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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
FILE NO. 3-15124

DAVID F. BANDIMERE and JOHN O. YOUNG	:

OPENING BRIEF OF RESPONDENT DAVID F. BANDIMERE

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Respondent David F. Bandimere, through his attorneys, Davis Graham & Stubbs LLP, under SEC Rule of Practice 450, submits this brief.

I. INTRODUCTION AND BACKGROUND

David Bandimere was duped in two related Ponzi schemes; he was targeted as an early investor in those fraudulent schemes, and realized high returns. Predictably, he shared his success with family members and friends who then invested. Although providing high returns to a respected figure, who informs others of the opportunity, is a ploy frequently used by Ponzi operators,[1] an administrative proceeding was initiated against Mr. Bandimere.

The Order Instituting Proceedings ("OIP") named Mr. Bandimere and John O. Young.[2] The OIP alleged that Mr. Bandimere described IV Capital and UCR ". . . in a materially positive way . . ." but failed to disclose ". . . material red flags and negative facts." "Moreover, Bandimere acted recklessly in selling these investments because these red flags should have alerted Bandimere that IV Capital and UCR were likely frauds." OIP II.A.2. The OIP identified 15 "red flags," OIP II.E.35.a-o, and alleged "[t]hese numerous material red flags and negative facts . . . should have alerted Bandimere to the fact that IV Capital and UCR were likely frauds. Bandimere recklessly ignored these obvious signs of fraud." OIP II.E.36. The OIP alleged that Mr. Bandimere assured investors ". . . that the investments were 'low risk' and 'very good investments.'" *Id.*

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[1] *See*, Speech by SEC Commissioner Luis A. Aguilar, "Combating Securities Fraud at Home and Abroad," Third Annual Fraud and Forensic Accounting Education Conference, Atlanta, Georgia, May 28, 2009; "Affinity Fraud," posted on the SEC website www.sec.gov last changed September 6, 2006; SEC Investor Bulletin: Affinity Fraud, posted on the SEC website, September, 2012.

[2] Young consented to the entry of an order on liability. An Initial Decision on sanctions was issued by the law judge on October 4, 2013, and was declared final on November 22, 2013.

Mr. Bandimere moved for a more definite statement, which was granted in part.[3] The law judge required the Division to identify the individuals which it claimed were defrauded, identify when Mr. Bandimere made misrepresentations, and when Mr. Bandimere learned of the facts which the Division alleges should have been disclosed.

Mr. Bandimere's efforts to get information relevant to his defense, including documents relevant to his affirmative defense of a denial of equal protection, were rebuffed. The law judge sustained the Division's objections based on privilege, work product, and undue burden without requiring even minimal support for its objections. Order on Motion to Quash, February 5, 2013.

An evidentiary hearing was held in Denver, Colorado over five days, concluding on May 2, 2013. Twelve fact witnesses and one expert testified. The transcript of proceedings exceeded 1,300 pages, and 145 exhibits were introduced.

The law judge issued an 89 page Initial Decision (the " I.D.") on October 8, 2013, finding that Mr. Bandimere willfully violated Sections 5(a) and 5(c) of the Securities Act of 1933 (the "Securities Act"), willfully violated Section 15(a) of the Securities Exchange Act of 1934 (the "Exchange Act"), and willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5.[4] The law judge imposed "severe" sanctions of a cease and desist order, a full associational bar, a $390,000 civil penalty, and ordered disgorgement of $638,056.33, with interest accruing from February 1, 2010. He concluded that all the violations alleged in the OIP had been proved, except for scheme liability under Section 17(a)(1) and (3) and Rule 10b-5(a) and (c), which the Division disclaimed, and violations of Section 206(4) of the Advisers Act, and Advisers Act Rule 206(4)-8, which the Division

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[3] Mr. Bandimere's request that the Division identify the statements rendered misleading by the omissions was denied.

[4] The Division did not pursue claims of scheme liability. I.D. 56, n.39. Therefore Section 17(a)(2) of the Securities Act and Rule 10b-5(b) are the only anti-fraud provision at issue.

conceded were not proved. Division Post-Hearing Brief, p. 14, n.2. Mr. Bandimere challenges all findings of violation and all sanctions.

Although the law judge found all the violations alleged, he did not find that the Division proved the facts alleged in the OIP which resulted in those violations. The law judge found that the Division failed to prove that Mr. Bandimere knew, or should have known, IV Capital or UCR were Ponzi schemes. I.D. 79. That finding is not challenged. The law judge found that Mr. Bandimere defrauded six investors who testified at the hearing, Moravec, Blackford, Loebe, Davis, Koch, and Radke. The law judge did not find that any other investors had been defrauded. I.D. 63-75. Mr. Bandimere challenges the finding that any investors had been defrauded, but does not challenge the law judge's finding the Division failed to prove that any other investors had been defrauded.

The law judge found further that the Division failed to prove certain allegations that Mr. Bandimere knew of "red flags" or that the "red flags" were facts. I.D. 65-75. Mr. Bandimere does not challenge these findings, except for the finding the Division proved the allegations in OIP II.E.35.l as to Loebe.

Mr. Bandimere filed a Petition for Review which the Commission granted on January 16, 2014.

II. RELEVANT FACTS

David Bandimere is 68 years old, is married, and has children and grandchildren. He spent his professional life working in his family's automotive businesses. He is a devout Christian, and has been active in the Denver faith-based community. Tr. 1185-7; I.D. 6.

Mr. Bandimere sold his interest in the family businesses to his brother in 2004, which, for the first time, provided him with significant cash available for investment. One person he spoke

with about how to invest this cash was Richard Dalton, a friend for approximately 30 years, who he met through church, and with whom he served on the board of a local ministry. I.D. 5

With Dalton as a friend, Mr. Bandimere needed no enemies. Dalton introduced Mr. Bandimere to Larry Michael Parrish, who ran IV Capital, which purported to return approximately 2% per month. On the recommendation of Dalton (who said he was working with Parrish), Mr. Bandimere invested $100,000 with IV Capital in December, 2005, and an additional $100,000 in March, 2006. I.D. 5.

The investment performed as represented. Over time, Mr. Bandimere mentioned the success he had enjoyed in IV Capital to family members and a few friends, who asked to participate. Mr. Bandimere allowed them to do so through his account. I.D. 5-6.

One of those friends was Cameron Syke, a lawyer and accountant, and former stockbroker. Tr. 718; 738; 781-2. Syke and Mr. Bandimere were friends through faith-based humanitarian activities, and were board members of Global Connections International, ("GCI"), a Christian humanitarian group. Mr. Bandimere identified IV Capital as a possible investment for GCI during a board discussion about where GCI might put its funds. Tr. 723-5. Syke conducted due diligence on IV Capital as a possible investment, both for GCI and himself personally. Because of Syke's review, both GCI and Syke invested in IV Capital through Mr. Bandimere's account.[5] I.D. 7-8; Tr. 775-6; 786-8.

By the middle of 2007, Syke decided to offer IV Capital to his friends and family. He created Exito, LLC ("Exito"), which he co-managed with Mr. Bandimere, as a vehicle through which investors could participate in IV Capital. I.D. 7-8. Syke prepared the Exito Operating Agreement, which provided he and Mr. Bandimere would receive compensation for managing

[5] GCI required that Mr. Bandimere personally guaranty its investment in IV Capital. Mr. Bandimere satisfied that guaranty when IV Capital collapsed. Exh. 200 and 201.

Exito. Significant management services were provided. Mr. Bandimere (and his wife) performed substantial bookkeeping and other administrative services for Exito, and Syke provided tax and legal advice. I.D. 8-11; Tr. 742-3. The management fee was paid by Parrish, and was 10% of the profits earned by Exito members. Syke testified he believed that fee to be "relatively small." Tr. 745.

Syke also advised Mr. Bandimere about the legalities of their activities. He told Mr. Bandimere that investor funds should not be commingled in his personal account, but that a limited liability company ("LLC") should be formed as a vehicle. Tr. 735. He also advised Mr. Bandimere that unregistered interests in LLCs could be offered and sold legally under an exemption for non-public offerings, which, he explained, could not involve a general solicitation and must be limited to a few investors. Tr. 734-6.

Syke's advice missed two critical issues. First, while Syke recognized an exemption was needed for the sale of unregistered interests in an LLC, he missed the issue that IV Capital could be considered an investment contract which would itself need an exemption from registration. Tr. 804-5.

Syke also did not recognize that bringing investments to the attention of others and receiving compensation related to the amount invested might fall within the definition of a "broker" and create liability under Section 15(a) of the Exchange Act. Tr. 800-802.

Syke prepared an operating agreement for Victoria Investors, LLC ("Victoria") virtually identical with the operating agreement for Exito. Tr. 746. Victoria, which was managed by Mr. Bandimere, was a vehicle for involvement in IV Capital for those people who had invested in IV Capital through Mr. Bandimere's personal account. Over time, other friends of Mr. Bandimere, or people referred to Mr. Bandimere, invested through Victoria. Victoria

received from Parrish the same management fee for services performed for Victoria as was provided to Exito.

About the time that Exito and Victoria were established in 2007, Dalton ended his relationship with Parrish and IV Capital. About a year later, Dalton approached Mr. Bandimere with a note trading program conducted by a trader in Singapore which he was providing through an entity called Universal Consulting Resources ("UCR"). I.D. 8. Later, Dalton introduced Mr. Bandimere to a program where investors financed the purchase of diamonds in Africa, which were to be resold in the United States or Europe. Mr. Bandimere invested heavily in both UCR programs, and brought them to the attention of his friends and family, including Syke, some of whom invested. Dalton paid the LLCs a management fee of 2% of invested funds per month.

