg* sets forth exactly the legal principle for which the Division cited it, namely that preclusion is limited "to the transaction at issue in the first action. Litigation over other transactions, though involving the same parties and similar facts and legal issues, is not precluded." That is what the court found when it upheld the administrative law judge's ruling rejecting claim preclusion on the ground that that none of the violations alleged in the second case were at issue in the prior cases. *Id.* Pierce's attempt to distinguish *Greenberg* factually also fails, in that the Division does not seek a second opportunity to recover disgorgement based upon the same Section 5 claim that was alleged in the first OIP. *SEC v. First Jersey Securities*, 101 F.3d 1450, 1463-64 (2d Cir. 1996), in fact did state the general legal proposition that if the "second suit involved different transactions, and especially subsequent transactions, there generally is no claim preclusion." Moreover, the *First*

2. There Is No Identity Of Operative Facts

a. The Section 5 Claim Against Pierce In The Present Proceeding Arises From Facts And Evidence Different From That Required To Prove The Section 5 Claim Against Pierce In The Prior Proceeding

To evaluate whether there is identity of claims, factors to be considered include "whether the same evidence is needed to support both claims and whether the facts essential to the second were present in the first." *Shamrock Assoc. v. Sloane*, 738 F. Supp. 109, 116 (S.D.N.Y. 1990) (finding distinct acts of fraud in the two suits cannot be deemed identical because they were in connection with some of same stock purchases were allegations concerned different acts and conduct) (quotations and citation omitted). The scope of the litigation is framed by the complaint at the time it is filed. *Greenberg v. Board of Governors of the Fed. Reserve Sys.*, 968 F.2d 164, 168 (2d Cir. 1992); *see Computer Associates Int'l, Inc. v. Altai, Inc.*, 126 F.3d 365, 370 (2d Cir. 1997) (same, stating that res judicata doctrine does not apply to new rights acquired during the action which might have been, but were not, litigated). Pierce's res judicata argument fails to show an identity of claims, as the evidence and facts of the Section 5 violations are different in each proceeding.

In the prior proceeding, the Division alleged that Pierce violated Section 5 of the Securities Act through unregistered sales of 300,000 Lexington shares from his personal account at the Liechtenstein bank. *See* Buchholz Decl. II Ex. A (OIP) at ¶ 16.[2] To establish a *prima facie*

Jersey court added that "the fact that both suits involved essentially the same course of wrongful conduct is not decisive, nor is it dispositive that both proceedings involve the same parties, similar or overlapping facts, and similar legal issues." *Id.* at 1463 (citations omitted); s*ee also NLRB v. United Technologies Corp.*, 706 F.2d 1254, 1259-60 (2d Cir. 1983) ("the circumstances that several operative facts may be common to successive actions between the same parties does not mean that the claim asserted in the second is the same claim that was litigated in the first, and that litigation of the second is therefore precluded by the judgment in the first").

[2] For the sake of efficiency, in support of this reply brief, the Division relies on evidence specified below that was submitted in exhibits to the Declaration of Christopher Wells In

case against Pierce for his violation of Section 5 in connection with these sales, the Division put forth evidence showing, and the Hearing Officer found, that no registration statement was filed or in effect as to Pierce's sales of the 300,000 shares from his personal account, that Pierce directed the sales, and that the sales were made through interstate commerce. *See* Buchholz Decl. II Ex. J (Initial Decision) at 15; *see also id.* Ex. B (Division's Motion for Summary Disposition in prior proceeding) at 5. Accordingly, the Hearing Officer held that the Division presented a *prima facie* case against Pierce "for the sales from his personal account of Lexington stock that he acquired from the First S-8." Buchholz Dec. II Ex. J (Initial Decision) at 15. Based on evidence submitted by the Division calculating the proceeds Pierce received from the unregistered sales of the 300,000 shares through his personal account, the Hearing Officer ordered disgorgement of $2,077,969, finding that this amount represented the "actual profits Pierce obtained from his wrongdoing charged in the OIP." *Id.* at 20.

In the present proceeding, the Division has alleged that Pierce violated Section 5 of the Securities Act by making unregistered sales of 1.6 million Lexington shares through the Newport and Jenirob accounts at the Liechtenstein bank, and that these separate unregistered sales are distinct from the unregistered sales of 300,000 Lexington shares that Pierce made from his personal account. *See* Buchholz Decl. II Ex. M (OIP) at ¶ 25.

Support Of Respondent Pierce's related Motion For Summary Disposition ("Wells Decl.") and in the Declaration Of Steven Buchholz ("Buchholz Decl. III") in Support of the Division of Enforcement's Opposition to Respondent Pierce's Motion for Summary Disposition and attached exhibits. The Division cites the Declarations of Jeffrey Lyttle and Steven Buchholz In Support Of The Division of Enforcement's Motion for Sanctions and Entry of Default Judgment Against Respondents Newport Capital Corp. and Jenirob Company, Ltd and Anticipated Motion for Summary Disposition Against Respondent Pierce as "Lyttle Decl." and "Buchholz Decl. I" and the Declaration of Steven Buchholz in further Support of the Division of Enforcement's Motion for Summary Disposition Against Respondent Pierce as "Buchholz Decl. II."

