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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of MICHAEL BRESNER; RALPH CALABRO; JASON KONNER; and DIMITRIOS KOUTSOUBOS Respondents.	:	ADMINISTRATIVE PROCEEDING FILE NO. 3-15015

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REPLY BRIEF SUBMITTED ON BEHALF OF RESPONDENT JASON KONNER

HUTNER KLARISH LLP
1359 Broadway, Suite 2001
New York, NY 10018
p: 212-391-9235/ f: 212-981-9122

Attorneys for Respondent Jason Konner

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Respondent Jason Konner ("Konner"), by his attorneys, Hutner Klarish LLP, hereby submits his Reply Brief in further support of his contention that the Division of Enforcement (the "Division") has failed to meet its burden of proof and has not established any of the elements of the churning charge against him. In this Reply Brief, Konner addresses only the issues and arguments raised in the Division's Initial Post-Hearing Brief that relate to the charge against him, and will not address the material pertaining to the other respondents.

PRELIMINARY STATEMENT

As it relates to the charge against Jason Konner, the Division's Initial Post-Hearing Brief (cited herein as "Div. Br.") is a well-written, methodical memorandum, but does nothing to advance the cause of justice. It tells barely half the story, ignores whole swaths of evidence, and paints a picture so incomplete that it forces one to ask: "were they at the same hearing?"

In a sense, despite its legal sophistication, the Division's brief presents a startlingly simplistic and one-sided analysis of the evidence. What is presented is not much more than (1) a recap of the quantitative trading data as presented by the Division's so-called expert Louis Dempsey, (2) a myopic view of the testimony and documents concerning Messrs. Miller and Carlson and the relevant factors concerning them, principally their investment objectives and financial condition, and (3) a cursory and shockingly incomplete assessment of the facts that bear upon the issue of broker control over the clients.

With this reply, we will not burden the Court with a repetition of the factual and legal presentation put forth in our initial brief (cited herein as "Konner Br."). Instead, we will focus on the evidentiary and analytical gaps in the Division's brief, and identify the many respects in which it is wrong, incomplete or misleading.

ARGUMENT

I. THE DIVISION'S MISUSE OF THE RECORD, PRINCIPALLY IGNORING REAMS OF CRUCIAL EVIDENCE, DOES NOT SUPPORT THE CHARGE AGAINST KONNER.

Consistent with its entire approach to this four-part case, the Division in its post-hearing brief persists in an effort to establish guilt by association, to try and smear one respondent with information relevant solely to another. Thus, for example, the Division speaks (on pp. 1, 3) of the millions of dollars lost by the customers of the three broker-respondents; however, Konner's two customers in combination actually were profitable during the so-called "churn period."[1] Further, the Division speaks (on p. 2) of $720,000 in commissions and fees paid *collectively* by the customers from California, Louisiana, Iowa, North Carolina and Mississippi; however, Konner's commissions represented just 10.8% of that amount. Indeed, the Division's brief in numerous instances offers group characterizations purportedly applicable to all seven of the customers involved in the case, when plainly it is misleading to ascribe many of those remarks to Messrs. Carlson or Miller.

While perhaps advocacy excuses the excesses inherent in that group-guilt approach, in an enforcement proceeding such as this it surely does not authorize the representatives of the U.S. Securities and Exchange Commission to simply ignore the mass of evidence – largely provided in admissions from the Division's own witnesses – which undermines many of the assertions made in support of the charge against Jason Konner. The principal purpose of this reply brief, then, is to highlight for the Court's edification how the Division willfully turned a blind eye, and in so doing did a disservice to the parties and to the Court.

[1] Division expert Louis Dempsey testified that Miller's net loss inclusive of commissions was approximately $80,000. Then, as made clear during Dempsey's cross-examination, Carlson had a net gain during the relevant period inclusive of commission in excess of $100,000, owing to the $175,000 gain on the Quantum investment he made but which was improperly recorded in Dempsey's report. Added together, there is a combined profit not a loss.

A. The Division's analysis of the evidence relating to Gordon Miller is woefully deficient, and fails to substantiate the charge against Konner.