Both IV Capital and UCR were Ponzi schemes. IV Capital paid returns until May, 2009. Mr. Bandimere and Syke brought Parrish's scheme to the attention of the Division, and provided documentation supporting the fraud. The SEC brought an enforcement action against Parrish in 2012 in which he defaulted. Parrish also has pled guilty to criminal charges, and is serving a 9 year sentence.

UCR paid returns until March, 2010. Dalton also was sued by the SEC and defaulted. Dalton and his wife pled guilty to criminal charges and are serving sentences of 120 months and 60 months, respectively.

The investors in both IV Capital and UCR, including Mr. Bandimere, lost their investments, except to the extent that they had received payments during the life of the schemes.

III. MR. BANDIMERE DID NOT COMMIT SECURITIES FRAUD

A. Legal Standards.

The Division's burden of proof for all its claims is preponderance of the evidence. *Steadman v. SEC*, 450 U.S. 91, 1004-5 (1981).

Violations of Section 10(b) of the Exchange Act and Rule 10b-5(b) based on misrepresentations require proof of 1) a misrepresentation of material fact; 2) in connection with the purchase or sale of a security; 3) with *scienter*; and 4) use of the jurisdictional means. *Dolphin and Bradbury v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008); *SEC v. Wolfson*, 539 F.3d 1249, 1256-7 (10th Cir. 2008). Where a misrepresentation is by omission, the omission must be of ". . . a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, ..." Rule 10b-5(b).

For an omitted fact to be material there must be a substantial likelihood that disclosure of the omitted fact would have been viewed by a reasonable investor as significantly altering the total mix of information made available. *Zacharias v. SEC*, 569 F.3d 458, 468 (D.C. Cir. 2009) *citing Basic v. Levinson*, 485 U.S. 224, 231-2 (1988).

Scienter is "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). *Scienter* is a prerequisite to a finding of liability on claims alleging violation of Rule 10b-5. *SEC v. Wolfson*, 539 F.3d at 1256-7; *Dolphin and Bradbury v. SEC*, 512 F.3d at 639.

The Courts of Appeal hold that *scienter* can be established by proof of extreme recklessness. *Dolphin and Bradbury*, 512 F.3d at 639.[6] Recklessness is extreme conduct, more egregious than "white heart/empty head" good faith. *SEC v. Platforms Wireless Intrn'l Corp.*, 617 F.3d 1072, 1093 (9th Cir. 2010). Whether a person has acted recklessly has both a subjective and objective component. *Id.* Recklessness means that the propensity to mislead was so obvious that the actor must have known it.

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[6] The Supreme Court has not yet accepted that recklessness satisfies the *scienter* element. Mr. Bandimere's position is that it does not, and that proof of actual intent is required. However, Mr. Bandimere recognizes that recklessness suffices in the District of Columbia Circuit and the Tenth Circuit, and, without waiver of his position, addresses the recklessness standard.

Where fraud is alleged by omissions of material fact, *scienter* is established by proof that the defendant knew (or was reckless in not knowing) of the existence of undisclosed facts and that failing to disclose the fact would mislead. *City of Philadelphia v. Fleming Companies, Inc.*, 264 F.3d 1245, 1261 (10th Cir. 2001); *Dolphin and Bradbury, Inc.*, 512 F.3d at 639.

The elements of a fraud claim based on misrepresentations under Section 17(a)(2) of the Securities Act are essentially the same as for Rule 10b-5(b), although a violation of Section 17(a)(2) can be established through negligence. *SEC v. Wolfson, id.* Violating Section 17(a)(2) also requires proof that Mr. Bandimere ". . . obtain money or property . . ." by means of a misrepresentation. *SEC v. Syron,* 934 F.Supp.2d 609, 637 (S.D.N.Y. 2013).

B. Mr. Bandimere Made No Affirmative Misrepresentations

The only specific representations attributed to Mr. Bandimere in the OIP are that he told investors the investments were "low risk" and "very good investments." OIP II.E.36 (quotations in the original). There is no evidence he made either of those representations. The law judge did not find that Mr. Bandimere made these statements. Since the Division did not prove Mr. Bandimere made these statements and any violation dependent on those statements must fail.

C. Mr. Bandimere Made No Misrepresentations by Omission

Omissions of a material fact are actionable only where the omitted fact is necessary to make statements made, in light of the circumstances under which they were made, not misleading. *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1321-22 (2011) ("Rule 10b-5 do[es] not create an affirmative duty to disclose any and all material information."). That means that the omission ". . . alters the meaning of the statement . . ." that was made. *McDonald v. Kinder-Morgan, Inc.,* 287 F.3d 992, 998 (10th Cir. 2002). An omission is not actionable because a reasonable investor might want to know the omitted fact. *Kleinman v. Elan Corp., PLC*, 706 F.3d 145, 153 (2d. Cir. 2013); *SEC v. St. Anselm Exploration Co.*, 2013 WL 1313765,

at *11 (D. Colo. Mar. 29, 2013); *Richman v. Goldman Sachs Group*, 868 F.Supp.2d 261, 273-4 (S.D.N.Y. 2012). Nor is an incomplete statement necessarily misleading. *Brody v. Transitional Hospitals Corp.*, 280 F.3d 997, 1006 (9th Cir. 2002).

The OIP alleged, the Division argued, and the law judge found, that Mr. Bandimere violated Section 17(a)(2) and Rule 10b-5(b) by presenting a one-sided and unbalanced view of the investments. Particular statements constituting the alleged one-sided or unbalanced view were not identified in the OIP, the Division's more definite statement, or in the I.D.

The law judge stated "Bandimere's disclosure of positive information about the investments was rendered materially misleading in light of his failure to disclose other material facts to investors," without identifying any positive information that was rendered misleading, and without identifying any omitted material fact or facts which caused any particular statement to be misleading. I.D. 59. Violations of Section 17(a)(2) or Rule 10b-5(b) cannot be established without proof that a statement was made and was rendered misleading by failing to disclose a material fact. *E.g., Brody,* 280 F.3d at 1006; *Schlifke v. Seafirst Corp.,* 866 F.2d 935, 944-5, and n.11 (7th Cir. 1989). That proof is absent here.

None of the investors called by the Division had a clear recollection of Mr. Bandimere's statements regarding the investments (if he made any at all), apart from the returns that had been paid. Tr. 155-7; 160-162; 182-4; 189; 289-90; 303-5; 439-40; 448-9; 522-3; 527-8; 581-2; 584-5; 645; 669-70. There are no allegations, and no evidence, that Mr. Bandimere misrepresented those returns. The accurate disclosure of historical financial results is not rendered misleading by failing to disclose facts which may raise questions about whether similar results will be achieved; reasonable investors do not believe that historical success connotes the absence of potential problems that could affect future success. *Findwhat Investors Group v. Findwhat.com,*

658 F.3d 1282, 1306 (11th Cir. 2011); *In re Advanta Corp. Sec. Lit.*, 180 F.3d 525, 538 (3d Cir. 1999) (abrogated on other grounds); *Serabian v. Amoskeag Bankshares, Inc.*, 24 F.3d 357, 361 (1st Cir. 1994).

Part of the Division's burden of proof is to develop a record sufficiently detailed to allow the Commission to find that a violation has been committed. *Monetta Fin. Serv. Inc.*, Rel. No. 34-48001 (June 9, 2003). The Division has not done so with respect to misrepresentations by omission.

Further, the OIP's failure to identify any statements rendered misleading by the omission of material facts deprived Mr. Bandimere of the notice necessary to address facts that might support misrepresentations by omission. Failing to provide Mr. Bandimere notice of an integral part of the factual basis for allegations of fraud deprived him of fair notice of the grounds on which the fraud claims rested to which he was entitled. *Jaffee & Co. v. SEC,* 446 F.2d 387, 394 (2d Cir. 1971).

The law judge's findings that Mr. Bandimere knew of certain "red flags" alleged in the OIP are not supported by a preponderance of the evidence.

The allegation that Mr. Bandimere admitted to an investor he "knew" that Parrish had been "sued" by the Commission in 2005, OIP.II.E.35.a, went unproved. Pickering (who appears to be the investor to whom Mr. Bandimere allegedly admitted he knew about a lawsuit) testified that Mr. Bandimere told her in 2011 he had known of a matter with the SEC not considered a problem; she did not testify that Mr. Bandimere had referred to a lawsuit. Tr. 385-7. Mr. Bandimere testified he was told there was some problem with Parrish and a regulatory agency, but was told the matter was resolved, and that he did not know the nature of the problem. The Division's post hearing briefs did not argue that Mr. Bandimere knew that Parrish had been

sued by the SEC, but that he had faced some unspecified "regulatory action." Div.Br. 8, Div.Rep. 3.

Despite the absence of evidence that Mr. Bandimere knew that Parrish had been sued by the Commission, the law judge found he had that knowledge, based on an email from Pickering to the Division reporting on her 2011 conversation with Mr. Bandimere. I.D. 64. Pickering's email used the word "complaint" to describe the problem about which Mr. Bandimere had been informed, from which the law judge inferred that Mr. Bandimere knew about a lawsuit.

