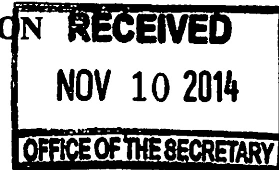
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-16182

In the Matter of **PAUL EDWARD "ED" LLOYD, JR., CPA,** **Respondent.**	**DIVISION OF ENFORCEMENT'S RESPONSE IN OPPOSITION TO RESPONDENTS' ANSWER AND MOTIONS (FILED OCTOBER 27, 2014)**

On November 4, 2014, the Court issued an Order which provided the Division of Enforcement (the "Division") an opportunity to file a response to Respondent's Answer and Motions (alternatively, "Motion for Summary Disposition") by November 7, 2014. To the extent that Respondent's pleading is viewed as a Motion for Summary Disposition, the Division submits the following:

A. **Respondent's Motion for Summary Disposition should be denied because it does not comply with the Commission's Rules of Practice.**

Rule 250 of the United States Securities and Exchange Commission's (the "Commission") Rules of Practice states, in pertinent part, as follows: "After a respondent's answer has been filed ... the respondent ... may make a motion for summary disposition of any or all allegations of the order instituting proceedings .... If the interested division has not completed presentation of its case in chief, a motion for summary disposition shall be made only with leave of the hearing officer."

In this case, Respondent filed his Motion for Summary Disposition contemporaneously with his Answer. Indeed, they were incorporated into a unitary pleading, styled "Answer and *Motions* of Paul Edward Lloyd, Jr., CPA" (emphasis added). Because (1) Lloyd did not wait until

after he filed his Answer to file his Motion for Summary Disposition, (2) the Division has not initiated, much less completed, the presentation of its case in chief, and (3) he filed it without first seeking "leave of the hearing officer", his Motion for Summary Disposition -- the bases of which are referenced in his First, Second, Third, Fourth, Sixth and Seventh Defenses (he did not list a "Fifth" Defense) -- should be denied.

Moreover, Rule 154 of the Commission's Rules of Practice specifically requires a movant to "state with particularity the grounds for" the relief sought and to submit "a written brief of the points and authorities relied upon." Respondent's purported "motion" fails these requirements, containing no explanation of the basis for the requested relief. Respondent also failed to submit any supporting brief or any authorities that purportedly support his naked conclusions. Such deficiencies also demand denial of his "motions,", particularly because they leave the Division to guess the rationale that supports his motions.

B. Respondent's Motion for Summary Disposition should be denied because his conduct involved the "purchase and sale of a security."

Lloyd contends in his First, Second, Fourth and Sixth Defenses that, since his conduct did not involve the "purchase and sale of a security", the proceedings against him should be dismissed. However, Lloyd has failed to offer a scintilla of support for his allegations (one sentence is devoted to each Defense). Saying it is so does not make it so. His Motion for Summary Disposition should be denied, because, at best, a genuine issue with regard to a material fact exists

1. The investments in the Forest Conservation entities are securities.

The Forest Conservation offerings orchestrated by Lloyd are securities because they are investment contracts. Respondent offers nothing to contest this conclusion. To be clear, the Forest Conservation offerings are investment contracts designed to pool investor funds for singular investments in the separate third-party real-estate-related offerings brokered by Broker A, namely:

Land Entities A, B, and C. The touchstone of any analysis as to whether a particular instrument is a security under Section 2(a)(1) of the Securities Act of 1933 ("Securities Act") and Section 3(a)(10) of the Securities Exchange Act of 1934 ("Exchange Act") is the substance rather than the form of the transaction, with an emphasis on economic reality. SEC. v. W.J. Howey Co., 328 U.S. 293, 298-99 (1946); United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 848 (1975). Investment schemes may fall within several of the categories of instruments included within the definition of a security. Tcherepnin v. Knight, 389 U.S. 332, 339 (1967). The Howey court, *supra*, defined an investment contract as a contract, transaction or scheme whereby a person: (1) invests his money; (2) in a common enterprise; and (3) is led to expect profits solely from the efforts of the promoter or a third party. See also Robinson v. Glynn, 349 F.3d 166, 170 (4th Cir. 2003).[1]

