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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.,	**RESPONDENT G. BRENT PIERCE'S OPPOSITION RESPONSE TO THE DIVISION'S BRIEF IN SUPPORT OF CROSS-PETITION FOR REVIEW OF THE INITIAL DECISION AGAINST GORDON BRENT PIERCE**
Respondents.	

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I. INTRODUCTION

This case is the second administrative proceeding to adjudicate G. Brent Pierce's liability and the remedy for registration violations in the trading of Lexington Resources, Inc. ("Lexington") common stock. *See* Initial Decision ("Decision") at pp. 1-2.[1]

The Division of Enforcement challenges the Decision's holding that "[i]n the absence of any additional considerations, res judicata would bar the present proceeding." Decision at page 16; Cross-Petition at pp. 2-3. In response, Pierce shows again that this is a classic res judicata case, and not even a close question. Under the general rule against claim splitting, a final decision merges the original claim into the judgment and extinguishes all remedies "with respect to all or any part of the transaction, or series of connected transactions, out of which the action arose." Here, the *same* evidence and grounds were presented and the *same* remedy was demanded against Pierce in two sequential enforcement proceedings, even though a "final decision" was issued before the second case was launched.

The very same evidence and arguments on which the Division now relies in this Second Case were presented in the First Case to determine the amount Pierce should be ordered to disgorge. The disgorgement order resulted from an illegal distribution of Lexington stock that generated $13 million in proceeds to "Pierce and his associates" in violation of the registration provisions of the Securities Act of 1933. The Division proposed that Pierce disgorge $9.6 million, but in a preliminary (initial) decision, the amount of disgorgement was limited to $2.1 million. The Commission's rules provided several procedural avenues to seek an increase in the disgorgement order to $9.6 million, but the Division decided not to take any of them and the $2.1 million disgorgement order became final.

[1] In this and other pleadings we refer to the instant case as the "Second Case" and the earlier Lexington enforcement proceeding as the "First Case."

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The Division vainly attempts to invoke exceptions to the rule against claim splitting. The exceptions are plainly inapplicable. This is not a case in which the parties "reserved" the $7.5 million claim for later adjudication; nor did the Commission notify Pierce of any such reservation before his appeal rights expired; nor was there any jurisdictional or statutory bar against a $9.6 million disgorgement order in the First Case. To the contrary, the Commission verified the propriety of the final disgorgement order by filing it in court *and collecting on it.* The Commission's own actions defeat the Division's attempts to escape the rule against claim splitting. If the Commission were to ignore principles of res judicata in a case this clear cut, not only would it evoke an appeal to the circuit court, it would call into question whether its administrative proceedings really afford due process. The Commission should not compromise the integrity of its administrative proceedings by artificially attempting to salvage this Second Case for the Division.

II. COUNTERSTATEMENT OF ISSUES FOR REVIEW

A. Did the Decision correctly hold there was a final decision on the merits in the First Case?

B. Has the Division proven any of the recognized exceptions to the general rule against claim splitting? Did the decision in the First Case contain an express reservation of an additional disgorgement remedy to be brought in a later case? Did the Commission have subject matter and personal jurisdiction over Pierce? Did the Division and the Commission have a remedy within the First Case to pursue the additional disgorgement?

C. Did the Decision correctly conclude that the $7.25 million disgorgement claim in the Second Case was one of the same claims made against Pierce in the First Case based on the illegal distribution generating $13 million in proceeds?

III. STATEMENT OF THE CASE

From the very outset of the investigation through the final order of the First Case, the Division consistently sought to hold Pierce accountable for *all* trading he sponsored, whether through his own accounts or those of the "associates" and "offshore companies" he controlled. The Division faltered in the First Case in its attempt to disgorge $7.5 million from Pierce for his improper sales through two of those companies—Newport Capital Corp. ("Newport") and Jenirob Company Ltd. ("Jenirob"). But instead of adhering to the Commission's rules, it snuck around them. From start to finish, it would be difficult to construct a stronger case of res judicata than this one.

A. This Second Case and the First One Sprang From A Single Investigation.

On May 4, 2006, the Commission issued its order directing private investigation into trading in Lexington stock. Decision's Findings of Fact at page 7. *In re Matter of Lexington Resources, Inc.*, File No. SF-02989 (Decl. of Christopher B. Wells, Ex. 1).[2] The order recited among other things the possibility of registration violations by unnamed "persons or entities" who were consultants, partners and/or affiliates of Lexington or directly or indirectly the beneficial owners of Lexington common stock. *Id.* Those same charges run through both cases.

B. The OIP in the First Case Alleged Wrongdoing By Pierce's "Associates" and "Offshore Companies."

More than two years after the Commission issued an order to investigate Lexington stock trading, it issued an order instituting proceedings (the "First OIP," Wells Ex. 2), *In the Matter of Lexington Resources, Inc., Grant Atkins, and Gordon Brent Pierce*, Admin. Proc. File No. 3-13109 (July 31, 2008) (the "First Case"). Decision at page 7. The First OIP's request for relief was broad. The OIP did *not* restrict cease and desist or disgorgement relief to registration

[2] We refer to paragraphs in the Wells Declaration as "Wells ¶ __" and exhibits to the Wells Declaration as "Wells Ex. ___."

violations resulting solely from trades in Pierce's personal account. The request was: "Whether Respondent Pierce should be ordered to pay disgorgement pursuant to Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act." Wells Ex. 2, Section III.D.

The predicate allegations for that broad request against Pierce included trading by "his associates" and "his offshore company:"

- Lexington and Atkins "issued nearly five million shares of Lexington common stock to promoter Gordon Brent Pierce and his associates." First OIP ¶ 1.
- "Pierce and his associates resold their stock to public investors through an offshore bank, netting millions of dollars in profits." *Id.*
- after receiving Lexington stock registered on Form S-8, Pierce sold "most of his S-8 shares through an offshore company that he operated." *Id.* ¶ 11.
- "almost immediately after receiving the shares, Pierce transferred or sold them through his offshore company." *Id.* ¶ 14.
- "Pierce and his associates deposited about 3 million Lexington shares in accounts at an offshore bank" and "between February and July 2004, about 2.5 million Lexington shares were sold through an omnibus brokerage account in the United States in the name of the offshore bank, generating sales proceeds of over $13 million" (*id.* ¶ 15), of which at least $2.7 million was for sales by Pierce personally through the offshore bank. *Id.* ¶ 16.

C. The Division Contended Throughout the First Case That Newport and Jenirob Were Pierce's "Associates" and "Offshore Companies."

As part of the res judicata analysis in the conclusions of law, the Decision at page 16 refers to the Division's post-hearing brief and the initial decision in the First Case. But the relevant record goes well beyond those pleadings. The Division consistently maintained that Newport and Jenirob were among the "associates" and "offshore companies" through which

Pierce had committed violations of the securities laws.[3] For example, the Division argued in its pre-hearing brief (Wells Ex. 3):

- "Pierce and his companies and cronies reaped millions of dollars in stock sale proceeds." Wells Ex. 3 at 1-2.
- "Pierce used Newport Capital to distribute about 2.5 million post-split Lexington shares without registering that distribution." *Id.* at 3.
- "Pierce transferred [2.52 million] shares to Newport Capital. Newport Capital then sold half of those shares directly to others and placed the other half of those shares in brokerage accounts before selling them to investors. Pierce therefore used Newport Capital, as described now, to distribute 2.52 million post-split Lexington shares." *Id.* at 6.
- Newport held nearly one million Lexington shares in its Hypo Bank account, and after third parties to whom Newport had sold other shares also transferred them to Hypo Bank accounts, vFinance sold 1.2 million shares for Hypo Bank for total net proceeds of $8.1 million. *Id.* at 7.

Indeed, the Division's focus on Newport as the "conduit" through which it claimed Pierce sold 2.52 million Lexington shares in violation of Section 5 was so complete that it referenced Newport some 38 times in the 9-page factual statement of its pre-hearing brief.

