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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-15974

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In the Matter of

NATURAL BLUE RESOURCES, INC., JAMES E. COHEN, and JOSEPH A. CORAZZI,

ORAL ARGUMENT REQUESTED

Respondents.

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# RESPONDENTS' REPLY BRIEF ON REVIEW OF THE INITIAL DECISION

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## TABLE OF CONTENTS

**Page(s)**

## TABLE OF AUTHORITIES

## PRELIMINARY STATEMENT

The Division's Brief fails to provide any reasonable basis for affirming the Initial Decision of the ALJ. Instead, the Division blatantly mischaracterizes the record evidence and misapplies the appropriate legal standard for determining whether an employee should be considered a "*de facto*" officer. Rather than focusing on whether Respondents had any policymaking *authority*, the Division focuses on the—irrelevant—fact that they were influential within Natural Blue Resources, Inc. ("Natural Blue" or the "Company"). Notwithstanding the Division's obfuscation, there is only possible conclusion in this proceeding: Cohen was *not* a *de facto* officer because "while [he] exercised **significant influence** . . . and was very close to [the CEO], ***he did not have the authority to make or implement any policy decisions***. Such authority lay with [others]." *SEC v. Prince*, 942 F. Supp. 2d 108, 136 (D.D.C. 2013) (emphasis added) (defining officer status with reference to Rule 3b-7 under the Exchange Act). On this basis alone, the Commission should reject the Division's argument, and should instead reverse the Initial Decision.

The Initial Decision should be reversed not only because it is contrary to the factual record developed at the hearing and misapplies the proper legal standard, but also because it subverts the well-established legal principle of ratification—abandoning the existing rational standard in favor of one predicated on the razor thin, effectively nonexistent, distinction between a "decision" as opposed to a "ratification"—an affirmative act that, by definition, constitutes a decision and an exercise of authority over policy decisions. In concluding that the "ratification" of Respondents' actions by Natural Blue officers and directors transformed them into *de facto* officers, the Initial Decision sets forth an unprecedented and untenable holding that, if affirmed, will have far reaching and unintended negative consequences for public corporations and their employees, officers, and directors. Were the Commission to accept the ALJ's novel

interpretation of "ratification," countless public filings by myriad companies would be rendered false and fraudulent simply because the officers and directors of those companies "ratify"—i.e., approve—and implement the proposals of consultants, employees, or others who are not identified in those filings as officers.

Equally troubling, the reasoning of the Initial Decision in this regard contradicts the Commission's own assertion that ALJs are not "officers," subject to the constitutionally required appointment process, because they do not possess ultimate decision making authority but, instead, must have their decisions "ratified" by the Commission. *See, e.g.*, *In the Matter of Raymond Lucia Companies, Inc.*, File No. 3-15006, Opinion of the Commission. If an officer's decision can be termed a "ratification"—rather than an approval—that transforms an employee into a corporate officer, then certainly ALJs must likewise be "officers" because the Commission merely ratifies the actions and decisions of those ALJs. Tellingly, the Division fails to address *any* of these issues, implicitly acknowledging these defects in the Initial Decision's reasoning and the consequences that flow therefrom. The Initial Decision should be reversed for this additional reason.

The Division also failed to demonstrate that Respondents are liable for the alleged misrepresentations because the record shows that these allegedly false statements were not "made" by Respondents: the statements were prepared and reviewed by the Company's attorneys and accountants, and issued and certified by its executives. Such statements cannot be used to try to impose "back door" scheme liability under Section 17(a). For that reason, the Commission should conclude that Respondents are not liable for the public filings of others, and the Initial Decision should be reversed for this separate basis as well.

Furthermore, Respondents' due process and equal protection rights were violated. The ALJ's Initial Decision is void because she was not properly appointed under the Constitution as an officer of the Commission for purposes of conducting the hearing. Equally critical is that Respondents were deprived of due process because the ALJ declined even to adhere even to the minimal evidentiary rules applicable to administrative proceedings, and the Initial Decision included factual findings not based on evidence. These violations of Respondents' constitutional rights constitute independent grounds for reversing the Initial Decision.

Finally, the Division has not carried its burden of showing that sanctions are appropriate under the *Steadman* factors. The Commission therefore should affirm the ALJ's decision not to order disgorgement, and should reverse the ALJ's imposition of a penalty and order of disbarment.

