UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File Nos. 3-16227 / 3-16229

In the Matter of

MIDDLEBURY SECURITIES, LLC and GREGORY OSBORN

Respondents.

DIVISION OF ENFORCEMENT'S SUPPLEMENTAL REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF ITS MOTION FOR SUMMARY DISPOSITION AND RELIEF AGAINST RESPONDENTS MIDDLEBURY SECURITIES, LLC AND GREGORY OSBORN

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The Division of Enforcement ("Division") respectfully submits this supplemental reply memorandum of law in further support of its motion seeking summary disposition and relief against Respondents Gregory Osborn ("Osborn") and Middlebury Securities LLC ("Middlebury", together, "Respondents").

PRELIMINARY STATEMENT

Given an additional opportunity to complete the picture of their supposedly dire financial conditions, Respondents Middlebury and Osborn have either continued to obscure their true abilities to pay or shown that they are in fact able to pay, while simultaneously asking for this Court's leniency in imposing civil penalties.

Middlebury has continued to refuse to provide evidence of its own current financial condition and, accordingly, Middlebury's inability to pay is not properly at issue. But, even if considered, Middlebury's incomplete submission, a FOCUS report but no statement of financial condition, shows income and the ability to pay expenses in the months preceding its dissolution. At most, Middlebury's assets have dwindled as it has sought to delay the imposition of penalties in this matter. The Court should not reward this conduct by sparing Middlebury from civil penalties here.

For his part, Osborn has continued to ignore the Division's—and now the Court's—request for complete documentation relating to his financial condition, but, more importantly, many of the documents Osborn has provided, relating to his taxes, his salary, and his upcoming bonuses, show that Osborn is in fact able to pay a civil penalty.

Accordingly, and for the reasons set forth below as well as in the Division's Opening Brief, dated July 28, 2016 ("Div. Br."), and its Reply Brief, dated August 28, 2016 ("Div. Reply"), the Court should order full disgorgement against Respondents on a joint and several basis and impose maximum third-tier civil penalties against each of them.

ARGUMENT

At the prehearing conference on the Division's motion for summary disposition and in subsequent orders, the Court granted Respondents an additional opportunity to document their inability to pay—only one of several Steadman factors that the Court considers in determining whether to impose civil penalties.[1] For the reasons discussed below, Respondents have not met their respective burdens.

A. Middlebury Has Failed to Show Inability to Pay

In its brief in opposition, Middlebury argued that one of the factors the Court should consider in determining whether to impose civil penalties was its supposed inability to pay. In support of that position, Middlebury offered only the then-available drafts of its FOCUS reports to show its then-current assets and liabilities. (See Robinson Decl., ¶¶ 8-9 & Ex. G; Robinson Supp. Decl., ¶¶ 2-4 & Ex. A).[2]

In response, the Division argued that the FOCUS report alone was insufficient to permit the Court to consider Middlebury's purported inability to pay. (See Div. Reply at 9; Tr. of Oral Arg. at 59:1-15.) Although the Court did not rule on this argument, it did "put[]

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[1] The Division respectfully refers the Court to its opening and reply briefs in support of its request for an order requiring Respondents to jointly and severally disgorge their ill-gotten gains from the Navagate frauds, and in reference to other factors relevant to the imposition of civil penalties. The Division notes that, although purporting at the prehearing conference to dispute the exact amount of funds that Osborn directed to Middlebury entities in connection with the fraud, see Tr. of Oral Arg. at 56:15-57:12 (Sept. 15, 2016), Respondent Middlebury has abandoned any claim that Osborn did not in fact direct the distribution of $311,150. Middlebury has also failed to provide its bank statements for the time periods in which it contested the receipt of funds, and does not dispute that Osborn was acting as Middlebury's principal when he directed the use of the funds at issue. Accordingly, the amount of disgorgement at issue is no longer in dispute.

[2] References to the "Robinson Supp. Decl." are to the Supplemental Declaration of James B. Robinson in Support of Respondent Middlebury Securities LLC's Opposition to the Division of Enforcement's Motion for Summary Disposition, dated September 7, 2016. All other capitalized terms not defined herein shall have the meaning ascribed to them in the Div. Br. or the Div. Reply.

[Middlebury] on notice that the more [it gives the Court], the more likely it is [the Court] will find that [Middlebury has] done what [it needs] to do to at least cross the threshold" for the Court to consider "the merits of an inability to pay argument." (Tr. of Oral Arg. at 59:16-25.) The Court then gave Middlebury an additional opportunity to file "financial information relevant to its inability to pay defense." (Order Following Prehearing Conference, File Nos. 3-16227, 3-16229 (Sept. 16, 2016).)