The Division's spotlight on Newport continued throughout the three-day hearing. The transcript has 200 references to Newport, including its sales of Lexington stock received from Pierce.[4] The Division submitted many hearing exhibits to establish Pierce's sales of Lexington stock through his associates, Newport and Jenirob -- *e.g.,* the Schedule 13D filed jointly by

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[3] Earlier, when he answered the OIP, Pierce had moved for a more definite statement identifying the "associates" and "offshore companies" covered by the OIP, voicing a concern that without such specification the "Division is bound to 'ambush' Mr. Pierce" (Wells Ex. 27 at 4). The Division declined to name those persons or entities, responding that it had made its investigative files available to Pierce, who was "aware of the entities he controlled that owned Lexington stock" (Wells Ex. 28 at 3), and the Hearing Officer did not order it to name them.

[4] The Division argued in its opening statement that Pierce transferred over 900,000 shares to Newport that it sold from Hypo Bank in 2004 and through a brokerage account in 2006. Wells Ex. 4 at 24. The Division argued that the movement of shares from Pierce to Newport and other entities, and then to brokerage accounts and individual purchasers, constituted a distribution of S-8 shares by Pierce. *Id.* at 26. It elicited testimony that Lexington listed Newport as a selling shareholder in a Form SB 2 registration statement, with Pierce having dispositive powers over those shares. *Id.* at 65. It showed that Newport had an account at Hypo Bank (*id.* at 97, 145) and argued that Newport's trading in the United States was established by Pierce's moving Lexington shares to Newport at Hypo Bank and by Hypo Bank having U.S. accounts at vFinance. *Id.* at 221. It repeatedly argued that Pierce made transfers of Lexington shares to Newport, which went to third parties or brokerage accounts. *Id.* at 586, 589.

Pierce and Newport, Wells Ex. 5, Exhibit 51, a chart detailing the movement of Lexington shares to and from Newport, Wells Ex. 6.

The Division also included in Exhibit 43 documentation of the transfer of 435,000 Lexington shares to Jenirob in January 2004. Wells Ex. 7. It offered Exhibit 33, showing Pierce's instructions to Hypo Bank to book sales of Lexington stock to Jenirob's account. Wells Ex. 8. And it offered Exhibit 70, account statements for a Newport bank account showing deposits of some $1.75 million coming from Jenirob, as well as nearly $900,000 coming from unspecified Hypo Bank accounts. Wells Ex. 9. This evidence of Pierce's registration violations was admitted well before the "new evidence" from Liechtenstein.

D. The Division's Motion to Admit New Evidence Further Litigated Its Claim That Newport and Jenirob Were Pierce's "Associates" and "Offshore Companies."

In this Second Case, the Decision's Findings of Fact at page 8 state that after the close of the three-day hearing in the First Case, the Division on March 18, 2009 "moved for the admission of [the Liechtenstein records] and argued that Pierce should be liable for a larger amount than previously requested." *See* Decision at page 8; *see also* Wells Ex. 10. The Division reminded the Hearing Officer that the OIP had alleged Pierce orchestrated an illegal distribution of stock generating $13 million in proceeds from stock sales through Hypo Bank. Wells Ex. 10, at 6.[5] The Division also cited the Hypo Bank records as establishing that "the vast majority" of those sales were of shares Pierce had "transferred to Newport or the other offshore companies; [which were] then sold by Pierce into the open market through Hypo Bank.[6] Therefore ... *Pierce*

[5] "The OIP alleges that Pierce orchestrated an illegal distribution of Lexington stock ... and that in total approximately $13 million in proceeds were generated by stock sales through Hypo Bank (including the $2.7 million in Pierce's personal account) as a result of Pierce's illegal distribution of Lexington stock."

[6] Remarkably, *the Division now contends that the First Case addressed registration violations resulting from trades in Pierce's personal account only – see, e.g.*, the Division's Brief at pp. 17-20.

received millions of dollars in additional ill-gotten gains from sales of Lexington shares that ***were part of his illegal stock distribution***." *Id.* at 7 (emphasis added).

E. The Division's Post-Hearing Brief and Proposed Findings and Conclusions Sought Disgorgement From Pierce for Trading By Newport and Jenirob.

In its proposed findings and conclusions (Wells Ex. 11) and post-hearing brief (Wells Ex. 12) in the First Case, the Division argued that Pierce should be required to disgorge not only $2.078 million in trading profits from his personal Hypo Bank account (Wells Ex. 11 ¶ 52), but also $5.454 million and $2 .069 million in trading profits from the respective Newport and Jenirob accounts at Hypo Bank, for a total of some $9.601 million. *Id.* ¶¶ 56-57. The Division referred to Newport 56 times and Jenirob 12 times. The Division proposed findings of fact that Newport and Jenirob were offshore companies whose Hypo Bank accounts were controlled by Pierce (Wells Ex. 11 ¶¶ 32, 54-58) and that Hypo Bank traded for those accounts through its omnibus vFinance account. *Id.* ¶ 34. The Division proposed conclusions of law that Pierce should be required to disgorge $9,601,347 in net proceeds from sales of S-8 shares through Hypo Bank and vFinance, using Newport and Jenirob as well as his personal account. *Id.* ¶¶ 51, 53. The Division plainly asserted that this $9.6 million disgorgement remedy derived from an illegal underwriting that included not only the Lexington stock sold in Pierce's personal account, *id.* ¶ 23, but also the 1.6 million shares he sold in Newport and Jenirob accounts,

> Additionally, Pierce distributed 1.6 million other Lexington shares using accounts for Newport and Jenirob at Hypo Bank. These facts establish that Pierce is an "underwriter" by engaging in a distribution of Lexington stock. *Id.* ¶ 28 (proposed conclusion).

The Division's post-hearing brief (Wells Ex. 12) trumpeted the same claim -- that Pierce should be required to disgorge the $9.6 million he allegedly obtained from trading in his own account and those of his "offshore companies" Newport and Jenirob. On the first page, it argued

that Pierce not only sold Lexington shares for net proceeds of $2.1 million in his personal account at Hypo Bank, but also received additional net proceeds of $7.5 million using Newport and "another offshore company" (*i.e.*, Jenirob). Wells Ex. 12 at 1. The brief repeated the same claim three pages later (*id.* at 4) and in its conclusion (this time specifying Jenirob by name). *Id.* at 28. Throughout its brief, the Division referenced Newport 64 times and Jenirob 13 times, often calling them the offshore companies Pierce controlled. *Id.* at 10. The Division argued that the bank records summarized in its proposed new Exhibit 89 (quantifying the $7.5 million claim, *id.* at 25) established the same conclusions it drew from other exhibits it had already offered at the hearing. *Id.* at 14 (citing Ex. 89 together with hearing Exs. 23, 24, 49, 50 and 66).

The Division concluded its disgorgement analysis by reiterating that Pierce should disgorge the net proceeds of $2,077,969 he realized using his personal account, $5,454,197 using Newport, and $2,069,181 using Jenirob, for a total disgorgement of $9,601,347 plus prejudgment interest. *Id.* at 25.

F. The Initial Decision in the First Case Found That Pierce Had Traded Lexington Stock Illegally Through Accounts at Newport and Jenirob, But Declined to Order Disgorgement by Pierce of His Profits From Those Accounts.

In this Second Case, the Decision's Findings of Fact at page 8 refer to the hearing officer's ruling in the First Case "that the new evidence would be admitted on the issue of liability but not on the issue of calculating disgorgement." *See* Apr. 7, 2009 order, Wells Ex. 13 at 2. The stated rationale was that "these entities are not mentioned in the OIP, and such disgorgement would be outside the scope of the OIP," *id.*, because "the Commission has not delegated its authority to administrative law judges to expand the scope of matters set forth for hearing beyond the framework of the original OIP." Id. at 2 n. 3 (the hearing officer's invitation to the Division to ask the Commission to expand the scope of the OIP).

Two months after this order, on June 5, 2009, the Hearing Officer in the First Case issued her initial decision. Wells Ex. 14. Echoing the Division's oft-repeated reliance on Newport's comprehensive role in Pierce's illegal distribution of 2.52 million Lexington shares, including Pierce's use of Newport and Jenirob to distribute 1,634,400 shares of Lexington stock to the public, the initial decision in the First Case made some 70 references to Newport and six to Jenirob. It repeatedly cited the Division's post-hearing exhibits, highlighting the fact that on multiple occasions Pierce sold Lexington shares "through Hypo Bank's omnibus account at vFinance from different accounts that Pierce controlled." *Id.* at 13-14 (citing Pierce's sales from both his personal account and the Newport and Jenirob accounts on June 24, 2004 and again from all three accounts on the following day). The hearing officer again ruled that disgorgement would not include proceeds Pierce realized through Newport and Jenirob because they had not been mentioned in the OIP and the Commission has not delegated to hearing officers its authority to expand the scope of matters set down for hearing beyond the framework of the original OIP; then she ordered that Pierce disgorge only $2,043,362.33, the "actual profits Pierce obtained from his wrongdoing." *Id.* at 20-21.

