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**UNITED STATES OF AMERICA**

**Before the**

**SECURITIES AND EXCHANGE COMMISSION**

**ADMINISTRATIVE PROCEEDING**
**File No. 3-15514**

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In the Matter of

FRANK H. CHIAPPONE, :
ANDREW G. GUZZETTI, :
WILLIAM F. LEX, :
THOMAS E. LIVINGSTON, :
BRIAN T. MAYER, :
PHILIP S. RABINOVICH, :

Respondents.

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# RESPONDENT WILLIAM F. LEX'S SUR REPLY TO DIVISION OF ENFORCEMENT'S SUPPLEMENTAL REPLY BRIEF

# [CORRECTED VERSION]

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## I. The ALJ did not, and could not, undertake a "fresh look" at the record and perform the reconsideration function with a "considered approach and thoughtful analysis."

The Division's characterization of Judge Murray's March 30, 2018 Order as evidencing a "considered approach and thoughtful analysis" is not obvious from the Order itself. That fact that the ALJ performed the mathematics required in the recalculation of disgorgement is neither "considered" nor "thoughtful." The judge was required to make the recalculation based on a decision of the United States Supreme Court. *Kokesh v. S.E.C.*, 137 S.Ct. 1635, 198 L.Ed.2d 86 (2017). Respondent Lex suggests that the nature of the hearing record itself (6,000 pages;1,000 exhibits; numerous written and oral motions) prevented Judge Murray (who was integrally and intimately involved in the 18-day hearing) from independently making a "detached and considered affirmation of the earlier decision."[1]

Following a 119 page Initial Decision ("ID"), opining on the 2014 hearing in which 90% of the evidence related to events and sales which occurred outside the allowable limitation period under §2462, the ALJ found Respondents to have committed "securities fraud." And the securities fraud was based upon, at most, negligence. The principal expert for the Division, Kerri Palen, having examined the evidence of the McGinn-Smith fraud for more than 2-1/2 years, concluded that none of the Respondents knew of McGinn-Smith's fraud, and Judge Murray in the ID adopted Ms. Palen's view.

Respondent Lex was cross-examined by the Division on three occasions during the 18-day hearing, and fully 90% of the cross-examination related to events which occurred between 2002 and September 2008. For instance:

[1] *Advanced Disposal Servs. E., Inc. v. NLRB*, 820 F.3d 592, 602-03 (3d Cir. 2016)

- N.T. p. 4891 – events from 2003 to 2007;

- N.T. pp. 4829-4920 (91 pages) – cross by Stoelting regarding events occurring in 2002 and pre-2003 due diligence. Judge calls Lex's discovery of pre-2002 to 2003 PPMs which were provided to him by David Smith "suspicious," despite Lex having produced over 25,000 pages of documents pursuant to a pre-hearing subpoena;

- N.T. pp. 4925-4959 – where Division used 2002 and 2003 events to attack Lex's credibility and inquires of conversation between Lex and David Smith from 2003 to 2007;

- N.T. p. 1557 – Lex cross-examined about the formation by IASG in 2003;

- N.T. pp. 1564-1640 – Lex questioned about 2003 initial offering of FIIN and other questions about the period 2003 to 2006;

- N.T. p. 1653 – questions about 2007 transaction involving TAIN;

- N.T. p. 1668 – questions about FIIN, a 2003 Four Fund offering;

- N.T. 1672-1683 – questions about transaction in August 2007 and questions about events occurring from 2003 to early 2008. Lex was roundly criticized for not remembering, in 2014, conversations which he had and documents presented to him in 2002 – 14 years later.

The Judge Murray never saw the 2011 subpoena to ascertain whether it was complied with or whether it was so broad that a person served might not remember the existence of all documents which were related to a 2003 event. Judge Murray stated in the ID that "Lex's credibility is highly suspect." (ID. p. 103). Having determined that Respondent Lex's credibility was "highly suspect," how is it then possible for that same judge to review the testimony of Respondent Lex, and that relating to Lex, under the lens of a fair and thoughtful analysis? Is it believable that a judge can now in 2018, go back to the transcript and give a "fresh look" at all the testimony? This is particularly egregious when one considers these impressions have been made based on Lex's testimony about sales and events which occurred anywhere between 6 and 12 years before the hearing, and with respect to products, which sales and transactions are barred

by the statute of limitations. Thus, while Judge Murray acknowledges the reason why statutes of limitations are important, she ignores these important policy and due process considerations when rendering her opinion.