To establish a *prima facie* case against Pierce in the present proceeding for his violation of Section 5 in connection with the Newport and Jenirob sales, the Division has put forth evidence that no registration statement was filed or in effect as to Pierce's sales of the 1.6 million shares through the Newport and Jenirob accounts, that Pierce directed the sales, and that the sales were made through interstate commerce. *See* Division's Motion for Summary Disposition at 10-12. The Division's evidence enumerates each of the specific unregistered sales that together constitute the 1.6 million shares Pierce sold through the Newport and Jenirob accounts between February and September 2004, and calculates that the net proceeds received from those sales was $7,247,635.75. *See* Division's Motion for Summary Disposition at 25 (citing Lyttle Decl. ¶¶ 3-24 and Exs. A-B; Buchholz Decl. I ¶¶ 2-35 and Exs. A-GG).

None of the unregistered sales included in the sales of 1.6 million shares that Pierce made through the Newport and Jenirob accounts are the same as the unregistered sales of 300,000 shares that Pierce made through his personal account. Pierce has not argued otherwise. Indeed, Pierce has not pointed to a single unregistered sale that he made through the Newport and Jenirob accounts that is the same as one of the unregistered sales that he made from his personal account (nor could he). The fact that there is no overlap between these unregistered sales is critical. As the Hearing Officer held in the prior proceeding, "Section 5 of the Securities Act is ***transaction specific*** . . . ." Buchholz Decl. II Ex. J at 15 (emphasis added).

There is no merit to Pierce's conclusory argument that the Division's present Section 5 claim for Pierce's unregistered sales of Lexington stock through Newport and Jenirob arises from the "same transactional nucleus of facts" as its prior Section 5 claim against Pierce. Although after it received the necessary evidence in March 2009, the Division sought additional disgorgement for Pierce's sales through Newport and Jenirob, the Hearing Officer ruled in the

Initial Decision that these sales were beyond the scope of the OIP. She definitively held that the only Section 5 claim charged in the first OIP -- and the only claim against which disgorgement could be obtained -- was for Pierce's sales through his personal account. Buchholz Decl. II. Ex. J at 15, 20. As Pierce did not appeal this ruling, he is conclusively bound by it and is now foreclosed from arguing otherwise.

b. Pierce Confuses Facts Showing He Was Not Entitled To An Exemption From Registration With Facts Establishing The Division's *Prima Facie* Case.

There is no merit to Pierce's argument that the Division's allegations that he participated in a distribution of Lexington shares show an identity of claims between the prior and present proceedings. Pierce confuses evidence the Division offered to rebut his claim of eligibility for a Section 4(1) exemption with evidence that established his *prima facie* Section 5 violations for his sales through his personal account.

In the prior proceeding, once the Division established a *prima facie* case, the burden shifted to Pierce to prove the availability of any exemptions from registration as an affirmative defense. *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953); *Swenson v. Engelstad*, 626 F.2d 421, 425 (5th Cir. 1980). It is in the context of showing that Pierce could not invoke an exemption to registration that the Division's allegations that Pierce participated in a distribution of Lexington stock by transferring shares to Newport and others became relevant. As the Hearing Officer found in her Initial Decision in the prior proceeding (Buchholz Decl. II, Ex. J at 16-17), Pierce was not eligible for an exemption under Section 4(1) of the Securities Act, 15 U.S.C. § 77d(1), because he fell within the statutory definition of an issuer under Section 2(a)(11) of the Securities Act, 15 U.S.C. § 77b(a)(11).

The Division also proved in its prehearing brief that "Pierce also could not qualify for this exemption because he fell within the Securities Act's definition of an underwriter when he

received and sold the 300,000 shares." *See* Wells Decl. Ex. 3 at 11-12. Section 2(a)(11) of the Securities Act defines an "underwriter" to mean "any person who has purchased from an issuer with a view to ... the distribution of any security, or participates or has a direct or indirect participation in any such undertaking." Pierce satisfied this definition because he purchased from an issuer (Lexington) and acquired shares from Lexington with the intention of selling – or distributing – the shares to public investors. *See Ira Haupt & Co.*, 23 S.E.C. 589, 597 (1946) (defining "distribution to be the entire process of moving shares from an issuer to the investing public). The fact that Pierce is similarly foreclosed from this exemption in the present proceeding does not transform the two distinct claims into one proceeding. The unregistered sales remain distinct – his same excuse for failing to register the sales remains unavailable.

Pierce's contention that the first OIP included claims against Pierce for sales by his "associates" is simply wrong. The first OIP's use of the term "associates" does not indicate that the Division asserted specific claims for violation of Section 5 for Pierce's sales through accounts other than his own, or that such claims were adjudicated in that proceeding. Rather, the Division put forward facts relating to his associates to prove that Pierce could not meet his burden on his affirmative defense to show he was entitled to an exemption from registration of his sales of Lexington shares from his personal account under Section 4(1). *See* Buchholz Decl. II Ex. B at 3-4. 6-7; Ex. J at 15-17; Wells Decl. Ex. 3 at 11-12.