As expected, the Division began its discussion regarding Mr. Miller by noting his long history as an Iowa farmer. It then proceeds to summarize at face value his direct testimony elicited by Division counsel. See Div. Br. at 29-32. In so doing, the Division ignores the following evidence provided either by Mr. Miller on cross or which Mr. Miller did not contest or dispute:

- Miller's admissions regarding his extensive history of speculative trading in commodities, before during and after the time that he had a working relationship with Konner. See Tr. 2001-04, 2082-87, 2128.
- Miller's admissions regarding his knowledge of what speculative investments are, and of his willingness to make speculative investments. See Tr. 2003-05, 2011-12, 2018-24, 2130.
- Miller's admissions about *his analysis* of why in 2009 he was willing to invest aggressively in the stock market, believing (based on what he had independently read) that the market decline had leveled off and that there was a good opportunity to make money in stocks. See Tr. 2010-12.
- Miller's admissions regarding his multiple sources of income, and about how his living expenses are covered by just one of his many streams of income. See Tr. 1980-83, 2097.
- Miller's admissions regarding his ability to pay for all of his stock purchases with funds in his checking account. See Tr. 2046-47. (Indeed, despite writing multiple checks for tens of thousands of dollars, see Ex. Konner-10, and admitting on cross that the account was not used for living expenses, the Division still quoted Miller's testimony that he "did not have large sums of loose cash for stock trading." Div. Br. at 58, quoting Tr. 1932. Plainly, that direct testimony was undermined by Miller's indisputable actions and other testimony about those funds, all ignored by the Division.)
- Miller's admissions regarding his rejection of Konner's recommendations that he make conservative investments to anchor the account during a turbulent period. See Tr. 2087-89.
- Miller's admissions regarding his multi-million dollar net worth, the fact that his home is not included in his calculation of net worth, and that the land that he owns which is farmed (by others) is not needed to support him. See Tr. 1968-72, 1976-77, 2046-47.

- Miller's admissions regarding the speculative stock investments that he made with brokers other than Konner (involving $140,000 or more). See Tr. 2080.

- Miller's admissions about never complaining, and about remaining at JP Turner through the present day with an account holding speculative stock investments. See Tr. 2077-78, 2081.

- Miller's admissions that while correcting his new account form, he specifically left unchanged and in fact acknowledged with his initials the aggressive investment objectives and his high net worth information recorded on the form. See Tr. 2009; 2023-24.

- Miller's admissions that he was well aware of his account activity (evidenced from receipt of multiple categories of documents, of remitting significant payments to acquire stock, etc.). See Tr. 2025, 2028, 2033, 2044-46, 2052-53, 2060-62, 2066, 2069.

- The fact that the funds sent to JP Turner represented a small fraction of his actual net worth. See Tr. 0437, 0447.

- And much, much more. (See Konner Br. at 6-16.)

Had any attempt been made to come to terms with the entirety of Miller's testimony (i.e., his unscripted answers to questions on cross-examination), the Division would not have been able to put forward such a cursory, simplistic and misleading summary of the evidence relating to this customer.

B. <u>The Division's analysis of the evidence relating to James Carlson is woefully deficient, and fails to substantiate the charge against Konner.</u>

Nor was the Division's presentation of the evidence relating to Mr. Carlson any better. Once again, as expected, the Division began its discussion regarding Mr. Carlson by noting his decades of experience as an Iowa farmer, and then proceeds to summarize at face value the direct testimony elicited by Division counsel: Mr. Carlson was an unsophisticated investor who lacked the intent and financial wherewithal to speculate with his investment funds. (Div. Br. at 24-28.) In so doing, the Division ignores the following evidence provided either by Mr. Carlson on cross or which Mr. Carlson did not contest or dispute:

- Carlson's admissions regarding his safe and conservatively held retirement account, which he was careful to distinguish from the money he sent to JP Turner for more aggressive investments. See Tr. 1658-61, 1671, 1697, 1747-57.

- Carlson's admissions that he decided against putting more money with the brokers who managed his retirement account or his other conservative account, the reason being that he wanted to go for something that had the potential for a big payoff. See Tr. 1754-56, 1672-75, 1918-19.

- Carlson's admissions regarding how his word is his bond, and when he signed his name to a legal document, it meant something and he expected that people would rely on it. See Tr. 1829-30. This testimony repudiated the Division's efforts to undermine the documents containing information about investment objectives and financial information that Carlson had completed, signed and initialed.

