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January 14, 2016

Via UPS Overnight

Hon. Cameron Elliot
Administrative Law Judge
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-2557

Re: In the Matter of James S. Tagliaferri;
Admin. Proc. File No. 3-15215

Dear Judge Elliot:

We represent the Division of Enforcement in this matter.

Enclosed are courtesy copies of the Division's submissions also sent to the Court by email, and to the Respondent by USPS Express Mail: Division's Reply in Further Support of Its November 19, 2015 Supplemental Submission and Its Motion for Summary Disposition; and my Declaration, executed January 14, 2016, in Support, and Exhibits.

Respectfully submitted,

Nancy A. Brown

cc: James S. Tagliaferri, Respondent (via USPS Express Mail)
Secretary's Office

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding
File No. 3-15215

In the Matter of

JAMES S. TAGLIAFERRI,

Respondent.

DIVISION OF ENFORCEMENT'S REPLY MEMORANDUM IN FURTHER SUPPORT OF ITS NOVEMBER 19, 2015 SUPPLEMENTAL SUBMISSION AND ITS MOTION FOR SUMMARY DISPOSITION

DIVISION OF ENFORCEMENT
Nancy A. Brown
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Dated: January 14, 2016

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The Division respectfully submits its Reply Memorandum of Law in Further Support of Its November 19, 2015 Supplemental Submission and Its Motion for Summary Disposition.

Preliminary Statement

Tagliaferri does not argue with the following points made in the Division's Moving Memorandum and Supplemental Submission:

- Tagliaferri advisory clients bought millions of dollars in notes issued by IEAH for which TAG received over $1.7 million in fees from IEAH. (Brown Oct. Decl.[1], Ex. G (Acquittal Order Motion at 2-3 (citing GX 400A and Tr. 889-90)).)

- Tagliaferri solicited investments in more than one issuer. (Supplemental Br. at 2, 5 (citing Brown Nov. Decl., Ex. A (GX 17-A, 1696, 2014)).)

- Tagliaferri negotiated the terms of each of the notes. (Supplemental Br. at 3, 5-6 (citing Brown Nov. Decl., Ex. A (GX 134, 607, 655, 656, 658 and 1202).)

- Tagliaferri selected the client accounts that funded the notes. (Supplemental Br. at 3-4 (citing Brown Nov. Decl., Ex. B (Tr. at 177-78; 536; 821-25; 1090-91; 1101-03; 1109-11; 1195).)

Because none of the arguments Tagliaferri makes detracts from these undisputed facts, the Division has demonstrated that Tagliaferri received transaction-based compensation for the placement of securities from the issuers, and was therefore acting as an unregistered broker.

ARGUMENT

A. The IEAH Notes Are Securities and Subject to Section 15(a) of the Exchange Act

The IEAH notes are securities and subject to all provisions of the Exchange Act,

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[1] "Brown Oct. Decl." refers to the Declaration of Nancy A. Brown, executed October 15, 2015. "Brown Nov. Decl." refers to the Declaration of Nancy A. Brown, executed November 19, 2015. "Supplemental Br." refers to the Division of Enforcement's Supplemental Submission in Response to the Court's October 30, 2015 Order to Show Cause and in Further Support of Its Motion for Summary Disposition. "Moving Memorandum" refers to the Division of Enforcement's Motion for Summary Disposition Against Respondent James S. Tagliaferri and Supporting Memorandum of Law, submitted October 15, 2015.

including the prohibition against their sale except by registered brokers or persons associated with a registered broker under Section 15(a).

Tagliaferri contends that the IEAH notes were properly denominated as "units," consisting of a note and an interest in a racehorse. (Tagliaferri Opp.[2] at 2-3.) In so arguing, Tagliaferri appears to concede that at least one portion of each "unit" was a security, but he argues that "race horses do not come under SEC jurisdiction." (Id. at 3.)

