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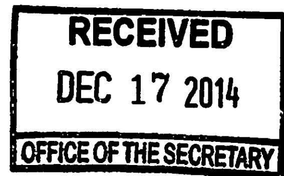

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15519

In the Matter of

Timbervest, LLC,
Joel Barth Shapiro,
Walter William Anthony Boden, III,
Donald David Zell, Jr.,
and Gordon Jones II,

Respondents.

DIVISION OF ENFORCEMENT'S REPLY BRIEF IN
SUPPORT OF ITS PETITION FOR REVIEW

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I. INTRODUCTION

The Division of Enforcement ("Division") submits this reply brief in support of its Petition for Review (the "Appeal"). In their response brief opposing the Division's Appeal ("Response"), Respondents claim that 18 U.S.C. § 2462 ("Section 2462"), as a matter of law, categorically prohibits revocation of registration and individual associational bars (collectively referred to as "associational bars") in this matter. They further claim that, even if associational bars were permissible, the evidence does not support the Division's claim that such sanctions are necessary and appropriate. They also dispute the Division's contention that Zell and Jones acted with scienter. Finally, Respondents challenge many of the ALJ's findings of fact which provide support for the Division's Appeal. Respondents' arguments should be rejected because they misstate the law and the record.

II. ASSOCIATIONAL BARS ARE PERMISSIBLE WHEN REMEDIAL

Respondents first argue that associational bars are not permitted by Section 2462 as a matter of law because such bars are penal by nature. Response at 3. This categorical pronouncement is not supported by authority. Associational bars can be either remedial or punitive depending on the degree of risk Respondents pose to the investing public. *See* Appeal at 40-43. Sanctions that are properly deemed to be remedial are not subject Section 2462, and an associational bar is remedial if the Commission determines that a bar is necessary to protect the public based on its finding that a person poses a realistic threat of future harm to investors. *See Johnson v. SEC*, 87 F.3d 484 (D.C. Cir. 1996)(stating, "[A six-month suspension] would less resemble punishment if the SEC had focused on Johnson's current competence or the degree of risk she posed to the public").

Respondents' erroneous claim that all associational bars are penal is partly premised on the notion that, from the perspective of the person being barred, such remedies feel like punishment. Response at 2 (quoting *Steadman v. SEC*, 603 F.2d 1126, 1139-40 (5th Cir. 1978)) (stating that "from Steadman's perspective, 'exclusion from the industry is clearly a penalty'"). The test for whether a bar is penal or remedial, however, is not a subjective one. *Johnson*, 87 F.3d at 488 ("It is obviously not enough that the person subjected to a sanction feels pain or finds the sanction disagreeable; as the Supreme Court has pointed out, 'even remedial sanctions carry the sting of punishment'")(quoting *United States v. Halper*, 490 U.S. 435, 447 n.7 (1989)). Moreover, as the Court noted in *Johnson*, a subjective test would "would render virtually every sanction a penalty"—including disgorgement and injunctive relief. *Id.* Instead, the test for whether a sanction is remedial or punitive is an objective one based on the facts and circumstances of the given case. If the Commission determines, based on the record, that there is a realistic threat of future harm, sanctions tailored to prevent such harm are properly viewed as remedial and thus not subject to Section 2462.

In support of their mistaken contention that all bars are penal, Respondents cite cases which they claim show that the Supreme Court and other lower courts deem associational bars to be penalties. Response at 3-4. Their citations are inapposite, however, as none of these cases sought to interpret the meaning of a "penalty" in the context of Section 2462. Indeed, Respondents' cases have nothing at all to do with Section 2462, much less with the distinction between remedial and punitive sanctions as it pertains to the five-year statute of limitations. *See Spevack v. Klein*, 385 U.S. 511 (1967)(defining "penalty" in relation to an individual's Fifth Amendment privilege against self-incrimination); *United States v. Lovett*, 328 U.S. 303 (1946) (discussing "punishment" in the context of the Constitution's prohibition against "bills of

attainder"); *Collins v. SEC*, 562 F.2d 820 (D.C. Cir. 1977) (discussing standards of proof with regard to imposing certain sanctions); *Dailey v. Vought Aircraft Co.*, 141 F.3d 224 (5th Cir. 1998) (holding that disbarment without prior notice and opportunity to be heard violated attorney's right to due process); *Nat'l Surety Co. v. Page*, 58 F.2d 145 (4th Cir. 1932) (discussing whether a proceeding to revoke an insurance license under state law supports malicious prosecution claim).

Moreover, in analogous contexts, Courts have found that orders barring defendants from their chosen profession should be viewed as remedial. *See Kornman v. SEC*, 592 F.3d 173, 189 (D.C. Cir. 2010) ("[t]he revocation of a privilege voluntarily granted, such as a debarment," is "remedial in nature because it is designed to protect the public, and the sanction is not historically viewed as punishment") (internal quotations omitted); *Hudson v. United States*, 522 U.S. 93, 104-05 (1997) (explaining that FDIC debarment historically has not been "viewed as punishment" but rather "serve[s] to promote the stability of the banking industry"); *Ex parte Wall*, 107 U.S. 265, 288 (1883) (describing attorney debarment as "not for the purpose of punishment, but for the purpose of preserving the courts of justice from the official ministration of persons unfit to practice in them").