Middlebury has now squandered this opportunity. Middlebury has continued to refuse to provide a complete picture of its financial condition, resting once again on little more than its (now final) FOCUS report. Middlebury still has not submitted sworn financial statements or records "from the date of the first violation," 17 C.F.R. § 201.630(b), at issue in this case, which began in late 2009 and continued through 2011. (Middlebury OIP, ¶¶ 1, 28, 33.) Nor has Middlebury submitted any tax returns or bank statements, either for the period in question or for the present day.

Instead, Middlebury has provided a series of irrelevant documents—its withdrawal of registration (Second Supp. Robinson Decl. Ex. A),[3] the text of a Commission Rule (id. Ex. B), its certificate of cancelation with the State of Delaware (id. Ex. E), and tax returns and ledgers that purport to show the amounts Middlebury's owner obtained (id. Exs. F-J)—all of which have no bearing on Middlebury's financial condition.

But even assuming, arguendo, that the Court may properly consider Middlebury's ability to pay defense, the relevant documents show that Middlebury is able to pay a civil penalty. Although Middlebury's FOCUS report lists a liability of $271,937, Middlebury's submission also reveals that this is a debt owed by Middlebury to Middlebury's sole owner.

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[3] References to "Second Supp. Robinson Decl." are to the Second Supplemental Declaration of James Robinson, dated January 13, 2017.

(See Second Supp. Robinson Decl. at ¶ 7 & Exs. C, K.) Accordingly, although Middlebury continues to refuse to provide its bank statements, even the FOCUS report demonstrates that Middlebury continues to have some cash on hand.

Middlebury's balance sheet and general ledger for 2016 also show nearly $90,000 in commission income from various sources over the last year. (Id. Ex. K at 7 (showing $48,219.27 in BD Fees & Commission income and $38,502.53 as Commissions on Regulated Work).) Middlebury's only other submission, a check paid to an attorney in connection with legal representation, (see id. Ex. M), and its statements regarding other expenses, are of no moment. As the Division noted in its Reply Brief, see Reply Br. at 9 n.6, the fact that Middlebury has had to incur fees for its operations in the last year (such as travel expenses and phone bills, see Second Supp. Robinson Decl., Ex. K at 8-10), is legally irrelevant to its ability to pay. In fact, many of Middlebury's expenses in the past year relate to its defense of this action, which debt should not be counted towards Middlebury's inability to pay. (See In the Matter of Russell C. Schalk, Jr., ID Admin. Proc. File No. 3-16498, 2016 WL 536129 *6 (Feb. 10, 2016) (refusing to consider debt incurred to defend Division's investigation of respondent in connection with inability to pay argument).)

If anything, the documents submitted by Middlebury show a steady erosion of its existing assets while it has continued to delay the imposition of penalties against it by the Commission. (Compare Robinson Decl. ¶ 9 (Middlebury had $146,000 in assets as of September 2016) with Second Supp. Robinson Decl. Ex. L (citing $13,483 in assets as of December 2016).) At most then, the evidence shows not an inability to pay, but a desire not to pay these liabilities.

While the Court may "consider evidence of ability to pay in determining whether a respondent should be required to pay disgorgement, interest, or civil penalties," such an ability to pay "is only one factor that informs . . . [the] determination and is not dispositive." In the Matter of Edgar R. Page, Rel. No. IA-4400, 2016 WL 3030845, at *14 (S.E.C. May 27, 2016) (citations and quotation marks omitted). Moreover, the "burden of proving financial inability to pay . . . falls upon the respondent[s]" and "[e]ven when a respondent demonstrates an inability to pay, [the ALJ] ha[s] discretion not to waive . . . disgorgement, . . . particularly when the misconduct is sufficiently egregious." Id. at **14-15 (quotation marks and citations omitted). "Although [Middlebury's] present and future financial condition . . . [may not] be robust, there are some gaps" in Middlebury's presentation of its financial condition sufficient to preclude weighing inability to pay as a factor against the imposition of third-tier civil penalties. SEC v. Nadel, No. 11 Civ. 215, 2016 WL 639063, at *26 (E.D.N.Y. Feb. 11, 2016).

Accordingly, the Court should order Middlebury to pay civil penalties.[4]

B. Osborn's Submissions Demonstrate an Ability to Pay

Like Middlebury, Respondent Osborn has also been given numerous opportunities by the Division and the Court to provide a full picture of his financial condition that would assist in determining his ability to pay a civil penalty. But, like Middlebury, Osborn has similarly chosen not to avail himself of these repeated opportunities.