Credibility determinations were made not only with respect to Respondent Lex, but with respect to other Respondents as well, and the only reasonable conclusion a "fresh look" should bring about is that these Respondents, who themselves along with their families invested and lost hundreds of thousands of dollars in the various investments, were also duped. Yet, Judge Murray finds *scienter* in connection with the sales to customers. Nevertheless, the Division insists that Judge Murray gave this a "considered approach and thoughtful analysis." The fact is, and human nature dictates, that her conclusions were based on her original impressions of the case, not a "fresh look." Having found Respondent Lex's credibility "questionable" in 2014, is it likely she believes him now?

There was no evidence in the March 30, 2018 decision that the Judge reconsidered the penalty, especially in light of the fact that an entire aspect of the case (Four Funds) was no longer a part of the Division's claims. The total sales of Respondent Lex within the limitations period (after September 2008) is $1,605,000, and all in trusts (other than Benchmark). It does not appear that the ALJ reconsidered the penalty in light of the change of the nature of the case based on the statute of limitations and the elimination, in Respondent Lex's case, of 96% of the sales originally claimed by the Division.

## II. The unconstitutionality of the original proceeding cannot be cured by the ratification and reconsideration process; but assuming *arguendo*, that the original proceeding could be repaired by ratification and reconsideration, the ALJ has given no indication as to how she went about performing the reconsideration, thus denying Respondents of Due Process.

Judge Murray did not provide a description of how she went about examining the record so that matters which would have been inadmissible or irrelevant (matters outside the statute of limitation) were dealt with properly on reconsideration. We are asked to accept "on faith" that she excluded from her deliberations and ignored testimony and documents which should never have been received in evidence. Judge Murray did not indicate whether and how she analyzed rulings which, based on subsequent appellate decisions, would have qualitatively changed the body of evidence available to her to render a decision.

Given the stakes for these individual Respondents, the ratification and remand process, to pass constitutional muster, should not be treated as a mechanical exercise. For due process to be afforded these Respondents, a new proceeding before a new judge was required. Of course, a new proceeding would be barred by §2462.

This would not be an unjust outcome or result. The Commission and the Division put these Respondents through an exhausting and grueling procedure, both in terms of time and expense. This was done in the face of repeated claims by Respondents that the statute of limitations barred any transactions prior to September 23, 2008. The ALJ refused to hear a motion for summary disposition which would have eliminated 90% of the testimony, exhibits, and charges. Judge Murray stated: "I work for the Commission. If they tell me to hear it, I have to hear it," ignoring the fact that the SEC hearing rules permit motions for summary disposition. (See SEC Rule of Practice 250). Furthermore, the Respondents complained that the matter

should not be heard as an administrative proceeding, but rather in federal court. The Division opted to utilize the administrative process with virtually non-existent discovery and onerously short time periods from institution of proceedings to trial.

In the Division's rush to bring these Respondents to trial, disadvantaged in every way, it neglected to bring them before a constitutionally appointed adjudicator – the ALJ – which it thought would be its most favorable forum. A forum in which the judge, in response to a motion for summary disposition on the issue of statute of limitations stated:

> "... **the agency does not want motions for summary disposition granted because you're second-guessing their decision that the case needs to get set down for hearing and that there is a legal basis for it** . . . I work for the Federal Government. I am an Administrative Law Judge. The case is in this office. **It's been assigned to me for decision. So I have to hear it.**" [Emphasis added]

[N.T. 1/21/14 – Pre-Hearing Telephone Conference, pp. 30, 33-34].

**III. Incorporation By Reference**

In connection with and as part of this brief, Respondent Lex incorporates by reference all of the briefs and submissions provided to this Commission by Respondent Lex and all other Respondents, including the Joint Briefs and Joint Reply Brief originally filed, pursuant to the appeal from the ID. In addition, Respondent Lex incorporates by reference all the arguments contained in all other Respondents' Briefs submitted in connection with Judge Murray's March 30, 2018 Order Revising and Ratifying Prior Actions, as well as Briefs submitted previously to the Commission, and all arguments before the Commission in connection with the original Petition for Review.

## IV. Conclusion

For the reasons set forth herein, and the briefs and arguments incorporated herein by reference, the proceedings against Respondent William F. Lex should be dismissed.

Respectfully submitted,

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**BY:** _____

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DATED: June 15, 2018

## CERTIFICATE OF COMPLIANCE

The within supplemental brief complies with the word limit in the Commission's Supplemental Briefing Order dated April 20, 2018. The brief contains 1,590 words, exclusive of the Table of Contents, the Table of Cites, this Certification and the Certificate of Service, as counted by Microsoft Word, the word processing system used to prepare it.

DATED: June 15, 2018

GILBERT B. ABRAMSON, ESQUIRE

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## CERTIFICATE OF SERVICE

Gilbert B. Abramson, Esquire, hereby certifies that on June 15, 2018, service of Respondent William F. Lex's Sur Reply to Division of Enforcement's Supplemental Reply Brief was made, upon the following persons in the following manner:

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June 15, 2018

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