Nothing in the Division's prehearing brief in the prior proceeding indicates that the Division sought to hold Pierce liable under Section 5 for his unregistered sales of Lexington stock through Newport or Jenirob, as the Division did not yet have the evidence showing that Pierce controlled accounts in the names of Newport and Jenirob at the Liechtenstein bank or that he personally benefitted from the sales. Rather, based upon transfer agent records showing

Pierce's initial transfers of Lexington shares, the prehearing brief described Pierce's distribution of Lexington stock, in part through Newport, to counter his defense that he was entitled to a Section 4(1) exemption for his unregistered sales through his personal account. *See* Wells Decl. Ex. 3 at 11-12. Evidence relating to Pierce's initial transfers of Lexington shares through Newport also was relevant to the Division's claim in the prior proceeding that Pierce failed to report his ownership or changes in his ownership of Lexington shares on Forms 3, 4 or 5 in violation of Sections 13(d) and 16(a) of the Exchange Act. Wells Decl. Ex. 3 at 9.[3]

The February 2009 hearing followed this general outline. The Division put forward evidence to prove all of Pierce's securities law violations alleged in the first OIP and, as summarized in the Initial Decision, submitted exhibits that included information about Newport to counter Pierce's alleged affirmative defense and show that he failed to file required reports under Sections 13(d) and 16(a) of the Exchange Act. *See* Buchholz Decl. II Ex. J at 15-18.

Pierce's attempt now, in effect, to expand the scope of the Division's claims in the first OIP is belied by the contrary position he took on this very issue in the prior proceeding. There, Pierce opposed the Division's motion to admit the new evidence from the foreign regulator and objected to the adjudication of claims relating to his Lexington stock sales through Newport and Jenirob in that proceeding. Pierce argued that re-opening the evidence after the hearing had been concluded would deny his "due process rights to notice of the claims" and "the reasonable opportunity to respond," including the right to discovery and to a hearing on the new evidence. *See* Buchholz Decl. II Ex. J at 2-9. In essence, Pierce previously contended that the prior OIP did *not* include a claim for his sales of Lexington shares through Newport and Jenirob or

[3] As explained in Section III.A.2.b of the Division's opposition to Pierce's motion for summary disposition, the Division could not have deduced from Pierce's Schedule 13D that Pierce was the beneficial owner of a Newport account at the Liechtenstein bank.

disgorgement of the sale proceeds and that the claim had *not* been adjudicated in the prior proceeding. This is the diametric opposite of his current position on this motion.

Pierce additionally argues that an identity of claims exists between the prior and present proceedings because his unregistered sales of Lexington shares in both proceedings arose from the "same alleged scheme" involving Pierce's associates. This flawed argument betrays Pierce's fundamental misunderstanding of the difference between a claim for unregistered sales of securities under Section 5 of the Securities Act and a claim for securities fraud under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. As the Initial Decision in the prior proceeding pointed out: "Section 5 of the Securities Act is transaction specific ... ." Buchholz Decl. II Ex. J (Initial Decision) at 15. That is, Section 5 requires that each particular sale of Lexington shares must be registered or subject to an exemption. *See, e.g.*, *SEC v. Cavanagh*, 155 F.3d 129, 133 (2d Cir. 1998). Thus, if no valid exemption applies, each separate unregistered sale constitutes a separate violation of Section 5.

In contrast, under Rule 10b-5, "a defendant can be liable for a fraudulent scheme if she has engaged in conduct that had the principal purpose and effect of creating a false appearance of fact in furtherance of the scheme." *SEC v. Berry*, 580 F. Supp. 2d 911, 923 (N.D. Cal. 2008) (quotations omitted); *see also SEC v. Fitzgerald*, 135 F. Supp. 2d 992, 1028-29 (N.D. Cal. 2001). The OIPs in both proceedings did not charge Pierce with engaging in a fraudulent scheme in violation of Section 10(b) and Rule 10b-5, but rather with making specific unregistered sales of securities in violation of Section 5. The distinction is vital. As explained above, in the first proceeding, the Division established Pierce's *prima facie* Section 5 violation by offering evidence of Pierce's specific unregistered sales of 300,000 Lexington shares from his personal account. In the present proceeding, the Division has offered evidence of Pierce's specific

unregistered sales of 1.6 million shares through the Newport and Jenirob accounts to establish Pierce's *prima facie* Section 5 violation. As Pierce well knows, neither OIP alleged, and the Initial Decision in the prior proceeding did not find, a "fraudulent scheme." *See* Buchholz Decl. II, Exs. A, M, J at 14-18.

