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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.

Joel Barth Shapiro's Reply in Support of his Appeal to the Commission

JOEL BARTH SHAPIRO'S REPLY IN SUPPORT OF HIS APPEAL TO THE COMMISSION

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Respondent Joel Barth Shapiro respectfully files this Reply Brief in support of his Appeal to the Commission, requesting that the Commission reverse the Initial Decision of Administrative Law Judge Cameron Elliot rendered on August 20, 2014 (the "Decision"). The Decision found that Shapiro aided and abetted and caused violations of §§ 206(1) and 206(2) of the Investment Advisers Act without any evidentiary basis to support the findings and imposed sanctions that are impermissible under the law and facts. The ALJ found Shapiro acted recklessly with respect to a pair of real estate transactions (the "Chen Transactions") and with respect to the disclosure of fees received by co-Respondent Boden. A careful review of the evidence shows that Shapiro acted in good faith on these matters, and certainly not recklessly or negligently. The Division failed to put forth any evidence or argument indicating that the Decision should be upheld. Accordingly, the Commission should find that Shapiro neither aided and abetted nor caused any violations of the Advisers act and should impose no sanctions against him.

I. There is no evidence that Shapiro acted recklessly or negligently with respect to the Chen Transactions.

As explained in Shapiro's Appeal to the Commission, there was no evidence presented at the evidentiary hearing that Shapiro acted recklessly or negligently with respect to the Chen Transactions. Shapiro's only involvement in the transactions was as a member of Timbervest's Investment Committee. (Tr. at 2255-57) He did not have day-to-day responsibility for reviewing purchase and sale contracts, nor was he involved in the negotiation of either the sale or purchase of the Tenneco Core property. (*Id.*) Instead, he evaluated the transactions as a member of the Investment Committee and ultimately decided that each transaction was a good deal for each client. (*Id.*) These facts necessarily point to the conclusion that Shapiro was neither reckless nor negligent with respect to the Chen Transactions.

Lacking direct evidence that Shapiro had any reason to question the two Chen Transactions, the Division claims that Shapiro acted recklessly:

1. because "[a]ccording to Barag's testimony, [he] was . . . aware that ERISA prohibited cross-trading of plan assets";
2. because he supposedly should have known that Tenneco Core was undervalued when sold; and
3. because of the "short time frame of the transaction." (Div. Br. at 21.)

None of these arguments supports a finding of recklessness or negligence, and Shapiro therefore should not be held liable for aiding and abetting or causing any violation relating to the Chen Transactions.

A. Shapiro's alleged knowledge of ERISA does not establish that he acted recklessly or negligently.

The Division first argues that Shapiro acted recklessly with respect to the Chen Transactions because according to Barag, Shapiro was "aware that ERISA prohibited cross-trading of plan assets." (Div. Br. at 21.) The Division fails to include any citation to Barag's testimony for this point, so it is nearly impossible to tell what the Division may be referring to. Presumably, though, it is referencing a 2003 or 2004 conversation that Barag had with the Partners about an *actual* cross trade, in which properties would be transferred from New Forestry directly to a Timbervest REIT. (Tr. at 1936-1937.) But there is no evidence that Shapiro had this alleged conversation, which took place years earlier, in mind when he was approving the sale and later approving the purchase of the property.

Moreover, even if Shapiro were aware that ERISA prohibited cross-trading plan assets, there is no evidence that Shapiro viewed the Chen Transactions as a cross trade. In fact, the evidence showed that Shapiro was not involved in any of the negotiations concerning the transactions and that he had no reason to suspect that Boden and Wooddall allegedly entered into a deal whereby they agreed that Timbervest would sell Tenneco Core and then later repurchase it at a higher price. (Tr. at 1478-79.) Instead, Shapiro viewed the two transactions as separate: he evaluated them separately and approved of them separately. (Tr. at 2255-2257.) Because, as discussed below, they each presented excellent deals for Timbervest's clients, he approved of the transactions. (*Id.*) In these circumstances, Shapiro's alleged knowledge of ERISA does not show that he acted recklessly or negligently.