The first element of the Howey test, that a person must invest money, means "that the investor must commit his assets to the enterprise in such a manner as to subject himself to financial loss." SEC v. Pinckney, 923 F. Supp. 76, 80 (E.D. N.C. 1996), quoting Hector v. Wiens, 533 F.2d 429, 432 (9th Cir. 1976). Here, the Division expects that its case in chief presented at the hearing will show that Respondent solicited individuals to provide funds to the Forest Conservation entities, promising each individual would receive his or her *pro rata* interest in the total ownership units that the Forest Conservation entities purchased through the real estate investment offerings sponsored by Broker A. The offering summaries for the companies selling ownership units through Broker A (Land Entities A, B, and C, respectively) explained that the company manager

[1] It should be noted that the Commission has taken the position that a common enterprise is not a distinct requirement for an investment contract under Howey. In re Barkate, SEC Release No. 49542, at *1, n.13 (April 8, 2004).

would recommend to members of each entity whether to pursue either an investment proposal, such as the development of land into residential lots for sale, or, in the alternative, a conservation easement proposal. Further, the Division's case in chief will show that the offering summaries explained that the companies were under no obligation to grant a conservation easement for any interest in land the companies acquired. Because Lloyd's clients committed funds and subjected themselves to the risk of financial losses, the first prong of Howey is satisfied.

The second element of Howey – requiring a "common enterprise" – has been interpreted differently among the nation's circuit courts. The Fourth Circuit, where Respondent resides and from where he offered and sold securities to investors in various states, has held that "horizontal commonality," whereby profits are distributed on a *pro rata* basis to investors whose assets were pooled together, is sufficient to show a common enterprise. Teague v. Bakker, 35 F.3d 978, 986 n. 8 (4th Cir. 1994) (also stating that the court "need not decide here whether there is some form of vertical commonality" because of the finding of horizontal commonality); SEC v. Unique Financial Concepts, Inc., 119 F. Supp. 2d 1332, 1336-1338 (S.D. Fla. 1998). The District of Columbia Circuit Court of Appeals, to which this matter could potentially be appealed, also has held that horizontal commonality is sufficient to show a common enterprise under the Howey test. S.E.C. v. Banner Fund Intern., 211 F.3d 602, 614 (D.C. Cir. 2000).). Here, the Division expects that its case in chief presented at the hearing will show that there clearly is horizontal commonality between the various individuals who contributed funds to the Forest Conservation entities, as Lloyd's clients wrote checks to the bank accounts identified by Lloyd. Subsequently, Lloyd used those pooled funds to make purchases of ownership units in the Land Entity A, B, and C offerings, respectively. As a result, Lloyd's clients who held ownership interests in the Forest Conservation entities were entitled, based on their *pro rata* purchases of ownership interests, to any profits or

losses achieved by Land Entities A, B, and C, respectively. Further, investors in the Forest Conservation entities ultimately shared in the net profit they achieved through *pro rata* tax deductions that reduced their individual taxable income and led ultimately to a greater savings in taxes paid than the funds they initially invested.

Some courts have held that the second Howey element also may be satisfied by a showing of "vertical commonality" which looks at the relationship between the investor and the promoter. Eberhardt v. Waters, 901 F.2d 1578, 1580 (11th Cir. 1990). Under the vertical commonality theory, a common enterprise exists where the "fortunes of the investor are interwoven with and dependent upon the efforts and success of those seeking the investment or of third parties." Eberhardt, 901 F.2d at 1580 (quoting Villeneuve v. Advanced Bus. Concepts Corp., 698 F.2d 1121, 1124 (11th Cir. 1983)). While neither the District of Columbia Circuit Court of Appeals, nor the Fourth Circuit has addressed whether vertical commonality alone may establish the second element of the Howey test, at least one district court under the Fourth Circuit has addressed the issue, holding that "a common enterprise may be established by showing that the investor's profits are directly related to the promoter's profits." Pinckney, 923 F. Supp. at 82.). Here, the Division expects that its case in chief presented at the hearing will show that the ability of the individual clients of Lloyd to receive profits flowing from their participation in the Forest Conservation entities is directly related to any singular profit which the Forest Conservation entities controlled by Lloyd each would have been entitled to receive by using the pooled investor funds to purchase ownership units in the private offerings. Because the fortunes of the investors were clearly interwoven with the efforts and successes of the Forest Conservation entities created, identified and managed solely by Lloyd, there is vertical commonality. See, e.g., SEC v. Reynolds, 2010 WL 3943729, *3 (N.D. Ga. 2010) (finding vertical commonality established because investors "were

dependent on [the promoter's] purported expertise in 'banking processes'," and the promoter claimed "the returns offered were possible because of [his] relationships with undisclosed banking partners").