Respondents also complain that the Division's citations to *Bartko*, 2014 WL 896758 (Mar 7, 2014); *Zubkis*, 2005 WL 3299148 (Dec. 2, 2005); and *Contorinis*, 2014 WL 1665995 (Apr. 25, 2014) are not relevant because those cases involved follow-on proceedings. Response at 4-5. They claim that the conduct which gave rise to the administrative proceeding (*i.e.*, the civil injunction or the criminal conviction) occurred within the limitations period specified in Section 15(b) of the Exchange Act, thereby obviating the need to determine whether Section 2462 applied. *Id.* Regardless of Respondents' belief that the Commission had no "need" to

determine if Section 2462 applied in those cases, the Commission chose to address the issue and held that Section 2462 did not apply. That there were independent grounds for the Commission's holdings does not negate the import of its recent determinations in the three separate appeals that Section 2462 is inapplicable to forward-looking associational bars.

In *Bartko*, the misconduct giving rise to Bartko's convictions took place from 2004 to 2005, and the OIP was filed against him in 2012. *See* 2014 WL 896758 at *1-5. The Commission held that Section 2462 did not apply for "two *independent* reasons," one of which was that "the five-year statute of limitations does not apply because this proceeding is not 'for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise' within the meaning of § 2462." *Id.* at *9 (quoting Section 2462)(emphasis added). The Commission stated:

> Bartko argues that the associational bars at issue in this proceeding are punitive sanctions covered by § 2462. But as we held in *Lawton*, the remedies analysis is not driven by the need to punish respondents; rather the analysis is prospective and focuses on Bartko's "current competence" and the "degree of risk" he poses to public investors and the securities markets in each of the areas covered by the remedies.

Id. (footnotes omitted).

In *Zubkis*, too, the Commission determined Zubkis's Section 2462 argument to be inapplicable as one of two independent bases for finding the proceeding not time-barred, stating: "[I]n determining that the public interest requires that Zubkis be barred, we are focusing on the respondent's 'current competence or the degree of risk [he] poses to the public.' Hence, the sanctioning assessment at issue in this proceeding is not punitive, as the court found it was in *Johnson*, but remedial, and therefore not subject to Section 2462. 2005 WL 3299148 at *4 (internal citation omitted). Likewise, in *Contorinis*, while the Commission did emphasize the Exchange Act's provision of a ten-year period from the date of the criminal conviction to initiate a proceeding based on the same, it also plainly stated: "[T]he five-year statute of limitations of §

2462 does not apply in this case because a follow-on proceeding seeking an industry-wide bar is not 'for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise' within the meaning of § 2462." 2014 WL 1665995 at *3 (internal citations omitted).

Respondents likewise take issue with the Division's citation to *Meadows v. SEC*, 119 F.3d 1219 (5th Cir. 1997). In particular, they claim that *Meadows* offers no guidance since the administrative proceeding in that case was instituted within five years of the relevant misconduct. Response at 5. Again, Respondents fail to address the Division's main point. In *Meadows*, the respondent relied on the D.C. Circuit's interpretation of Section 2462 in *Johnson* to support his claim that an associational bar was punitive. *Id.* at 1228 n.20. The Fifth Circuit rejected the respondent's argument, stating that his reliance on *Johnson* was misplaced. *Id.* The Court then went on to emphasize that, depending on the facts and circumstances of the case, associational bars can be remedial if, as the ALJ found in that case, "the reason for the sanction is the degree of risk petitioner poses to the public and is based upon findings demonstrating petitioner's unfitness to serve the investing public." *Id.*

Respondents attempt to distinguish several cases cited by the Division on the grounds that no bar was actually imposed. Response at 5-6 (discussing *SEC v. Brown*, 740 F. Supp. 2d 148 (D.D.C. 2010); *SEC v. Jones*, 476 F.Supp. 2d 374 (S.D.N.Y. 2007); and *Herbert Moskowitz*, 2002 WL 434524 (Mar. 21, 2002)).[1] Once again, however, Respondents fail to recognize that

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[1] Respondents claim that the Division misrepresented the holding in *Jones*. Response at 6 n.3. In fact, it is the Respondents who mislead by suggesting that equitable remedies (specifically injunctive relief) were unavailable as a matter of law. *Id.* at 6 (stating only that the remedies sought were "unavailable due to the passage of time"). Indeed, the Court in *Jones* did conclude that injunctive relief was unavailable, but in doing so the Court employed the same test that the Division advocates in this matter. *Jones*, 476 F.Supp.2d at 383 (stating, "[W]hether the Commission's action for a permanent injunction is subject to the five-year limitations period in § 2462 depends on whether the injunction is a penalty or a remedial measure").

each of those decisions specifically addressed the Division's central argument, namely that relief which is based on a threat of future harm to the public or on a showing that respondents are unfit to fulfill their professional obligations is remedial in nature and therefore not subject Section 2462.