However, Pickering's email does not constitute a preponderance of evidence that Mr. Bandimere knew that Parrish had been sued previously by the SEC. The word "complaint" has multiple meanings, the primary meaning not being a document that initiates a lawsuit, but "An expression of grief, pain, or dissatisfaction." *Merriam-Webster's Collegiate Dictionary* (11th Ed.), p. 254. There is no evidence that Mr. Bandimere used "complaint" to mean the document which initiates a lawsuit, as opposed to some expression of dissatisfaction.

A law judge is entitled to draw inferences from known facts if those inferences are reasonable. To be reasonable, an inference ". . . in the context of known facts, be one that springs readily and logically to mind and is not one of two or more inferences, both or all of which are about equally probable." *NLRB v. Martin A. Gleason, Inc.,* 534 F.2d 466, 474 (2d Cir. 1976).

The law judge selected one of several possible meanings of the word "complaint," but the record does not support the meaning he selected. There is no evidence that Mr. Bandimere even knew that "complaint" is the name of the document which initiates a lawsuit. The law judge's determination that Mr. Bandimere knew that Parrish had been sued by the SEC is not supported by the evidence, and is arbitrary and capricious.

Regarding the allegation that Parrish and Dalton ". . . often wired insufficient funds to the LLCs . . .", OIP II.E.35.l, the law judge found that ". . . the evidence clearly establishes . . ." that on a month to month basis, Mr. Bandimere knew that Parrish wired insufficient funds, which was not disclosed to Loebe. I.D. 75. That finding is not supported by a preponderance of evidence.

The Division presented only a single instance of Parrish sending insufficient funds, which occurred in May, 2008, when IV Capital mistakenly sent the amount due for March, instead of April. Exhibit 111, p. 44. That error resulted in a shortfall of $2,048 to one of the LLCs, and $2,714 to another LLC. *Id.* The error was corrected two days after it was brought to Parrish's attention. Ex. 138, p. 16. (general ledger entry reflecting supplemental payment.) That single insufficient payment does not support a finding Parrish "often wired insufficient funds" as found by the law judge.

Similarly, the law judge's finding Mr. Bandimere calculated the return that IV Capital earned is not supported by any evidence. I.D. 73. The evidence was undisputed that IV Capital provided Mr. Bandimere, monthly, the return expressed as a percentage. I.D. 17. Mr. Bandimere calculated the individual investor's share of those returns. *Id.*

D. Facts Found to be Omitted Were Not Material.

The OIP alleged the omitted facts were material because they "would have seriously called into question the legitimacy and quality of IV Capital and UCR." OIP II.E.36. However, the law judge's finding Mr. Bandimere neither knew nor should have known the investments were Ponzi schemes rejects that theory of materiality; if the omitted facts seriously raised a question about the legitimacy of the programs, Mr. Bandimere, presumably, would have been at least negligent in not knowing that the programs were fraudulent schemes.

Only once, at I.D. 72, regarding Dalton's prior business activities, did the law judge find an omission was material because if disclosed, the omitted fact would have significantly altered

the total mix of information available to investors, which is the test of materiality of an omission. *Zacharias*, 569 F.2 at 468. Even then, the test was recited in a conclusory manner with no discussion of how the proper test could be applied to the facts in the record and support a conclusion that the fact was material. The remaining findings on materiality set out at I.D. 63-75 were based on an incorrect standard of materiality, and must be rejected.

E. Mr. Bandimere Did Not Act With *Scienter*

1. The Law Judge's Findings on *Scienter* Were Based on Facts About Which Mr. Bandimere Had No Notice and Were Not Supported by a Preponderance of Evidence

The undisputed fact that Mr. Bandimere had hundreds of thousands of his own dollars invested in IV Capital and UCR when he was discussing those investments with others is powerful evidence he did not act with a fraudulent intent. *In re Merkin and BDO Seidman Sec. Lit.,* 817 F.Supp.2d 346, 357 n.8 (S.D.N.Y. 2011) ("... Merkin's significant personal exposure to Madoff's fraud also belies any inference of intent.").

Where recklessness is alleged to be failing to recognize the fraud of others, that recklessness must approximate an actual intention to aid in that fraud. *South Cherry Street LLC v. Hennessee Group, LLC*, 573 F.3d 98, 109-110 (2d Cir. 2009).

The OIP asserted specifically that Mr. Bandimere acted recklessly by ignoring red flags that indicated IV Capital and UCR were likely frauds. OIP II.A.2 and II.E.36. There was no language suggesting that *scienter* might be based on anything else. The law judge rejected the specific allegations relating to *scienter* when he found that the Division failed to prove that Mr. Bandimere knew or should have known IV Capital and UCR were Ponzi schemes. I.D. 79. That finding should have resolved the claims under Section 17(a)(2) and Rule 10b-5 in Mr. Bandimere's favor.

The law judge worked to save those claims by making five factual findings which he concluded proved that Mr. Bandimere acted with a high degree of *scienter*. I.D. 59-62. None of those facts were mentioned in the OIP, or the more definite statement. The first inkling that Mr. Bandimere had that *scienter* would be based on these facts is when his counsel reviewed the I.D. The law judge's findings relating to *scienter* were so foreign to the facts put in issue by the OIP that the Division did not argue in either of its post-hearing submissions that Mr. Bandimere's *scienter* was proved by the facts relied on by the law judge.

The law judge exceeded his authority by addressing facts not set out in the OIP. Rule 200(b)(3) requires an OIP to set out its factual and legal basis. OIP III.A provided that the hearing was to determine whether the allegations in Section II were true. The law judge had no authority to address facts that were not alleged. Doing so deprived Mr. Bandimere of a hearing conducted in accordance with the Commission's Rules and the OIP.

Further, because the OIP alleged none of the conduct on which the law judge based his finding Mr. Bandimere acted with *scienter*, Mr. Bandimere had no notice that the facts found to prove *scienter* would be at issue. He was deprived of a reasonable opportunity to defend himself against an essential element of the most significant claim, which also carried the dark stain of moral turpitude.

The law judge's reliance on Pickering's version of events regarding her investment in UCR in 2010, I.D. 60-61, was egregiously unfair. That transaction was not identified in the Division's more definite statement. In overruling Mr. Bandimere's objection to evidence of that transaction, the law judge held he could consider it as evidence of Mr. Bandimere's *scienter*. Tr. 108-110. That holding contravenes Commission precedent: where conduct is not alleged in the OIP, it should not be considered for any purpose. *Robert Thomas Clawson,* Rel. No. 34-48143

(July 9, 2003); *Russell W. Stein*, 2003 WL 1125746 (Rel. No. 34-47504 Mar. 14, 2003) n.34; *Wheat, First Sec., Inc.,* Rel. No. 34-48378 (Aug. 20, 2003); *Russell Ponce*, Rel. No. 34-43235 (Aug. 31, 2000).

Mr. Bandimere was deprived of both the opportunity to challenge the "facts" through cross-examination or rebuttal evidence during the hearing, and the opportunity to address the evidence relating to those "facts" in his post-hearing submissions. Mr. Bandimere could not make a meaningful post-hearing submission under Rule 340 on *scienter*, a critical element of both violation and sanction.

Had the Division argued *scienter* based on the matters found by the law judge for the first time in its Reply, the argument would be rejected as waived to protect Mr. Bandimere from being sandbagged. *See, New York Rehabilitation Care Mgt., LLC v. NLRB*, 506 F.3d 1070 (D.C. Cir. 2007) (arguments raised for the first time in a reply brief are waived to prevent "sandbagging"); *North Texas Production Credit Ass'n v. McCurtain County Nat'l. Bank,* 222 F.3d 800, 811 n.16 (10th Cir. 2000) (argument raised for the first time in a reply brief will not be considered). Sandbagging by a law judge is no less objectionable than sandbagging by an adversary.

Finally, the law judge's *scienter* findings were not supported by facts established by a preponderance of evidence, or did not support a reasonable inference that Mr. Bandimere acted with *scienter*, or both.

The law judge found that Pickering's investment in the UCR trading program showed that Mr. Bandimere acted with *scienter* because Syke emailed Mr. Bandimere earlier that month expressing his dissatisfaction with the performance of the UCR diamond program, and stating his opinion that no one should invest in UCR at all. I.D. 61-62. However, at the time Pickering

made her investment, in March 2010, the UCR trading program paid returns, as represented, since July 14, 2008. Ex. 137. The most recent payment from UCR was received on March 23, 2010, just three days before Pickering's investment and weeks after Syke's email. Ex. 137. Mr. Bandimere's reliance on historical performance does not support a finding that he was "wildly deceptive," a conclusion strongly supported by Pickering's willingness to invest in UCR after Syke disclosed his concerns to her directly. Tr. 842. Indeed, Pickering testified that the information about UCR she received from Mr. Bandimere was in 2008 – long before she invested! Tr. 339-40; 363. There is no duty to disclose information to someone who reasonably should already be aware of it. *John P. Flannery*, I.D. Rel. No 438 (October 28, 2011) at 40. These facts do not raise a reasonable inference that Mr. Bandimere intended to defraud Pickering or anyone else.

The "bullying" of Koch found to have occurred in May, 2011, I.D. 60, is similarly remote from the investments found to have been induced by fraud, and for that reason alone is not evidence that Mr. Bandimere acted with *scienter* in discussing investments with his friends. Further, while deception is prohibited under the securities laws, bullying is not, and the law judge did not explain how bullying evidences an intent to deceive.