Finally, the third element of Howey, that the investor expected its profits to come solely from the efforts of others, requires a court to examine "(1) that the opportunity provided to offerees tended to induce purchases by emphasizing the possibility of profits, (2) that the profits are offered in the form of capital appreciation or participation in earnings ..., and (3) that the profits offered would be garnered from the efforts of others." Teague, 35 F.3d at 987. Here, the Division expects that its case in chief presented at the hearing will show that there are two ways in which Respondent's clients reasonably expected profits from the efforts of others. First, the clients reasonably expected profits from their participation in the Forest Conservation entities because the offering summaries for the third-party offerings in which the Forest Conservation entities intended to buy ownership units explained that the issuers intended to acquire a controlling interest in land which, under one scenario, could be developed for profit through the development and sale of residential lots. Separately, Lloyd's clients also reasonably expected profits from the efforts of others because Lloyd induced his clients to invest in the Forest Conservation entities by emphasizing that each client would receive a tax deduction and corresponding decrease in income taxes owed of greater value than each client's initial investment, *i.e.*, a net profit earned through participation in the anticipated conservation easements.

Case law regarding the relationship between tax benefits and the existence of an investment contract has developed over the course of the last several decades. In United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 853-58 (1975), the Supreme Court held that residents of a government-financed co-op building who bought "shares" in the co-op in exchange for residential

space did not purchase "securities" under the Howey test because the residents purchased the shares for "personal consumption or living quarters for personal use" and "were attracted solely by the prospect of acquiring a place to live, and not by financial returns on their investments." Further, the Court held that mortgage interest paid by the residents, while deductible for the residents' tax purposes, did not constitute a "security" because such "tax benefits are nothing more than that which is available to any homeowner who pays interest on his mortgage." Id. at 855. Subsequently, in 1986, the Supreme Court, in Randall v. Loftsgaarden, 478 U.S. 647, 667 (1986), held that "tax benefits" from an investment in a tax shelter were not to be used in calculating "actual damages," *i.e.*, the court did not reduce the investor's recovery by the tax benefits actually received from a tax shelter investment which involved fraud in the offering terms. The Randall case was a dispute concerning whether tax benefits would reduce an investor's recovery under a theory of rescission. Randall did not address the Howey analysis *in any way*. Case law before and after Randall, however, has found that a "security" may exist in the form of tax benefits where promoters take sufficient steps to create the reasonable expectation of profits on the part of a purchaser. Newmyer v. Philatelic Leasing Ltd., 888 F.2d 385, 394 (6th Cir. 1989), cert. denied, 495 U.S. 930 (1990) (holding that tax benefits alone do not satisfy the "profit" element under Howey, but also finding a material question of fact existed as to whether a tax shelter involving leasehold interests of postage stamp printing plates was an investment contract under Howey, and observing in *dicta* that a trier of fact would likely examine the promoter's appraisals, offering memorandum and "glowing" description of the popularity of stamp collecting in determining whether a reasonable expectation of profits existed); see also Investors Credit Corp. v. Extended Warranties, Inc., 1989 WL 67739 at * 28 (M.D. Tenn. 1989) ("As to profits, tax benefits which are the dominant inducement for investing are properly considered to be profits in satisfaction" of the

Howey test). For a pre-Randall analysis of the issue, see Kolibash v. Sagittarius Recording Co., 626 F. Supp. 1173, 1179 (S.D. Ohio 1986) (holding that "where ... tax benefits are the primary or dominant economic inducement for investing, such tax benefits may properly be considered 'profits' within the meaning of Howey").

Regardless of whether the third-party entities at issue in this matter ultimately chose to develop the land for profit or seek tax deductions through conservation easements, any such profits or tax deductions would be garnered by the efforts of others, *i.e.*, Lloyd, as manager of and investment adviser to the Forest Conservation entities, as well as by Land Entities A, B, and C. Any earnings expected, whether profits or tax deductions, would come from the efforts of others, as Lloyd's clients' only meaningful role was to write checks and wait for their *pro rata* profit. Once Lloyd's clients provided their investment funds to the Forest Conservation entities, they had no role in the success or failure of the ventures. Lloyd was the only manager and had complete control over the Forest Conservation entities' interactions with Broker A and Land Entities A, B, and C. He went on to wire investor funds contributed to the Forest Conservation entities to the escrow accounts for the real estate offerings. In the case of Forest Conservation 2012, Lloyd also misappropriated $130,000 from the entity's account over which he exercised total control. In each of the three offerings, once land was preserved through a conservation easement, a tax deduction was transmitted to the Forest Conservation entities, through which Lloyd subsequently issued Schedule K-1s in order to prepare the taxes (including the resulting tax deduction generated by the easements) for his individual clients. As such, the investor funds provided to the Forest Conservation entities meet the third prong of the Howey test because there was clearly a reasonable expectation of profits on the part of Lloyd's clients who invested in the Forest Conservation entities.