Accordingly, Pierce fails to meet the first element of the res judicata test because he cannot show an identity of claims between the prior and present proceedings.

c. Res Judicata Is Inapplicable Because Pierce's Concealment Of Evidence Prevented Inclusion Of The Present Section 5 Claims In The Prior Proceeding

Res judicata is inapplicable for the additional reason that Pierce's concealment of evidence prevented inclusion of the Division's present Section 5 claim in the prior proceeding. Pierce does not put forward a single fact disputing that he concealed evidence of the unregistered Newport and Jenirob sales and misled the Division during his investigative testimony. Nor does he put forward any facts disputing that his concealment prevented the Division from obtaining the evidence it needed to include a Section 5 claim for these sales in the first OIP.

Indeed, the Division indisputably did not possess the evidence showing Pierce's specific unregistered sales of the 1.6 million shares through the Newport and Jenirob accounts in Liechtenstein at issue in the present Section 5 claim until March 2009, when it was finally produced by the Liechtenstein regulator more than one month after the hearing in the prior proceeding. *See* Buchholz Decl. III at ¶¶ 8-11 and Exs. G-I. This evidence included the statements showing all transactions relating to Lexington stock in the Newport and Jenirob accounts in Liechtenstein, as well as documents showing Pierce's beneficial ownership of the accounts and instructions for trading in the accounts. *See* Buchholz Decl. I ¶¶ 11-13, 15, 17, 23-24, 26, 30 and Exs. J-L, N, P, V-W, Y, CC; Buchholz Decl. III ¶¶ 10-11 and Exs. H-I. Despite his beneficial ownership and control of the Newport and Jenirob accounts, Pierce never produced

any of this evidence to the Division, even though it was squarely called for in the Division's investigative letter request and subpoena. See Buchholz Decl. III Exs. A-B. Pierce's assertion in his Opposition to this motion that the Division was not prevented by Pierce's concealment from bringing the present Section 5 claims when the first OIP was instituted is simply false. *See* Pierce's Opposition at 11. Pierce contends that the Division should have waited (indefinitely) to bring the first OIP until the foreign regulator had responded to its requests. Of course, Pierce's argument overlooks his own failure to produce the requested information, as well as the fact that Pierce himself intervened with the foreign regulator in an attempt to prevent the production. *See* Buchholz Dec. III Ex. K. While such indefinite delay may reward an obstructionist respondent, it does not serve the needs of justice.

Given the conclusive evidence of Pierce's concealment, Pierce's characterization of certain facts in his opposition must be corrected. First, Pierce misunderstands the reason why the Division focused on the sales from his personal account in its motion for summary disposition in the prior proceeding. *See* Pierce Opposition Brief at 3. He ignores the fact that that the only evidence of Pierce's unregistered sales of Lexington stock available to the Division at the time it filed its first OIP pertained to Pierce's sales through his personal account, which he had produced. It therefore should come as no surprise to Pierce that these sales were the subject of the first OIP and that the Division's Motion for Summary Adjudication relied on evidence of Pierce's *prima facie* violation of Section 5 based solely on these sales. Buchholz Decl. II Ex. A at ¶ 16 & Ex. B at 1, 5.

In addition to misstating in his Opposition the evidence available to the Division, Pierce is wrong that the hearing evidence showed that Newport and Jenirob were two of Pierce's associates. In support, Pierce cites Exhibits V and W to Buchholz Declaration I (also, Buchholz

Decl. III Exs. H & I), which he apparently lumps together as evidence presented during or after the hearing. As the Buchholz Declaration III makes clear, the Division did *not* receive this evidence from the foreign regulator until March 2009, a month after the hearing. *See* Buchholz Decl. III ¶¶ 8-11 & Exs. G-I.

Pierce also incorrectly suggests that the Division had evidence throughout the first proceeding that Pierce directed sales of Lexington stock through Newport and Jenirob and that the Division knew that he was the beneficial owner of the accounts. This, too, is false. During his sworn investigative testimony on July 27-28, 2006, Pierce denied that he held any beneficial ownership interest in Newport, testifying as follows:

> Q Do you have an ownership stake of any kind in Newport Capital Corp.?
> A No.
> Q Neither directly or indirectly through other entities?
> A Correct.

Buchholz Decl. III Ex. C at 197:8-13.

Pierce additionally denied that he held any beneficial ownership interest in Jenirob and further denied that he directed any trading for Newport and Jenirob through the Liechtenstein bank.[4] When Pierce was questioned about a document (Testimony Ex. 98, *see* Wells Decl. Ex. 8) containing emails that had been produced by vFinance involving Pierce, Mast and a broker at vFinance, he acknowledged receiving the emails. He then testified that he had no interest in the U.S. trading account through which he, Newport and Jenirob sold Lexington stock. Pierce characterized it as an account connected to Mast that conducted trades in Lexington stock, but Pierce denied giving trading instructions for any securities transactions in that account. Pierce also did not disclose that he was the beneficial owner of the Newport and Jenirob accounts that

[4] After denying that he had a beneficial ownership interest in Newport, Pierce later ambiguously indicated that, although he had no interest in Jenirob, he had an unspecified interest in Newport or a Newport account at the Liechtenstein bank. *See* Buchholz Decl. III Ex. D at 396:1-5.

were selling Lexington stock through the U.S. trading account. Buchholz Decl. III ¶ 5 & Ex. D (Pierce Investigative Testimony Tr., 7/28/06) at 394:19-397:20. As a result of Pierce's concealment and misleading testimony, the Division did not have the evidence demonstrating Pierce's unregistered sales of Lexington shares through the Newport and Jenirob accounts in Liechtenstein until after the hearing was concluded.