The law judge's foundational finding that Mr. Bandimere bullied Koch is not supported by the evidence. Koch did not claim he was bullied. There was no evidence his 2011 conversation with Mr. Bandimere was heated. Koch, who demanded that Mr. Bandimere return his principal and the profit he hoped to realize, testified that Mr. Bandimere said that Koch was being harsh, a characterization which Koch did not dispute. Tr. 601. The finding that Mr. Bandimere accused Koch of not being a good Christian has no evidentiary support. Koch never claimed that such an accusation was made, and when the law judge asked him if he agreed

that Mr. Bandimere had made that accusation, Koch could not agree. Tr. 602. Koch admitted he told Mr. Bandimere he had a religious-based obligation to return the investment and expected earnings. Tr. 654.

The law judge's reasoning in finding that Mr. Bandimere's *scienter* was established by his failure to disclose Dalton's involvement in both IV Capital and UCR to Radke and Koch because both testified they would not likely have invested if they knew of Dalton's involvement, I.D. 59-61, is flawed because there is no evidence that Mr. Bandimere knew or believed that either Radke or Koch saw Dalton's involvement as a negative. Evidence of that knowledge or belief is essential to the inference which the law judge drew, without which those inferences are unreasonable. *Martin A. Gleason, Inc.,* 534 F.2d at 474. Further, the law judge ignored evidence that Mr. Bandimere rarely disclosed Dalton's identity to other investors who did not know Dalton at all, which contravenes the law judge's conclusion that the reason Dalton's identity was not disclosed to Radke and Koch was to deceive them. I.D. 59-60.

The law judge held that Loebe was credible, based on his demeanor, when he testified that Mr. Bandimere told him that excess returns to the limited liability company would go to charity. I.D. 59. However, the law judge ignored Loebe's admission that his recollection of his discussions with Mr. Bandimere was "thin," and that he was testifying only about the impressions he got from Mr. Bandimere, as opposed to his words. Tr. 303-5. The law judge also ignored that Loebe confused the characteristics of IV Capital with those of UCR, which further showed that Loebe's memory was unreliable. Tr. 289; 291; 304. Loebe's testimony is further undercut because no other witness indicated that Mr. Bandimere had made a similar representation, and there was no evidence that Mr. Bandimere had any reason to believe that

telling Loebe his compensation would go to charity would enhance the likelihood that Loebe would invest.

The law judge found that Mr. Bandimere intentionally lied when he told Koch he promised anonymity to the UCR principal because there was no evidence of Mr. Bandimere making such a promise to Dalton. I.D. 60. The truth of that statement was never an issue, and if it had been, the Division would have the burden of showing that Mr. Bandimere made no such promise. However, the Division did not introduce evidence of falsity of that statement, which the law judge found to be a lie. If Mr. Bandimere had notice that the veracity of a statement he promised anonymity to Dalton was at issue, and if the Division introduced evidence showing that no such promise had been made, Mr. Bandimere could have, and would have introduced evidence to establish the truth of what he said. But Mr. Bandimere did not have the burden of proving the truth of every statement he made, and had no reason to do so in this case since the Division never alleged that he lied about promising anonymity to Dalton.

For these reasons, the allegations that Mr. Bandimere violated the anti-fraud provisions must be dismissed.[7]

IV. THE DIVISION FAILED TO PROVE A WILLFUL VIOLATION OF EITHER SECTION 5 OF THE SECURITIES ACT OR SECTION 15(a) OF THE EXCHANGE ACT

A. The Law Judge Applied an Improper Standard of Willfulness

The law judge found that Mr. Bandimere "willfully" violated Section 5 of the Securities Act and Section 15(a) of the Exchange Act by intending to do the acts that constituted the violation. I.D. 51-52; 56. Construing "willful" to mean only an intentional physical act renders the term devoid of meaning.

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[7] In addition, the alleged violation of Section 17(b)(2) must fail because the Division failed to prove that Mr. Bandimere "obtained" money by misrepresentation. *SEC v Syron*, 934 F.Supp.2d at 638-640.

The applicable statutory scheme reflects a congressional intent that a "willful" violation differs qualitatively from a violation that is not "willful." Section 15(b) allows administrative proceedings to address, and, under Section 21B(a) to impose civil penalties for "willful" violations. Section 21C allows administrative proceedings to address violations that are not willful, but, for the period at issue, Section 21B authorized civil penalties only for violations that were "willful."[8]

Defining "willful" as merely intending the physical act which constitutes the violation does not capture a qualitative difference between a violation that is "willful," and subject to civil penalties, and a violation that is not "willful," for which civil penalties are not available. Except where a person is in a trance or sleepwalking, neither Section 5 nor Section 15(a) can be violated by an unintentional physical act. It is absurd to think that Congress used the term "willful" to ensure civil penalties were not imposed on sleepwalkers.

We have found no instance where the Commission actually applied the "willfulness" standard used by the law judge to a case that did not involve at least negligent conduct. The Commission, in *International Shareholders Service Corp.,* 1976 WL 160366 (SEC Apr. 29, 1976), *as amended* 1976 WL 182458 (SEC June 8, 1976), dismissed the law judge's finding of a "willful" Section 5 violation against a broker who sold unregistered securities in reliance on an exemption made inapplicable by the issuer's conduct. The Commission rejected the argument that a willful violation existed by where the acts constituting the violation were done by the respondent while in possession of his faculties, stating that because the broker had no knowledge that the exemption relied upon had been lost and could not have known if it had made inquiry,

[8] Although Section 8A of the Securities Act and Section 21B were amended in the Dodd-Frank Act to allow civil penalties for non-willful violations, those amendments post-dated Mr. Bandimere's conduct and cannot be applied retroactively. *E.g., Landgraf v. USI Film Products*, 511 U.S. 244 (1994).

"In these circumstances, a finding that respondents' violations were 'willful' would deprive that term of any significant meaning."

When the law judge rejected Mr. Bandimere's argument that the Commission did apply the "non-sleepwalking" test for "willfulness," he cited only *Joseph S. Amundson*, Rel. No. 34-69406 (Apr. 18, 2013). I.D. 51, where a "willful" violation was found where the respondent provided information which the respondent knew to be incorrect.

The law judge's reliance on *Wonsover v. SEC*, 205 F.3d 408, 415 (D.C. Cir. 2000) is misplaced. The *Wonsover* court did not confirm any meaning of willful, but recognized that the question was unresolved. In finding that the SEC properly determined that a failure to conduct an appropriate investigation resulted in a willful violation of Section 5, the Court noted that the Commission did not endorse the standard used by the law judge here, and stated that the Commission found that Wonsover acted willfully because he failed to conduct an adequate investigation to determine whether a registration exemption existed. *Wonsover*, 205 F.3d at 413-5.[9]

Although the court's decision in *Wonsover* provides no definitive insight to the meaning of willfulness, the Commission decision in *Jacob Wonsover*, 1999 WL 1000935 (Rel. No. 34-1123, Mar. 1, 1999) is instructive because it addressed arguments similar to those now made by Mr. Bandimere. The respondent in *Jacob Wonsover* argued, based on *Cheek v. U.S.*, 498 U.S. 192 (1991) and *Ratzlaf v. U.S.*, 510 U.S. 135 (1994), that the maxim that "ignorance of the law is no excuse," which is the foundation of the non-sleepwalking construction of "willful," is subject

[9] Although the law judge highlighted the *Wonsover* court's reference to its "traditional formulation of willfulness," I.D. 51, as supporting the test he applied, in context, the formulation to which the court referred was one where it rejected that willfulness required a specific intent to violate the law. 205 F.3d at 414. Rather than parsing its language, the law judge should have focused on what the court in *Wonsover* actually did. *See, Witt v. Dept. of the Air Force*, 527 F.3d 806, 816 (9th Cir. 2008) ("In these ambiguous circumstances, we analyze . . . by considering what the court actually *did,* rather than by dissecting isolated pieces of text.").

to an exception in the case of "highly technical statutes that presented the danger of ensnaring individuals engaged in apparently innocent conduct." *Bryan v. U.S.*, 524 U.S. 184, 194 (1998).

The Commission rejected that argument because the regulatory context for Section 15(b)(4) was one in which the persons subject to a Section 15(b)(4) proceeding were licensed securities professionals in a highly regulated industry, who had a duty to know what the law required. *Jacob Wonsover*, at *10; *Abraham and Sons Capital, Inc.*, 2001 WL 865448 at *8 (Rel. No. IA-1956, July 31, 2001) (failure of securities professionals to be knowledgeable requirements is reckless, and therefore, "willful").

Because Mr. Bandimere was not registered as a broker, and had never been so registered, Joint Stipulations 3 and 4, and cannot be charged knowing the securities laws, *Wonsover* is distinguishable and provides no support for the law judge's interpretation of "willful." Further, because both Section 5 and Section 15(a) are the type of technical statutes that present "the danger of ensnaring individuals engaged in apparently innocent conduct," *Bryan, id.,* and there is no indication that Congress intended a "willful violation" to be one of strict liability, a willful violation must involve some type of culpability, if only negligence.

B. Mr. Bandimere Did Not Act Willfully

The Commission need not articulate a precise standard of culpability necessary to find that a non-securities professional acted willfully, since Mr. Bandimere was not culpable at all. The record reflects he acted reasonably by consulting with counsel regarding the legality of his activities. Syke, the counsel who advised Mr. Bandimere, admitted he had missed the issues that IV Capital and UCR could be securities whose sale required either registration or an exemption, and that assisting individuals to participate in those programs, and obtaining compensation in management fees, could cause acting as an unregistered broker. Tr. 800-1; 804-5.