C. Lloyd's Motion for Summary Disposition should be denied because the Division has identified violations of the Broker/Dealer Registration Provisions of the Exchange Act of 1934.

Additionally, Respondent's argument in his First Defense that the Commission lacks jurisdiction over this matter also should be denied because Lloyd was acting as an unregistered broker/dealer. Section 3(a)(4) of the Exchange Act defines a "broker" as "any person engaged in the business of effecting transactions in securities for the account of others." The phrase "engaged in the business" connotes a regular participation in securities transactions and can be evidenced by such things as holding oneself out as a broker-dealer or receiving transaction-based compensation. See e.g. Massachusetts Fin. Servs., Inc. v. Sec. Investor Prot. Corp., 411 F. Supp. 411, 415 (D. Mass. 1976), aff'd, 545 F.2d 754 (1st Cir. 1976); SEC v. Hansen, 1984 WL 2413, at *10 (S.D.N.Y. 1984).

Section 15(a)(1) of the Exchange Act prohibits a broker or dealer from effecting any transactions in, or inducing or attempting to induce the purchase or sale of, any security without registering as, or associating with, a registered broker-dealer, unless such broker or dealer (1) is registered with the Commission in accordance with Section 15(b) of the Exchange Act; (2) in the case of a natural person, is associated with a registered broker-dealer; or (3) satisfies the conditions of an exemption or safe harbor. SEC v. Martino, 255 F. Supp. 2d 268, 283 (S.D.N.Y. 2003), aff'd, 94 F. App'x 871 (2d Cir. 2004). To establish a violation of Section 15(a)(1) of the Exchange Act, the Commission must establish that a broker or dealer: (1) used interstate commerce or the mails; (2) to effect transactions in securities or to induce or attempt to induce others to purchase or sell securities; (3) while not registered with the Commission as a broker or dealer, or in the case of a natural person, not associated with a registered broker-dealer. Scienter is not an element of a violation of Section 15(a) of the Exchange Act. Id.; see also SEC v. George, 426 F.3d 786, 797

(6th Cir. 2005). Other indications that a person may be a broker include the person's active solicitation of investors, handling customer funds and securities, participating in negotiating securities transactions, making valuations or providing advice as to the merits of investments, or receiving transaction-related compensation. See e.g. Hansen, 1984 WL 2413, at *10 (S.D.NY 1984).

The registration exemption for associated persons is not available if an associated person engages in securities transactions that are not within the scope of his employment with the registered firm, and the registered firm is unaware of or has not approved of the associated person's involvement in the transactions. This practice is called "selling away." A registered representative who is selling away may be liable for violations of Section 15(a). See, e.g., SEC v. Ridenour, 913 F.2d 515, 517 (8th Cir. 1990) (bond salesman violated Section 15(a)(1) by engaging in a series of undisclosed, private securities transactions as part of private bond business of which registered firm had no knowledge or opportunity to supervise).

Lloyd, as a registered representative of LPL, was an associated person of a broker-dealer registered with the Commission at the time of the fraud. With regards to the Forest Conservation entities, Lloyd acted as a broker-dealer by: (1) actively soliciting and inducing individuals to invest in these Forest Conservation entities; (2) requiring investors to pay him transaction-based compensation for the offerings in the case of Forest Conservation 2011 and 2012 II, respectively, while misappropriating client funds as his compensation for Forest Conservation 2012; (3) handling investor funds in bank accounts which Lloyd controlled; and (4) by purchasing ownership units in the real estate offerings using the investors' pooled funds. Lloyd testified that he created and sold investments through interstate commerce in the Forest Conservation entities in 2011 and 2012, and then used the funds raised to purchase ownership units in the real estate offerings

without informing or seeking approval from LPL. As such, Lloyd was "selling away" from LPL in 2011 and 2012 and, therefore, was engaged in securities transactions that were not within the scope of his employment with the registered firm, and the registered firm was apparently unaware and did not approve of Lloyd's involvement in these transactions. As a result, Lloyd violated Section 15(a) of the Exchange Act by acting as a broker-dealer without registration.