Finally, Respondents attempt to distinguish two cases cited by the Division, (*SEC v. Alexander*, 248 F.R.D. 108 (E.D.N.Y. 2007), and *SEC v. Quinlan*, 373 Fed. App'x 581 (6th Cir. 2010)) based on the assertion that officer and director ("O&D") bars are more narrowly tailored than associational bars. Response at 6. This, however, is a distinction without a difference. As the Division has already demonstrated, the remedial or punitive character of relief imposed by the Commission does not turn on whether the relief feels like punishment to the Respondent. Moreover, O&D bars and the associational bars sought against the Respondents are highly analogous. Like an O&D bar, a bar from associating with an investment adviser does not preclude the recipients of such bars from exercising their skill sets in other sectors of the economy. In this matter, an associational bar would not prevent Respondents from continuing to work in the timber management or commercial real estate industries. It would not prevent Boden from continuing to sell real estate as a licensed broker or Jones from continuing to practice law. Zell would be completely free to manage operations, including backroom accounting, for any company not implicated by the bar. Similarly, Shapiro could continue his activities as an investor in various private ventures or serving as an officer of a company outside the scope of the bar. In sum, an associational bar would be directed only to the highly regulated areas in which Respondents' continuing disregard toward their fiduciary responsibilities makes them a threat to the investing public, and over which the Commission has jurisdiction. *See Conrad P. Seghers*, Advisers Act Rel. No. 2656 (Sept. 26, 2007) (The securities industry "presents continual

opportunities for dishonesty and abuse, and depends heavily on the integrity of its participants and on investors' confidence").

Respondents simply cannot support their claim that Section 2462 applies to all associational bars as a matter of law. Associational bars that are aimed at protecting the public from harm are not subject to Section 2462.

III. THE RECORD SUPPORTS THE CONCLUSION THAT ASSOCIATIONAL BARS ARE APPROPRIATE

Respondents next contend that, even if associational bars are not precluded as a matter of law, such sanctions would be inappropriate in this matter. Their claim is belied by the facts in the record and by the ALJ's findings.

A. The Division Presented Ample Evidence that Associational Bars are Necessary and Appropriate

As argued at length in the Division's Appeal (*see id.* at 5-39), Respondents engaged in highly calculated schemes to defraud their client by unlawfully cross-trading its assets and by paying themselves millions of dollars in undisclosed fees which were disguised in a structure that resembled money-laundering. Respondents then took numerous steps to conceal their misconduct. The two witnesses who could have corroborated Respondents' denials of wrongdoing (*i.e.*, Wooddall and Schwartz) inculpated them instead.[2] The Respondents have refused to recognize the wrongful nature of their misconduct. Indeed, they have never even conceded that they harmed their client, instead arguing—audaciously—that the undisclosed

[2] The ALJ found these witnesses to be credible, and his findings are entitled to "considerable weight and deference." *Guy P. Riordan*, 2009 WL 4731397 at *10 (Dec. 11, 2009).

brokerage fees actually benefitted their client.[3] *See* Timbervest, LLC's Appeal to the Commission at 3. Moreover, they have provided no credible assurances against future misconduct, but instead have shown a blatant disregard for their fiduciary obligations. Respondents remain associated with an investment adviser and intend to remain in that industry for the foreseeable future. *See* I.D. at 64. They still manage timber and environmental funds, some of which will remain in existence until 2024 (and which offer limited avenues for investors to exit), and are seeking to launch additional funds. Tr. 61:4-62:3; 1377:3-1378:13; 1850:9-1851:5. The record therefore clearly supports the determination that associational bars are necessary to protect the public from a realistic threat of future harm by persons who are unfit to serve as investment advisers.

Moreover, additional evidence developed at the hearing shows that Respondents engaged in other misconduct which *further* demonstrates their cavalier attitudes toward their fiduciary duties. Such evidence includes: (1) Respondents' 2005 attempt to cross-trade the Glawson property using Hailey as a middleman (a plan that only ceased after Zachry Thwaite's attorney threatened to sue them if the cross trade went through); (2) their undisclosed construction of a hunting lodge on the Glawson property using New Forestry's funds; (3) their undisclosed use of the Glawson property to entertain Timbervest's clients and to court potential clients; (4) their misleading statements to AT&T regarding the payment of fees and the cross trade of Tenneco Core after their fraud was discovered in 2012; and (5) their uncooperative behavior during the transition of New Forestry to new managers by, among other things, failing to provide the client with access to the general ledger showing expenditures related to the property.

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[3] The ALJ characterized this argument as "silly." *See Timbervest, LLC*, Initial Decision Rel. No. 658 (Aug. 20, 2014) [hereinafter "I.D."] at 55.