Tagliaferri is mistaken for at least two independent reasons. First, at trial, Tagliaferri testified that the IEAH notes were "convertible notes," explaining that such instruments were "convertible into the underlying shares of the company." (Declaration of Nancy A. Brown, executed January 14, 2016 ("Brown Jan. Decl."), Ex. A (Tr. at 1785).) Under the "family resemblance test" of Reves v. Ernst & Young, 494 U.S. 56, 64-65 (1990), courts have held that convertible notes acquired for investment purposes, like those Tagliaferri bought for TAG clients, are securities. E.g., SEC v. Constantin, 939 F. Supp. 2d 288, 304 (S.D.N.Y. 2013) (citing cases).

Second, interests in animals themselves can be securities, so long as they meet the Howey test of a security. Section 3(a)(10) of the Exchange Act defines "security" as including any "investment contract." Under SEC v. Howey Co., 328 U.S. 293 (1946), an investment contract is a security when a "person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party. . ." Id. at 298-99. The definition of a security "embodies a flexible rather than a static principle, one that is capable of adaptation

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[2] "Tagliaferri Opp." refers to Respondent's Opposition to Division of Enforcement's Supplemental Brief, in Response to the Court's Order of October 30, 2015, and in Further Support of Respondent's Opposition to the Division's Motion for Summary Disposition, dated December 22, 2015.

to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." Id. at 299.

In applying the Howey test, courts have held that investors purchasing an interest in animals buy a security when they lack the ability or power to select or care for the animal, or rely on the expertise of others to generate a profit from the investment. Thus, the Fourth Circuit has held that interests in cattle embryos are securities because the investors relied on the skill and expertise of the sponsor to select and crossbreed the resulting calves, from which the investors hoped to earn a profit when their newly created superior breed of cattle was sold. Bailey v. J.W.K. Properties, Inc., 904 F.2d 918, 923-25 (4th Cir. 1990). See also Sheets v. Dziabis, 738 F. Supp. 307, 312 (N. D. Ind. 1990) (interests in two horses for breeding program were securities under Howey). Like the investors in Bailey and Sheets, Tagliaferri's investors had limited involvement in the IEAH horse racing enterprise and relied on the skill and expertise of others to select the horses, and care for and race them. They were neither experienced in horse ownership, nor racing, and there is no evidence that any had any right to involve himself in the care or maintenance of his investments, nor that any of them did any of those things. (See, e.g., Brown Jan. Decl., Ex. A (Tr. at 230-32 (investor Temkin testifying about her surprise at learning of her interest in a racehorse); 539-41 (Gordon (same)); 1200 (Unger (same)).)[3]

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[3] Nor could Tagliaferri succeed in challenging the Galanis-related notes as securities. While most were of shorter maturity than nine months, courts have routinely held that notes of such a short duration are securities under Section 3(a)(10) so long as they are different from "the general notion of commercial paper." SEC v. R.G. Reynolds Enters., 952 F.2d 1125, 1132 (9th Cir. 1991) (citing, inter alia, Zeller v. Bogue Elec. Mfg. Corp., 476 F.2d 795, 800 (2d Cir. 1973).) And as the Supreme Court made clear in Reves, it is Respondent's burden to rebut the presumption that every note is a security. Reves, 494 U.S. at 64. Finally, Tagliaferri, himself, identified at least one of the Galanis-related notes as a one year note. (Brown Jan. Decl., Ex. A (Tr. at 2112-13 (Tagliaferri identifying an Equities Media note sold to an advisory client as a "one-year note" for which he received a fee of $100,000 from Galanis)).)

B. Tagliaferri Is Estopped from Arguing that He Did Not Receive Fees for the Sale of the IEAH and Galanis-Related Notes

Tagliaferri's argues that he did not receive transaction-based compensation for investing his clients in the notes issued by IEAH, (Tagliaferri Opp. at 3, 6), insisting instead that IEAH's payments to him were "NOT compensation for investing [TAG VI] clients' funds in IEAH." (Id. at 3.) He makes the same argument with respect to the Galanis-related notes. (Tagliaferri Opp. at 7 (disagreeing with trial testimony from a TAG employee that fees were paid on Galanis-related notes listed at GX 1696[4]).) But the District Court already rejected just that argument, finding that "ample evidence supports a finding that the fees Tagliaferri received were in exchange for his investment of his clients' funds into IEAH and the Galanis entities." (Brown Oct. Decl., Ex. G (Order on Acquittal Motion) at 7.) In support of her ruling, the Court credited the testimony of IEAH employees and emails between Tagliaferri and Jared Galanis, all of which made clear that the fees were in exchange for the client investments. (Id. (citing testimony of IEAH employees and emails between Tagliaferri and Jared Galanis; see also Brown Nov. Decl., Ex. A (GX 17-A at SEC-USDOJ-E-0013196[5] (admission by Tagliaferri that "TAG VI invested [a client's funds] in notes of private companies (Life InvestmentCo., Drexel Holdings and Equities Media)).) In each case, TAG VI received UNDISCLOSED 'referral' fees.").)[6]