The court in *Howard v. SEC,* 376 F.3d 1136, 1148, n. 20 (D.C. Cir. 2004) recognized that even for securities professionals, compliance with the securities laws was sufficiently difficult that laymen have no real choice but to rely on counsel, and the proper functioning of the securities markets depends on the ability to rely on counsel. Concluding that relying on counsel is irrelevant, or a negative, as did the law judge here,[10] can only be a disincentive to obtaining advice from counsel.

The law judge's rejection of Mr. Bandimere's reliance on Syke's advice because Syke was not fully informed of the numbers of investors who would participate in the LLCs which Mr. Bandimere managed, I.D. 52, is incorrect.

The onus is not on the client to disclose to the lawyer everything the lawyer must know to give advice on which a client may rely. As noted by the court in *U.S. v. DeFries*, 129 F.3d 1293, 1308-9 (D.C. Cir. 1997): "No client ever tells his or her lawyer every single fact that a good lawyer probes before giving advice. Indeed, clients do not typically even know which facts a lawyer might think relevant. (That is, in part, why they consult lawyers.)" There is no evidence that Mr. Bandimere withheld any fact he or Syke thought to be pertinent, or that Syke was unaware of any pertinent fact regarding whether a Section 5 violation might arise from involving people in IV Capital or UCR (as opposed to the LLCs) or whether Mr. Bandimere's activities could result in a Section 15(a) violation. Therefore, because Mr. Bandimere acted reasonably by consulting and relying on Syke, he did not commit a willful violation of either Section 5 or Section 15(a).

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[10] The law judge characterized the evidence that Mr. Bandimere relied on Syke as attempting to "shift blame to Syke" which he considered to reflect a failure to recognize the wrongfulness of his conduct, as part of the sanction determination. I.D. 80. That conclusion is contrary to both *Howard v. SEC, supra,* and *Blinder, Robinson & Co, Inc. v. SEC,* 837 F.2d 1099 (D.C. Cir. 1988), which held that evidence of the relationship with counsel was necessary for a complete record on the issue of sanction. It is chilling and contrary to law for a law judge to hold a respondent's counsel who elicits and argues exculpatory evidence has demonstrated the need for a harsher sanction against his client. *SEC v First City Fin. Corp.*, 890 F.2d 1215, 1229 (D.C. Cir. 1989).

C. Mr. Bandimere was not a Seller of Securities

Mr. Bandimere was not a "seller" of IV Capital or UCR securities within the meaning of the Securities Act because his motivation in having others participate in those programs was to serve their financial interests, and not his own. In *Pinter v. Dahl*, 486 U.S. 622, 647 (1988), the Supreme Court held that a seller of securities did not include someone not motivated to serve the financial interest of either the issuer of the securities, or his own financial interest.[11] Mr. Bandimere testified his motivation in telling people about IV Capital and UCR was to provide a benefit to them, and not himself. Tr. 1185-7. Blackford, Radke, and Syke all testified that Mr. Bandimere was not making a sales presentation, but rather, providing information that would benefit potential investors. Tr. 469:18-470:19; 704:8-23; 783:2-22. There was no evidence that Mr. Bandimere was soliciting others to serve his financial interests.

Mr. Bandimere's motivation to benefit others is supported further by his guaranteeing the investments of two ministry foundations of which he was a director, investing $50,000 for his son, and funding an account for George Stepán, a minister who Mr. Bandimere had known for many years. Exh. 200; Tr. 1079-1083.

The law judge ignored the variety of evidence that Mr. Bandimere's motivation was to serve the financial interest of others, and referred only to the management fees he was paid. I.D. 50. The law judge assumed that Mr. Bandimere involved others in the investments to increase his management fees, but pointed to no evidence to support that assumption. He also ignored facts inconsistent with his assumption, such as that Mr. Bandimere involved people in IV Capital through his personal account prior to the payment of any management fee.

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[11] The law judge's reliance on *Zacharias v. SEC* to distinguish *Pinter* is misplaced. I.D. 50-51. *Zacharias* distinguished *Pinter* only with respect to whether a substantial participant in a sale could be a statutory seller. *Zacharias* did not involve an alleged seller who was motivated solely to benefit the purchaser.

Although Mr. Bandimere's altruistic motivation may be uncommon, the depth of his faith and his life-long commitment to helping others are uncommon as well. There is no evidence that Mr. Bandimere ever was motivated to have other people invest in either IV Capital or UCR to serve his financial interest rather than the interest of prospective investors. Without such evidence, Mr. Bandimere was not a statutory seller of securities.

D. Mr. Bandimere Was Not a Broker

The law judge's finding Mr. Bandimere acted as a "broker" is not supported by a preponderance of evidence. The term "broker" is defined in Section 3(a)(4)(A) of the Exchange Act. An essential element of that definition is a person be "in the business" of effecting transactions in securities for the account of others. Mr. Bandimere was not "in the business" of effecting transactions in securities for the account of others.

The Exchange Act does not define what it means to be ". . . engaged in the business of effecting transactions in securities for the account of others." Rather, a non-exclusive number of factors are considered, none of which is dispositive. *E.g. SEC v. Kramer*, 778 F.Supp.2d 1320, 1334-5 (M.D. Fla. 2011).

Although transaction based compensation has been held to be the "hallmark" of acting as a broker, *SEC v. Sky Way Global, LLC*, 2010 WL 5058509 (M.D. Fla. Dec. 6, 2010), a "finder" may receive transaction based compensation without being considered a broker. *Kramer*, 778 F.Supp.2d at 1339; *DeHuff v. Digital Ally, Inc.*, 2009 WL 4908581, at *4 (S.D. Miss. Dec. 11, 2009). A person who is "facilitating" transactions in a security is not necessarily "effecting" transactions within the meaning of Section 3(a)(4) or 3(a)(5). *SEC v. M&A West, Inc.*, 2005 WL 1514101, at *9.[12]

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[12] The uncertainty surrounding the activities that may cause a person being found a broker creates a due process problem, since a person of reasonable intelligence cannot differentiate between activities permissible for

The law judge's analysis suffers from the same shortcomings as the SEC's argument in *SEC v. M&A West, Inc.*, 2005 WL 1514101 (N.D. Cal. June 20, 2005), *aff'd on other grounds*, 538 F.3d 1043 (9th Cir. 2008). Here, as in *M&A West*, the law judge pointed to activities in which he contends Mr. Bandimere engaged, and concluded those activities show he acted as an unregistered broker, without explaining why those activities, which may be conducted by persons not considered to be brokers, result in broker status, or why the factors which did not apply to Mr. Bandimere did not lead to the conclusion that he was not a broker. I.D. 53.

Most of the factors to be considered in determining whether a person is a "broker" did not apply to Mr. Bandimere. Mr. Bandimere did not negotiate the terms of any arrangement between investors and IV Capital or UCR. He did not hold himself out as having any investment expertise, and did not actively solicit investors.

Mr. Bandimere did not evaluate the financial needs of any investor or issuer. He did not engage in any advertising or approach anyone about investing other than family or close friends, which is not broker activity. *SEC v. Kramer*, 778 F.Supp.2d at 1340 (solicitation of family members and intimate friends not broker activity).[13]

Mr. Bandimere did not have, or claim to have, the ability to effectuate transactions in securities. He had to go through Parrish to participate in IV Capital, and through Dalton to participate in UCR. The Commission, in its enforcement actions against Parrish and Dalton established that each was acting as a broker in their activities for IV Capital and UCR. Exhibit 78; Exhibit 83. A person who does not have the ability to make a transaction in

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anyone, and activities which require registration as a broker. Even Syke, an experienced lawyer and former stockbroker, did not see the activities in which he and Mr. Bandimere engaged as implicating the need to register as a broker. Tr. 802:4-14. Punishing Mr. Bandimere for not understanding a legal concept so unclearly defined would violate due process due to a lack of notice of what the law requires.

[13] Hunter, Radke, Koch, and Syke were all people who Mr. Bandimere had known for decades. Moravec, Loebe and Blackford all approached Mr. Bandimere about investing. Pickering was referred to Syke by Parrish. Davis was referred by Dalton.

securities happen, and does not hold himself out as having such an ability, but who must go through a broker, does not engage in the business of effecting transactions in securities, and is not a broker. *See, In re Slatkin,* 525 F.3d 805, 817-8 (9th Cir. 2008) (construing the definition of "broker" under bankruptcy law, which is identical to the definition under securities law).

Mr. Bandimere did not handle investor paperwork or obtain signatures for either IV Capital or UCR; there is no evidence that investor paperwork or signatures were required for those programs. The only investors who had any agreement with IV Capital were Pickering and Hunter, through a trust, both of whom dealt directly with Parrish. There is no evidence that Mr. Bandimere "handled" the paperwork for the investments of either Pickering or Hunter's trust. Ex. 120, p. 1480.

Because the hallmark of "being in the business" of affecting transactions in securities for the account of others is the receipt of commissions or transaction-based compensation, the Division focused on trying to prove that Mr. Bandimere received "commissions." However, Mr. Bandimere received no commission. The only remuneration which he received was for performing recordkeeping and other administrative functions.

Evidence that the management fees paid to the limited liability companies was for administrative services, and not sales compensation, was found in Pickering's testimony. She became an investor with IV Capital with no involvement of Mr. Bandimere or Syke. After she invested with Parrish, Parrish referred her to Syke because she wanted administrative services, including tax advice, which Parrish could not provide. Tr. 209-211; 260; 261-264. Although Pickering provided no evidence she was ever solicited or encouraged by Mr. Bandimere to make any investment with IV Capital, Exito was paid a management fee for Pickering's contributions.