Despite Pierce's unavailing attempts to distinguish the case law cited by the Division, it is beyond question that courts have recognized the existence of an exception to the application of res judicata when, as here, "fraud, concealment, or misrepresentation have caused the plaintiff to fail to include a claim in a former action."[5] *Harnett v. Billman*, 800 F.2d 1308, 1313 (4th Cir. 1986); *see also Mpoyo v. Litton Electro-Optical Sys.*, 430 F.3d at 988 ("ignorance of a party does not . . . avoid the bar of res judicata unless the ignorance was caused by the misrepresentation or concealment of the opposing party"); *Western Sys., Inc. v. Ulloa*, 958 F.2d at 871-72 (same); *Johnson v. Ashcroft*, 445 F. Supp. 2d 45, 49 (D.D.C. 2006) ("Newly discovered evidence normally does not prevent the application of res judicata, unless the evidence was either fraudulently concealed or when it could not have been discovered with due diligence"); *In re Genesis Health Ventures, Inc.*, 355 B.R. 438, 454 (Bkrtcy. D. Del. 2006) (applying, on motion to dismiss, rule that that former judgment is not a bar to suit "where plaintiff's omission of an item

---

[5] Notably, three of the cases the Division cites in support of this widely-recognized principle (*Mpoyo*, *Ulloa* and *Johnson*) were also cited by Pierce himself either in his opposition to the Division's motion for summary disposition or in his moving papers in support of his motion for summary disposition. Indeed, in a parenthetical to a case he cites, *Theodore v. District of Columbia*, ___ F. Supp. ___, 2011 WL 1113372, at *5 (D.D.C. Mar. 28, 2011), Pierce omits key language setting forth this principle. See Pierce Opposition Br. at 12 n.5. The actual statement reads: "newly discovered evidence normally does not prevent the application of res judicata *unless the evidence was either fraudulently concealed or when it could not have been discovered with due diligence*." (Emphasis added to indicate omission.) As noted above, the *Johnson* case Pierce cites in the same footnote also states this principle.

of his cause of action was brought about by defendant's fraud, deception or wrongful conduct") (citation omitted).[6] Pierce cites no cases holding otherwise, nor is the Division aware of any.

The concealment exception to res judicata is directly applicable here. The Newport and Jenirob accounts were held at a bank in Liechtenstein, a country that had no applicable mechanism for assisting the Commission when the prior action was instituted. Pierce actively misled the Division in testimony under oath about his ownership interest in, and control over, the Newport and Jenirob accounts, then further concealed the Newport and Jenirob sales by refusing to produce the relevant subpoenaed records. He even attempted to block the foreign regulator from producing the documents requested by the Division. Pierce's deliberate concealment prevented the Division from including claims pertaining to those sales when the OIP was instituted in the prior proceeding.

Pierce's contention that the exception is a "red herring" because the Division received the evidence during the pendency of the prior proceeding is without merit. Pierce neglects to mention that the Division did not receive the evidence from the foreign regulator until after the hearing and that the Hearing Officer ruled that the Division could not obtain liability for, or disgorgement based on, the Newport and Jenirob sales in the first proceeding because the sales were outside the scope of the first OIP. Pierce's concealment of evidence therefore bars him from invoking a res judicata defense to avoid the Division's present claims against him.

---

[6] Pierce's attempt to distinguish *Genesis Health Ventures* on the ground that the court was ruling on a motion to dismiss is unavailing. The court clearly would not have ruled that the plaintiffs could proceed with their manipulation claims had it not applied the fraudulent concealment exception to application of res judicata in that context.

3. No Final Judgment Was Entered On The Merits Of The Division's Present Section 5 Claim

a. The Section 5 Claim For Pierce's Unregistered Sales Of Lexington Stock Through Newport And Jenirob Was Not Adjudicated On The Merits In The Prior Proceeding

Pierce cannot show that a final judgment on the merits was reached in the prior proceeding on Pierce's unregistered sales of Lexington shares through Newport and Jenirob. As the Supreme Court has explained:

> In order that a judgment may constitute a bar to another suit, it must be rendered in a proceeding between the same parties or their privies, and the point of controversy must be the same in both cases, and must be determined on its merits. *If the first suit was dismissed for defect of pleadings, or parties, or a misconception of the form of proceeding, or the want of jurisdiction, or was disposed of on any ground which did not go to the merits of the action, the judgment rendered will prove no bar to another suit.*

Costello v. United States, 365 U.S. 265, 286 (1961) (emphasis added). Adjudication on the merits "has a well settled meaning: a decision finally resolving the parties' claims, with res judicata effect, that is based on the substance of the claim advanced, rather than a procedural or other ground." *Sellan v. Kuhlman*, 261 F.3d 303, 311 (2d Cir. 2001) (adjudication involves the final settlement of the rights and duties of the parties on the merits of the issues raised).