Accordingly, since Respondent's conduct plainly involved the "purchase or sale of a security," his Motion for Summary Disposition should be denied.

D. Lloyd's Motion for Summary Disposition should be denied because the Division has identified violations of the Antifraud Provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, and violations of the Prohibited Transactions of the Investment Advisers Act of 1940.

Lloyd summarily contends that there was no violation of Section 17(a) of the Securities Act (his Second Defense), no intent to deceive, manipulate or defraud any person (his Third Defense), no violation of Section 10(b) of the Exchange Act of 1934 or Rule 10b-5 thereunder, and no violation of Section 206 of the Investment Advisers Act (his Sixth Defense). Again, since he has failed to support his allegations in this regard, his Motion for Summary Disposition should be denied on that basis alone.

1. Violations of the Antifraud Provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934.

Section 17(a) of the Securities Act prohibits fraud in the offer or sale of a security by the use of interstate commerce or the mail, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit fraud in connection with the purchase or sale of securities by use of interstate commerce or the mail. Specifically, Section 17(a), in the offer or sale of a security, prohibits: (1) employing any device, scheme or artifice to defraud; (2) obtaining money or property by means of making material misstatements of fact or omitting to state material facts; or (3) engaging in any

transaction, practice or course of business which operates as a fraud or deceit. Separately, Section 10(b), in connection with the purchase or sale of securities, prohibits any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors. Rule 10b-5, thereunder, prohibits: (1) employing any device, scheme or artifice to defraud; (2) making any untrue statement of a material fact or omitting to state a material fact; or (3) engaging in any act, practice or course of business which operates as a fraud or deceit. Further, to establish a violation of Section 17(a)(1) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, the Commission must prove scienter, defined as "a mental state embracing intent to deceive, manipulate or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n. 12 (1976); Gotchey, 1992 WL 385284 at *2. Violations of Sections 17(a)(2) and (a)(3) of the Securities Act may be established by a showing of negligence. SEC v. Morgan Keegan & Co., Inc., 678 F.3d 1233, 1244 (11th Cir. 2012).

In this case, Lloyd's actions establish scheme liability under Section 17(a)(1) and (a)(3) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5(a) and (c), thereunder. Lloyd established and operated a scheme or business through interstate commerce using Forest Conservation 2012 to offer or sell securities to individuals in different states, and fraudulently declaring that the funds would be used on the individuals' behalf in order to acquire ownership interests in the real-estate-related offerings. Lloyd never formally presented three clients (Clients A, B, and C) to Broker A for review and, therefore, kept them from participating in the offering and acquiring ownership interests in the Forest Conservation 2012 entity. Further, Lloyd ultimately tried to cover up his scheme by issuing Schedule K-1s to all seventeen clients, thereby

diminishing the ownership interests owed to the fourteen investors known to Broker A. As such, Lloyd evidenced a mental state embracing an intent to deceive, manipulate or defraud.

Lloyd's actions also establish misrepresentation or omission liability under Section 17(a)(2) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5(b), thereunder. As noted above, Section 17(a)(2) of the Securities Act requires obtaining money or property by means of material misstatements or omissions, and Rule 10b-5(b) under the Exchange Act requires the making of material misstatements or omissions. A misrepresentation or omission is material if there is a substantial likelihood that under all circumstances it would have assumed actual significance in the deliberations of a reasonable investor. Basic, Inc. v. Levinson, 485 U.S. 224, 231 (1988); TSC Indust., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); SEC v. Gotchey, 981 F.2d 1251, 1992 WL 385284 at *1 (4th Cir. 1994).

Lloyd made material misstatements and omissions to clients. He told Clients A, B, and C, respectively, that their funds were being used to acquire ownership interests in Forest Conservation 2012, but instead, Lloyd misappropriated their funds. Lloyd also took steps to conceal that he had misappropriated $130,000 from these three tax-planning clients, deliberately hiding those individuals' funds from Broker A, who was evaluating participants as accredited investors for the Land Entity A offering. Lloyd's misstatements and omissions, described above, were material because they concerned the very nature of the investment offered and sold by the proposed respondent to individuals who gave funds to Forest Conservation 2012. SEC v. Research Automation Corp., 585 F.2d 31, 35-36 (2d Cir. 1978) (misleading statements and omissions concerning the use of money raised from investors are material as a matter of law). Further, Lloyd, through emails produced to the staff, informed as least some of the fourteen individuals approved as accredited investors in Forest Conservation 2012 that their entire contribution amounts were

going toward acquiring ownership interests in the real estate offerings, and Lloyd did not mention to these individuals, prior to their investing, that he would be claiming a portion of the contribution checks as his tax-planning fees. These statements were all material as there is a substantial likelihood that such information about the actual amount used for contribution purposes would have been significant in the deliberations of a reasonable investor. Reynolds, 2010 WL 3943729 at *3. Again, Lloyd's actions evidence the requisite scienter that must be shown, as described above.