G. The Division Failed to Exercise Its Opportunities to Appeal the Initial Decision to the Commission

In this Second Case, the Decision's Findings of Fact at page 8 recount how neither party appealed the Initial Decision in the First Case and "it became the final decision of the Commission on July 8, 2009." The Division had four options to keep the $7.5 million claim alive until a final decision in the First Case. It could have asked the Commission for interlocutory review of the Hearing Officer's evidentiary decision under Rule of Practice 400(a).

It could have asked the Commission to admit the new evidence under Rule of Practice 452.[7] It could have asked the Commission to expand the scope of the OIP under Rule of Practice 200(d)(l) as the Hearing Officer had suggested. Or, if it believed the Initial Decision had wrongly concluded that the OIP's references to Pierce's associates and offshore companies were insufficiently broad to permit disgorgement from Pierce of his net profits through Newport and Jenirob—notwithstanding the evidence that they were among the associates and offshore companies referenced in the OIP—it could have appealed the Initial Decision to the Commission pursuant to Rule of Practice 410. The Division passed up all these opportunities, and allowed the Initial Decision to become final, on July 8, 2009 (Wells Ex. 15).

H. The Second OIP Seeks From Pierce Exactly the Same Disgorgement of Newport and Jenirob's Trading Profits That Was Rejected in the First Case.

In the absence of any further action by either party, the initial decision became final on July 8, 2009, and Pierce believed that this matter was behind him. Wells Ex. 16, ¶¶ 1-6. To his surprise six months later, the Division advised Pierce that it intended to launch a second administrative proceeding against him, along with Newport and Jenirob, seeking to disgorge profits from the very same Newport and Jenirob trades charged against Pierce in the First Case (Wells Ex. 17). Pierce responded the following month with a Wells Submission (Wells Ex. 18) in which he raised the same the res judicata defense discussed in the briefs and the Decision.

Undeterred, the Division obtained from the Commission a Second OIP on June 8, 2010, instituting proceedings entitled *In the Matter of Gordon Brent Pierce, Newport Capital Corp., and Jenirob Company Ltd.*, Admin. Proc. File No. 3-13927 (Securities Act Release No. 9125)

[7] The Division cited Rule 452 as authority for the hearing officer to admit the new evidence in the First Case (Wells Ex. 10 at 2, footnote 1), arguing, "The Commission's rules do provide a specific procedure for submitting additional evidence after the filing of a petition for review of an Initial Decision, but before the Commission's issuance of a decision on appeal ... If the rules permit the admission of additional evidence after appeal of an Initial Decision, the same showing should permit the hearing officer to admit additional evidence before an Initial Decision." *Id.* (Citations omitted.)

(Wells Ex. 19, the "Second OIP"). The Second OIP repeated many of the allegations in the First OIP (*cf.* Wells Ex. 2 *with* Wells Ex. 19). Indeed, the Commission acknowledged that, "***Before issuance of the Initial Decision in the prior action, the Division moved to admit the new evidence ... and also sought the additional $7.7 million in disgorgement*** **[and despite the preliminary order to disgorge only $2.1 million]** ... ***Neither party appealed the Initial Decision and it became the final decision of the Commission on July 8, 2009.*** (Wells Ex. 19 at ¶¶ 29-30) (emphasis added).

The Second OIP continued to refer to Newport and Jenirob as "offshore companies" controlled by Pierce (*id.* at ¶ 1) and to Lexington's issuance of stock to "Pierce and his associates" (*id.* at ¶ 13). It described 300,000 shares transferred to Newport in January 2004 as issued to "one of Pierce's associates" (*id.* at ¶ 14) and shares transferred to Jenirob in May 2004 as issued to "Pierce's associate" (*Id.* 15 at ¶ 15). Excluding reporting violations, the Second OIP concludes by requesting the same cease and desist and disgorgement order as had been sought against Pierce in the First OIP (*Id.,* p.6 at III).

I. The Division Further Confirmed the Finality of the Initial Decision's Limited Relief Against Pierce By Seeking and Obtaining From Pierce Full Payment of the Ordered Disgorgement.

On the very same day it issued the Second OIP, the Commission filed an application in federal district court in San Francisco seeking an order requiring Pierce to pay the final award ($2.9 million including interest) in the First Case. *SEC v. Pierce*, No. CV-10-80129 MISC (N.D. Cal.) (Wells Ex. 20).[8] Pierce has completed payment to the Commission as ordered by the court (Wells Ex. 24), thereby effectuating the established remedial relief.

[8] Pierce responded by filing a complaint and motion papers for declaratory and injunctive relief in the same court, *Pierce v. SEC*, No. CV-10-3025 (N.D. Cal.) (Wells Ex. 21), seeking to enjoin prosecution of the Second Case. (Pierce attached his federal court complaint and motion papers as Exhibit A to his July 9, 2010 Answer in this

VII. ARGUMENT

A. This is a classic res judicata (claim preclusion) case.

Res judicata "is not a mere matter of practice or procedure ... It is a rule of fundamental and substantial justice, 'of public policy and private peace,' ..." *Federated Dep't Stores, Inc. v. Moittie*, 452 U.S. 394, 401 (1981). "Res judicata precludes parties from 'relitigating issues that were or could have been raised in' the prior action." Decision at pages 13-14 (citing *San Remo Hotel v. City and Cnty. of S.F., Cal.*, 545 U.S. 323, 336 n. 16 (2005); *Allen v. McCurry*, 449 U.S. 90, 94 (1980)). The First Case precludes the additional disgorgement because that remedy "' [was] or could have been raised in' the prior action." *Id.*[9]

Res judicata or "[c]laim preclusion refers to the effect of a judgment in foreclosing litigation of a matter that never has been litigated, because of a determination that it should have been advanced in an earlier suit. Claim preclusion therefore encompasses the law of merger and bar." *Migra v. Warren City Sch. Dist. Bd. of Educ.*, 465 U.S. 75, 77 n. 1 (1984) (citing Restatement (Second) of Judgments, Introductory Note before § 24 (1982)). The doctrine of merger dictates that when there is a final decision in an adjudication in favor of the plaintiff, the "original claim is extinguished and rights upon the judgment are substituted for it."[10] When a final decision "extinguishes the plaintiff's claim pursuant to the rules of merger and bar, the **claim extinguished includes all rights of the plaintiff to remedies against the defendant with respect to all or any part of the *transaction, or series of connected transactions*, out of which**

Second Case.) The Commission argued that injunctive relief was unnecessary because Pierce could raise his res judicata and estoppel defenses under Rule 220(c) and in a motion for summary disposition (Wells Ex. 22). The Court on September 2, 2010 issued a decision dismissing Pierce's action for lack of federal jurisdiction and ordering enforcement of the disgorgement order in the First Case, without reaching the merits of Pierce's res judicata allegations (Wells Ex. 23).

[9] *Dynaquest Corp. v. U.S. Postal Serv.*, 242 F.3d 1070, 1075 (D.C. Cir. 2001) (res judicata "precludes the parties or their privies from relitigating issues that were or could have been raised" in an earlier action); *Owens v. Kaiser Found. Health Plan*, 244 F.3d 708, 713 (9th Cir. 2001) (res judicata "bars litigation in a subsequent action of any claims that were raised or could have been raised in the prior action").

[10] Restatement (Second) of Judgments § 18 cmt. a (1982) (entitled "The doctrine of merger").

the action arose."[11] And this is not a case where the general rule must be extended to *new* evidence or a *new* remedy. The Division has presented precisely the *same* evidence, grounds and remedy as in the First Case. This is a classic res judicata case.

B. The Decision Correctly Concluded Res Judicata (Claim Preclusion) Applied.

In its Conclusions of Law at pages 13 and 14, the Decision correctly recaps the three-part test for proving res judicata:

> ... Three elements must be proven to establish res judicata: the earlier suit (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).