This analysis is consistent with case law holding that dismissals for lack of jurisdiction or similar procedural grounds do not operate as an adjudication on the merits. For example, in *Criales v. American Airlines, Inc.*, 105 F.3d 93, 96-97 (2d Cir. 1996), the court noted that a dismissal would not bar a subsequent suit where the plaintiff had failed to comply with a precondition requisite to the court's going forward to determine the merits of his substantive claim. As the court observed, "in properly seeking to deny a litigant two days in court, courts must be careful not to deprive him of one." *Id.* at 98 (citations and quotations omitted). Similarly, in a case determining the claim preclusive effect of a federal judgment dismissing an

action on statute of limitations grounds, the Supreme Court explained that the common connotation of the term "judgment on the merits" is "one in which the merits of a party's claim are in fact adjudicated for or against the party after trial of the substantive issues." *Semtek Int'l Inc. v. Lockheed Martin Corp.*, 531 U.S. 497, 502 (2001). The Court added that, as the term "judgment on the merits" has evolved, it remains generally recognized that a dismissal without prejudice is the opposite of an adjudication on the merits. *Id.* at 505-06 (analyzing facts in context Federal Rule of Civil Procedure 41(b), which governs involuntary dismissals).

Procedurally, the Initial Decision's ruling that the Division could not seek disgorgement from Newport and Jenirob (once it belatedly obtained the necessary evidence) in the prior proceeding is analogous to a dismissal of that claim without prejudice for lack of authority to adjudicate it. Specifically, the Initial Decision found that Newport and Jenirob "are not mentioned in the OIP, and such disgorgement would be outside the scope of the OIP. The Commission has not delegated its authority to administrative law judges to expand the scope of matters set down for hearing beyond the framework of the original OIP." Buchholz Decl. II Ex. J at 20. A procedural finding that the Hearing Officer was without authority to adjudicate the claim for disgorgement of the proceeds of the unregistered Newport and Jenirob sales simply cannot be transformed into a decision on the substance of that claim, as Pierce contends. Nowhere does the Initial Decision even discuss whether the Newport and Jenirob sales violated Section 5, much less whether disgorgement of the proceeds of those sales would be an appropriate sanction for the violation. It is also significant that the Initial Decision does not state that its finding was made with prejudice.

Pierce's related argument that that res judicata should apply here to prevent "piecemeal litigation," at a minimum, fails to recognize an exception set forth in Section 26(1)(c) of

Restatement (Second) Judgments. This exception states that res judicata does not apply in a second action when the plaintiff was unable to obtain certain relief in the first action because of limitations on the court's jurisdiction or restrictions on the court's authority. Further, Section 83, comment *g*, of the Restatement cautions that "[t]he qualifications and exceptions to the rule of claim preclusion have particular importance with respect to adjudications by administrative agencies" because, in contrast to Article III courts, the jurisdiction of administrative agencies is more limited. In the context of adjudications by administrative agencies, as here, "limitations on the authority of the tribunal should carry corresponding limitations on the scope of 'claim' for purposes of the rule of claim preclusion." *See Texas Employer's Ins. Assoc. v. Jackson*, 862 F.2d 491, 502-03 (5th Cir. 1988) (denying application of res judicata where administrative proceeding was without jurisdiction to hear matters asserted in the plaintiff's state suit and citing Wright Miller & Cooper § 4412 at 93, explaining "[i]t is clear enough that a litigant should not be penalized for failing to seek unified disposition of matters that could not have been combined in a single proceeding, and even clearer that no penalty should be inflicted if a deliberate attempt to combine such matters has been expressly rejected").

The above exceptions raise yet another reason why res judicata should not apply here. The Hearing Officer's ruling in the prior proceeding acknowledged that her adjudicative authority was restricted only to claims contained in the first OIP. As a result, the only Section 5 claim adjudicated in the first OIP was for Pierce's unregistered sales from his personal account and the only disgorgement that could have been imposed was for the proceeds of those particular illegal sales. This is analogous to *Texas Employer's Insurance Association*, in which the Hearing Officer lacked jurisdiction to hear the plaintiff's state law claims. For similar reasons, the

Division should not be penalized by the Hearing Officer's finding, on procedural grounds, that she could not adjudicate the Division's present claim against Pierce in the first proceeding.

Also related is the principle that "if a judgment does not depend on a given determination, relitigation of that determination is not precluded." *Conservation Northwest v. Rey*, 674 F. Supp. 2d 1232, 1244 (W.D. Wash. 2009) (citing *Restatement (Second) Of Judgments* § 27, comment h). Evidence of the Newport and Jenirob sales was not required to establish the Division's *prima facie* Section 5 case against Pierce for his personal sales of Lexington stock. Further, there was sufficient evidence in the record at the close of the hearing to rebut Pierce's defense of a claimed exemption. *See* Wells Decl. Ex. 3; *see also* Buchholz Decl. Exs. B, J. Hence, under this principle, too, res judicata should not bar the Division's present claim.