## STATEMENT OF FACTS

Respondent Cohen rejects the "facts" cited in the Division's Brief that are inconsistent with the record evidence, and reasserts those facts identified in Respondents' Brief. *See generally* Resp. Br. at 7-27. In particular, but not to the exclusion of other factual mischaracterizations, Cohen takes issue with the following descriptions of the record in the Division's Brief:

- The Division incorrectly describes the formation of Natural Blue. *See* Div. Br. at 4-5. Contrary to the Division's suggestion that Natural Blue was solely Respondents' creation, the record evidence demonstrates that Governor Toney Anaya ("Governor Anaya" or "Anaya") was interested, *of his own accord*, in leading "a green-related company," *suggested* a project relating to water in New Mexico, and was *heavily involved* in the discussions with Respondents that led to the formation of Natural Blue and his appointment as CEO. Anaya Tr. 1048:9-1049:12, 1053:4-1058:19; Div. Ex. 9; Cohen Ex. 420.

- The Division improperly suggests that Anaya had no involvement in any part of Natural Blue's reverse merger with Datameg in 2009, citing evidence only showing Cohen's involvement. In fact, the record reveals that both Governor Anaya and the Natural Blue Board of Directors (the "Board") anticipated that

Natural Blue would go public through a reverse merger, and that Datameg was an acceptable candidate for such a transaction. *See, e.g.*, Anaya Tr. 1064:25-1065:13 (testifying that a reverse merger "made sense because it would bring Natural Blue in as a publicly-traded company. And I understood what that meant."); Pelosi Tr. 537:18-538:5 (agreeing "that from the time that [Pelosi] founded Natural Blue, Nevada the plan of the Board Members of the company was to become a public company"); Anaya Tr. 821:11-14 (testifying that Board received a proposed nonbinding term sheet with Datameg); Div. Ex. 9 (Board resolution "that James Cohen, Sr., investigate and report alternatives to the board for the Corporation concerning funding and becoming a reporting public company.").

- The Division incorrectly states that the ALJ found that Respondents "studiously avoid[ed] any public disclosure of their roles and/or disciplinary background." Div. Br. at 9. Yet the portion of the Initial Decision cited by the Division for this proposition contains no such finding. The Division points to no other record evidence in support of this "fact," because it is simply not true. Rather, the evidence shows that Respondents' backgrounds were known to the CEO, CFO, and Natural Blue's attorneys. *See, e.g.*, Anaya Tr. 1212:13-25, 1287:13-1289:3, 1292:23-1293:10; Decker Tr. 1537:13-25, 1568:7-21; Vuksich Tr. 410:20-411:10.

- With respect to the roles Respondents held within Natural Blue, the Division mischaracterizes the Respondents' relationship with the Company by simply regurgitating snippets of the record with no contextual analysis. *See* Div. Br. 10-11. Yet, this evidence only sets forth the different roles Respondents occupied in the Company. Nothing in these potions of the record cited by the Division shows that Respondents held policymaking *authority*.

- The Division incorrectly states that Cohen "unilaterally" made the decision to hire Walter Cruickshank as CFO of Natural Blue. Div. Br. at 11. The Initial Decision contains no such finding, and the record evidence is to the contrary as well. *See, e.g.*, Murphy Tr. 69:24-70:5, 172:24-174:9, 175:3-10 (testifying that Cohen did not direct Murphy's vote for officers, and confirming that Murphy decided on how to vote his own shares, including his vote for Cruickshank, who was unanimously selected by the Board)

- The Division mischaracterizes the transaction Natural Blue entered into with Atlantic Drilling in 2011 by omitting Anaya's involvement in the deal. *See* Div. Br. at 17-18. The ALJ found, and the record fully supports, that Anaya was involved in the negotiation and closing of the Atlantic Drilling deal. *See* Init. Dec. at 20-21 (discussing Anaya's involvement).

- The ALJ rejected as "unreliable" and "dubious" the figures presented by the Division in support of disgorgement. Init. Dec. at 33. The Commission should reject the "facts" set forth by the Division relating to Respondents' alleged financial gain on the same bases. *See* Div. Br. at 21-22.

Finally, but perhaps most significantly, the Division misconstrues Natural Blue's acquisition of Eco Wave LLC ("EcoWave") in 2009, and in doing so, repeats the same error committed by the ALJ. *See* Div. Br. at 9-10 (citing Init. Dec. at 10-11). The Division wholly ignores convincing and persuasive record evidence when it states that EcoWave had already been acquired by Natural Wave at the time it was presented to the Board on August 1, 2009. Div. Br. at 9 ("[T]he August 1, 2009 board minutes reflect that EcoWave *had already been acquired.*"). But the *only* record evidence arguably in support of this alleged fact are the summary Board minutes. All other evidence in the record is to the contrary. Anaya testified that, at that meeting, the "Board voted that day [to invest in EcoWave] upon recommendation of Mr. Cohen, Sr. and Daryl Kim and Samir Burshan, the company voted to invest in the technology" of EcoWave. Anaya Tr. 849:12-15. Anaya further testified that the acquisition of EcoWave was completed *two weeks* after the presentation to the Board on August 1, 2009. Anaya Tr. 1130:5-19; Cohen Ex. 432 (press release of August 19, 2009, that Natural Blue had acquired "Eco Wave LLC"). In other words, the persuasive record evidence shows that it was only through the Board's authorization on August 1, 2009—and not by Cohen's own actions at any time prior—that the EcoWave transaction was consummated and able to close two weeks later. The ALJ's finding to the contrary is not supported by the competent record evidence; the acquisition of EcoWave was not a "*fait accompli*" but a deal, like all others, that required the authorization of the Natural Blue Board. To the extent that the Division relies on this erroneous finding, that reliance is misplaced.