The Division has abandoned the earlier contention that the third element (identical parties or privies) was not established, but it still challenges the ruling on the second element (final judgment on the merits), still attempts to apply an exception to the rule against claim splitting, and still contests the first element (involved the same claim or cause of action as the later suit).

1. The Decision correctly ruled that the second element (final judgment on the merits) was established.

The Decision at page 14 ruled that the First Case satisfied the second element (final judgment on the merits) for res judicata:

> The Division argues that Pierce has not demonstrated the second element of the res judicata test. This contention lacks merit. A final judgment generally resolves all claims at issue as to all parties. *See American States Insurance Co. v. Dastar Corp.*, 318 F.3d 881, 889 (9th Cir. 2003). That some but not all issues are adjudicated on the merits "is simply irrelevant." *See Costantini v. Trans World Airlines*, 681 F.2d 1199, 1201 (9th Cir. 1982); *Mpoyo*, 430 F.3d at 987-88. Under this test, the First Proceeding clearly resulted in a final judgment on the merits. Buchholz Decl. II, Exs. J and K. That liability for the additional disgorgement suggested by the Liechtenstein Documents was not adjudicated makes no

[11] *Id.* § 24 ("Dimensions of 'Claim' for Purposes or Merger and Bar -- General Rule Concerning Splitting). The "Exemplifications" of the general rule against splitting demonstrate its broad application, "even though the plaintiff is prepared in the second action ... [t]o present new evidence or grounds or theories of the case not presented in the first action, or [t]o seek remedies or forms of relief not demanded in the first action." *Id.* § 25 (Exemplifications of General Rule Concerning Splitting).

> difference under *Costantini* and *Mpoyo*. *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 322 F.3d 1064 (9th Cir. 2003), on which the Division relies, is not to the contrary. In *Tahoe-Sierra*, the Ninth Circuit noted that a prior case in the Eastern District of California resulted in dismissal of all claims, and held that such a judgment was one on the merits. 322 F.3d at 1081 (citing *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 992 F.Supp. 1218, 1221 (D.Nev. 1998)). *Tahoe-Sierra* is silent on the issue of whether the existence of issues left unadjudicated, because they were found not part of the first action, undermines the finality of the first judgment.

(Underline added). The Division's Brief at page 24 challenges the ruling "[t]hat liability for the additional disgorgement suggested by the Liechtenstein Documents was not adjudicated makes no difference." The ruling explicitly cited *Constantini* and *Mpoyo,* yet the Brief conspicuously ignores *Constantini* and *Mpoyo,* then misconstrues the "judgment on the merits" test.

The Division's Brief at page 25 asserts that 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." Brief at 25 (citing *Sellan v. Kuhlman*, 261 F.3d 303, 311 (2nd Cir. 2001)). But that quotation is from a decision that does not address the "merger" principle of res judicata at issue here. And though the opinion cites to *Semtek Int'l Inc, infra,* the Division's extraction is merely dictum in a decision construing the statute governing standards for federal *habeus* review of state court actions. *Sellan,* 261 F.3d at 308 (construing 28 U.S.C. § 2254(d).[12]

The Brief's next citation is to *Semtek Int'l Inc. v. Lockheed Martin Corp.*, 531 U.S. 497, 502, 505-06 (2001). In a parenthetical to the citation, the Brief remarks that the common connotation of judgment on the merits is "one in which the merits of a party's claim are in fact

[12] Ironically, the *Sellan* opinion, though not applicable here, goes more to the point that defeats the Division -- a claim not raised in a prior action is lost to the plaintiff equally with one that was brought and rejected, absent a "procedural or other ground" not applicable here, as discussed below. The *Sellan habeus* action was based on a claim of ineffective counsel defending a state criminal proceeding. The *habeus* plaintiff's counsel had allegedly failed to make claims on appeal in the plaintiff's state court case, which claims then could not be relitigated, leading the plaintiff implicitly to use "claim preclusion" as the harm suffered because of ineffective legal counsel.

adjudicated for or against the party after trial of the substantive issues." Brief at 25 (citing and quoting *Semtek Int'l Inc.* 531 U.S. at 502). This quotation comes from Restatement (Second) of Judgments § 19 comment a, regarding the general rule of "bar," when a judgment rendered *in favor of the defendant* bars another action by the plaintiff on the rejected claim. **But this Second Case against Pierce involves the general rule of "merger," where a judgment *in favor of the plaintiff* extinguishes the original claim**. When read carefully, the *Semtek* analysis explains why the Division's surgical excision of an inapt quote imports the wrong res judicata test here. In the discussion following the Division's excerpt, *Semtek Int'l Inc* observes that "the term 'judgment on the merits' 'has gradually undergone change,' ... That is why the Restatement of Judgments has abandoned the use of the term ["judgment on the merits"] – 'because of its possible misleading connotations." 531 U.S. at 502-03 (citations omitted).[13]

There was a "judgment on the merits" in the First Case against Pierce. Disgorgement for $2.043 million was granted. The Division enforced that final order in federal court. The denial of the additional $7.5 million disgorgement sought does not alter the judgment on the merits and the merger of possible (much less proposed) remedies into the final order. The Division focuses solely on the principle of "bar" while pretending that the principle of "merger" does not exist. Or perhaps, like the appellant in *Constantini*, the Division has "apparently confused res judicata with the related but distinct doctrine of collateral estoppel, which does apply only when 'an issue

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[13] "Claim preclusion refers to the effect of a judgment in foreclosing litigation of a matter that never has been litigated, because of a determination that it should have been advanced in an earlier suit. Claim preclusion therefore encompasses the law of merger and bar. See *id.*, Introductory Note before § 24 ... In order to avoid confusion resulting from the two uses of "res judicata," this opinion utilizes the term "claim preclusion" to refer to the preclusive effect of a judgment in foreclosing litigation of matters that should have been raised in an earlier suit. For a helpful explanation of preclusion vocabulary, see Wright et al., *supra*, § 4402." *Migra v. Warren City Sch. Dist. Bd. of Educ.*, *supra*, 465 U.S. 75, 77 n. 1 (1984).

is actually and necessarily determined.'" *Constantini*, 681 F.2d at 1201 n. 2 (citation omitted). The Division has itself relied on the doctrine of collateral estoppel to prosecute this Second Case against Pierce, but that does not excuse addressing the wrong principle now. In the context of res judicata, rather than collateral estoppel, the "contention that the question involved in [t]his present action was never actually litigated in the prior action is simply irrelevant." *Constantini*, 681 F.2d at 1201. "It is a misconception of *res judicata* to assume that the doctrine does not come into operation if a court has not passed on the 'merits' in the sense of the ultimate substantive issues of a litigation." *Angel v. Bullington*, 330 U.S. 183, 180 (1947).

In *Mpoyo*, the Ninth Circuit ruled that even though "several claims were dismissed without prejudice," there was a decision on the merits. The plaintiff in *Mpoyo* was denied leave to amend the new claims. The Ninth Circuit concluded: "Denial of leave to amend in a prior action based on dilatoriness does not prevent the application of res judicata in a subsequent action." 430 F.3d at 989. The holding in *Mpoyo* "is consistent with the case law in the First, Second, Third, Fifth and Eighth Circuits that bars under res judicata the subsequent filing of claims denied leave to amend." *Id.* (citations omitted).[14] The Ninth Circuit looked to Restatement § 25, which is entitled "Exemplifications of General Rule Concerning Splitting," for the governing principles: "Different theories supporting the same claim for relief must be brought in the initial action." 430 F.3d at 988 (citing § 25, cmt. d). Also regarding the claims asserted in a denied application for leave to amend: "It is immaterial that the plaintiff in the first action sought to prove the acts relied on in the second action and was not permitted to do so because they were not alleged in the complaint and the application to amend was too late." § 25,

[14] In the First Case here, the Division never even tried to amend or otherwise ask the Commission to increase disgorgement after the hearing officer's preliminary refusal, placing the Division even more firmly in the grip of res judicata than the *Mpoyo* plaintiff, who at least tried to keep his claim alive with a belated effort to amend.

cmt. b. Instead of addressing the foregoing dispositive rules, which were explained and applied in *Mpoyo and Constantini*, the Division's Brief sidetracks into the irrelevant *Sellan* and *Semtek* discussion, and starts its analysis with an irrelevant block quotation from *Costello v. United States*, 365 U.S. 265, 286 (1961).[15]

Costello illustrates the "curable defect" exception to res judicata where a "precondition requisite" was not met in the first case (*e.g.*, the failure to file an affidavit of good cause in a denaturalization proceeding, the lack of proper service, lack of diversity, bringing a 1934 Act claim in a state court, etc.) so that the first case is dismissed without prejudice.[16] If the defect is cured after the dismissal, a second case may proceed. That principle clearly does not apply here, because "there [was] at least one decision on a right between the parties," so that the "right adjudicated or released in the first suit ma[d]e it a bar" to a second suit. *Costello*, 365 U.S. at 285.[17] In the First Case against Pierce, there was a final decision on many of the "right[s] between the parties," thereby barring this Second Case. The final disgorgement order satisfied the second element for res judicata (final judgment on the merits).