Accordingly, because no final judgment on the merits was entered in the prior proceeding as to the Division's present Section 5 claim for Pierce's unregistered sales of Lexington stock through Newport and Jenirob, Pierce fails to meet the second element of the res judicata test.

b. The Division Was Not Obligated To Pursue Its Present Section 5 Claim Against Pierce In The Prior Proceeding, Nor Would Pursuing The Claim Have Promoted Judicial Economy

Pierce nonetheless argues that, "having put the claim [for the unregistered Newport and Jenirob sales] in play" by moving to admit evidence from the foreign regulator and seeking additional disgorgement in the prior proceeding, the Division was "obligated" to pursue the claim only in that proceeding through amendment or appeal. This argument fails. Such a course of conduct was not only unnecessary, but would not have served judicial economy – a primary policy goal of res judicata. *See, e.g., Montana v. United States*, 440 U.S. at 154-55; *Tahoe Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 322 F.3d 1064 at 1077. The Division was not required to pursue any of the so-called "avenues" of review Pierce posits and was instead entitled to bring the Section 5 claim against Pierce in the present proceeding.

Specifically, Pierce contends that, after receiving the Hearing Officer's (April 7, 2009) ruling in the first proceeding (*see* Wells Dec. Ex. 13), the Division was required to file a motion to the Commission, pursuant to Rule of Practice 200(d), seeking leave to amend the OIP in the prior proceeding to include a Section 5 claim for Pierce's sales through Newport and Jenirob. However, Comment (d) to this Rule explains that the Commission has authority to amend the OIP "where an amendment is intended to correct an error and is within the scope of the original order" -- neither of which would have been true here. *See In re Wise*, Exchange Act Release No. 48850, 2003 SEC LEXIS 2807 (Nov. 26, 2003) at *3 (allowing amendment to correct error in respondent's first name where no hearing had been set because proceeding had been stayed pending resolution of parallel criminal action). Further, amendment of OIPs is subject to the consideration that "other parties not be surprised or their rights prejudiced." *See, e.g., In re Barlow*, Exchange Act Release No. 42109, 199 SEC LEXIS 2357 (Nov. 5, 1999) at *2-3 (allowing amendment within scope of original order to conform the relief requested to the charges alleged by the Commission where hearing was not scheduled to begin for several months).

Filing a motion for leave to amend the first OIP was neither a necessary nor a viable option in light of the fact that the hearing had been concluded before the new evidence was even received, the 300-day deadline for issuance of an initial decision was near, and Newport and Jenirob were not parties in that proceeding (and thus would have had to be served and afforded a full opportunity to litigate the claims). *See* Buchholz Decl. II Ex. J at 20. Amendment would not have conserved judicial resources because, as Pierce himself argued, additional discovery and a new hearing might have been needed to adjudicate the new claim for the Newport and Jenirob sales. *See* Buchholz Decl. III Ex. J at 2-9. *Cf. Lockheed Martin Corp. v. Network Solutions,*

Inc., 194 F.3d 980, 986 (9th Cir. 1999) (need to re-open discovery and delay proceedings supports district court's finding of prejudice from a delayed motion to amend). Indeed, by contending that the Division needed to amend the first OIP to bring a claim against him for his Newport and Jenirob sales, Pierce implicitly acknowledges that the claim was not included in the first proceeding. Further, Pierce previously argued that inclusion of such evidence in that proceeding would violate his due process right to fair notice. *See* Buchholz Decl. III Ex. J at 2-9.

Nor was there any reason for the Division to appeal the rulings of the Initial Decision on the merits of the allegations in the OIP, in which the Hearing Officer found Pierce liable for all of the violations alleged and granted all of the relief the Division had requested in the OIP. This argument fails at the outset because it is based on an incorrect premise. As explained above, no judgment on the merits of the present Section 5 claim was ever entered in the first proceeding inasmuch as the Hearing Officer ruled the claim was beyond the scope of the first OIP. Appealing the Hearing Officer's procedural ruling therefore would have amounted to a request that the Commission grant leave to amend the OIP and re-open the prior proceeding to litigate a new claim through discovery and a new hearing. There was no need to adjudicate this new and separate claim within the confines of a proceeding that had already concluded, particularly when the requisite evidence for the claim was not available until after the hearing, due to Pierce's concealment, and Newport and Jenirob were not even parties to the proceeding. This avenue, too, would not have conserved the resources of either the Hearing Officer or the parties – one of the purposes of res judicata. *See, e.g., Tahoe Sierra Preservation Council*, 322 F.3d at 1077.

The final two proposed "avenues" Pierce contends the Division should have used under Rules of Practice 400(a) and 452 concern interlocutory review of the Hearing Officer's evidentiary rulings. Such review was unnecessary inasmuch as the Hearing Officer admitted the

evidence the Division requested and the ruling limiting the disgorgement sanction concerned only the Hearing Officer's authority, not the merits of the claim. By its terms, Rule 400(a) review is disfavored, applies only in extraordinary circumstances and requires certification by the Hearing Officer of conditions not at issue here. Pierce's citation of Rule of Practice 452 is particularly puzzling, as that rule pertains to proceedings already pending before the Commission and it was therefore inapplicable.