Finally, the Supreme Court limited persons who may be held primarily liable for "making" a misleading statement under Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder to those "with ultimate authority over the statement, including its content and whether and how to communicate it." Janus Capital Group, Inc. v. First Derivative Traders, 131 S. Ct. 2296, 2302 (2011). Lloyd may be held directly liable for making the material misstatements and omissions to individuals who invested in Forest Conservation 2012. Lloyd, through emails, verbal statements and written documents, made the material misstatements and omissions to individual clients whom he lured into investing in Forest Conservation 2012 before he subsequently misappropriated investor funds and then attempted to conceal his scheme. Lloyd also made material misstatements and omissions to Broker A, from whom Lloyd hid the contribution of funds and accredited-investor paperwork provided by Clients A, B, and C. Accordingly, the proposed respondent violated Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Respondent's Motion for Summary Disposition should be denied.

2. Violations of the Investment Advisers Act.

Section 206(1) of the Advisers Act makes it unlawful for an investment adviser to employ any device, scheme or artifice to defraud any client or prospective client. Section 206(2) makes it

unlawful for an investment adviser to engage in any transaction, practice or course of business that operates as a fraud or deceit upon any client or prospective client. Both Sections 206(1) and 206(2) of the Advisers Act apply to all investment advisers meeting the statutory definition, regardless of their registration status. Section 206(1) requires a showing of scienter; Section 206(2) does not. SEC v. Steadman, 967 F.2d 636, 641 n.3, 643 n.5 (D.C. Cir. 1992).

An investment adviser is defined by Section 202(a)(11) of the Advisers Act as someone who in return for compensation, engages in the business of advising others as to the advisability of investing in, purchasing, or selling securities. The Division expects that its case in chief presented at the hearing will show that during the course of the fraud, Lloyd was an associated person of LPL, a registered investment adviser. Lloyd entered into advisory contracts with his LPL clients providing him with discretionary authority to trade securities for them. Further, Lloyd's individual role as an unregistered investment adviser – activity which was hidden from LPL – is evidenced by his creation, identification and recommendation of the Forest Conservation 2012 offering to his pre-existing advisory clients (*i.e.*, Lloyd alone advised his clients to invest in Forest Conservation 2012). Lloyd also served as an investment adviser to the Forest Conservation 2012 fund, advising the fund as to which securities to purchase and how much, resulting in his trading of the fund's assets in exchange for the purchase of ownership units in the real estate offering by Land Entity A. The subsequent misappropriation of investor funds by Lloyd served as his compensation for advising the Forest Conservation 2012 fund and his LPL clients.

The Division expects that its case in chief presented at the hearing will show that Lloyd violated Sections 206(1) and (2) by misappropriating the assets of his client, the Forest Conservation 2012 fund, which he advised on how to invest. Instead of advising the fund to use all its assets to acquire ownership units in Land Entity A, Lloyd misappropriated $130,000 which had

been provided by Clients A, B, and C, collectively, for Forest Conservation 2012 to use in the acquisition of Land Entity A ownership units. Further, Lloyd also violated Sections 206(1) and (2) by making misrepresentations and omissions of material fact to his four advisory clients participating in the Forest Conservation 2012, LLC concerning, among other things, the amount each individual was investing and the size of each individual's *pro rata* ownership interest in Forest Conservation 2012. As noted above, Lloyd acted with the required scienter to establish a charge under Section 206(1).