- Carlson's admissions that he independently developed investment ideas. See Tr. 1749-50. The testimony that he rejected conservative investment ideas presented by Konner (Tr. 4379-82) also was never rebutted.

- Carlson's admissions that he was not unhappy with how Konner handled his account, and the fact that he remained a client of Konner or JP Turner for many years after the so-called "churn period" notwithstanding multiple disclosures of the full extent of account activity. See Tr. 1758.

- Carlson's admissions that he was well aware of the activity in his account (as even conceded by the Division's supervision expert John Pinto) including the turnover of his money and the aggressive trading. See Tr. 1778-79, 1787-88, 1855-63.

- Carlson's admissions that he was well aware of the commissions being charged, on both principal (markup/markdown) and agency trades, and he acknowledged that he continued to fund the account with new money even with that knowledge. See Tr. 1867-68, 1832-48, 1807-08.

- And much, much more. (See Konner Br. at 16-24.)

In effect, the Division takes the position that virtually all of the information appearing on all of the documents prepared for Carlson's signature (but only information about his objectives and net worth) was wrong, and any form that he personally completed was also wrong, having been told that whatever he wrote simply did not matter. In other words, the entire documentary record relating to James Carlson is to be disregarded, because Carlson – a witness who was led to believe he had a financial interest in the Division winning its case – on direct stated that Konner told him to "write whatever – it doesn't matter," even though Konner explained exactly what that meant: write whatever you want, we just need to know what the actual numbers are. See Konner Br. at 21 n. 10 (Konner testimony also corroborated by John Williams who never heard of any instance of Konner inducing a client to provide false information; no customer prior to the hearing in this case even insinuated as much).[2]

C. The Division's analysis of the evidence ignores crucial testimony from non-party witness John Williams.

While the Division embraces the direct testimony of Miller and Carlson – witnesses they met in advance that Division counsel spent hours preparing to testify[3] -- they altogether discounted the testimony of another non-party, former JP Turner on-site Compliance officer John Williams. Williams, on the Division's own witness list though ultimately called by respondent Bresner, testified about Jason Konner and his work ethic and the two customers. Thus, while we hear that Konner "was a great salesman" and was "pushy," the Division gave no voice to the fact that no customer ever complained about Konner's practices, actions or ethics, and that Williams testified under oath that, despite their close physical proximity at the office, he never observed

[2] It is comical that in the face of overwhelming documentation and Carlson's admission that he stands by what he signed, the Division could say that "Carlson never told anyone at JP Turner that his investment objectives were speculation or short-term trading." Div. Br. at 27. Cases establishing that customers cannot disavow their written representations have also been brought to the Court's attention. See Koutsoubos Post-Hearing Br. at 32.

Analogously, regarding Mr. Miller, the Division not only misstated his testimony about not having other brokerage accounts (Div. Br. at 29; compare Tr. 1826), they fail to acknowledge that Mr. Miller admitted having another account and to making a direct investment in stocks, all having nothing to do with JP Turner or Jason Konner. See Tr. 2081-82, 2086-87.

[3] While the undersigned would be pleased to take credit for effective cross-examination, the undeniable fact is that Mr. Miller and Mr. Carlson, once they got off the script prepared by the Division for their direct testimony, opened up and told a very different story when presented with contemporaneous documents and other information regarding their own actions. Such a turnaround demonstrates how the direct testimony elicited by the Division is circumspect if at all credible. In that context, the references to alleged unauthorized trading (see Div. Br. at 28, 63) from a witness who often had recall problems merit little discussion. Not only did Konner emphatically reject this insinuation (Tr. at 4404-05), but Carlson never complained about this and notwithstanding its long and extensive investigation, the Division never alleged or charged such conduct, and surely would have if there was evidence to support it.

Konner to have acted in an unethical fashion or in an over-the-top way in dealing with his customers. Tr. 3665-66, 3668-70.

Williams was an important witness, and he corroborated the importance of the documents signed by Miller and Carlson acknowledging investment objectives and financial condition, and in fact emphasized the system designed at JP Turner to ensure that the information was presented clearly to the customer and expressly acknowledged by the customer. Though a plainly independent voice, because his testimony was not consistent with the testimony of the witnesses that the Division had the opportunity to prepare, the Division simply ignored him.