2. The Division has failed to prove that any of the recognized exceptions to the rule against claim splitting apply.

The Division's brief in the sections addressing the second element, "final judgment on the merits," and the section on the application of res judicata to administrative proceedings attempt

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[15] The Supreme Court ruled that an affidavit of good cause was a prerequisite to the initiation of a denaturalization proceeding, but had not been filed with the complaint. *Id.* at 267-68. The Government subsequently brought a new proceeding under an affidavit of good cause and complaint. *Id.* In the new proceeding, the Supreme Court held the Government was not barred from bringing the second suit. *Id.* at 288. The Court "held a dismissal for failure to file the affidavit of good cause is a dismissal 'for lack of jurisdiction' within the meaning under Rule 41(b)." *Id.* at 285.

[16] *Dozier v. Ford Motor Co.*, 702 F.2d 1189, 1192(D.C. Cir. 1983) ("What all these cases have in common is that the jurisdictional deficiency could be remedied by *occurrences subsequent to the original dismissal.*"). *Id.*

[17] In the block quote from *Costello* at page 25 of its Brief, the Division omitted immediately preceding language that explains why *Costello* would apply res judicata here, "In *Haldeman v. United States*, 91 U.S. 584, 585-86, which concerned a voluntary nonsuit, this Court said, 'there must be at least one decision on a *right* between the parties before there can be said to be a termination of the controversy, and before a judgment can avail as a bar to a subsequent suit. . . . There must have been a right adjudicated or released in the first suit to make it a bar, and this fact must appear affirmatively.'" *Costello,* 365 U.S. at 285.

to invoke exceptions to the rule against claim splitting.[18] But the Division has failed to show that any of those exceptions apply in this case. *See* Restatement (Second) of Judgments § 26(1)(a)-(f), entitled "Exceptions to the General Rule Concerning Splitting."[19]

a. <u>There was no agreement or express order permitting claim splitting.</u>

The Division wisely does not argue that either of § 26(1)'s first two exceptions apply in this case. First, the parties did not agree that the Division could split its claims. § 26(1)(a). Second, the decision in the First Case did not "expressly reserve the [Division]'s right to maintain the second action." § 26(1)(b). To fabricate an exception, however, citing no authority whatsoever, the Division argues that the First Case's final decision is "*analogous* to a dismissal of a claim *without prejudice* for lack of authority to adjudicate." Br. at 26 (Italics added). But the final decision in the First Case did not state it was "without prejudice"; nor was there any ruling that "expressly reserved" a right to bring a second action for the additional disgorgement. See § 26(1)(b) (exception to general rule against splitting, where court "**has expressly reserved**" the right to maintain the second action) (bold added). To the contrary, the hearing officer's observation that the Commission had the power to resolve the claim, along with the Commission's rules requiring the Division to take steps in the First Case to preserve its claim, did the very opposite. They implicitly if not expressly warned the Division that its claim would *not* be reserved.

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[18] Br. at § VI. C, at pp. 24-26; *id.* § VI. D, at pp. 24-26; *see, e.g, id.* at page 26 (quoting *Computer Assocs. Int'l, Inc. v. Altai, Inc.*, 126 F.3d 365 (2d Cir. 1997) citing *Burgos v. Hopkins*, 14 F.3d 787, 790 (2d Cir. 1994), which quotes Restatement (Second) of Judgments § 26(1)(c), cmt. c).

[19] Very generally stated, the exceptions include (a) express reservation of a claim by agreement of the parties or (b) express reservation by court order, (c) inability to prosecute the claim in the first action due to jurisdictional or similar restrictions on the authority of the forum, (d) splitting the claim would be necessary to suit the constitutional or statutory scheme involved, (e) in cases of continuing or recurring harm, allowing the option of intermittent suits for damages to date but subsequent to prior suits, in place of a single suit for total damages, and (f) overarching policy reasons such as invalidity of a prior restraint or relating to a condition vital to personal liberty or to avoid an otherwise incoherent disposition of the controversy.

b. There was no jurisdictional or other restriction on the Commission's authority to handle the claim for additional disgorgement in the First Case.

The third exception applies where a plaintiff is unable to rely on a certain remedy in the first case "because of the limitations on the subject matter jurisdiction of the courts or restrictions on their authority to entertain multiple theories or demands of multiple remedies or forms of relief." § 26(1)(c). An example in § 26, comment c(1) is where a federal statute requires enforcement exclusively in federal courts.[20] In that event, a prior state court action does not bar a subsequent action in federal court to enforce the federal right. § 26, comment c (1) & illus. 2. Another example is where a state court has personal jurisdiction over an out-of-state defendant for tort claims but not for a breach of contract. *Id.* Similarly, in *Computer Assocs. Int'l, Inc. v. Altai, Inc.*, 126 F.3d 365 (2d Cir. 1997), which the Division relies upon, the district court in New York lacked personal jurisdiction over the French distributor. Thus, "the absence of personal jurisdiction ... preclude[d] the application of res judicata ..." *Id.* at 370-71.[21] There was no such impediment here. The Commission asserted jurisdiction in the First Case over Pierce and the subject matter – the registration violations of "Pierce and his associates" entailing $13 million in illegal proceeds -- upon which the disgorgement order was based. Clearly, the lack of jurisdiction or authority exception cannot apply here.

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[20] *E.g.*, "[T]he Court in [*Wilko v. Swan*] noted that ... the 1934 Act ... provides for suit only in the federal district courts that have 'exclusive jurisdiction,' 15 U.S.C. § 78aa, [and not state courts] thus significantly restricting the plaintiff's choice of forum." *Scherk v Alberto-Culver Co.*, 417 U.S. 506, 514 (1974).

[21] The Division's Brief at page 27 quotes from Restatement § 83 which governs administrative res judicata. § 83(1) states the general rule that "a valid and final adjudicative determination by an administrative tribunal has the same effects under the rules of res judicata, subject to the same exceptions and qualifications, as a judgment of a court." The Brief at page 27 quotes from § 83's comment g that "[t]he qualifications and exceptions to the rules of claim preclusion have particular importance with respect to the rule of claim preclusion by administrative agencies." The comment's illustrations address situations where two agencies with different enabling legislation may have separate remedies, parallel remedies, or preclusionary remedies. § 83's cmt. g, ill. 8-11. For example, "a worker's compensation commission usually lacks authority to consider claims for punitive damages for injuries intentionally inflicted on an employee in the course of employment; an employment discrimination agency may lack authority to consider claims based on breach of contract." § 83's cmt. g.

c. There is no statutory term or rule that authorizes claim-splitting here.