The law judge's finding that the administrative fees were disguised sales compensation is not supported by a preponderance of the evidence. The law judge suggests that Mr. Bandimere and Syke were lying when they testified that the fees were for management services, because payments were not on an hourly basis, and there was no evidence of discussions between Mr. Bandimere on one hand, and Parrish and Dalton, on the other, regarding the services to be provided. I.D. 55. However, there is no authority (and the law judge cites none) that supports his assumption that fees for administration must be based on an hourly rate, determined after detailed conversations in which specific administrative tasks are discussed and agreed to. Nor does the evidence show that Parrish and Dalton lacked an understanding of the administrative services provided. Parrish knew Syke was available to provide tax advice, as reflected by his referral of Pickering to Syke. Parrish and Dalton both knew they were not communicating with investors to answer questions, or accepting funds from LLC members, or allocating profits among the LLC members, or preparing tax returns or forms K-1 for the members, which were tasks they had to know must be performed by someone.

Basing compensation on profits or assets under management does not make that compensation a sales commission, even though the compensation may be affected by the amount invested. *See, Financial Planning Association v. SEC*, 482 F.3d 481, 488 (D.C. Cir. 2007) (account management fees not considered sales compensation). Many service providers in the financial industry, such as custodians, shareholder servicing charge on the basis of the assets. Further, the law judge did not explain why, if Mr. Bandimere was being compensated for finding investors, he would have been willing to spend a large amount of time, and incur significant expense, performing administrative functions for no compensation.

M&A West teaches that pointing to a few of the various factors to be considered in determining whether a person is a broker, and then asserting broker status has been proved, is insufficient. *Accord, SEC v Benger*, 697 F.Supp.2d 932, 945 (N.D. Ill. 2010) (allegations of only some but not all factors may not adequately plead broker status). However, that is all the law judge has done. The finding is arbitrary and capricious.

V. SANCTIONS IMPOSED WERE ARBITRARY, CAPRICIOUS AND NOT IN ACCORDANCE WITH THE LAW

A. Cease and Desist Order

There is no formula for determining an appropriate sanction. Although the law judge claimed to rely on the factors discussed in *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds Steadman v. SEC,* 450 U.S. 91 (1981), those factors have been rejected as a formula on which to base sanctions. *PAZ Securities v. SEC*, 566 F.3d 1172, 1175 (D.C. Cir. 2009). The *Steadman* factors include whether a defendant recognized the wrongful nature of his conduct; but, in *SEC v. First City Financial Corp.*, the court held that a failure to admit wrongdoing was not a legitimate consideration in determining the appropriate relief. *First City Financial*, 890 F.2d at 1229. The court in *First City Financial*, 890 F.2d at 1228, held further that ". . . whether the violation was flagrant or deliberate or merely technical in nature . . ." were appropriate factors to consider. The *Steadman* factors do not encompass these important considerations.`

In considering whether to impose a cease and desist order, some likelihood of a future violation must be shown. *Russell W. Stein, et al.,* 2003 WL 1125746, at *8. A cease and desist order against Mr. Bandimere is not warranted even if violations are found. The only inference that a future violation may occur arises only from a past violation. That bare inference is outweighed by other factors.

Mr. Bandimere is 67 years old. He has never been in the securities business. Speculation that in the future he is likely to involve others with investments, after the disastrous consequences he experienced, has no support in the record, and defies common sense.

The law judge pointed to the recency of the violations and the harm to investors as supporting a cease and desist order. I.D. p. 81. However, there is no logical connection between the likelihood of a future violation and the passage of time since a prior violation, or investor loss, or failing to admit that prior conduct was illegal.[14] Those inferences *are* affected by whether past violations are flagrant or deliberate. *First City Financial*, 890 F.2d at 1228.

The law judge found flagrant and deliberate violations of the anti-fraud provisions, but to do so, he relied on facts and theories never alleged in the OIP, and not even argued by the Division. Those findings cannot be sustained. Violations of Section 5 and Section 15(a) were determined under a strict liability theory, but were inadvertent if they occurred. The requirements of Section 5 and Section 15(a), while important, are technical, and not obvious to a layman; they were not obvious to Syke, who was both a trained securities professional and a lawyer. There is no evidence that Mr. Bandimere was trying to be aggressive and misjudged a line between proper and improper behavior. He was trying to be cautious. Even if violations of Section 5 and Section 15(a) are sustained, they warrant no cease and desist order.

B. Disgorgement

Disgorgement is an equitable remedy by which a person or entity may be required to surrender ill-gotten gains that are causally related to violations of the federal securities laws.

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[14] It is telling that the wrongdoing which the law judge contends Mr. Bandimere should have admitted could be known only after the law judge decided the case. Should Mr. Bandimere have admitted to employing a scheme to defraud, even though the Division abandoned that claim shortly before the hearing? Should he have admitted to violations of the Advisers Act, even though the Division has admitted that it failed to prove that claim. Should he have admitted knowing facts which the law judge found the Division failed to prove he knew, or were facts at all? And, since the law judge found that Mr. Bandimere made misrepresentations that were not alleged in the OIP, how was Mr. Bandimere to know what he should have admitted, and when should he have made the admissions?

First City Financial Corp., 890 F.2d at 1231. The purpose of disgorgement is not to punish, or to compensate others. Rather, disgorgement is imposed to avoid unjust enrichment, and to deter violations.

The causation is not "but for" causation, since profits attenuated from the wrongdoing should not be disgorged. *First City Financial Corp.*, 890 F.2d at 1232. Disgorgement is not available as a mechanism by which a person can be forced to pay money that is not a "gain." *SEC v. Hately*, 8 F.3d 653, 655-656 (9th Cir. 1993); *SEC v. Miller*, 2006 WL 2189697, at *12 (N.D. Ga. July 31, 2006).

The Division must prove both that disgorgement is appropriate, and that the disgorgement sought is at least a reasonable approximation of wrongfully obtained profits. *E.g., SEC v. First City Financial Corp.,* 890 F.2d at 1231; *SEC v. Miller*, *supra*; *SEC v. Collins*, 2003 WL 21196236, at *5 (N.D. Ill. May 21, 2003).

For disgorgement, "gains" are equivalent to "profits." *E.g., SEC v. DiBella,* 409 F.Supp.2d 122, 127 (D. Conn. 2006). Therefore, funds received which merely restore a person to a previous financial condition are not considered to be profits. *SEC v. Collins*, *supra,* at *8-9. Further, all circumstances must be considered to determine whether a wrongdoer has realized gains. *SEC v. Hately*, *supra,* (where agreement establishing a violation allowed defendant to retain only a portion of proceeds, disgorgement could not include proceeds which the agreement required to be paid to others).

Mr. Bandimere did not realize a "gain" which is subject to disgorgement. As shown by Exhibits 200 and 201, Mr. Bandimere's net financial outcome from his activities with IV Capital and UCR was a loss. An order of disgorgement would increase that loss; it would not deprive

him of any gain. Because disgorgement should force no one to pay money that is not a gain, disgorgement is not available.

In *Hately*, the court considered whether the SEC acted within its discretion by affirming disgorgement where a brokerage firm which had received a commission resulting from improper activities of a salesman was required to disgorge the entire commission, although it had paid 90% to the salesman. The court held that the SEC abused its discretion by attributing the entire commission to the broker for purposes of disgorgement. *Hately*, 8 F.3d at 655-6.

In *SEC v. McCaskey*, 2002 WL 850001 (S.D.N.Y. Mar. 26, 2002), the SEC calculated disgorgement sought from a defendant who manipulated the price of a stock by considering only profitable trades, which were more than offset by unprofitable trades. The court did not allow the SEC to obtain disgorgement when there was no actual gain. *McCaskey,* 2002 WL 850001, at *10.

Implicit in the law judge's refusal to consider Mr. Bandimere's losses as part of the calculation of "gains" is the assumption his losses were unrelated to those gains. That assumption is contrary to the evidence.

The law judge's conclusion that Mr. Bandimere's investments into IV Capital and UCR were unrelated to his violative conduct ignores reality. Mr. Bandimere's investments were not lost in legitimate investment activities, but were used to make payments either to himself or to other investors as part of a fraudulent scheme. *In re Slatkin*, 525 F.3d at 814-5. Mr. Bandimere was never paid real investment returns or management fees; he was paid with his own money, or, to the extent his money was paid to another investor, from contributions of other victims.

To the extent Mr. Bandimere's contributed funds were returned to him as management fees or investment returns, he realized no gains or profits until he received more than he put in.

That point never occurred. Mr. Bandimere either got his own money back, or, if some money he received came from other investors, some or all of the money he contributed to other victims as Ponzi payments, thereby reducing their losses. Unless Mr. Bandimere knew or should have known of the fraudulent scheme (and the law judge found he did not), Mr. Bandimere was not unjustly enriched.

Mr. Bandimere's "investments" were integral to the investments of his friends and family. His large personal investments influenced others to invest in the programs in which he invested. Tr. 305; 528; 536-7; 546-7; 669. The Commission recognizes that Ponzi schemers induce prominent people like Mr. Bandimere to invest and provide them with high returns, anticipating that their apparent success is likely to attract other victims. *See*, n.1. Mr. Bandimere, who was a victim of a fraudulent scheme, should have at least the same benefit as the defendant in *McCaskey*, who perpetrated a fraudulent scheme, to have his losses considered in determining whether he realized any improper gains.