## ARGUMENT

The standard for determining whether an employee is a *de facto* officer under the securities laws is, and should remain, the decision in *SEC v. Prince*, 942 F. Supp. 2d 108 (D.D.C. 2013). That decision—the only one relied on by the Division for this issue—eschews any

esoteric "economic function" and states clearly that an employee is a *de facto* officer only when that employee has actual policymaking *authority*. As amply demonstrated both in Respondents' submissions to the Commission and the ALJ's own factual findings in the Initial Decision, Respondents lacked any such policymaking authority. At all times Respondents needed to obtain authorization from Governor Anaya or the Board of Directors. The Division points to no evidence to the contrary. Instead, in a misguided attempt to support the ALJ's conclusion, the Division seeks improperly to take the clear holding of *Prince* and shred it into an unmanageable compendium of irrelevant factual distinctions between that case and the instant matter. But the facts relied upon by the Division are not germane to the analysis under *Prince*; they do not in any way demonstrate that Respondents were *de facto* officers.

Furthermore, former Governor Toney Anaya—an accomplished and respected professional—was not a mere "figurehead" CEO; he exercised ultimate authority at Natural Blue, alongside the Board, and was guided by the advice of the Company's attorneys. Application of existing law to these circumstances supports only one results: these Respondents were not *de facto* officers because they lacked policymaking authority, and thus the Company's filings—prepared by counsel and filed by its officers—were not false.

Given this disconnect between the law and these facts, the Division did not even attempt to demonstrate that it satisfied the *Prince* standard, but instead put forth at trial an entirely unprecedented and remarkably unworkable concept of an "economic function" standard—a standard that would leave public companies and their counsel without any manageable guidelines for disclosing corporate officers, and would permit selective prosecution in any instance in which management seeks, receives, and approves the actions of others. Because the adoption of the

Division's theory in the case would wreak havoc on public companies—and would do so for no purpose—that theory must be rejected, and the Initial Decision reversed.

This same result attends irrespective of the ALJ's use of the word "ratification" to describe the actions of Anaya and the Board. As laid out in Respondents' Brief, "ratification" ***is*** approval; indeed, the fact that Respondents' acts required ratification further demonstrates that they *lacked* policymaking authority. To conclude otherwise, as does the Initial Decision, would lead to a host of negative unintended consequences: any time an employee's action is "ratified" by an officer or director of a company and treated as an act of the corporation itself, that employee would be automatically transformed into a corporate officer. Corporations would then face securities fraud liability for "ratified"—i.e., properly approved—acts of their employees and consultants unless each and every one of those employees or consultants is disclosed as an officer in the company's public filings. Such a rule is neither fair, reasonable nor workable. For that separate and independent reason, the Commission should reverse the Initial Decision.

Finally, in its Brief, the Division does not: provide a basis for finding that Respondents could be considered the "makers" of the allegedly false statement; convincingly respond to Respondents' arguments that the proceedings before the ALJ and the Initial Decision are constitutionally infirm; or demonstrate that sanctions are appropriate in this matter. For each of these additional reasons, the Commission should reverse the decision of the ALJ.

## I. The Division Misinterprets and Misapplies Prince to Support Its Argument that Respondents Were *De Facto* Officers

The Division throughout its presentation relied on its unprecedented "economic function" theory. Now, in its submissions, it relies on an incorrect and misguided reading of *SEC v. Prince* to try to distract from the clear clash between its trial theory and governing law. Setting aside the Division's misapplication of the law and applying the proper standard from *Prince* leads

instead to the inescapable conclusion that Respondents were not *de facto* officers of the Company. Furthermore, because the Division has now effectively abandoned its "economic function" theory, and instead analyzes whether Respondents' were *de facto* officers of Natural Blue solely under the *Prince* standard—offering no alternative standard—Respondent Cohen submits that *Prince* should control the Commission's own analysis as well.