Accordingly, there is no merit to Pierce's argument that the Division was obligated to litigate its claim for the Newport and Jenirob sales to conclusion in the prior proceeding or be barred by res judicata from litigating in the present proceeding. Indeed, the argument that the Division should have sought leave to amend or appealed implicitly acknowledges that the claim was not adjudicated in the prior proceeding. This is inconsistent with the thrust of Pierce's primary argument that res judicata should apply because the claim actually was adjudicated.

4. Two Parties In This Proceeding, Newport And Jenirob, Were Not Named In The Prior Proceeding

Pierce faces the additional hurdle that the present OIP brings claims against not only Pierce, but also against Jenirob and Newport, which the Hearing Officer found were not parties to the first proceeding. *See* Wells Decl. Ex. 14 at 20. *Cf. Facchiano Construction Co. v. U.S. Dept. of Labor*, 987 F.2d 206, 212 (3d Cir. 1993) (declining to apply res judicata in part because not all parties were the same in both actions). The basis for limiting operation of res judicata to the parties involved in the earlier litigation is the "concept that everyone is entitled to his or her 'day in court'" before they are bound by a judgment. 18 *Moore's Federal Practice* § 131.40[1] (2011). As the Supreme Court explained, "[i]t is a violation of due process for a judgment to be binding on a litigant who was not a party or a privy and therefore has never had an opportunity to be heard." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 327 n.7 (1979).

Pierce misses entirely the critical fact that although Newport and Jenirob were in privity with Pierce as their beneficial owner, the claims in the present proceeding were not asserted against them (or Pierce) in the prior proceeding, as Pierce had concealed both this relationship and the particular transactions at issue. Neither Pierce nor Newport and Jenirob were ever heard on these claims in the prior proceeding. Accordingly, this third element of res judicata, too, is not met and Pierce's res judicata defense must fail in its entirety.[7]

C. Pierce Does Not Dispute That His Other Affirmative Defenses Are Meritless

The Division's opening brief on this motion sought a ruling that Pierce's affirmative defenses are meritless. In his Opposition, Pierce disputes only the Division's arguments concerning his res judicata defense. In his own motion for summary disposition, however, Pierce attempts to prop up his equitable estoppel, judicial estoppel and waiver defenses, but as the Division argued in its opposition to Pierce's motion, these defenses are inapplicable. Pierce has abandoned his laches and statute of limitations defenses. Thus, for the reasons set forth in the Division's opening brief on this motion and in the Division's opposition to Pierce's motion, all of Pierce's other affirmative defenses must fail, as well.

---

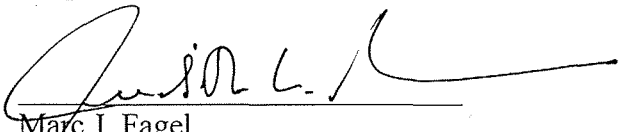
[7] None of the cases Pierce cites disturb this result. *Bethesda Lutheran Homes v. Born*, 238 F.3d 853, 857 (7th Cir. 2001), concerns joinder of plaintiffs where the relevant events were the same in both proceedings – obviously not the case here. *United States ex rel. Robinson Rancheria Citizens Council v. Borneo, Inc.*, 971 F.2d 244, 249 (9th Cir. 1992), merely stands for the proposition that "the naming of additional parties does not eliminate the res judicata effect of a prior judgment so long as the judgment was rendered on the merits, the cause of action was the same and the party against whom the doctrine was asserted was a party to the former litigation." None of the conditions listed by the court is present here, as no judgment was rendered on the merits of the claim for the Newport and Jenirob sales, the Section 5 violation in the prior proceeding concerned different sales and therefore was not the same as that asserted in the present proceeding and Newport and Jenirob were not parties to the prior proceeding. *Stratosphere Litig. LLC v. Grand Casinos*, 298 F.3d 1137, 1143 (9th Cir. 2002) is similarly inapt, as there was no ruling in the prior proceeding that would bind Pierce, as Newport's and Jenirob's representative, for the Section 5 violation asserted in the present proceeding. Pierce's attempt to distinguish *Facchiano Construction* is also unavailing, as Pierce misunderstands that the present proceeding is not based on the same violative conduct as the prior proceeding.

III. CONCLUSION

For all the foregoing reasons, the Division requests that the Hearing Officer grant its Motion for Summary Disposition Against Pierce in its entirety.

Dated: April 18, 2011

Respectfully submitted,



Marc J. Fagel
Michael S. Dicke
John S. Yun
Judith L. Anderson
Steven D. Buchholz
44 Montgomery Street, Suite 2600
San Francisco, CA 94104
Phone: (415) 705-2500
Fax: (415) 705-2501
Attorneys for DIVISION OF ENFORCEMENT