Likewise, the ALJ's findings, which were supported by the evidence developed at the hearing and detailed in his 73-page initial decision, also support the conclusion that Respondents lack the "current competence" to meet their fiduciary obligations. *See Johnson*, 87 F.3d at 489. The ALJ found that Respondents engaged in egregious misconduct evidencing their "obliviousness to their fiduciary duties, which continues today." I.D. at 65. Rather than admit their wrongs, the ALJ observed that Respondents "brazenly argue[] that Boden's fee agreement 'was designed to benefit New Forestry,' and that the Tenneco Core cross trade was 'a good sale for New Forestry.'" I.D. at 64 (citing Timbervest's Post-Hearing Brief). Moreover, the ALJ noted that Respondents' assurances against future violations were not sincere, given their "utter lack of recognition that their conduct violated the law." I.D. at 64. He likewise found that their claim that Boden's "agreement" has expired only indicated that Respondents are not likely to defraud their clients again *in that manner*. I.D. at 64-65 ("That there is no current fee agreement comparable to Boden's does not mean Respondents cannot suffer from other conflicts of interest in the future").[4] In sum, both the record itself and the ALJ's conclusions drawn from it, support the Division's claim that associational bars in this matter are necessary to protect the public from future harm.

B. Respondents' Complaints Regarding Additional Evidence Developed at Trial <u>Must be Rejected</u>

With the benefit of hindsight, Respondents apparently recognize that the evidence developed at trial supports the conclusion that they are unfit to serve as investment advisers. They therefore attempt to rewrite the record by demanding that the Commission disregard all conduct related to Glawson and to their interactions with AT&T in 2012 when considering

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4 Respondents raise this argument again in their Response. *See id.* at 9.

whether associational bars are warranted. Response at 9-10. Respondents complain that these issues were not pled in the OIP, leaving them with no notice that their current conduct or competence would be at issue at trial. *Id.* at 10. Their complaints are disingenuous and their demands must be rejected.

Contrary to the Respondents' claims, the OIP need not identify all of the evidence on which the Division intends to rely at the hearing. *Murray Securities Corp.*, 1957 WL 52415 at *1 (May 2, 1957); *Morris J. Reiter*, 1959 WL 59479 at *2 (Nov. 2, 1959); *J. Logan & Co.*, 1959 WL 59528 (Feb 3, 1959). The OIP only has to give notice of the charges laid against the Respondents and the theories of liability to be tried. *Murray Securities Corp.*, 1957 WL 52415, at *1.

Respondents concede these points (*See* Reply to the Division of Enforcement's Opposition to Respondents' Motion to Strike Uncharged Allegations, or, in the Alternative, to Introduce New Evidence [hereinafter "Motion to Introduce Evidence"] at 3-4), which leaves them no choice but to claim that the issues related to Glawson and AT&T somehow represented allegations of wrongdoing and theories of liability that were never pled. *Id.*; *see also* Response at 10. Nonsense. The Division's theories of liability have been manifestly clear to the Respondents since (at the very least) they received their Wells notice in January 2013. The Division has consistently alleged that Respondents violated Sections 206(1) and (2) of the Advisers Act by failing to disclose the conflicts of interest associated with (1) the sale and repurchase of Tenneco Core and (2) Boden's collection and sharing of the fees taken from New Forestry's assets. *See* Timbervest Wells Submission, Div. Ex. 74 at 1("The Wells Notices [of January 17, 2013] state that these violations are based on the 'sale and repurchase of the Tenneco core timberland in 2006 and 2007' and the 'collection of advisory fees on the sale of Tenneco in

2006 and the sale of the Kentucky timberlands in 2007'"). These theories of liability (and these theories only) were tried at the hearing, and the remedies imposed flow directly from the ALJ's finding that the Division carried its burden in regard to these allegations.[5]

Moreover, the Division made clear from the beginning of the Wells process that it planned to seek associational bars against the Respondents.[6] *See* Div. Ex. 74 at 29 (stating, "The Staff also indicated that it may seek revocation of Timbervest's registration as an investment adviser and associational bars as to the Partners"). As discussed above, a major component of the analysis for determining whether such associational bars are warranted is a determination of the Respondents' current competence or the degree of risk they pose to the public. *See Johnson,* 87 F.3d at 489.[7] Respondents are well aware of this, as they argued in their Reply Brief in Support of Motion for Summary Disposition that it was undisputed that "Respondents pose no risk of future misconduct." *Id.* at 13. Furthermore, when the ALJ informed the parties that he believed associational bars would not be available in this case, the Division filed a Notice of

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5 Respondents concede that no additional theories of liability were pled. Response at 10.

6 Respondents make the meritless claim that the passage of time between the issuance of the Wells notice and the filing of the OIP cuts against the Division's expressed views regarding the egregiousness of their conduct. Response at 7. Respondents fail to disclose, however, that any delays were the result of the protracted—but ultimately unsuccessful—settlement discussions between the parties. As Respondents' counsel noted, the settlement discussions failed because of the Division's insistence on associational bars. *See* Pre-Hearing Conference Tr. 29:19-25; 56:11-57:19. Accordingly, for Respondents to now seek to use the time spent on settlement negotiations to avoid a bar is disingenuous.