Thus, no effort is made to distinguish the fact that Williams confirmed with Carlson (and made the appropriate correction or notation on the form) that his net worth was $2 million. That inconvenient fact for the Division's attempt to downplay Carlson's net worth, or at least the facts that he repeatedly represented as the truth to multiple JP Turner personnel, is just ignored. The Division fails to acknowledge that Williams reviewed documents which were signed, completed and/or initialed by Carlson and Miller over a multi-year period, all of which substantiated Konner's understanding that they were suitable clients for Konner's aggressive investing approach. Indeed, the fact that Carlson had an opportunity to speak with compliance/ management about the "erroneous" information or about the high level of trading in his account yet felt no need to complain or inquire, was ignored by the Division. See Tr. 3704-05.

D. <u>The Division's conclusions regarding the metrics of excessive trading and indicia of broker control are unsupportable.</u>

Only with its skewed factual analysis could the Division support the conclusions set forth in the sections entitled "Expert Findings" on the Miller Account and the Carlson Account regarding turnover ratio and the cost-equity factor (Div. Br. at 28, 32-33). A fair assessment of the evidence leads inexorably to the conclusion, as the case law cited by Konner, the other respondents, *and the Division itself* makes clear, that there are no established benchmarks for the metrics used to assess excessive trading where the account is intended to be not a conservative one but one designed as an aggressively traded account.[4]

Similarly, the Division recites a partial list of factors relevant to the issue of broker control, but with nothing approaching a critical assessment of the evidence. Div. Br. at 61-63. In effect, they rely principally on basic facts that to a greater or lesser extent characterize the vast majority of broker-client relationships: broker makes and customer accepts recommendations; customers trust and rely upon their brokers; customers do not do independent research and rely on brokers for information. These common characteristics of the relationship are then garnished with generic statements that the customers lack the ability to manage their accounts and with facts which are plainly wrong (for example, that Miller never had another brokerage account, when the record indicates he had at least one other, and also purchased stock directly from an issuer). The clear weight of the evidence establishes that these men, far from being led down a treacherous path by a sinister broker, knew what they wanted with the portion of their money placed at JP Turner, and what they wanted was compatible with the facts and circumstances of their lives.

Indeed, the cases cited by the Division regarding control, see Div. Br. at 60-61, do not present a fair assessment of the law on this issue, and the argument unduly presumes that Miller and Carlson – despite the vast amount of evidence to the contrary – were utterly incapable of making a rational decision to place a small portion of their assets in an aggressive trading account in the hope that they could do better there than in the accounts handled by their more

[4] See *infra* at 10-12; Konner Br. at 30-32; Calabro Post-Hearing Br. at 21-22 & fn. 13; Koutsoubos Post-Hearing Br. at 33 (all detailing discussion of case law regarding importance of investment objectives in determining appropriate benchmarks for evaluating excessive trading).

conservative brokers. That conclusion is not supported by the evidence adduced at the hearing.

E. <u>The Division ignored critical admissions and errors made by its own expert witness, Louis Dempsey.</u>

What is perhaps the most egregious part of the evidence ignored by the Division, arguably unforgiveable even in this adversarial context, is the obvious error in Mr. Dempsey's "expert" report relating to the Carlson account. As became evident during the course of the hearing, the so-called independent expert Dempsey merely went along with the report generated by SEC staff. That report purported to set forth the performance of the Carlson account during the so-called "churn period." However, on cross-examination, it was pointed out that $175,000 of the amount calculated by Dempsey to be the funds invested by Carlson was actually investment profit derived from the appreciation in value of the Quantum PIPE offering stock. And once that error is acknowledged, Carlson's $54,000 loss reported by Dempsey (and his handlers) turns out to be a profit of $100,000. Tr. 3176-84; see Konner Br. at 29. The failure to acknowledge this, we respectfully submit, undermines the Division's credibility here and more broadly. We would expect more, and believe we are entitled to more, from the representatives of the U.S. Securities and Exchange Commission.