### A. The *Prince* Standard Looks to Whether the Employee Had Actual Policymaking Authority.

At its core, the standard set forth in *Prince* for determining whether an employee is a *de facto* officer focuses on whether the employee in question had the actual *authority* to make decisions on behalf of the corporation. Thus, in determining that the employee in question, Prince, was not a *de facto* officer of the company for which he served as a consultant, the *Prince* court relied on the lack of evidence that Prince had authority to make or implement policy for the company: "The record is clear that, while Prince exercised significant influence at Integral and was very close to Chamberlain [the CEO], *he did not have the authority to make or implement any policy decisions*. Such authority lay with Chamberlain and the heads of the various Groups." *Prince*, 942 F. Supp. 2d at 136 (emphasis added); *id.* at 135 ("Chamberlain [and not Prince] was the only person who had *authority* to make company policy for Integral." (emphasis added)); *id.* ("Each of the former Integral employees testified that Prince did not have the *authority* to make policy." (emphasis added)); *id.* ("The testimony . . . that Prince did not have any *authority* to make policy is particularly significant." (emphasis added)); *see also id.* at 136 ("[N]o evidence was presented that Prince ever signed any contract.").

Ignoring this clear holding, the Division instead argues that Respondents should be considered *de facto* officers because they had influence over many aspects of Natural Blue.[1] *See* Div. Br. at 28-29. Not only is the Division's focus on Respondents' "influence" contrary to the express reasoning of *Prince*, it is also unprincipled, subjective and unworkable. The standard seemingly suggested by the Division—that an employee is a *de facto* officer when the employee exerts "too much" influence—would require case-by-case review of the facts with no guidance on what amount of influence transforms that employee into an officer of the company. In contrast, the standard set forth by *Prince* is principled, objective and workable: an employee is a *de facto* officer only when that employee has the actual authority to make policy decisions. Indeed, the Division's—and ALJ's—focus on the amount of influence that Respondents exercised over Natural Blue is precisely the what *Prince* court explicitly rejected: "To decide that the Regulations reach individuals involved in discussing company strategy and policy, but who do not have the ***authority*** to actually implement such policy, would expand the scope of *de facto* officer far beyond what any court has to date recognized as policy making authority." *Id.* at 136 (emphasis added). The standard—the sole test—under *Prince* for determining whether an employee is a *de facto* officer is whether that employee had the actual authority to make and implement policy.

### B. The Division's Attempt to Distinguish *Prince* Factually is Misplaced and Without Merit

The Division attempts—in vain—to distinguish *Prince* factually on two primary bases, arguing that in that case: (1) the CEO was a strong leader, and (2) a specific role was "carved out" for Prince, in order to avoid the need for company to disclose his past felony conviction. With respect to the first purported distinction, the Division argues that Anaya was not as strong

[1] By focusing in its Brief on Respondents' "influence," the Divisions should be considered has having abandoned its (deeply flawed) trial theory that Respondents were *de facto* officers because of their "economic function" within Natural Blue.

as the *Prince* CEO, susceptible to being overly influenced by Respondents. With respect to the second purported distinction, the Division points out that there is no evidence of a similar "carve out" in place at Natural Blue for Respondents. Neither of these arguments merits a determination that Respondents were *de facto* officers.

The Division argues that in *Prince*, the CEO was regarded as a strong leader who pushed back on Prince's influence, contrasting this to Natural Blue's CEO, Anaya, whom the Division describes as being unable to control Respondents. Div. Br. at 28. The Division is wrong both in its reading of *Prince* and characterization of Anaya. The court in *Prince* found that Prince held "substantial influence and involvement" with core aspects of the company—to such an extent that this caused the company's outside counsel to resign because they felt uncomfortable about Prince's role.[2] *See Prince*, 942 F. Supp. 2d at 126. Nor, as detailed in more depth *infra*,[3] was Anaya the "weak" CEO the Division describes. In any event, the Division's focus on the level of influence Respondents exerted over officers and the Board of Natural Blue is immaterial under *Prince*. Again, the amount of influence is not the standard for determining whether an employee is a *de facto* officer—the inquiry focuses only on whether the employee held "final, policy making authority." *Id.* at 135 ("[W]hile Prince had substantial influence and involvement with regard to mergers and acquisitions issues, he did not have final, policy making *authority* over that program." (Emphasis added.)). In this proceeding, the Division has not and cannot point to any such authority held by Respondents.

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[2] Indeed, in some ways, Prince exercised even more control over the company's operations than did Respondents over Natural Blue, in that Prince had the power to hire and fire the employees he supervised. Significantly, the *Prince* court rejected the notion that Prince's hiring and firing power "constituted an ability to make policy." *Id.* at 136. Here, there is no evidence in the record that Respondents had hiring and firing power. Again, the record evidence demonstrates that all personnel decisions recommended by Respondents had to be signed off by Anaya or the Board. *See supra*, note 7.

[3] *See* Section I.E.