Further, the compensation paid to Mr. Bandimere is too attenuated from any violation to be the proper subject of disgorgement. *SEC v. One or More Unknown Traders in the Common Stock of Certain Issuers,* 853 F.Supp.2d 79, 83 (D.D.C. 2012). All the violations involved other people contributing funds to participate in either IV Capital or UCR. However, Mr. Bandimere retained none of those funds; he transmitted them, under the investors' instructions, to IV Capital or UCR. The compensation he received was not for raising funds, but for providing substantial administrative services. However, providing those services does not violate the law. Therefore, his compensation was not causally connected to an alleged violation, and is not subject to disgorgement. *SEC v. Perry*, 2012 WL 1959566, at *6 (C.D. Cal. May 31, 2012), *citing SEC v.*

Resnick, 604 F.Supp.2d 773, 783 (D. Md. 2009) (compensation earned for performing valuable functions that did not violate the law should not be disgorged).

The law judge tried to patch this hole in the evidence by finding payments for administrative services were "in furtherance" of selling unregistered securities while operating as an unregistered broker. I.D. 84. Even if true (which Mr. Bandimere disputes), there is no authority that funds used in furtherance of violations are ill-gotten gains subject to disgorgement.

The law judge also found that none of Mr. Bandimere's compensation was related to legitimate activities because he made misrepresentations to investors. I.D. 84. However, the law judge found misrepresentations were made only to six investors. I.D. 63-75. The law judge does not explain how the small number of investors found to have been defrauded results in all administrative fees being the result of violations of the law, and subject to disgorgement.

The law judge seems to suggest that all payment for administrative services should be disgorged because Mr. Bandimere acted as a broker to all the investors because he distributed their monthly returns, and received transaction based compensation. I.D. 85. Even if those activities made Mr. Bandimere a broker (which they did not), Section 15(a) does not prohibit unlicensed persons from conducting all activities that brokers perform. Only effecting transactions in securities, or inducing or trying to induce purchases or sales of securities, without registration, violate the law, and only compensation derived from those activities is subject to disgorgement.

The Division had the burden to differentiate between legally and illegally obtained compensation, with only illegally obtained compensation subject to disgorgement. *SEC v. Razmilovic,* 738 F.3d 14, 31 (2d Cir. 2013). The Division, not Mr. Bandimere, had the financial records relating to Parrish's and Dalton's activities, and already had calculated where the money

went. Ex. 58, p. 10-12; Ex. 207, p. 465-8. Neither the law judge nor the Division differentiated between compensation received for legitimate administrative activities, and compensation paid for improper activities. Further, the Division made no allowance for payments made to other investors with Mr. Bandimere's money, either unknowingly through the operation of the Ponzi scheme,[15] or knowingly as shown by Ex. 200. As a consequence, the Division failed in its initial burden to present evidence of a reasonable approximation of an amount subject to disgorgement. The only evidence that provides a basis for an allocation came from Mr. Bandimere, who estimated that as much as 90 percent of the time spent on IV Capital and UCR related to bookkeeping and administrative matters. Tr. 1211-1212. Based on that evidence, only 10 percent of what Mr. Bandimere received as compensation is subject to disgorgement.

The Division, presumably to be aggressive, took the position that every penny of management fees should be disgorged, and offered no alternative calculation. While the Division is free to be aggressive, it must live with the consequences of its tactical choice. Where an aggressive position is not a reasonable approximation of ill-gotten gains, the Division has failed in its initial burden, and no disgorgement is appropriate.

C. Civil Penalties

The law judge imposed a civil penalty of $390,000, representing the maximum civil penalty available for three units of violation of the anti-fraud provisions. I.D. 87-88. However, there is no statutory basis to impose any civil penalty.

Because all of the violations found to have occurred pre-dated the Dodd-Frank Act, the availability of civil penalties must be based on the law as it existed prior to Dodd-Frank. *See, Landgraf,* 511 U.S. at 1502 (punitive provisions will not apply retroactively absent clear intent).

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[15] The Division, though not Mr. Bandimere, had this information, as evidenced by the tracing of funds done by the Division in the injunctive actions brought against Parrish and Dalton.

Civil penalties under Section 8A(g) of the Securities Act and Section 21B(a)(2) of the Exchange Act, which do not require "willful" violations, are not available because those provisions that were added by Dodd-Frank, became law in July, 2010.

Civil penalties are available here under Section 21B(a)(1) only to proceedings initiated under Section 15(b)(4) and 15(b)(6) of the Exchange Act.

The law judge imposed civil penalties on Mr. Bandimere solely under Section 15(b)(6), which allows a proceeding to be brought against any person who is, or was at the time of the alleged misconduct, associated, or seeking to become associated, with a broker or dealer, or who was participating in an offering of a penny stock. I.D. 86. However, there was no evidence, and no allegation in the OIP, that Mr. Bandimere met those criteria; initiating the proceeding under that provision was improper. Therefore, Section 15(b)(6) is inapplicable, and the law judge's imposition of civil penalties under that section must be vacated.[16]

Nor does Section 15(b)(4) allow civil penalties to be imposed on Mr. Bandimere. In *Jacob Wonsover*, the Commission recognized that only registered professionals in the securities industry are subject to a proceeding under Section 15(b)(4). 1999 WL 100935, at *10 ("Wonsover—like everyone else subject to a Section 15(b)(4) proceeding—is a registered professional . . . .") Mr. Bandimere was not, and has never been a registered securities professional. I.D. 3.

D. Associational Bar

The law judge imposed an industry wide associational bar against Mr. Bandimere under Section 15(b)(6). However, Section 15(b)(6), by its terms, applies only to a person associated with a broker, or dealer, who was seeking to become associated, or who was participating in a

[16] The law judge's reliance on *Vladislav Steven Zubkis*, 2005 WL 3299148 (Rel. No. 34-52876, Dec. 2, 2005) is misplaced because the respondent in *Zubkis* was a person associated with a broker (as well as someone involved in a penny stock offering) and fell squarely within Section 15(b)(6).

penny stock offering. There was no allegation, and no evidence that Mr. Bandimere did anything to bring him under Section 15(b)(6). Therefore, the bar under Section 15(b)(6) must be vacated.

VI. EQUAL PROTECTION CLAIM ESTABLISHED

The SEC sues Ponzi schemers in the federal courts. Exhibit 228. Mr. Bandimere is the exception in that a claim alleging he must have known he was getting investors involved in a Ponzi scheme has been brought as an administrative proceeding. The result is he has been singled out and denied the opportunity for a trial by jury, presided over by an Article III judge, and denied discovery under the Federal Rules of Civil Procedure which would have been available to him if the SEC had sued him in federal court. The denial of these important rights has impaired his ability to mount a full defense to the claims raised against him. As a consequence, Mr. Bandimere has been denied equal protection of the laws. *Gupta v. SEC,* 796 F.Supp.2d 503, 513 (S.D.N.Y. 2011).

The law judge held that he lacked the authority to afford relief on this claim, because he could not "second guess" the Commission. I.D. 76. However, the law judge was not asked to "second guess" anything; he was only presented with a defense like any other, to be decided under the law and the facts. For the law judge to characterize that as beyond his authority suggests that he considered himself powerless to reject factual or legal theories asserted in the OIP, lest he be accused of "second guessing" the Commission.

Mr. Bandimere proved he has been singled out through Exhibit 228, which summarizes enforcement actions brought against alleged perpetrators of Ponzi schemes in civil injunctive actions, and in administrative proceedings since December, 2008 through March 2013.[17] That summary shows that during that time period, the Commission initiated 198 civil injunctive

[17] The analysis began in December, 2008, because that was when the Madoff scheme came to light, and began an enforcement initiative at the SEC against Ponzi schemes.

actions against alleged Ponzi schemers, but only 13 Ponzi scheme cases which were brought, in the first instance, as administrative proceedings. One of the 13 cases brought administratively was the case against Mr. Bandimere.

Of the 12 administrative proceedings brought against those other than Mr. Bandimere, nine were filed as settled actions. (*Thomas Blackwell, Dustin J. Lunt, Paul H. Heckler, Jack W. Luna, Jeffrey A. Lindsey, Dominic O'Dierno, Benjamin R. Daniels, Steve Persad, and David R. Smith*). Such cases implicate no deprivation of a respondent's procedural rights since the respondent, by the settlement, has determined not to contest the allegations. Of the three cases, other than the case brought against Mr. Bandimere, that were not brought as settled cases, two cases, *Capital Financial Services* and *Daniel Bogar*, did not allege that the respondents knowingly involved investors in a fraudulent scheme, and all were brought against licensed securities professionals.

The law judge considered this evidence to be irrelevant by saying that there were no allegations in the OIP that Mr. Bandimere knew that IV Capital or UCR were Ponzi schemes, or that he intended to defraud anyone by operating or promoting Ponzi schemes. I.D. 76.[18] However, OIP II.A.2 alleges that Mr. Bandimere acted "recklessly" in not knowing that "IV Capital and UCR were likely frauds." OIP II.E.36 alleged that Mr. Bandimere was reckless in ignoring obvious signs of fraud. The Division argued in its Pre-Hearing and Post Hearing Briefs that Mr. Bandimere recklessly ignored facts suggesting IV Capital and UCR "were not legitimate." Division Pre-Hearing Brief, p. 24; Division Post Hearing Brief, p. 20. Since IV Capital and UCR were Ponzi schemes, the references to "likely frauds" and entities that were not legitimate, can only be references to Ponzi schemes.