A further example of the Division's selective use of the evidence brought out during Mr. Dempsey's testimony pertains to his admissions (utterly ignored by the Division) that there are no established benchmarks for turnover ratio and the cost-equity factor in accounts that are intended as aggressive short-term trading accounts. Tr. 3201-03. Despite this, the Division nonetheless relies on, without justification, explanation or authority, the benchmarks often used in evaluating activity for traditional accounts with conservative investment objectives.

The Division also persists in using Dempsey's testimony far beyond what even he conceded were his limits. It is thus no surprise that for both Carlson and Miller, the Division states that Dempsey had offered an opinion about broker control (Div. Br. at 28, 33), when Dempsey expressly said he had no opinion about that non-quantitative issue. (Tr. 3160-61.)

* * *

In sum, the Division's brief ignores much, and takes many liberties with the evidence. We respectfully submit that the evidence ignored, a sampling of which is presented above, demonstrates that the arguments made by the Division are weak and certainly fail to reflect anything resembling a dispassionate take on the record as a whole. And with respect to the numerous mischaracterizations of the evidence in the Division's brief, we further submit that they were largely anticipated in our initial brief, and would refer the Court to that document rather than repeat on reply what was stated there.

II. THE CASES RELIED UPON BY THE DIVISION INVOLVE BROKERAGE CUSTOMERS WHOSE CIRCUMSTANCES AND OBJECTIVES ARE MARKEDLY DIFFERENT FROM WHAT IS PRESENTED HERE REGARDING MILLER AND CARLSON AND AS SUCH ARE DISTINGUISHABLE.

In its brief, the Division states without qualification that a turnover ratio in excess of six and a 20% cost-to-equity ratio are generally presumed to reflect excessive trading. However, the Division in its argument ignores a crucial distinction not missed in the cases which it cites where the so-called benchmarks were referenced: context matters and "there is no clear line of demarcation" regarding turnover ratio and quantitative metrics. *Mihara v. Dean Witter & Co.*, 619 F.2d 814, 821 (9th Cir. 1980).

In fact, the cases relied upon by the Division all make one thing quite clear: the context and the circumstances of the customers in question and their accounts are paramount. Thus, in *In re Sage Advisory Services*, Exchange Act Release No. 44600, 2001 SEC LEXIS 1482 (July 27, 2001), the Commission stated that the standard quantitative metrics relied upon were useful in the context of "a conservative account." Consistent with that, in *In re Sandra Simpson*, Exchange

Act Release No. 45923, 2002 SEC LEXIS 1278 (May 14, 2002), it was held by the Commission that "all of the customers involved in this case were conservative investors," and that the activity there was excessive "[i]n light of the situation and financial goals of these customers," because suitability must be evaluated "in terms of the investor's financial situation, tolerance for risk, and investment objectives." And *In re Laurie Jones Canady*, Exchange Act Release No. 41250, 1999 SEC LEXIS 669 (Apr. 5, 1999), the Commission stated that "no single test determines whether a broker churned an account" and that the metrics typically cited revealed trading that was excessive "[i]n light of these customers' conservative investment objectives."

Profoundly different circumstances abound in the cases relied upon by the Division. For example, in *Mihara,* the plaintiff was not an accredited investor, had less than $50,000 in savings, and was worried about funding the education and ensuring the financial security of his two young daughters. Id. at 817. In another case cited by the Division, *Franks v. Cavanaugh,* 711 F. Supp. 1186, 1188 (S.D.N.Y. 1989), the plaintiff "was nearing retirement age and was interested in income safety...[and sought out a] conservative investment portfolio, existing solely of tax-free municipal bonds." And in the *Canady* case, *supra*, "none of these customers, all of whom were widows and, in the case of two of the three, elderly, had any meaningful knowledge of or experience with securities matters." The metrics used in such cases are inapposite here, but in failing to acknowledge the differences, the Division mischaracterizes those cases and their relevance to the instant case.[5]

[5] The Division also cited *Arceneaux v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 767 F.2d 1498 (11th Cir. 1985), but in that case the court decided to let stand a jury verdict, and did not offer any analysis of the issues. Other cases regarding the use of benchmark figures that the Division relies upon involve conservative account objectives or accounts where preservation of capital was paramount. *See, e.g., Costello v. Oppenheimer & Co.*, Inc., 711 F.2d 1361, 1368 (7th Cir. 1983) (broker had discretion over account whose owner was "primarily concerned with preserving capital"); *Cruse v. Equitable Securities of New York, Inc.*, 687 F. Supp. 1023, 1030 (S.D.N.Y. 1987) (on 12(b) motion to dismiss, court noted allegation regarding account with "conservative investment objective").