B. Shapiro was not reckless in allegedly undervaluing Tenneco Core.

The Division next contends that Shapiro "would have known that Tenneco Core was undervalued since the Wolf Creek properties were fetching prices that were anticipated as early as August 2006" and that this undervaluation shows that Shapiro acted recklessly. (Div. Br. at 21.) But Shapiro had no crystal ball. He did not know what the Wolf Creek package was going to sell for until it, in fact, sold. There is no evidence in the record that Shapiro had any involvement in the Wolf Creek auction process or listing agreement. There is no such evidence because a third-party broker handled all aspects of these transactions, and consequently, Shapiro would not have known contract prices until contracts were signed and delivered to Timbervest. And Shapiro and the other Timbervest Partners had no idea what the sales price would be until the results from the open bid on the properties, in which Timbervest had no communication with any buyer, came in on October 30, 2006.

In any event, the August 2006 report to which the Decision cites did not report the *value* of the Wolf Creek tracts (or Tenneco Core). (Div. Ex. 16.) It simply reported the estimated sale prices for a number of properties that Timbervest hoped to get for each property. (*Id.*) It did not report actual sales or prices that were, in any manner, assured. In fact, the complete sales program for the Wolf Creek properties would ultimately encompass over forty separate property sales spanning more than four years and yield average prices materially below those of the first four sales in November 2006.

Moreover, the sale of Tenneco Core was a good one for New Forestry. In 2006, New Forestry wanted a substantial reduction in its timberland holdings. (Div. Ex. 47.) In fact, it wanted more than $220 million in sales over a three-and-a-half year period. (Div. Ex. 47; Tr. at 102-03, 476.) For those properties that remained in its portfolio, New Forestry wanted properties that would generate cash flow of 2% per year. (Div. Ex. 47.) Tenneco Core, though, consisted of 75% pulpwood, meaning that the majority of trees were young and would not be income-producing for quite some time. (Tr. at 201, 483-84.) Selling Tenneco Core would therefore fit both of New Forestry's mandates: dispositions to reduce its timberland holdings and dispositions of property that would not generate substantial income.

The terms of the sale also were excellent for New Forestry. Based on Timbervest's own valuation policies, which every client, including New Forestry and its beneficial owners (first, BellSouth, and then AT&T), understood and approved of, the $13.45 million sales price exceeded Tenneco's value by $1.4 million, or 11.7%. (Div. Ex. 26; Tr. at 1111-12, 1627, 1605.) Moreover, an August 2005 appraisal from the James Sewall Company (the most recent appraisal available to Timbervest based on its valuation policy), valued Tenneco Core at $12.13 million. (Res. Ex. 52; Tr. at 207, 211, 1665.)The final sales price exceeded the appraised value by 11%. And importantly, Sewall appraised the bare land at $438 an acre, whereas the sale to Chen Timber provided New Forestry with $547 an acre for bare land—an increase of almost 25%. (Resp. Ex. 52; Tr. at 200-01, 207, 210.) With these facts, it is impossible to say that Shapiro was reckless or negligent, and the ALJ's finding on this point was in error.

The purchase transaction was also good for TVP. In 2006 and 2007, TVP was looking for properties that would fit its long-term growth investment strategy. (Tr. at 83.) TVP was willing to inject capital into property—necessary for the future success of Tenneco Core, given its younger timber profile and "big, bulky tracts." (Tr. at 233-34.) Moreover, the economic indicators available to Timbervest showed the repurchase price to be fair. First, between the sale and purchase, the value of the timber on the land increased by more than $950,000—making up nearly the entire difference in prices. (*See* Tr. at 200-01.) Moreover, the price was supported by the sale of the nearby Wolf Creek properties, which were averaging $1,461 per acre. (Div. Ex. 128.) In contrast, TVP secured the property at a price of $1,116.37 per acre. (Div. Ex. 18.) Likewise, the NCREIF timberland fund had an 8.5% increase in value, and the Plum Creek REIT saw a 15% increase in value over the same timeframe. (Div. Ex. 83; Tr. at 205, 853-54.) TVP, though, secured the property at an increase in price of less than 8%.

Shapiro acted reasonably in approving these two transactions, each of which provided excellent value for Timbervest's clients. There is no evidence that he believed the sale of Tenneco Core to be undervalued, and the Division's suggestion to the contrary should be dismissed out of hand.