The Division's reliance on the "carve out" in *Prince* as a distinguishing fact could not be more misplaced. Nowhere in holding that Prince was not *de facto* officer does the *Prince* court rely on—let alone address—the fact that a carve out existed. The only time the *Prince* court refers to the carve out is in analyzing the allegation that Prince violated Section 10(b) and Rule 10b-5 of the Exchange Act—neither of which are part the alleged violations committed by Respondents.[4]

Even in that context, the discussion of the "carve out" does not help support the Division's position the Respondents were *de facto* officers. In dismissing the alleged Section 10(b) and Rule 10b-5 violations, the *Prince* court relied on the fact that it had *already* concluded that Prince was not a *de facto* officer. *Prince*, 942 F. Supp. 2d at 137 (holding that the SEC could not prove Section 10(b) and Rule 10b-5 violations because "[t]he Court has already concluded that the SEC failed to establish that Prince was acting as a *de facto* officer"). Only after dismissing these claims on that basis did the *Prince* court proceed to address—in *dicta*—that the SEC also would have been unable to prove other elements required to show Section 10(b) and Rule 10b-5 violations. *Id.* ("However, the Court finds that, even if Prince was a *de facto* officer . . . the SEC has not established important other elements of its 'scheme to defraud' claim.").

Even here, in this *dicta*, the court only commented on the "carve out" in connection with Prince's advice of counsel defense, regarding whether he lacked the necessary scienter to establish a Section 10(b) and Rule 10b-5 violation—and not as to whether Prince was a *de facto* officer. *Id.* at 139-140. At no other point does the *Prince* court discuss the fact that Prince was walled-off within the company as being relevant to—let alone dispositive of, as the Division

[4] *See* Init. Dec. at 25 n.13 ("The Division abandoned claims that Respondents violated Section 10(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder.").

would have the Commission believe is the case—the analysis of whether Prince was a *de facto* officer. In short, contrary to the Division's strained attempt to find some distinguishing factor, careful review of *Prince* makes abundantly clear that the existence of a "carve out"—or any other similar fact—is immaterial to determining whether an employee is a *de facto* officer.[5] Under *Prince*, an employee is a *de facto* officer if and only if that employee has actual authority to make and implement policy—which the record evidence here shows was not the case for Respondents.

### C. The Division Points to No Evidence that Respondents Had Actual Policymaking Authority.

The foregoing demonstrates that the crux of the analysis in determining whether Respondents were *de facto* officers turns on evidence that they had the actual authority to make and implement policy on Natural Blue's behalf. Yet, the Division fails to point to any record evidence that Respondents had the authority to implement policy—nor could it, because there is none. The Division's entire argument in this regard rests on the ALJ's conclusion that Respondents "assumed responsibility for Natural Blue's operations and strategic plans." Div. Br. at 29-30 (quoting Init. Dec. at 27-28). Even assuming that this conclusion is supported by the record—which, as explained in Respondents' Brief and herein, is not the case—the mere fact that Respondents may have taken on certain responsibilities at Natural Blue does not show that they had the actual authority to make and implement policy.

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[5] The Division also contends that *Prince* is distinguishable on the basis that the auditors in *Prince* condoned Prince's role within the company, whereas the auditors for Natural Blue resigned "because of their discomfort with the degree of control that Cohen exhibited over the company." Div. Br. at 29. Again, this argument is misplaced. In concluding that Prince was not a *de facto* officer, the *Prince* court did not rely on the auditors' opinion of Prince's role, and thus the opinion of Natural Blue's auditors is similarly irrelevant to determining whether Cohen was a *de facto* officer. That the opinion of a company's auditors or advisors is not a factor in the *de facto* officer analysis is made even more apparent by the fact that in *Prince*, the company's legal counsel resigned over concerns similar to those expressed by Natural Blue's auditors—an aspect of *Prince* that the Division conspicuously omits from its brief. *Prince*, 942 F. Supp. 2d at 126.

To the contrary, the record evidence unmistakably shows that Anaya maintained and exercised his "ultimate" authority. *See generally* Resp. Br. at 7-27 (citing evidence). Ample evidence reveals, for example, that Respondents did not have the authority to enter into the reverse merger with Datameg or otherwise bind Natural Blue by contract,[6] or to make any personnel decisions.[7] Only Anaya or the Board could take these actions.[8]

The ALJ's decision itself further confirms that Respondents did not have the authority to take action without approval from Anaya or the Board. *See, e.g.*, Init. Dec. at 6-7 ("*Cohen proposed* that Natural Blue Nevada reverse merge with Datameg . . . ." (emphasis added)); *id.* at 7 ("At a March 31, 2009, Board meeting, *Cohen presented a proposed nonbinding term sheet* with Datameg." (emphasis added)); *id.* at 9 ("Cohen identified Natural Blue's officers, whom *the Board approved* at its first meeting . . . ." (emphasis added)); *id.* ("Cohen and Corazzi selected individuals to become officers and directors, and *Anaya approved* the selections." (emphasis added)); *id.* ("*Cohen recommended* that Natural Blue hire Florida audit firm Cross, Fernandez & Riley (Cross), and *Anaya accepted* the recommendation." (emphasis added)); *see also id.* at 20-21 (discussing Anaya's heavy involvement in the closing of the transaction between Natural Blue and Atlantic Dismantling in January 2011). Significantly, the ALJ concluded: "Various Board members, officers, employees, attorneys, and auditors were *recommended by Cohen and Corazzi* and . . . *approved by Anaya* or shareholder vote. . . . *The Board approved* the consulting