The cases cited by the Division cannot help but highlight that the facts pertaining to Mr. Miller and Mr. Carlson present a real stretch, and that the Division is trying to fit a square peg into a round hole. In contrast to the customers in the cited cases, the facts here are very, very different: speculative investors, wealthy men looking to make significant profits, investors with the ability to invest aggressively with excess cash not needed to sustain them, customers who had repeatedly acknowledged in writing that they had aggressive investment objectives and a high level of risk tolerance, and so forth. These distinctions explain why the cases do not speak to benchmarks in a case like this one, because facts like these do not present a case for churning.

III. THE SANCTIONS PROPOSED BY THE DIVISION ARE DISPROPORTIONATE TO THE CONDUCT IN QUESTION.

Respondent Konner respectfully submits that the totality of the evidence, even when viewed in a light most favorable to the position advanced by the Division, presents at worst a very close case. Miller and Carlson never (ever) complained, despite full knowledge of what was going on, there was much to suggest that they were on board with the aggressive approach, and while they lost money, they were not unduly harmed. Further, Konner plainly worked hard for his clients and has had a spotless career to date showing that his hard work has left many people happy or at least satisfied, and so on. In this light, we note that even in cases cited by the Division where the Commission evaluated the issue of aggressive trading vs. excessive trading and the conduct at issue was palpably worse, see *In the Matter of Shearson Lehman Hutton, Inc.*, Exchange Act Release No. 26766, 1989 SEC LEXIS 778 (Apr. 28, 1989); *In re Michael David Sweeney*, Exchange Act Release No. 29884, 1991 SEC LEXIS 2455 (Oct. 30, 1991), the sanctions were far less severe than what has been proposed here.

In *Shearson*, the Commission affirmed a censure and $3,000 fine, and in *Sweeney*, the Commission affirmed a censure, a $5,000 fine and disgorgement, even though the objectives of the three modest clients (two of whom were elderly widows) were "basic, secure investment" that would generate much-needed income for retirement, with no interest in speculation. Obviously, such sanctions – in cases entailing much greater harm and misconduct – are a far cry from the career-ending bar that the Division seeks here.[6]

Were this Court to find against Konner, it would be a miscarriage of justice to impose the sanctions proposed by the Division. Any potential sanctions against Konner should be considered based only on the record as it relates to him (and not the other respondents, much as the Division tries to join them at the hip), and based on that (and the record regarding Konner's financial inability to pay), the proposed civil penalty, amount of disgorgement, and bar are grossly unwarranted.

CONCLUSION

Despite the significant resources expended by the Division in its case against Konner (and the other three respondents), it was not established that Konner churned the Miller or Carlson account. The decision to bring a case against him, the performance at hearing, and the Division's brief all suffer from the same failings: the failure to consider the evidence as a whole, the failure to get beyond the superficial level of what the evidence proved and represented, the failure to even try to be even-handed. We respectfully submit that an objective assessment of

[6] In *Shearson*, the Commission also left undisturbed the finding that the broker did not act with intent, where the broker who had actual control (it was a discretionary account) was handling an account that the customer wanted to be aggressively invested. And in *Sweeney*, in affirming disgorgement of approximately $15,000 in commissions, the Commission indicated that whether the customer incurred a loss should be taken into account, and as noted previously, a proper accounting for Mr. Carlson indicates that his account (including his Quantum investment) had a net gain during the relevant period.

Konner's business, and of his dealings with Messrs. Miller and Gordon, leads to but one conclusion, and that is dismissal of the churning charge against Jason Konner.

Dated: New York, New York
May 10, 2013

HUTNER KLARISH LLP
1359 Broadway, Suite 2001
New York, NY 10018
p: 212-391-9235/ f: 212-981-9122
ehutner@hutnerklarish.com

By: ______________________
Eric S. Hutner

Attorneys for Respondent Jason Konner