Section 206(4) of the Advisers Act prohibits investment advisers from engaging in any "act, practice or course of business which is fraudulent, deceptive, or manipulative." Rule 206(4)-8(a)(1) defines as a fraudulent practice an investment adviser's making false statements of material fact to any investor or prospective investor in a pooled investment vehicle, or failing to state material facts necessary to make statements made to such investors not misleading. Rule 206(4)-8(a)(2) further defines as a fraudulent practice an investment adviser's engaging in any act, practice, or course of business that is fraudulent, deceptive or manipulative, with respect to any investor or prospective investor in the pooled investment vehicle. Scienter is not required to find a violation of this Rule. See Vernazza v. SEC, 327 F.3d 851, 859-60 (9th Cir. 2003) ("It is undisputed that scienter is a required element for violations of ...Advisers Act § 206(1). Scienter is not required for the other violations of the Advisers Act."); see also Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles, Release No. IA-2628, 2007 WL 2239114 at *5 & n.38 (August 3, 2007) ("We read the language of section 206(4) as not by its terms limited to knowing or deliberate conduct").

A "pooled investment vehicle" is defined under Rule 206(4)-8(b) as any investment company as defined in Section 3(a) of the Investment Company Act of 1940 or any company that

would be an investment company under Section 3(a) of that Act but for the exclusion provided from that definition by either Section 3(c)(1) or Section 3(c)(7) of that Act. Here, Lloyd and, through him, Forest Conservation 2012, pooled investor money in the Forest Conservation 2012 bank account in the name of, or for the benefit of, Lloyd's clients and himself personally, purportedly for the purpose of investing or trading in securities (ownership unit offerings). As such, Forest Conservation 2012 meets the definition of an investment company under Section 3(a)(1)(A) of the Investment Company Act which defines an investment company as including an issuer which "is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities." Here, the Division expects that its case in chief presented at the hearing will show that the primary purpose of Forest Conservation 2012, as Lloyd told his clients, was to pool investor funds in order to acquire ownership units in an entity that was expected to preserve land through a conservation easement, thereby generating profits through tax deductions which were larger than the individuals' initial investments. However, Forest Conservation 2012 was not bound by its Operating Agreement to acquire units in Land Entity A or any other specific offering. Lloyd advised the Forest Conservation 2012 as to which securities to acquire and how much to acquire. Lloyd's fraudulent misconduct as related to investors in Forest Conservation 2012 – consisting of misappropriating investor funds, making false statements and omissions to investors about the use of their funds, making false statements and omissions to Broker A in connection with the transactions, and creating misstated Schedule K-1s – violated Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. Accordingly, his Motion for Summary Disposition should be denied.

E. **Lloyd's Motion for Summary Disposition should be denied because he has not established that his Constitutional rights were violated during this proceeding.**

As an initial matter, Lloyd's claim (his Seventh Defense) of a constitutional violation is premised entirely on speculation. He fails to acknowledge that Congress has given the Commission the statutory discretion to address misconduct of the type alleged here by either bringing an action in federal district court (see 15 U.S.C. §§ 78u(d)(1), 80a-41, 80b-9(d)) or by instituting an administrative proceeding (see 15 U.S.C. §§ 77h-1, 78u-3). He also has not presented evidence or an offer of proof that the Commission has interfered with his ability to defend himself by instituting an administrative proceeding against him. Accordingly, his Motion for Summary Disposition should be denied.

The Commission's Rules of Practice set forth the procedures governing administrative proceedings. See 17 C.F.R. § 201.100 et seq. The Commission initiates a proceeding by issuing an order instituting proceedings ("OIP"), which sets forth the nature of the charges to be decided in the hearing, the legal authority and jurisdiction under which it is held, a statement of the facts and law upon which it is based, and the relief sought. 17 C.F.R. § 201.200. Any person named as a respondent is entitled to file an answer to the OIP in which it may admit, deny or state it does not have sufficient information to admit or deny the factual allegations. 17 C.F.R. § 201.220. Respondents must assert any matter constituting an affirmative defense in their answer.

The Rules of Practice provide, among other things, that the Division must promptly make available to any party documents (other than privileged documents) obtained in the investigation leading to the Division's recommendation to institute the proceedings. 17 C.F.R. § 201.230. The Division cannot withhold material exculpatory evidence on grounds of privilege, consistent with the doctrine in Brady v. Maryland, 373 U.S. 83 (1963). 17 C.F.R. § 201.230(b)(2). In addition, a

respondent may ask the Administrative Law Judge ("ALJ") to issue both document and testimony subpoenas to obtain additional information. 17 C.F.R. § 201.232.