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[6] *See, e.g.*, Resp. Br. at 15 ("At a March 17, 2009 Board of Directors meeting, Cohen reported back on 'several discussions . . . with James Murphy, the CEO of Datameg Corporation,' and stated that he and Murphy had agreed to 'recommend entry into a nonbinding term sheet' for a reverse merger transaction, 'subject to the approval of each company's board.' Div. Ex. 10; Pelosi Tr. 539:1-8.").

[7] *See generally* Resp. Br. at 18-20 (setting forth evidence that Anaya, not Respondents, had the final say in performing personnel functions).

[8] The EcoWave transaction is not to the contrary. As explained in detail in the Statement of Facts, *supra*, the preponderance of the record evidence demonstrates that the EcoWave transaction required Board approval before the deal could close.

agreements by which Cohen and Corazzi received compensation." Init. Dec. at 27 (emphasis added).

The evidence thus leads to only one possible conclusion under the standard set forth in *Prince*: Respondents were not *de facto* officers because they did not have actual policymaking authority. For this reason, the Commission should reverse the Initial Decision.

### D. The Company's Ratification of Respondents' Actions Did Not Transform Respondents into *De Facto* Officers

The Division's brief is glaringly deficient in how it fails to address the troubling ramifications, identified in Respondents' Brief, of the ALJ's conclusion that Respondents could be considered *de facto* officers by virtue of the fact that Anaya and the Board "ratified" certain of Respondents' actions. This reasoning in the ALJ's decision is unprecedented, and will lead to far reaching, and unintended, negative consequences.

The record evidence and the ALJ's own findings show that Respondents did not have policymaking authority. Instead, Respondents' actions required the approval of Anaya or the Board. That this approval may have come in the form of ratification does not alter the conclusion that Respondents' lacked policymaking authority. Ratification is a long established and widely accepted legal principle that, broadly speaking, permits a principal to make an agent's actions legal and proper. *See generally* Restatement (Third) of Agency, Ch. 4, Introductory Cmt. (2006). Once an action is ratified, the legal consequences "relate back" to the time of the action—in other words, it is as if the original action was taken by and under the authority of the ratifying individual. *See id.*, § 4.02 & cmt. b; *see also Hannigan v. Italo Petroleum Corp.*, 47 A.2d 169, 173 (Del. 1945) (explaining that ratification "relates back and gives validity to the unauthorized act or contract, as of the date when it was made and affirms it

in all respects as though it had been originally authorized. *The act is legalized from its inception.*" (Emphasis added.)).

Thus, the effect of Natural Blue's ratification, by Anaya or the Board, of Respondents' actions is no different than had Anaya or the Board directed Respondents to perform those actions. In short, ratification is the same as approval, and serves as further evidence that Respondents were not *de facto* officers of Natural Blue because they did not have authority to make policy—they needed approval, in some form, from Anaya or the Board. The ALJ's conclusion otherwise— that ratification had no such effect—is contrary to well-established legal principles. Indeed, neither the ALJ nor the Division cite *any* precedent, let alone provide persuasive reasoning, in support of the notion that undisputedly proper ratification by Natural Blue of Respondent's actions is somehow evidence that Respondents were *de facto* officers.

Discarding the long recognized legal principle of ratification—as accepting the ALJ's decision requires—would be unprecedented, counterfactual, and would wreak havoc on how corporations operate. Ratification is a critical component of modern-day decision making by corporate boards. *See, e.g.*, Model Business Corporation Act, Sec. 8.70 & cmt. (2007) (describing how director can seek board ratification of taking of corporate opportunity to avoid liability for usurping); *Lewis v. Vogelstein*, 699 A.2d 327, 334-335 (Del. Ch. 1997). If the newly devised interpretation of "ratification" employed by the ALJ is accepted by the Commission, it would render false the filings of an untold number of companies whose officers routinely evaluate, "ratify," and implement the proposals of consultants, employees, or others who are not identified in public filings as "officers." Additionally, accepting the ALJ's reasoning that "ratification" somehow transforms an employee into a corporate officer would undercut the Commission's own stated defense of the appointment process of ALJs: the Commission could

no longer argue that it held the ultimate authority over administrative proceedings in circumstances where the Commission approves—i.e., "ratifies"—the decision of an ALJ. For these reasons, the Commission should reject the ALJ's attempt to subvert the concept of "ratification," and should reverse the Initial Decision for this additional reason.