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[18] The law judge's analysis is the equal protection claim is dicta, since he concluded that he lacked the authority to decide the question. I.D. 76.

By alleging that Mr. Bandimere was reckless in not knowing IV Capital and UCR were likely fraudulent schemes, the Division alleged in substance that it was so obvious that he must have known it. *Dolphin and Bradbury,* 512 F.3d at 639. The law judge does not explain why the difference between "knew" or "must have known" was material to his analysis whether Mr. Bandimere was treated differently than others accused of defrauding people through Ponzi schemes. Nor does the law judge explain why the difference between a "Ponzi scheme" and a "fraudulent scheme" or that IV Capital or UCR "were not legitimate" was significant to him in rejecting evidence that Mr. Bandimere was treated differently from others similarly situated.

The law judge pointed to Young and David Smith as being "persons with whom [Mr. Bandimere] is most similarly situated" who were subject to administrative proceedings. I.D. 77. However, they were not similarly situated. The proceeding against Mr. Smith, which was filed as a settled matter, alleged and found Mr. Smith was merely negligent in ignoring indications of fraud. *David R. Smith,* OIP III.17 and 19; (Rel. No. 33-9373 Dec. 6, 2012). In substance, the allegation against Mr. Bandimere was that he "must have known" IV Capital and UCR were likely frauds. Mr. Young, who was charged in the OIP here, was not alleged to have been even negligent in not recognizing IV Capital and UCR were likely frauds. OIP II.F.45.

Nothing in the record suggests a benign explanation for why Mr. Bandimere was treated differently than others who the Commission contends involved others in schemes they knew or must have known were fraudulent. The Division declined to offer any evidence that explained the Commission's decision to proceed against Mr. Bandimere in an administrative forum. The Division's claim that the reason for suing as an administrative proceeding was privileged was groundless. The reasons for an agency's decision are not protected by either the deliberative process privilege or the attorney/client privilege. *Safecard Services, Inc. v. SEC*, 926 F.2d 1197,

1203-4 (D.C. Cir. 1991). The fact that the Division could have provided an innocent explanation (if one existed) but did not supports an inference there was no innocent explanation. *Rowe v. Maremont Corp.*, 650 F.Supp. 1091 (N.D.Ill. 1986).

There was no apparent advantage to using the administrative process to obtain a more expeditious resolution of the case, or to obtain remedies that would not be available in a civil injunctive action. This case does not involve complicated and technical issues under the securities laws which would be difficult to resolve by a lay judge and jury, even with the help of expert testimony.

The lack of benign reasons to proceed against Mr. Bandimere administratively contrasts with an obvious improper reason: to deprive Mr. Bandimere of his right to a jury trial, presided over by a judge who is not an employee of the Commission, and which is governed by procedural rules which would provide greater opportunities to prepare a defense than are available under the Commission's rules of procedure. The advantages of the administrative forum enjoyed by the Division and the Commission's enforcement agenda, which raise issues of fundamental fairness, have gotten public attention. "At the S.E.C., a Question of Home-Court Edge," Gretchen Morgenson, New York Times, October 5, 2013. Concerns about the fairness of the administrative process have been raised at the Commission level, and identified the particular problem of policy implementation affecting the ability of commissioners to act as impartial adjudicators in particular cases. *The Stuart-James Co., Inc.*, 1991 WL 291802, at **7-13 (Jan. 23, 1991) (concurring opinion of Commissioner Fleischman).

These factors all combine to raise an inference this case was brought as an administrative proceeding for the purpose of impairing Mr. Bandimere's ability to defend serious charges,

where others, who were charged with similar misconduct, had the advantage of a court proceeding, with attendant procedural safeguards, in particular, the right to a jury trial.

VII. PROCEDURAL ERRORS

A. The Law Judge's Decision to Quash Mr. Bandimere's Pre-Hearing Subpoena Was Arbitrary, Capricious and not in Accordance with Law.

Mr. Bandimere sought a subpoena of several categories of documents in the possession of the Commission on January 14, 2013, after he had received the Division's initial production under Rule 230(a)(1). Before the Division filed any objection, the law judge issued an order stating Mr. Bandimere's request for a subpoena was "at least colorably objectionable." January 15, 2013 Order. With that invitation, the Division moved to quash on January 22, 2013, and objected to everything requested by the subpoena, asserting various privileges and contending that producing the documents requested was unduly burdensome and oppressive. The Division's Motion to Quash was not supported by any declarations or other evidence showing the objections had merit. The law judge quashed the subpoena in its entirety, and, by doing so, acted arbitrarily, capriciously, and not in accordance with law.

The documents requested were factual portions of documents withheld on the grounds of work product (Item 1); the investigative file for the Commission's previous investigation of Parrish (Item 2); various documents filed in the SEC's litigation against Parrish initiated in 2005 (Items 4 through 6); SEC training materials indicating the existence of a Ponzi scheme (Item 7); and the factual portions of all documents reflecting or relating to the Commission's decision to initiate an administrative proceeding against Mr. Bandimere, rather than a civil injunctive action.

Motions to quash are governed by Rule 232(e)(2), which provides that the only basis for quashing or modifying a subpoena is it is "unreasonable, oppressive, or unduly burdensome." The party seeking to quash must show these grounds exist, which is not satisfied by contentions

that the subpoena seeks information that is not relevant, nor reasonably likely to lead to the discovery of relevant evidence. *Hector Gallardo*, APR Rel. No. 667 Order on Motion (Feb. 25, 2011).

The law judge acted arbitrarily and capriciously in granting the motion to quash. The law judge summarily rejected arguments supported by cases decided under the Federal Rules of Civil Procedure, even though decisions recognize that, while not binding, those cases can be useful in deciding issues, under the Commission's rules. The Division's generalized claim of excessive hardship was unsupported by any declaration specifying what the burden would be. The claim of deliberative process privilege was not supported by a declaration of anyone, let alone someone with the requisite seniority, willing to state under oath, that specific documents were subject to a proper application of that privilege.

The law judge relied heavily on a purported lack of relevance of the requested documents, and speculated that the factual portions of documents relating to the decision to proceed administratively (relevant to Mr. Bandimere's equal protection defense and not covered by the deliberative process privilege) would contain no relevant information. The law judge did not have sufficient information on which to grant the Division's Motion to Quash, and a fair reading of his order indicates he relieved the Division of its burden of making a sufficient showing to warrant quashing the requested subpoena, but shifted the burden to Mr. Bandimere to show why the subpoena should not be quashed. Therefore, the law judge acted arbitrarily and capriciously in denying to Mr. Bandimere documents that could have assisted in preparing his defense.[19]

[19] The law judge also denied Mr. Bandimere's Motion for Interlocutory Review of his order quashing the subpoena which Mr. Bandimere had requested.

B. The Law Judge Erroneously Admitted Evidence that Was Irrelevant, and Relied on that Evidence

Rule 320 provides that the law judge "may" admit relevant evidence, but "shall" exclude evidence that is irrelevant. The law judge violated this rule by admitting evidence of the impact that investor losses had on the lives of investors. Mr. Bandimere was prejudiced by this irrelevant evidence because the law judge relied on it.

The Division adduced, and, over Mr. Bandimere's objection, the law judge admitted, without explanation of the relevance, evidence of the impact that investor losses had on some investors. Tr. 177; Tr. 248; Tr. 467-8; Tr. 699. That evidence was irrelevant to any issue. None of the violations alleged have investor impact as an element, and investor impact is not relevant to the sanction under the *Steadman* factors, or anything else.[20]

The law judge relied on investor impact evidence in determining sanctions. I.D. 87. Because imposing "heavy" sanctions rested in part on inadmissible evidence that should have been excluded, the law judge's sanction order must be vacated.

VIII. CONCLUSION

Mr. Bandimere is a law-abiding citizen who had a right to have serious charges against him decided in a fair proceeding which provided him proper notice of the matters he must defend, where facts are determined by a preponderance of the evidence and are applied to correct legal standards. He was denied those rights. The Division failed to prove the facts it alleged constituted violation of the law. The claims against Mr. Bandimere should be dismissed.

Dated this 18th day of February, 2014.

Respectfully submitted:

DAVIS GRAHAM & STUBBS LLP

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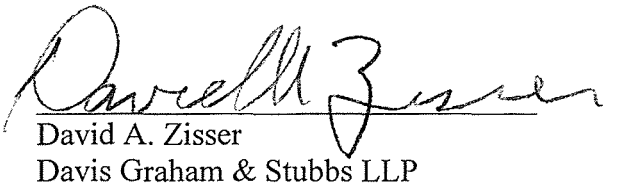
[20] Even if the impact of losses could be relevant where there is a foundation that Mr. Bandimere knew what the impact might be at the time of the investment, no such foundation was laid.



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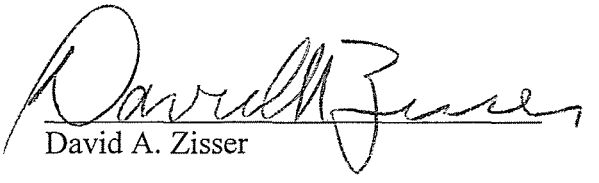
CERTIFICATE OF COMPLIANCE

This brief complies with SEC Rule 450 in that it contains 13,865 words.



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