7 Respondents' contention that *Steadman* does not provide the proper analysis for considering associational bars (*see* Response at 6-7) is incorrect. Any analysis performed under *Steadman* regarding the need for a cease-and-desist order is germane to the issue of whether associational bars are also appropriate. As the Second Circuit has noted, "[We] read the *Steadman* factors, which closely resemble the *Patel* [61 F.3d 137 (2d Cir. 1995)] factors, as suggestive and non-exclusive indicators of unfitness to serve as a fiduciary." *SEC. v. Bankosky,* 716 F.3d 45, 49 (2d Cir. 2013).

Intent to Pursue Associational Bars. Doc. 29. Respondents claim that they were unaware that allegations concerning their unfitness to serve as investment advisers would be an issue at the hearing must therefore be rejected.

Finally, as detailed in the Division's Opposition to Respondents' Motion to Introduce Evidence, the Respondents' complaints as to notice and the opportunity to impeach regarding the issues of Glawson and their interactions with AT&T in 2012 are baseless. First, Respondents cannot credibly contend that they were unaware that the Glawson cross trade would be an issue at the hearing, as they interviewed Hailey after the Division disclosed its intention to call him as a witness. Tr. 877:1-890:15. Respondents knew that Hailey's only testimony would relate to the attempted cross trade of Glawson. Moreover, Respondents' counsel (who also represented Ralph Harrison) took steps to prepare for the issue by producing new relevant documents on the eve of trial and providing an affidavit in which Harrison admitted to giving false testimony to the Division during the investigation. Tr. 568:25-575:11. Second, the issue of Respondents' use of the property for personal gain was not initiated by the Division, but was part of Frank Ranlett's response to a question posed to him by Respondents' counsel. Tr. 1143:4-1145:14. Respondents cannot complain about lines of inquiry which they opened and have since come to regret. Third, Respondents' 2012 letters to AT&T contain misrepresentations and omissions that go the very heart of the conduct charged in the OIP. Fourth, Respondents cross-examined Ranlett with regard to AT&T's transition of the New Forestry account, and they never indicated that they thought they needed more time to sufficiently address the issue. Tr. 1087:11-1089:18; 1208:25-1214:09. They then rested their case without calling a single witness. Having had ample opportunities to offer additional evidence and to impeach the Division's witnesses, Respondents' claims must be rejected.

IV. THE ALJ'S FINDINGS SUPPORT THE CONCLUSION THAT ZELL AND JONES ACTED WITH SCIENTER

Respondents also mistakenly contend that the ALJ was correct in determining that Zell and Jones did not act with scienter with regard to the disclosure of Boden's fees to the client. Response at 22. Although on balance he concluded to the contrary, in weighing the evidence the ALJ found that numerous factors "weigh[ed] in favor of finding scienter as to Zell and Jones" regarding the payment of Boden's fees. I.D. at 53. He also stated: "To be sure, there is evidence that Zell and Jones knew that Boden's fees were categorically prohibited under ERISA, and thus that Zell and Jones could not have believed that Shapiro's disclosure was legally effective." I.D. at 54. If the ALJ is correct on this point, as the Division contends that he was, then it is impossible that Zell and Jones could have reasonably believed Shapiro's representation that he obtained consent from the client to pay the fees to Boden, and the ALJ's findings on this point must be deemed erroneous.

The receipt of ancillary fees by a principal of Timbervest was strictly prohibited by Timbervest's written agreements with its client. As the ALJ noted, the fee agreement "provided for compensation to Timbervest, and by extension to the other Respondents, *only by way of management fees and disposition fees*." I.D. at 48 (emphasis added). Furthermore, Timbervest agreed not to engage in prohibited transactions under ERISA, which cannot be cured by disclosure.[8] *See* Expert Report of Arthur H. Kohn, Div. Ex. 137 at 18. Moreover, Barag's testimony demonstrates that Jones was knowledgeable about his responsibilities under ERISA and that he specifically knew that he could not collect fees from New Forestry that were outside

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[8] ERISA presupposes that fiduciaries know their duties under the law. *See* Div. Ex. 137 at 28.

of the management agreement.[9] Also, as the President, General Counsel, and Chief Compliance Officer at the time of the violations, Jones, a former law partner, was charged with ensuring that the firm met all of its regulatory and legal responsibilities. Jones' defense of wholesale ignorance as to his compliance duties is simply an attempt to evade responsibility for his role in defrauding his client.