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[4] The Division cited GX 1696 in its original submission, but copies may not have been included. GX 1696 is submitted herewith as Brown Jan. Decl., Ex. B. The Division sent another copy of GX 1696 to Mr. Tagliaferri, which he has advised that he received on January 5, 2016. (Brown Jan. Decl. ¶ 3.)

[5] Tagliaferri complains that this page, as well as other pages in this exhibit, is "virtually blank" or "largely redacted." (Tagliaferri Opp. at 5.) But the Division offers the Exhibit as it was admitted in the criminal proceeding, pursuant to stipulation, without objection by Tagliaferri. (See Brown Jan. Decl., Ex. A (Tr. at 942).)

[6] In support for his contention that the fees IEAH paid were not compensation for TAG client investments, Tagliaferri points out that four of the 16 transactions depicted on GX 2014 resulted in fees paid "months after 'TAG VI' client fund transfers to IEAH." (Tagliaferri Opp. at

C. Tagliaferri's Contention that His Attorneys Approved of These Transactions Is Both Irrelevant and Estopped

Tagliaferri attempts to assert an "advice of counsel" or "presence of counsel defense," contending that "[o]n all private transactions, Respondent relied on 'TAG VI's' outside counsel . . . and in-house counsel . . . for advice related to disclosure to client-investors." (Tagliaferri Opp. at 6, 7-8.) But Tagliaferri's reliance on such advice is both irrelevant and precluded.

First, lack of disclosure is not an element of a Section 15(a) violation. If Tagliaferri was acting as a broker in selling his clients IEAH or Galanis-related notes, and receiving transaction-based compensation for those investments from the issuers, he is liable under Section 15(a) whether he disclosed those fees or not. Thus, whether Tagliaferri was advised by counsel that he need not disclose the fees he obtained by placing his clients in IEAH and Galanis-related notes is irrelevant to his liability for accepting those fees without being associated with a registered broker-dealer.

Nor is scienter an element of a violation of Section 15(a). Matter of David B. Havanich, Jr., Admin. Proc. File No. 3-16354, 2016 WL 25746, at *5 (ID Jan. 4, 2016) ("Scienter is not required to establish a violation of this provision.") (citations omitted). Therefore, any reliance Tagliaferri placed on advice from any counsel would be irrelevant to whether he violated Section 15(a) because the defense works only to mitigate a respondent's scienter. Cf. Matter of David F. Bandimere, Admin. Proc. File No. 3-15124, 2013 WL 5553898, at *49 (ID Oct. 8, 2013) ("reliance on counsel 'is of no consequence' to [the Commission's] determination of violations

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3.) True enough, but Tagliaferri says nothing about the remaining 12 transactions that did result in contemporaneous fees paid by IEAH to TAG. Tagliaferri also offers the Declaration of Michael Iavarone, founder and CEO of IEAH, dated January 24, 2011. Appended to the Brown Jan. Decl. as Exhibit C is the Declaration of Michael Iavarone ("Iavarone Decl."), executed April 22, 2011, in which he recants his January 24, 2011 Declaration, and swears "TAG provided capital to the Company for which he was paid certain fees . . . ." (Iavarone Decl. ¶ 10.)

of Securities Act Section 5 because the 'advice-of-counsel defense only goes to the question of scienter' and scienter is not an element of Section 5 violations.") (quotations omitted), aff'd in relevant part, 2015 WL 6575665 (S.E.C. Oct. 29, 2015).