The Division contends that the rule against claim splitting should not apply due to "the procedural limitations of cease and desist proceedings," which allow the Commission to move quickly but limit discovery and the hearing officer's authority, and disfavor extensions of time for the initial decision beyond 300 days from the service of the OIP. Br. at 28-29. The point of this argument is to invoke one of the exceptions to the rule against claim splitting. Where the sense of the statutory scheme is to permit the plaintiff to split its claim, there can be an exception. § 26(1)(d) & cmt. e. But such statutory terms are very specific, arising from exclusive jurisdiction or express reservation of claims, and bear no resemblance whatsoever to this situation.[22] An example is a statute that provides a landlord with both an unlawful detainer remedy and a subsequent action for past due rent.[23]

Here, the Division has failed to identify (i) any statutory term that specifically authorizes claim splitting or (ii) an ambiguous statutory term supplemented by legislative history supporting the implied reservation of claims in Commission adjudications. This is no surprise. While the Rules of Practice acknowledge the existence of a res judicata defense, *e.g.*, Rule 220(c), those rules do not give express or implied notice of any special exceptions to that defense in

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[22] *Compare Valley Disposal, Inc. v. Central Vt. Solid Waste Mgmt. Dist.*, 31 F.3d 89, 97-99 (2d Cir. 1994) (prior state court action did not preclude subsequent action in federal court under Sherman Antitrust Act, because state court did not have subject matter jurisdiction over the claim); *Bio-Technology Gen. Corp. v. Genentech, Inc.*, 80 F.3d 1553, 1562-64 (Fed. Cir. 1996) (in a patent case, ruling "in view of the jurisdictional limitations on the relief available" in United States International Trade Commission ((ITC), its administrative decision had no preclusive effect; ITC's dismissal with prejudice of defendant's claim for unfair practices in import trade; statute permitted cease and desist order and seizure order in the ITC administrative proceeding; but the award of damages for patent infringement is within the exclusive jurisdiction of federal courts); *North v. Walsh*, 881 F.2d 1088, 1093-94 (D.C. Cir. 1989) (ruling claim preclusion did not bar Oliver North's Freedom of Information Act suit, "because he could not have invoked FOIA during the grand jury proceeding," even assuming for the sake of argument that his prior FOIA request sought the same document); *Dionne v. Mayor & City Council of Baltimore*, 40 F.3d 677, 682-83 (4th Cir. 1994) (state administrative proceeding for terminated public employee did not preclude subsequent § 1983 claim challenging federal procedural due process in the course of the termination, where constitutional theories and remedies for future earnings and emotional distress were not recoverable in the administrative action).

[23] The second action is not precluded if the statutory system discloses a purpose to give a landlord a choice between a single comprehensive action and the alternative of an expedited proceeding to reclaim possession followed by a regular action for rent. § 26(1)(d), cmt. e, ill. 5 (suggested by *Tutt v. Doby*, 459 F.2d 1195 (D.C. Cir. 1972).

administrative proceedings before the Commission. There is no basis in the applicable statutes or rules here for claim splitting. And the Supreme Court has made crystal clear that there is no general equitable exception, based on the grounds of unfairness or injustice, to the application of res judicata. *Federated Dep't Stores*, 452 U.S. at 395-98.

d. The Division "had its day in court."

The Division's Brief at page 25 invokes the adage, "in properly seeking to deny a litigant two days in court, courts must be careful not deprive him one day," citing *Criales v. Am. Airlines Inc.*, 105 F.3d 93, 96-97 (2d Cir. 1997). But that adage does not apply here. The Division had its "day in court" in the First Case and prevailed on some of its claims. In contrast, in *Criales*, the pro se "plaintiff never had a day in court on his Title VII claims." The entire suit had been dismissed without prejudice due to his failure to exhaust his administrative remedies.

There was no such barrier to the additional disgorgement remedy in the First Case. The Division merely made a "strategic decision" to harvest the low hanging fruit (the original disgorgement award). It declined to appeal the denial of additional disgorgement and assumed the risk of preclusion. The Division made the conscious decision to forego the following options:

- The Division could have moved the Commission to amend the first OIP pursuant to Rule of Practice 200(d)(1) "to include new matters of fact or law," but did not.
- The Division could have moved to admit "additional evidence" before the Commission pursuant to Rule of Practice 452, but did not.
- The Division could have moved for an interlocutory appeal from the Hearing Officer's evidentiary decision pursuant to Rule 400(a), but did not.
- The Division could have petitioned the Commission to review the Initial Decision pursuant to Rule of Practice 410, but did not.

The Division's opportunity to amend is an independent ground for claim preclusion, as in *Mpoyo* and other decisions.[24] Despite the Division's apparent belief otherwise, these decisions have consequences, and it cannot now be permitted to "get a second bite at [the] same apple." *Natural Res. Def. Council v. EPA*, 513 F.3d 257, 261 (D.C. Cir. 2008); *Owens*, 244 F.3d at 715 (no exception to res judicata where plaintiffs "fail[ed] to exercise" available options. . . .").[25] The timing of the hearing officer's admission of the "new" evidence in the First Case and her refusal to order disgorgement of Pierce's profits from Newport and Jenirob trading have no bearing on the question whether the claims share a common nucleus of operative fact. *See Aunyx Corp. v. Canon U.S.A., Inc.*, 978 F.2d 3, 8 (1st Cir. 1991) ("The record reflects that [plaintiff] knew enough about the facts of this case to have been able to assert its horizontal conspiracy claim at the outset before the ITC. It is immaterial that the plaintiff in the first action sought to prove the acts relied on in the second action and was not permitted to do so because they were not alleged in the complaint and an application to amend the complaint came too late . . . . [t]hus, we hold that Count 8 is barred, as a matter of law, by res judicata"). Here, the Division's position is even weaker. It did not apply to amend the OIP at all. Instead, it ignored Rule 200(d), got the new evidence admitted anyway, and never asked the Commission to address the $7.5 million

[24] *Havercombe v. Dep't of Educ. of the Commonwealth of Puerto Rico*, 250 F.3d 1, 7 (1st Cir. 2001) (res judicata applied despite plaintiff's contention that discrimination claims for the period during 1997-1999 could not be brought since he did not receive from the EEOC a right to sue letter until shortly before jury trial began on claims for the period from 1990 to 1997; given the similarity of the alleged discrimination in the two periods and the policy permitting liberal amendment, "his failure to so amend has foreclosed him from bringing them at all."); *Owens v. Kaiser Found. Health Plan, Inc.*, 244 F.3d 708, 714-15 (9th Cir. 2001) (Title VII claims were precluded by prior judgment even though plaintiff had not completed Title VII administrative proceedings where plaintiff did not seek to amend those claims and did not seek stay for the purpose of pursuing administrative remedy); *Yapp v Excel Corp.*, 186 F.3d 1222, 1226-28 (10th Cir. 1999) (employee's first suit against employer for overtime compensation precluded subsequent suit for wrongful termination, where employee realized the risk of claim preclusion but made no effort to have the district court revisit its interlocutory and discretionary order either by adding language to preserve his wrongful discharge action or to unwind the maintenance of two separate lawsuits; along with the risk of claim preclusion, the employee took a monetary settlement).

[25] The Division "chose to purse a one track strategy" and "is barred by res judicata from now using Alternative Theories." *Aboudaram v. De Groote*, No. 05-988 (RMC), 2006 WL 1194276 , at *5 (D.D.C. May 4, 2006). "*Hussein v. Ersek*, 2009 WL 633791 at *4 (D. Nev. 2009) (plaintiff's failure to amend complaint after finding new evidence during discovery barred a later-filed complaint).

claim after the hearing officer's ruling. *See also Western Sys., Inc. v. Ulloa*, 958 F.2d 864, 871-72 (9th Cir. 1992) (party's previous "ignorance" of facts underlying second claim "insufficient to avoid the bar" of res judicata where claims were "part of the same 'transaction' that was litigated in" an earlier action). The Division may have prematurely initiated the First Case, before it had acquired every last document tracing Lexington share sale proceeds in the distribution. But the res judicata doctrine requires that it now be bound by the consequences.

Even without an appeal by the Division, and assuming the hearing officer had correctly assessed the limit of her authority, the Commission nevertheless was empowered to review the Division's proposal for additional disgorgement in the First Case:

- The Commission could have initiated its own interlocutory review pursuant to Rule of Practice 400(a), but did not.
- The Commission could have initiated a review of the Initial Decision under Rule of Practice 360(b)(1), but did not.