The evidence developed at the hearing also demonstrates that Zell's violation respecting the fees constituted more than mere negligence. As noted, the management agreements prohibited Timbervest from collecting any compensation other than disposition and management fees. In addition, Zell managed the same New Forestry account on behalf of BellSouth before joining Timbervest. Tr. 1532:16-1534:21. Moreover, Barag testified that he worked with Zell on several ERISA-related issues and that ERISA came up "all the time" in the context of managing New Forestry. Tr. 1942:10-1943:1. Zell also disingenuously downplayed his knowledge of ERISA at the hearing, and even unwittingly demonstrated his knowledge of ERISA when he testified that he thought New Forestry met the criteria for the Real Estate Operating Company ("REOC") exception.[10] Tr. 1597:18-1598:9; *see also* Div. Ex. 137 at 10;

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[9] Respondents' claim that Barag testified that there was no conversation about "commissions" is highly misleading. Response at 24. The Division has never argued that Barag spoke with the Respondents about "commissions." Rather, the Division noted, consistent with the record, that Barag had conversations with Jones and Shapiro about *compensation under ERISA*, and that both Shapiro and Jones knew, based on Barag's comments to them, that Respondents could not get any compensation other than what was provided for in the management agreements. *See* Appeal at 24.

[10] The Respondents attempt to use ERISA's potential complexity as a shield to their scienter, claiming that even Schwartz, who had served as an ERISA expert in another matter, testified that he would need to seek advice from qualified legal counsel to answer ERISA questions. Response at 25. Respondents fail to point out, however, that Schwartz found the analysis of whether Boden's fees were prohibited under ERISA to be simple. Indeed, when asked whether he would need to consult legal counsel if Shapiro had told him that Timbervest

continued . . .

I.D. at 53. Given Zell's personal knowledge of ERISA and his experience managing New Forestry on behalf of BellSouth, the payment of fees to Boden which were not provided for in the management agreement would have presented enormous red flags which he could only have ignored if he were acting recklessly or intending to deceive his client.

Finally, nothing in the record supports Respondents' completely unsubstantiated claims that Jones and Zell subjectively believed that ORG, as a qualified pension asset manager ("QPAM"), could "make decisions on behalf of New Forestry and approve [Boden's fee] agreement." Response at 24, 26. Jones and Zell never testified to such, and Respondents make no effort to cite to the record on this point. Also, while Schwartz testified that ORG was a QPAM, he also testified that he did not recall making such a representation to anyone at Timbervest. Tr. 2145:22-2146:5. Moreover, as discussed in the Division's expert report, the QPAM exception is a technical aspect of ERISA. *See* Div. Ex. 137 at 20-21 n.1. To assert that Jones and Zell subjectively believed that ORG, as a QPAM, approved the fees is to admit necessarily that they in fact possessed a highly sophisticated sense of what ERISA requires, something which the Division contends and which Barag's testimony supports. Indeed, to claim, as Respondents do, that Jones and Zell had at most a passing knowledge of ERISA (Response at 24, 25), but understood that a QPAM could make decisions on behalf of New Forestry and approve Boden's fee arrangement, is akin to saying that a person does not understand baseball but comprehends the Infield Fly Rule.

. . . *continued*
wanted to pay fees to one of its partners, Schwartz responded, "That would have been an easy one because we would have absolutely said, 'No way.'" Tr. 2060:8-15.

Furthermore, to the degree they understood that ORG was in fact a QPAM, they would have known, as Schwartz testified, that a QPAM has to negotiate any such deal independently. Tr. 2061:10-2062:11; 2146:6-20; *see also* Div. Ex. 137 at 20-21 n.1. This would have raised yet another red flag, because, under *no version* of events presented at trial did ORG negotiate Boden's supposed fee agreement in 2002.[11] Finally, irrespective of their subjective belief regarding whether ORG was a QPAM, the record clearly shows that, upon hiring ORG, BellSouth sent a letter to Timbervest, addressed specifically to Zell, which noted that BellSouth still expected Timbervest to report to them regarding New Forestry's activities. Div. Ex. 178; Tr. 1529:19-1532:15.

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[11] In a convoluted attempt at misdirection, Respondents equate Timbervest's disposition fee agreement, which was negotiated between Timbervest and BellSouth and memorialized in written, executed contracts, with the oral fee agreement negotiated between Boden and Shapiro. Response at 24-25. They then make the extraordinary claim that Jones and Zell somehow took comfort from these similarities. *Id.* at 25 (noting "Jones had no reason to think New Forestry and ORG would consent to one such conflict but not the other"); *id.* at 26 (claiming that Zell had no reason to doubt that ORG, as a QPAM, had consented to Boden's fees because it had already approved a "similar conflict" with regard to the disposition fees). Leaving aside the fact that Jones and Zell never testified that this was their basis for believing that Schwartz had agreed to the fees, this claim actually implicates them further. To the degree that they did consider the two situations analogous, they would have certainly noticed the differences between the two fees—namely that the disposition fees were negotiated by opposing sides and that the agreement culminated in a written, executed contract. Having noticed these differences, it is highly unlikely that Zell, as the former manager of the account, and Jones, as the CCO and General Counsel of the firm, would have formed the belief that a mere oral announcement to ORG of Respondents' intent to unilaterally pay extra fees to Boden amounted to effective disclosure.