C. The timing of the two transactions does not show recklessness.

The Division also argues that Shapiro was reckless because the timing of the two transactions was ostensibly suspicious.[1] (Div. Br. at 21.) But this argument is insupportable because the timing of the two transactions was not suspicious and is not indicative of recklessness or negligence. Nearly seven months passed between when the Investment Committee would have evaluated the sale and when it would have evaluated the purchase. That

[1] The Division argues that there "numerous red flags presented" by the deal but then goes on to identify only one: "the short time frame of the transaction." (Div. Br. at 21.)

is, the Investment Committee would have evaluated the sale, at the latest, in June 2006 because, on dispositions, the Investment Committee evaluates at the time that contracts are received or sent. (Tr. at 856 1422-24.) It then would have evaluated the purchase in January 2007, when the due diligence period on the purchase expired, because when evaluating acquisitions, the Investment Committee looks at whether it is a good deal shortly before the due diligence period ends and earnest money goes hard. (Tr. at 1422-24.) A sale in June and a purchase in January is not suspicious on its face, especially when those two transactions were evaluated pursuant to the timberland valuation policy, as every sale or acquisition is, and found to be beneficial to each client. Thus, the timing of the transactions does not show that Shapiro acted recklessly or negligently.

At bottom, there is no evidence that Shapiro aided and abetted or caused any violation of the Advisers Act with respect to the Chen Transactions. The Division has failed to put forth any reasonable evidence or argument to the contrary, and the Commission should therefore reverse the Decision to the extent that it found that Shapiro acted recklessly and negligently.

II. There is no evidence that Shapiro acted with scienter or negligently with respect to Boden's fees.

There was also no evidence to support the finding that Shapiro acted recklessly with respect to the disclosure of Boden's fee arrangement. The Division contends, however, that there was "simply no way that he could have believed that he actually obtained the informed consent of either Schwartz or of BellSouth/AT&T based on his own testimony . . . ." (Div. Br. at 22.) But the evidence shows that Shapiro acted reasonably and undertook to disclose the fee arrangement to New Forestry's fiduciary, Ed Schwartz at ORG. While Schwartz did not recall all the details of this disclosure, which took place nearly nine years before the evidentiary hearing, that fact alone does not establish that he acted with scienter.

Shapiro should be credited for his candor about his lack of memory regarding the conversation. Shapiro does not recall the precise words he used during the conversation. (Tr. at 1776-77.) And while the Division suggests that Shapiro testified that he did not disclose the specific terms of the agreement, this suggestion is simply untrue. Shapiro simply testified that he could not recall what details he gave to Schwartz about the agreement, given that his memory of the conversation had faded over the years. (*Id.*) Regardless of the details of the conversation, Shapiro walked away thinking that Schwartz had consented to the fee arrangement. (*Id.*) Indeed, he testified, both in his investigative testimony and at the evidentiary hearing, that Schwartz's response during the conversation was that the agreement was fine and was not a big deal. (Tr. at 1785.) It was such a non-event that Shapiro cannot recall Schwartz's exact words. (*Id.*)

The Division, however, urges the Commission to accept Schwartz's version of the disclosure: that the conversation was about a "hypothetical" person and that Schwartz said he would have to run the arrangement by legal counsel before he could consent. (Div. Br. at 3-4.) As explained in Shapiro's Appeal to the Commission, Schwartz's version of the disclosure cannot be accepted because he is an entirely unreliable witness. Schwartz has contradicted himself on numerous occasions concerning the substance of his 2005 conversation with Shapiro, while Shapiro's version of events has always remained the same: he discussed Boden's fee agreement with Schwartz and came away thinking that Schwartz had consented to the agreement.

The Division does not contest that Schwartz's story has changed on multiple occasions over the years. Instead, it argues that Respondents should have called witnesses to testify about what Schwartz said during several calls and meetings with the Arizona Public Safety Personnel Retirement System ("AZPSPRS") in June 2012. (Div. Br. at 5-6.) But the Division seemingly ignores that two witnesses *did* testify that Schwartz told AZPSPRS that he had been made aware of Boden's fee arrangement. First, Jones testified that he recalled two phone calls with AZPSRS in June 2012 in which Schwartz acknowledged he was aware of Boden's fee arrangement and that the fees Boden received were essentially compensation for work done prior to becoming a partner at Timbervest. (Tr. at 1471.) Schwartz even coined the fees a "tail payment" to Boden. (Tr. at 1471.) Shapiro likewise testified that he recalled a meeting with AZPSPRS during which Schwartz described the fees as "Bill's tail payment for work he had done prior" to becoming a Timbervest partner. (Tr. at 2252-53.) Respondents were not required to call every single participant in the calls and meetings to establish that Schwartz made these statements, and the Division gives no reason why Jones's or Shapiro's testimony should not be credited on this point.