Therefore, for the purpose of res judicata analysis, the Division and the Commission are treated as one body. *Accord, Corestate Bank, N.A. v. Huls Am., Inc.*, 176 F.3d 187, 197 (3d Cir. 1999) (ruling a bankruptcy judge's limited powers with respect to non-core related claims do not limit the effect of the doctrine of claim preclusion since "the bankruptcy judge and the district court together could do so" and following the Second, Sixth, and Ninth Circuits). Because the hearing officer and the Commission "together" could have altered the outcome regarding additional disgorgement in the First Case, no exception to the rule against claim splitting can apply. Claim preclusion has already been applied to the Commission. *SEC v. Crofters, Inc.*, 351 F. Supp. 236, 257-58 (S.D. Ohio 1972) (granting summary judgment on the basis of res judicata barring SEC's second suit for an injunction), *rev'd on other grounds sub nom, SEC v. Coffey*, 493 F.2d 1304, 1309 (6th Cir. 1974) (stating SEC had not appealed the res judicata ruling).

In summary, there was a final judgment on the merits in the First Case and the Division had an opportunity to litigate the claim for additional disgorgement. Therefore, the Decision correctly ruled that the second element for res judicata was established.

3. The Decision correctly ruled that the First Case involved the same claim as the Second Case. The first element for res judicata was established.

a. The Two Cases Have The Same Nucleus of Operative Facts

Applying the four factor test, the Decision at pages 15 to 16 concludes there was identity of the claim in the First Case and the Second Case. *Id.* The record supports each of the four factors.

The fourth factor (whether the two suits arise out of the same transactional nucleus of facts) is sufficient by itself to resolve the question of the identity of claims. *Id.* at 15. Here, the nucleus of facts was identical.[26] The Division openly admitted this complete overlap when it submitted no new evidence whatsoever in the Second Case, even as it asserted the very same additional disgorgement claim, "***Before issuance of the Initial Decision in the prior action, the Division moved to admit the new evidence ... and also sought the additional $7.7 million in disgorgement ...***" (Wells Ex. 19 at ¶¶ 29-30) (emphasis added).

The First OIP sought disgorgement from Pierce for an allegedly "illegal distribution" of S-8 shares of Lexington stock because he "acted as an underwriter" of those shares when he "transferred or sold them through his offshore company" (Wells Ex. 2 ¶ 14). This alone would bar the Division's attempt to re-litigate disgorgement in this Second Case, even if Newport and

[26] The Decision at page 16 lists as examples eight material facts that the two cases share: (1) Lexington shares and options, (2) distributed through Pierce's IMT conduit, (3) the Lexington officer who instructed the transfer agent, (4) the US brokerage vFinance selling the shares, (5) the Liechtenstein brokerage (Hypo Bank) that opened the account at the US brokerage, (6) Pierce controlling the sale of Lexington shares sold by Newport and Jenirob, (7) the time frame from late 2003 to mid 2004, and (8) Pierce's promotion of Lexington shares. Id. at 16. These facts were cited in "[the initial decision in the First Case] or the Division's post-Hearing brief as proof that Pierce was an affiliate of Lexington." *Id.* These operative facts were related in "time, space, origin, [and] motivation," and "form a convenient trial unit." *Apotex, Inc. v. FDA*, 393 F.2d 210, 217 (D.C. Cir. 2004).

Jenirob had never been mentioned by name at all in the First Case.[27] But the unity of the two proceedings – at least as to Pierce -- runs far deeper due to the First OIP claims against "Pierce and his associates" and "offshore companies" (Wells Ex. 2 ¶¶ 1,15), which the Division's statements and evidence made clear were Newport and Jenirob.[28] *See supra* Sections II B-E.

With understatement, the Decision correctly ruled that the identical "facts are closely related, and the issue of the legality of the Newport and Jenirob sales could have conveniently been tried" in the First Case. Decision at 16. Therefore, the most important factor (transactional nucleus of facts) favored the application of res judicata. The Division's Brief at pages 15 to 20 argues that separate and distinct violations were alleged in the First Case and the Second Case. But that is irrelevant. While the Division is now busy parsing out registration violations transaction by transaction, it cannot hide from an abundant record of successfully urging that Pierce was the underwriter of an entire illegal distribution of more than 2.5 million shares, which included the 1.6 million sold by Newport and Jenirob, generating $7.5 million of the $13 million in proceeds:

> (Division's Proposed Findings of Fact in the First Case:)
> 55. Based upon documents that it received from Liechtenstein ... Pierce had moved to the Newport and Jenirob accounts at Hypo Bank a total of 1,634,400 Lexington shares that had been issued purportedly pursuant to Form S-8 registration statements ... Pierce sold these shares into the open market through the Newport and Jenirob accounts at Hypo Bank ...
> 57. Including his personal account and the Newport and Jenirob accounts at Hypo Bank, Pierce sold a total of two million S-8 shares ...
> 58. Pierce's sales through the three accounts at Hypo Bank were part of Hypo Bank's sale of Lexington shares through its omnibus account at vFinance ...

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[27] *Adams v. Southern Farm Bureau Life Ins. Co.*, 493 F.3d 1276, 1290 (11th Cir. 2007) (finding nucleus of facts broad and applying res judicata where first action "alleged an overarching scheme" of fraud and deception) closely analogous to the broad scheme to violate registration requirements (without fraud) alleged in the two cases here.

[28] *See, e.g.*, Wells Ex. 12 at 22 ("Additionally, Pierce distributed 1.6 million other Lexington shares using accounts for Newport and Jenirob at Hypo Bank. These facts establish that Pierce is an 'underwriter' by engaging in a distribution of Lexington stock") and *compare* Wells Ex. 19 (Second OIP) ¶¶ 20-25.

(Division's Proposed Conclusions of Law in the First Case:)
23. One compelling indication of Pierce's "underwriter" status is the short time period between his acquisition of the Lexington shares in November 2003 and his sale of those shares through Newport's account at Hypo Bank ... Pierce cannot rely upon the exemption from registration set forth in Section 4(1) of the Securities Act. *SEC v. M&A West, supra,* 538 F.3d at 1050-51.[29]
28. Additionally, Pierce distributed 1.6 million other Lexington shares using accounts for Newport and Jenirob at Hypo Bank. These facts establish that Pierce is an "underwriter" by engaging in a distribution of Lexington stock."

Wells Ex. 11. The hearing officer in the First Case accepted the new evidence "on the issue of liability but not for the purpose of disgorgement ..." Wells Ex. 13, at p. 2. The hearing officer then used the new evidence pertaining to the $7.5 million disgorgement claim to establish Pierce's liability as an underwriter who facilitated the distribution of more than 2.5 million Lexington shares in violation of Section 5, including the 1.6 million he sold through Newport and Jenirob. *See, e.g.* (excerpts from the initial decision in the First Case):

(findings of fact:)
Pierce is the beneficial owner of ... Newport Capital ... He is also the beneficial owner of Jenirob Company ... (at p. 5)
Newport also had brokerage accounts with Hypo Bank ... Pierce traded Lexington stock on behalf of Newport in all these accounts ... (at p. 6)
IMT served as a placeholder for distribution of stock option shares to the ICI/IMT consultants ... Several Lexington share blocks were immediately assigned to Newport, and then other individuals and entities, at Pierce's direction. (at p.11)
[S]everal trades appear to be blocks of Lexington shares that were sold through Hypo Bank's omnibus vFinance account from different accounts that Pierce controlled ... On June 25, 2004, Pierce sold 73,432 shares from his personal account, 30,000 shares from the Jenirob account, and 22,000 shares from the Newport account ... (pp.13-14)

(conclusions of law:)
The Division has shown that Pierce committed a prima facie violation of Section 5 ... and, thus ... the focus is on Pierce's transactions, not Lexington's filing of a Form S-8 (at p. 15)

[29] In *M&A West,* 538 F.3d 1043 (9th Cir. 2008), the court addressed a series of transactions purportedly involving non-affiliates -- but in economic reality involving affiliates -- who circumvented registration requirements and distributed shares of several companies to the public without providing the information required. Ostensible non-affiliates sold shares transferred to them in violation of Section 5, and those transactions became part of the illegal distribution as well. *Id.* 538 F.3d at 1050-54.