### E. The Record Shows That Natural Blue's Officers and Directors Independently Reviewed Respondents' Proposals and Actions.

The Division incorrectly suggests in its Brief that Anaya or the Board automatically approved, without any further consideration, Respondents' proposals. *See* Div. Br. at 28-29. Yet, the Division points to nothing—because there is nothing—in the record that shows that Anaya or the Board approved of Respondents actions, whether outright or by ratification, by merely "rubber stamping" every single one of Respondents' proposals. To the contrary, the ALJ's findings and the record evidence demonstrate that Anaya and the Board engaged in ongoing and vigorous discussions over Respondents' proposals as well as their roles within Natural Blue.

Judge Foelak found that Anaya and the Board held meaningful power over Respondents. For example, the Initial Decision includes a finding describing how Respondents refused to continue in their role as consultants for Natural Blue without authorization from the Company in the form of formal agreements, which were reviewed and debated by the Board as a whole before being executed. Init. Dec. at 11. Perhaps even more significantly, Anaya had the power to suspend, with the Board's support, Respondents' consulting agreements, which he did when they failed to act in accordance with the company's interests in the purchase of certain real property. *Id.* at 13. These facts, among others, amply demonstrate that neither Anaya nor the Board was beholden to Respondents.

The record is replete with other evidence showing that Anaya consistently retained control of his position as CEO throughout his tenure as an officer of Natural Blue. For example, Anaya testified that he, not Cohen, had the *final* authority on behalf of Natural Blue to enter into contracts and to hire or fire legal counsel. Anaya Tr. 1019:13-1020:7, 1033:24-1034:13. Anaya also restricted Cohen's ability to interact directly with outside counsel. Anaya Tr. 1188:25-1189:25, 1190:6-23, Cohen Ex. 148. Anaya, not Cohen, had the authority to approve and finalize legal documents and filings. Anaya Tr. 1114:9-15. Anaya never relinquished control to Respondents, even up through the Atlantic deal that occurred in his final months as CEO; Anaya directed that certain changes be made to the Atlantic deal documents, stating that "they had to because I'm the one that had—if I didn't agree, I wasn't going to sign it." Anaya Tr. 985:4-11; 1021:12-18. Indeed, Anaya confirmed that he "rejected" the initial structure of the Atlantic steel deal that Respondents presented to him. Tr. 1169:7-25; *see also* Init. Dec. at 21 ("In the end . . . Cohen and Corazzi did agree to a few changes Anaya proposed.").

It also bears repeating that Anaya was not the inexperienced CEO that the Division attempts to portray him as in its Brief. Anaya has a wealth of high-level and executive public and private sector experience, serving as: an assistant district attorney; chief of staff for a New Mexico governor; New Mexico's attorney general; governor of New Mexico; a licensed attorney for over 37 years, specializing in business and corporate law; and in executive level or and board positions with a variety of corporations, including Valor Telecom, a private company that Anaya helped form, Burger King, where he served on an Advisory Board, and NuAmerica Bank, a chartered bank that Anaya helped found. Anaya Tr. 783:22-784:6, 785:1-5, 992:14-21, 993:3-997-25, 998:1-8, 998:24-999:18, 1002:9-1004:22; Div. Ex. 269. Through these roles,

Anaya gained experience in managing large organizations, and was amply prepared to manage Natural Blue.

## II. Respondents Did Not "Make" the Allegedly False Statements

The Division fails to point to sufficient evidence to show that Respondents "made" statements in furtherance of a scheme to defraud.[9] Moreover, the Division ignores the relevant discussion in *SEC v. Prince*, 942 F. Supp. 2d 108, 144 (D.D.C. 2013). As discussed in more detail in Respondents' Brief, the *Prince* court—in analogous circumstances—found no "scheme to defraud" where the filings in question had been reviewed by numerous other individuals other than Prince. *See* Resp. Br. at 39-40. The same result should attend in this case. The record here shows that, like in *Prince*, Natural Blue's public filings involved the executives and the lawyers who prepared and approved those filings. *Id.* at 22-27 (identifying record evidence). The conclusion in the Initial Decision that the alleged fraudulent scheme could somehow exist absent Respondents' participation is baseless; no scheme existed and no liability exists under Section 17.

## III. Respondents' Constitutional Rights Were Violated

### A. The Proceeding Before the ALJ Was Constitutionally Infirm

The Division fails to meaningfully respond to Respondents' contention that the SEC's appointment of its ALJs violates the Appointments Clause—rendering the proceedings in this matter constitutionally infirm—and Respondents stand on the reasoning set forth in their Brief that this alone constitutes a basis for reversal of the Initial Decision.

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[9] The Division misinterprets the argument raised Respondents' Brief on this issue: *Janus Capital Group v. First Derivative Traders*, 131 S. Ct. 2296 (2011), although involving Rule 10b-5 of the Exchange Act, provides helpful guidance in determining analyzing whether Respondents engaged in a scheme to misrepresent Natural Blue's public filings.