The Division also argues that the Respondents should have called a third party to testify about statements made to Timbervest's in-house and outside counsel in 2012 in which Schwartz said that he had been made aware of Boden's fee agreement and had agreed to it. (Div. Br. at 6.) But no third-party testimony was necessary to corroborate these claims because Timbervest clearly laid out Schwartz's statements in its Wells submission. The Division claims that counsel's statements from the Wells submission are "entitled to no evidentiary weight" (Div. Br. at 6), but such a position is curious in light of the fact that the Division itself introduced the Wells submission into evidence. (Div. Ex. 74.) Once admitted into evidence, it was usable for any purpose. It was admitted without the ALJ placing any limitations on its use. The Division's position is also seriously undermined by its later argument that the Division's notes of what Schwartz told to the Division's attorneys themselves do not constitute exculpatory information under *Brady* because Respondents' counsel already had listed in its Wells submission what they understood Schwartz to have told the Division. (Div. Br. at 30-31.) In any event, what Schwartz told to Respondents' counsel is largely immaterial, given that Schwartz had provided similar information, which contradicted his hearing testimony, both during AZPSPRS meetings and to the Division itself.

Unsurprisingly, the Division wholly fails to address the fact that Schwartz gave inconsistent information to the Division in 2012, before he obtained counsel and before he realized that there may have been a problem with the payment of fees to Boden. At the hearing, Schwartz testified that he did not know about Boden's fee agreement or that it was Boden, in particular, who had the fee arrangement. (Tr. at 2063-64, 2090-91.) In sharp contrast, he told the Division in 2012 that he was "informed of the arrangement and the possibility of . . . payments" to Boden.

He also testified at the hearing that he was unaware that the person who held the fee agreement was Boden (Tr. at 2063-64), but in his telephone interview with the Division in 2012, he clearly "recall[ed] a discussion he had with either Zell or Shapiro about 'a broker who eventually came into the company, Bill Boden'" and that his "understanding was that [Timbervest] was considering bringing on Boden in some capacity other than that of a broker." Schwartz told the Division in his 2012 interview that he had reached an understanding with Shapiro "that Boden could finish up whatever he had started in connection with acting as a broker for New Forestry property.

Schwartz likewise testified that the arrangement would have presented a clear conflict of interest under ERISA and that there was no way he would have consented to the agreement without counsel's advice. (Tr. at 2057, 2059-60, 2091, 2105-06, 2201-02.) But he told the Division in 2012: "I said, and BellSouth agreed, we didn't think it was appropriate to pay a brokerage fee two times. So, if he was truly acting as a broker, the same as if it was done outside, and it was not disadvantageous to Bellsouth, that would be okay." He also "said the idea was not different than many companies that use in house resources instead of third party resources and charge for them." And "that from an ERISA/fiduciary standpoint, he saw no problem with the arrangement that he discussed with Shapiro/Zell because services were to be performed by a broker." But when pressed by the Division's attorneys about the minutiae of ERISA, he said that he would need to talk to a lawyer about the ERISA questions. (Div. Ex. 94.)

It is entirely possible that, given the passage of time, Schwartz's memory of the conversation is off. For example, it is reasonable that Shapiro told Schwartz in 2005 that it is "hypothetical that Mr. Boden would receive a fee," rather than that there was a "hypothetical person who would receive a fee." This simple transposition of the sentence completely changes the meaning of the disclosure. A disclosure that it was "hypothetical" that a fee would actually be paid would be consistent with Mr. Boden's actual fee agreement—any payment was hypothetical and not realized or paid until a transaction closed that fulfilled all the parameters of the arrangement. (Tr. at 1771-1772.) In fact, during testimony, Mr. Shapiro explained that "[t]his was all hypothetical . . . [H]e had earned the fee, but he hadn't been paid." (*Id.*) Similarly, he likely conflated two different conversations he had about Boden's fee agreement—the 2005 one with Shapiro and the 2012 one with the Division—when he testified that he would need to speak with a lawyer about any ERISA issues before approving the deal. That is, he told the Division that he wanted to speak with a lawyer before answering any further questions about ERISA but then, two years later, when testifying at the hearing, confused that statement with what he had told Shapiro.