V. RESPONDENTS' MISCELLANEOUS FACTUAL ARGUMENTS ARE AT ODDS WITH THE CONTEMPORANEOUS DOCUMENTS AND THE TESTIMONY OF CREDIBLE WITNESSES

A. Respondents Distort the Record with Regard to the Cross Trade of Tenneco Core

Respondents make several false and misleading statements with regard to the cross trade of Tenneco Core which must be addressed. First, Respondents incorrectly claim that Wooddall's memory of the repurchase has been evolving. Response at 30. They also state that Wooddall was simultaneously negotiating another deal with Timbervest regarding a Texas property at the time of the Tenneco Core sale. *Id.* With no support, Respondents then posit that Wooddall could be "blurring his memories" of the two discussions. *Id.* This is fanciful speculation that has no basis in the record. Moreover, it is completely nonsensical to suggest that Wooddall confused the two deals, as the Texas deal did not involve an anomalous agreement to "land bank" the property for later repurchase by Timbervest.

Respondents also contend that they voluntarily disclosed the cross trade and the payment of Boden's fees to the Division (*see* Response at 30, 34). This is false. Respondents only "volunteered" the information regarding the cross-trade in response to the Division's subpoena for information regarding all properties that were once owned by one Timbervest client and later came to be owned by another Timbervest client. *See* Div. Ex. 79 at 5. Likewise, as the ALJ noted, Timbervest's so-called disclosure of Boden's fee agreement "took place after issuance of a subpoena asking for all records of payments by Chen or Wooddall to Boden or Timbervest, and it was hardly fulsome, in view of [Seabolt's disclosure letter to AT&T] just months later." I.D. at 55; *see also* Div. Ex. 115. Responding to a compulsory process cannot reasonably be considered voluntary.

Respondents also point out that, following conversations with Barag in 2003 or 2004, Zell was unwilling to engage in a cross-trade of BellSouth's properties because it would suggest that "Timbervest was more interested in getting control of the assets than maximizing performance of the separate account." Response at 31 (citing Tr. 1936-37). They go on to claim that the Division "has no explanation for why Zell and Shapiro would have refused to engage in a cross trade earlier but then supposedly approve of one later." Response at 31. Of course they are wrong. The reason Respondents approved the 2006 cross trade of Tenneco Core is simply because they thought no one would find out about it. As Barag testified, Zell refused to alert BellSouth to the notion that Timbervest was coveting its assets for its other funds because it would "strike a bad tone." Tr. 1936:22-1937:16; *see also* Division of Enforcement's Post-Hearing Brief at 14-15. However, when the opportunity came along to transfer a BellSouth property *without the client's knowledge*, Zell and the other Respondents did not hesitate to do so.

Respondents also dispute that they attempted to conceal the cross trade. In support of their denials they raise several points which they think are inconsistent with the Division's allegations of concealment. Response at 31. First, they note the availability of the transactional records in the county courthouses of Alabama. *Id.* Their claim that the availability of these documents somehow amounts to transparency fails, however, since there is no evidence on file of Boden's promise to repurchase the property before it was initially sold. Respondents also claim, again, that they "voluntarily" disclosed the deals to the Division. *Id.* As discussed above, this is patently false and demonstrates the Respondents continuing attempts to distort the factual record. Finally, they claim that the deal documents were available to anyone who asked. *Id.* Again, this is misleading, as there was no documentation of Boden's agreement with Wooddall to repurchase the property (Boden refused to memorialize the agreement, a lesson he presumably

learned when his attempts to cross-trade Glawson through Hailey were discovered by Zachry Thwaite). Moreover, Respondents' claim is belied by the fact that they misled their client about the nature and severity of their misconduct after the fraud was discovered in 2012. *See* Appeal at 36-39. The suggestion that they would have been more transparent before their fraudulent conduct was discovered than they were after the fact strains credibility.

Respondents also unsuccessfully attempt to explain away the concealment evidenced by the contemporaneous documents. First, they claim that the Spec Book for the repurchase of Tenneco Core (renamed "Gilliam Forest") was not drafted by the Respondents.[12] They ignore the fact, however, that each Spec Book had checked boxes at the end, which signaled the Respondents' individual approvals of the document. Moreover, the Division presented evidence demonstrating that Respondents were involved in reviewing that very document. *See* Div. Exs. 175-176 (Zell's emails forwarding drafts of the Gilliam Spec Book to Shapiro and other employees).