The rules also provide a procedure for seeking summary disposition where there are legal issues that can be resolved without a hearing. 17 C.F.R. § 201.250. And the presiding ALJ can certify issues for interlocutory review by the Commission (i.e., the five Commissioners who head the SEC) if a "ruling involves a controlling issue of law as to which there is substantial ground for difference of opinion" and "[a]n immediate review of the order may materially advance the completion of the proceeding." 17 C.F.R. § 201.400(c).

Although the Commission has not adopted the Federal Rules of Evidence, when an administrative proceeding results in a hearing, the Rules of Practice provide that the ALJ "shall exclude all evidence that is irrelevant, immaterial or unduly repetitious." 17 C.F.R. § 201.320. Respondents have an opportunity to cross examine all of the Division's witnesses and to present their own witnesses and evidence. Following a hearing, the ALJ issues an initial decision, and any party may seek *de novo* review of that decision by the Commission. 17 C.F.R. § 201.410.

The Commission's Rules of Practice set deadlines for issuing an initial decision after a hearing and for scheduling a hearing itself. Rule 360(a)(2) provides:

> In the order instituting proceedings, the Commission will specify a time period in which the hearing officer's initial decision must be filed ... In the Commission's discretion, after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors, the time period will either be 120, 210 or 300 days from the service of the order. Under the 300-day timeline, the hearing officer shall issue an order providing that there shall be approximately 4 months from the order instituting the proceeding to the hearing, approximately 2 months for the parties to obtain the transcript and submit briefs, and approximately 4 months after briefing for the hearing officer to issue an initial decision.

17 C.F.R. § 301.360(a)(2)

The Commission's rules also permit respondents to seek, for good cause, extensions of time to file any pleadings and the postponement or adjournment of any hearing. 17 C.F.R. § 201.161(a). While the Commission disfavors such requests, it has identified several factors to be considered in determining whether to grant such relief, including the number of prior requests for extensions, the stage of the proceeding, the ability of the ALJ to complete the hearing in the time period specified by the Commission, and any other matter as justice may require. 17 C.F.R. § 201.161(b).

The Securities Act of 1933, the Investment Advisers Act of 1940, and the Investment Company Act of 1940 all provide that final SEC decisions in administrative proceedings are subject to review in a court of appeals. For example, Section 9(a) of the Securities Act provides in relevant part that:

> Any person aggrieved by an order of the Commission may obtain a review of such order in the court of appeals of the United States, within a circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such Court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part.

15 U.S.C. § 77i(a); see also 15 U.S.C. §§ 80a-42(a), 80b-13(a). Section 9 of the Securities Act also prescribes a comprehensive process for judicial review of final SEC orders. Among other things, Section 9 identifies what constitutes the record before the agency, provides the scope of review, and explains the relief available (the court may affirm, modify or set aside the Commission's order in whole or in part). *See generally* 15 U.S.C. § 77i(a). Section 9(a) also provides for supplemental proceedings if necessary to adduce additional evidence or make additional findings:

> If either party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the hearing before the Commission, the court may order such

> additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as the court may deem proper.

Id.

Thus, under the federal securities laws applicable in an administrative proceeding, courts of appeal can consider any objection raised before the Commission, can order that additional evidence be taken before the Commission, and can modify, or set aside, in whole or in part, any Commission order. 15 U.S.C. § 77i(a); see also 15 U.S.C. §§ 80a-42(a), 80b-13(a). Lloyd cannot be heard to complain about the burden of litigation in an administrative proceeding, because the Supreme Court has specifically recognized that such a burden does not constitute irreparable injury. TTC v. Standard Oil Co., 449 U.S. 232, 244 (1980) (the "expense and annoyance" of litigation does not constitute irreparable injury).

Lloyd's vague and unsupported allegations that the Commission's initiation of an administrative proceeding against has violated his constitutional rights is without merit, and his Motion for Summary Disposition should be denied.

WHEREFORE, the Division respectfully requests an Order denying the Respondent's "motions."

This 7th day of November 2014.

Respectfully submitted,

*

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*By my signature, I certify that this document complies with the length limitation of Rule 154. The word count of this document is 6,964 words.

CERTIFICATE OF SERVICE

The undersigned counsel for the Division of Enforcement hereby certifies that he has served the foregoing document by UPS overnight mail and/or electronic mail, as specified below:

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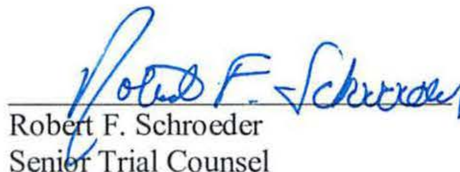

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