> Thus, the burden shifts to Pierce to prove the availability of any exemptions ... Pierce has failed to prove his claimed exemption ... Pierce was an affiliate ... "A control person ... is an affiliate of an issuer, and is treated as an issuer when there is a distribution of securities." (at p. 16)
> [T]he account documents [Pierce] submitted to Hypo Bank demonstrate he was the beneficial owner. Pierce caused Newport to purchase Lexington stock in a private placement ... The totality of the circumstances – Pierce's sway over Lexington's CEO, Atkins, his substantial ownership of Lexington stock, his control over the consultants assigned to work for Lexington – all point to Pierce's control of Lexington. His control of Lexington demonstrates that he was an affiliate, and thus cannot claim the Section 4(1) exemption. Thus, it is concluded that Pierce sold his Lexington stock without a valid registration statement or exemption from registration, violating Section 5 of the Securities Act. (at 17)

Wells Ex. 14.

The foregoing findings and conclusions proposed by the Division and adopted by the hearing officer in the First Case flatly contradict the Division's newly minted contentions that there were distinct rights for each unregistered sales transaction, Br. at 15-23. The overlap of the two cases is so complete that the Division has submitted no new evidence or grounds whatsoever in the Second Case, even as it now contends the registration violations in the Second Case are different than in the First. But the record clearly shows that the same statutory right and remedy were asserted by the same party (the SEC) in both cases.[30]

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[30] The Division spends pages analyzing why each transaction presents a registration violation by itself. But it forgets that it comprehensively alleged that ***every*** transaction in the illegal 2.5 million share distribution netting proceeds of $13 million by "Pierce and his associates" was a Section 5 violation of the underwriter, Pierce. Not a single case cited by the Division applies here, or even comes close. In *NLRB v United Technologies Corp.* 706 F.2d 1254, 1259-60 (2d Cir. 1983), "events giving rise to the two proceedings occurred at different places, and more than a decade apart; they concerned different employees engaged in different acts; and they involved different employer conduct in response to those acts. Plainly the claim at issue here could not have been adjudicated on the basis of the events, facts, or evidence involved in [the first case]"). *Id.* at 1260. *Greenberg v. Board of Governors of the Fed. Reserve Sys.,* 968 F.2d 164, 168 (2d Cir. 1992) did not construe the effect of a contested adjudication as in this case but rather construed the effect of prior settlements. In *Greenberg,* the later action was for a remedy that categorically differed from the agreed remedies in the prior settlements. The later action sought the debarment of the Greenbergs from the affairs of any federally supervised financial institution. Unlike the later debarment remedy, one of the prior settlements was for a civil monetary penalty which was assessed and suspended on the same day. *Id.* at 169. The penalty covered "only the transactions settled" in the notice and was not given "expansive effect" to "all other transactions investigated along the way," which were not mentioned in the settlement. *Id.*
Regardless of the kind of remedy, the preclusive effect was not an issue decided by the court because the Greenbergs "had not demonstrated that any transactions included in the notices were at issue" in the later debarment proceeding. *Id.* at 169-70. In contrast, Pierce has demonstrated that the "illegal distribution" resulting in $13

Res judicata extinguishes "all rights of the plaintiff to remedies against the defendant with respect to all or any part of the transaction, or series of connected transactions, out of which the [prior] action arose." Restatement § 24(1) (underlined added). The extinguishment applies to the government's overlapping remedies even when granted under separate statutes. *See, e.g., U.S. v. Liquidators of European Fed. Credit Bank in Liquidation*, 630 F.3d 1139, 1151-52 (9th Cir. 2011) (ruling civil forfeiture action final judgment under lower burden of proof precluded government's criminal forfeiture action). Once the government has followed [a] path to final judgment," it is not entitled to "a second bite at the same apple." *Id.* at 1152.

b. All factors in the res judicata test were satisfied.

The Decision correctly concluded the second factor (infringement of the same right) and fourth factor (same transactional nucleus of facts) were satisfied, Decision at 15-16, as the foregoing analysis confirms. Likewise, the third factor (substantially the same evidence) was satisfied by the Division's use of *exactly the same evidence*. Decision at 16.[31]

The first factor is whether the rights or interests established in the prior judgment would be impaired or destroyed by the prosecution of the second case. As to the first factor, the

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million in Lexington stock sale proceeds and $7.5 million claim included in the First Action are also "at issue" in the Second Case. The Division's Brief at p. 15 asserts that *Computer Associates, supra,* is in *accord.* But as explained above, *Computer Associates* fit the jurisdictional impediment exception to claim preclusion, which clearly does not apply here. The Division cites *SEC v First Jersey Secs.,* 101 F.3d 1450, 1463-64 (2d Cir. 1996), but the second case there entailed *unlawful acts that post-dated complaints addressing earlier conduct. Id.* at 1464-65. *Shamrock Assoc. v. Sloane,* 738 F. Supp. 109, 116 (S.D.N.Y. 1990), like *Greenberg*, does not involve identical claims of misconduct, "The two actions are not identical here because they are founded on plaintiff's allegations of different acts by defendants, different types of conduct by defendants and different effects of defendants' acts." *Id.* at 117. *Harris v. Jacobs,* 621 F.2d 341, 344 (9th Cir. 1980) likewise involved two distinct claims. The first was that plaintiff had received deficient medical treatment from prison personnel while the second was that he had been denied a right to consult with non-prison medical professionals at his own expense.

[31] *Adams v. Cal. Dept. of Health Servs.*, 487 F.3d 684, 691 (9th Cir. 2007) (res judicata barred second action where "substantially the same evidence was and would be presented in both actions"). "When a defendant is accused of successive acts, or acts which though occurring over a period of time were substantially of the same sort and similarly motivated, fairness to the defendant as well as the public convenience may require that they be dealt with in the same action. The events constitute but one transaction or connected series." § 24 cmt d ("Successive acts or events as transaction or connected series; considerations of business practice.")

Decision at page 15 misreads the *Chao* decision[32] and erroneously rules that the first factor weighs against the application of res judicata in this case. In the First Case, Pierce sacrificed his appeal rights to earn freedom from liability for the additional $7.5 million disgorgement. Thus, rights for which Pierce paid dearly would be impaired or destroyed by this Second Case. Moreover, Pierce's expenditure of resources litigating the First Case is now duplicated and impaired by the Second Case. Conversely, the Division's interests and rights established in the First Case are neither impaired nor destroyed by protecting Pierce's rights.[33] Indeed, the Division cemented the Commission's disgorgement rights by suing Pierce in court to collect the disgorgement award; and the Commission's rights were satisfied and extinguished when Pierce paid the judgment in the First Case.

VIII. CONCLUSION

The Decision correctly concluded that res judicata applied. As explained in Pierce's Opening Brief, the Decision should not have applied the "fraudulent concealment" exception to res judicata when the allegedly concealed evidence was never actually concealed and instead was obtained and actually used in the First Case. Pierce's res judicata defense is impregnable. The Commission should dismiss all claims for liability against Pierce brought in this Second Case,

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[32] In *Chao*, the prior action was an employer's suit in small claims court against former employees for breach of non-compete agreements including counterclaims asserted by some of the employees. *Chao v. A-One Medical Servs., Inc.*, 346 F.3d 908, 920 (9th Cir. 2003). One employee, Millard, asserted an unsuccessful counterclaim for unpaid overtime. *Id.* The secretary of labor subsequently brought a suit to recover overtime wages for Millard and other former employees. *Id.* at 911, 913-14. The district court ruled res judicata did not bar the second claim for overtime wages for Millard. Id. at 921-22. The Ninth Circuit reversed and ruled the claim was barred. *Id.* at 923. Regarding the second factor in the res judicata test, the Ninth Circuit concluded the "same right" was involved – a claim for overtime wages and the employer had won a right not to pay Millard the overtime wages. For example, if Millard had prevailed, the Secretary of Labor could not have included those wages in its claim. *Id.* at 921-23. Exactly so, if the Division had obtained the additional $7.5 million disgorgement it sought in the First Case, it could not bring this Second Action against Pierce for that same $7.5 million and same cease and desist order against further registration violations.

[33] Therefore, the first factor (impairment/destruction of a right/interest) either weighs in favor of the preclusionary bar or has no effect at all since "it begs the question." *Liquidators of European Fed. Credit Bank in Liquidation*, 630 F.3d at1151 n. 7 (9th Cir. 2011) (first factor ... is unhelpful here because it begs the question).

based on the affirmative defenses of res judicata, equitable and judicial estoppel and waiver, and because no further disgorgement from Pierce is appropriate. Pierce should be awarded all costs including attorney fees incurred to defend the claims brought in this Second Case.

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