The Division's only attempt to rehabilitate Schwartz's testimony is to claim that Steve Gruber, who also worked at ORG, did not know about the fee arrangement. (Div. Br. at 4.) But there is no reason to think that Gruber would have known about the fee arrangement. Although the Division characterizes Gruber as having "primary responsibility for overseeing Timbervest's management of New Forestry," Shapiro did not deal with him frequently and instead discussed issues with Schwartz. (*Id.*; Tr. at 2271.) Even Schwartz testified that Gruber did not speak with Shapiro often. (Tr. at 2041-42.) Schwartz himself had most of the conversations with Shapiro. (*Id.*) Thus, there is no reason to think that Shapiro would have or should have discussed the fee agreement with Gruber. Nor is there any reason to think that Schwartz necessarily disclosed the fee agreement to Gruber, given that Schwartz thought the arrangement was fine and not a big deal. (Tr. at 1785.) At bottom, Schwartz's testimony is not to be trusted. And without it, there is absolutely no evidence that Shapiro did not disclose Boden's fee agreement to New Forestry's representative.

Shapiro testified consistently and honestly. He was honest about his difficulties recalling a conversation from nearly a decade ago. And there is simply no basis to use Schwartz's testimony to support a finding that Shapiro acted recklessly or negligently. The consequences to Shapiro are simply too grave to rely on Schwartz's faded and inconsistent memory.

III. The sanctions imposed against Shapiro are penal and barred.

Shapiro did not act with scienter or negligence either with respect to the Chen Transactions or with respect to Boden's fee arrangement. Therefore, the evidence does not support the imposition of any sanction against him, and the ALJ's decision to impose disgorgement and a cease-and-desist order against him was in error. Moreover, the sanctions imposed are wholly barred by the statute of limitations. Disgorgement is penal for the reasons discussed in Timbervest's Appeal to the Commission at 20-23.

The Division also wholly failed to address Shapiro's arguments that a cease-and-desist order would be penal as applied against him. But, as discussed in his Appeal to the Commission, a cease-and-desist order would be penal because his reputation in the business community would be forever tarnished, and because he would be severely circumscribed in his ability to earn a living, due to the "bad actor" rule on the Dodd-Frank Act. This is because the "covered persons" under Rule 506(d) disqualification include issuers, affiliated issuers, owners, directors, general partners, managing members, executive and other officers, promoters and investment managers and its principals, among others. 17 C.F.R. §§ 230.506(d)(v)(A), 230.506(d). Notably, Regulation D and the Rule 506 exemption are the primary capital offering tools used by all U.S. businesses, irrespective of industry, company type, company size or the amount of the capital raise,[2] making a "bad actor" disqualification particularly severe. Moreover, the Division's reliance on cases pre-dating Frank-Dodd for the proposition that the cease and desist is remedial is simply not valid given the collateral consequences of the "bad actor" rule which are clearly punitive to Shapiro. Accordingly, the Commission should overturn the Decision's sanctions against Shapiro.

IV. Conclusion

The Initial Decision plainly erred in finding that Shapiro acted recklessly with respect to the Chen Transactions and Boden's fees, and nothing in the Division's Brief changes that conclusion. The evidence shows that he acted in good faith. He was not involved in the Chen Transactions except as a member of the Investment Committee, and he undertook to disclose Boden's fee arrangement to New Forestry's fiduciary. The Commission should therefore reverse the Initial Decision's findings against Shapiro and the sanctions imposed against him.

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[2] *See* U.S. Securities and Exchange Commission, Capital Raising in the U.S.: An Analysis of Unregistered Offerings Using the Regulation D Exemption, 2009-2012, July, 2013. Capital raised through Regulation D offerings was over $900 billion in 2012; Regulation D offerings occur with far greater frequency than any other offering method; Rule 506 accounts for 99% of amounts sold through Regulation D and is the primary offering tool for smaller entities; From 1999-2012 there were more than 40,000 Rule 506 issuances by non-financial issuers with a median offer size of less than $2 million (and 50% less than $1 million).

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