### B. The ALJ Committed Errors During the Proceeding that Violated Respondents' Due Process Rights

As explained in more detail in Respondents' Brief, Respondents' due process rights were violated when the ALJ allowed the Division to offer evidence that was unreliable. Such evidence included, but was not limited to, hearsay evidence and the purported expert testimony of Robert M. Daines. Respondents' due process rights were further violated when the ALJ issued factual findings in the Initial Decision that were contrary to the record evidence.[10] For these additional reasons, the Commission should reverse the Initial Decision to avoid violating Respondents' constitutional rights.

## IV. The ALJ Properly Denied Disgorgement and No Penalty is Warranted Under the *Steadman* Factors

The ALJ properly concluded in the Initial Decision that the Division failed to support its request for disgorgement with any credible evidence. Instead, the Division relied almost exclusively on an analysis by SEC accountant Sofia Hussain that was predicated on skewed slivers of information and based on direction from Division attorneys, rendering the evidence unreliable. The Division provides no new or otherwise convincing basis to support its disgorgement claim in its Brief, and the Commission should therefore affirm the ALJ's decision to deny disgorgement.

The Commission should reverse the ALJ's imposition of other sanctions imposed on Cohen—namely, the officer and director bar and civil money penalty—for the reasons laid out in Respondents' Brief: the evidence established that Respondents did not violate the federal securities laws, and they certainly did not commit any intentional or willful act; at worst, Respondents were certainly unaware of a the not-yet articulated rule developed by the ALJ in

[10] The erroneous findings of the ALJ are detailed in the Respondent's Motion to Correct Manifest Error, the Petition filed in support of Review of the Initial Decision, and Respondents' Brief.

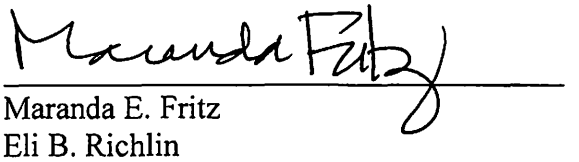
this case regarding "*de facto*" officers. *See Steadman v. SEC*, 603 F.2d 1126, 1137 (5th Cir. 1979) ("when the Commission chooses to order the most drastic remedies at its disposal, it has a greater burden to show with particularity the facts and policies that support those sanctions and why less severe action would not serve to protect investors"), *aff'd on other grounds*, 450 U.S. 91 (1981). The Division fails to provide any persuasive rationale to the contrary. In any event, the Division's request for imposition of a third-tier penalty should be rejected outright as unsupported by the record.

## CONCLUSION

For the foregoing reasons, the Commission should find that the Division failed to establish that Cohen acted as a *de facto* officer of Natural Blue, engaged in any scheme to defraud, or in any way violated Section 17(a) of the Securities Act, or any other provision.

Dated: January 25, 2016

Respectfully Submitted,



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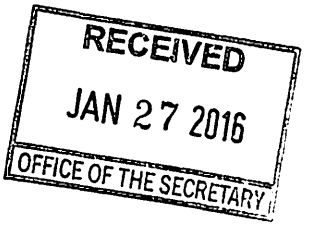
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15974




In the Matter of

NATURAL BLUE
RESOURCES, INC.,
JAMES E. COHEN, and
JOSEPH A. CORAZZI,

Respondents.

## RESPONDENTS' RULE 450(d) CERTIFICATE OF COMPLIANCE

Pursuant to Commission Rule of Practice 450(d), I certify that Respondents' Reply Brief on Review of the Initial Decision is 6,481 words exclusive of cover page, table of contents, table of authorities, and certificate of service using Microsoft Word 2010's word count function.

Respectfully Submitted,

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Dated: January 25, 2016

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## CERTIFICATE OF SERVICE

I hereby certify that a true copy of **RESPONDENTS' REPLY BRIEF ON REVIEW OF THE INITIAL DECISION** was served on the on this 25th day of January, 2016, in the manner referenced:

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Washington, DC 20549

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January 25, 2016

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**BY FACSIMILE AND FEDEX**

Mr. Brent Fields
Secretary
United States Securities and Exchange Commission
100 F. Street, N.E.
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**Re: In re Natural Blue Resources, Inc., A.P. No. 3-15974 – Respondents' Reply Brief**

Dear Mr. Fields:

We represent Respondents in the above-referenced matter. Enclosed for filing please find Respondents' Reply Brief on Review of the Initial Decision.

Thank you for your attention to this matter.

Respectfully submitted,

Maranda Fritz

Maranda E. Fritz

Enclosures

cc: Rua Kelly (via email)
Mayeti Gamechu (via email)
Joseph Corazzi (via email)

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