In any event, Tagliaferri is precluded from arguing the advice of counsel defense, even if it were relevant. At his criminal trial, Tagliaferri's counsel admitted that Tagliaferri could not satisfy all of the elements of an advice of counsel defense. As the Court stated in advising Tagliaferri that the Court would not give an advice of counsel instruction: "Defendant explained on Tuesday that he was not seeking this instruction because he does not expect the evidence to show that Mr. Tagliaferri sought specific legal advice on any particular legal issue." See Brown Jan. Decl., Ex. A (Tr. at 83.) Having made that concession at his criminal trial, despite the opportunity to fully litigate the issue, Tagliaferri is estopped from asserting that defense here. Matter of Eric S. Butler, Admin. Proc. File No. 3-13986, 2011 WL 3792730, at *5 (S.E.C. Aug. 26, 2011) ("we have long held that follow-on proceedings based on a criminal conviction are not an appropriate forum to 'revisit the factual basis for,' or legal defenses to, the conviction")(quotations omitted).[7]

D. The Division Satisfied Its Obligations to Make Its Investigative File Available

Tagliaferri does not contest that the Division offered to make its entire database available to him throughout the period prior to his incarceration. (Tagliaferri Opp. at 9, referring to Brown

[7] For this reason, Blinder, Robinson & Co. v. SEC, 837 F.2d 1099, 1109 (D.C. Cir. 1988), is of no help to Tagliaferri, even considering the other, scienter-based securities fraud and investor adviser fraud violations for which he was criminally convicted. In that case, the D.C. Circuit reversed the Commission's affirmance of an ALJ's ruling that the defendant could not put on advice of counsel evidence in a follow-on proceeding, holding that such evidence could directly lessen the egregiousness of his violations by mitigating his scienter. Id. But unlike the respondent in Blinder, Robinson, who was able to produce evidence of his reliance on the advice of counsel, but was precluded from doing so, Tagliaferri has already conceded in the Criminal action that he cannot produce such evidence. That concession is binding on him here.

Nov. Decl., Ex. E ("if you change your mind about reviewing [the documents] in the currently available Concordance format, we can arrange for you to do so . . . so long as you provide me with at least 24 hours' notice so that I can arrange a conference room and laptop for your use.").) Because there is no disagreement about that fact, the Division has satisfied its obligations under the Rule of Practice 230.

Tagliaferri maintains that the Division's offer was an empty one because he was "subject to home confinement." (Tagliaferri Opp. at 9; see also Tagliaferri December 22, 2015 Declaration at ¶ 18 ("Respondent [was] subject to a bail condition of home confinement.") But he fails to note that his bail conditions specifically allowed him to travel to the Southern District of New York (which includes the Division's New York Office). (Brown Jan. Decl., Ex. D (Order entered July 25, 2014).) Therefore, during the one month period prior to his incarceration, Tagliaferri presumably could have obtained his probation officer's consent to his travel to New York to review the Division's documents.

CONCLUSION

For the foregoing reasons, and those cited in the Division's Moving Memorandum[8] and its Supplemental Submission, the Division respectfully requests that its motion for summary disposition be granted, and that an order issue barring Tagliaferri from (1) associating with any broker, dealer, investment adviser, municipal securities dealer or transfer agent and participating in any offering of a penny stock; and (2) serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or

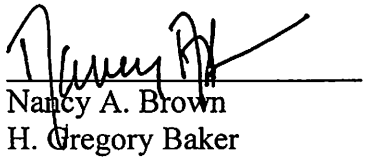
[8] The Division respectfully incorporates its analysis of the Steadman factors, provided at pages 10-13 of its Moving Memorandum, by reference herein.

principal underwriter.

Dated: New York, New York
January 14, 2016

Respectfully submitted,

DIVISION OF ENFORCEMENT

By: 

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CERTIFICATE OF SERVICE

I hereby certify that I caused the foregoing Division's Reply Memorandum of Law in Further Support of its Motion for Summary Disposition to be served on Respondent James Tagliaferri this 14th day of January 2016 by sending him a copy of the same to him by United States Postal Service Express Mail at the following address:

James S. Tagliaferri
[redacted]
Beaver, WV [redacted]

Nancy A. Brown