It is also worth pointing out that Respondents concede that the descriptions of the properties in TVP's files versus those sent to New Forestry are "seemingly inconsistent." Response at 32. What is remarkable, however, is that Respondents admit that they were likely drafted that way to deceive their clients. They state, "It is no surprise that the documents' drafters would want to downplay the property when trying to inform New Forestry about the sale

[12] Respondents' claim that the Spec Book (Div. Ex. 162) was prepared for internal use only is directly contradicted by Boden's testimony. Tr. 239:15-21; 240:5-12 (stating that the Spec Book was a resource for informing interested investors about an acquisition). Moreover, their contention that this Spec Book was never finalized is undermined by the fact that it possessed all of the indicia of finality: it was in color; it included color property maps; it was posted to the internet and available by internet search; it had boxes checked indicating approval of the purchase by each member of the Investment Committee; and, counsel for Timbervest, represented on the record that there was no "more recent or final version" than Div. Ex. 162. Tr. 985:2-986:1.

of the property and would want to advertise the long-term benefits of the acquisition when trying to inform TVP about the purchase." Such arguments show Respondents' continuing obliviousness to their fiduciary responsibility, which obligates them to act in the best interests of their client. If, as they claim, the Tenneco Core property possessed long-term cash flow benefits (*see* Response at 33) then New Forestry was entitled to that information. As Frank Ranlett stated, "[I]f this is such a screaming deal . . . I should at least be presented with the option of buying it back into New Forestry." Tr. 1056:18-21.

B. Respondents Distort the Record with Regard to the Payment of Boden's Fees

Respondents also make numerous misstatements regarding the payment of Boden's fees. First, Respondents falsely claim that Zachry Thwaite's agreement was *oral* and *unknown*, which they say raised concerns for Boden. Response at 35. The record clearly shows, however, that Thwaite's agreement was *in writing* and *in the files at Timbervest* before Boden began working for the company.[13] Stipulations of the Parties, Doc. 44 at ¶20. Second, Respondents claim that Boden's concerns also stem from his knowledge that "Chambers had entered into a brokerage agreement with Bob Suter." Response at 36. The problem with this claim, however, is that there was never any agreement with Suter, but only a letter describing Suter's rates if New Forestry asked him to sell or trade property. Res. Ex. 86. Tr. 520:16-523:14.

Respondents also assert that there was no evidence that Boden "knew or should have known that receiving fees [through the creation of unregistered real estate brokerage companies]

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[13] Respondents also state, misleadingly, that "Thwaite's oral brokerage agreement was the subject of a lawsuit filed by New Forestry in 2006" and that this lawsuit served as additional motivator for Boden to seek protection." Response at 35. These statements are rife with mischaracterizations. First, it was Thwaite's *written* agreement which was the basis of the lawsuit. Moreover, it was the Respondents who sued Thwaite, not the other way around. To the degree that Boden was actually afraid of being sued, he was surely looking the wrong direction.

was improper."[14] Response at 39. Boden himself, however, conceded that he knew that it was illegal for unlicensed brokers in Georgia and other states to collect brokerage fees. Tr. 388:22-389:3. He also testified that he thought brokers needed to be licensed in the states where they were active. Tr. 384:9-13. Boden did attempt to explain that he was not breaking the law because his activities were 'advisory,' despite having all the characteristics of brokering, but the ALJ rightly determined, "This explanation is utterly incredible, nothing more than doublespeak, and erodes his overall credibility." *Id.*

Finally, Respondents' arguments regarding possible spoliation of relevant documentary evidence are rank speculation that must be disregarded. Response at 41.[15] Respondents have testified that Boden's fee agreement and the supposed disclosure of the fees to Schwartz were never written down. Moreover, given Schwartz's credible testimony that he never consented to such payments—along with Shapiro's own testimony showing that his so-called "disclosures" to Schwartz were, in the ALJ's words, "woefully inadequate"—the possible destruction of documentary evidence showing that Respondents somehow obtained authorization for transactions which plainly violated ERISA's bedrock fiduciary principles, is, to say the least, highly unlikely.

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[14] Respondents contend that Boden's waiver of attorney-client privilege with respect to his conversations with Harrison demonstrates that "he had nothing to hide." Response at 36. As the ALJ noted, "This argument is substantially undercut, though, by the fact that the attorney, Harrison, was himself represented by Boden's own counsel, and continued to be so represented during the hearing." I.D. at 55.

[15] Here, and at various other points, Respondents attempt to smuggle in new evidence which the Commission has not had the opportunity to test. Response at 42; *see also id.* at 11. As discussed in the Division's Opposition to Respondents' Motion to Introduce Evidence, admitting such evidence would be fundamentally unfair to the Division, especially when, as here, the ALJ found that the Respondents lacked credibility on many crucial issues. The Commission should therefore disregard all evidence not already in the record and strike all references made thereto.

V. CONCLUSION

For the reasons discussed above, the Commission should impose associational bars against the Respondents, find that Respondents Zell and Jones knowingly or recklessly violated Section 206(1) of the Advisors Act, and uphold all of the ALJ's conclusions as to areas unrelated to these issues. Furthermore, the Commission should strike all references and citations to new evidence proffered by the Respondents.

This 15th day of December, 2014.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE WITH SEC'S RULE OF PRACTICE 450(c)

I hereby certify that this brief complies with the length limitation set forth in SEC Rule 450(c). According to the word processing system used to prepare this document, the brief contains 6,973 words.

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