In his first untimely submission in opposition to the Division's motion, Osborn provided a statement of financial condition purporting to evidence his inability to pay. As

[4] The civil penalty will also have the deterrent effect against other broker-dealers that civil penalties were designed to create. See In the Matter of Francis V. Lorenzo, Rel. No. 33-9762, 2015 WL 1927763, at *14 (S.E.C. Apr. 29, 2015) (noting that sanctions against a broker-dealer who commits fraud "will deter other market professionals from engaging in similar misconduct").

the Court observed in a subsequent order, Osborn's contentions were deficient in numerous ways, including for failing to document a supposed debt of a substantial sum to Osborn's former company, Nuvel, for failing to submit statements from financial institutions, and for failing to provide complete tax returns for the relevant years. (Order, File Nos. 3-16227, 3-16229 (Dec. 8, 2016).)

Osborn's latest submissions do not fully address these problems. They do not include all of Osborn's relevant tax returns (the 2014 return is missing, as are other returns relevant to the time in question—2009 and 2010) or full bank statements (scant records of a Capital One account are provided). Moreover, Osborn's latest submission contains additional, uncorroborated statements of his financial condition, including purported debts of $12,000 to the State of New York, "$7,00" [sic] apparently to the IRS, and "of course $960,00 [sic] in federal lean [sic]." This supposed $960,000 debt is reasserted elsewhere in Osborn's papers, along with a series of undocumented debts owing to friends and family. The Court should not give any weight to these unsupported assertions of debt.

And where Osborn has complied with the Court's directive, the submissions reveal that, contrary to his protestations of imminent bankruptcy, Osborn has access to at least some resources. In his latest filing, for example, Osborn clarified that, contrary to his prior statement that he owed over $200,000 to Nuvel (see Osborn Ex. 10 at 4), he in fact owns 47,000 shares in a reconstituted form of that company, which he believes may trade between $5 and $9 a share, a potential value of between $235,000 and $423,000. (Osborn Submission at ¶ 3.) While he purports to have pledged those assets to debtors, Osborn's accounts at Citibank show transfers of thousands of dollars from Nuvel throughout 2016, with a transfer as recent as August 26, 2016. Osborn's prior submission similarly showed

that he received $134,000 in 2016 following the sale of stock in another company he founded. (Osborn Ex. 15 at 26.)

Osborn does appear to have complied with the Court's directive that he provide current statements of his mortgage and home equity loan, although the documents together do not definitely establish the amount owed. (Compare "House Value by Town" E-mail (showing tax assessment over home valued at $1.5 million) with M&T Bank Mortgage Statement (showing amount due of $224,642, which includes past due principal payments totaling nearly $1 million) and Chase Statement (home equity loan of $749,216).)

Similarly, to the extent Osborn did submit tax returns, they show that Osborn had substantial income during one of the years of the fraud at issue in this case—over $800,000 in 2011 alone. (See Osborn Ex. 15 at 18.) The tax documents also show over a half a million dollars in gross adjusted income (after deducting for business expenses) in 2012, and nearly another half a million in 2013. Although the 2014 return is missing, the 2015 return similarly shows a net positive adjusted gross income. But the key question raised by the one return provided for the relevant time period (2011) is unanswered—where did all the money go?

Osborn's current employment situation also adds to the resources at his disposal. In response to the Court's direction that Osborn clarify the salary and bonus to which he is entitled at his new position, Osborn has submitted documents that show his salary to be [redacted] (see "ZapGo Sept. 2016 Agreement"), and a potential bonus of $100,000 from his employer for the fourth quarter of 2016 alone, of which he may be the sole recipient (see "US ZapGo Bonus"). And, as the Division noted in a filing to the Commission in response to Osborn's request to reconsider his industry bars, Osborn represented to a

potential employer that he was receiving a base salary of [redacted] plus an additional $300,000 in bonus. In one of the documents in his latest submission, Osborn makes the self-serving statement that he received only "$115 [thousand, presumably]" in 2016 from his employer. In another, he asserts he "made $157,000" including the first bonus. It is hard to give much weight to Osborn's statements in light of his continually changing story regarding his income and financial condition but, whether $115,000, $157,000, or $300,000, the fact remains that Osborn's salary makes him able to pay civil penalties.

Osborn's bank statements further show his ability to pay. His Citibank statements show numerous transfers from his employer as well as from other sources such as the aforementioned Nuvel, unexplained deposits from Brio Financial Group ($3,465 in September of 2016), and handsome deposits of cash ($10,491 on September 29, 2016). These statements also evidence expenses ranging from payments to Amex credit cards, expenditures at Sporting Goods stores, and car payments.

Osborn's incomplete Capital One statements show a similar picture. First, they evidence over $3,000 in serial cash withdrawals during the first week of this year in Las Vegas, Nevada. These withdrawals accompany other unexplained deposits ($10,000 from Dezaio Productions on December 19, 2016), large payments to Amex credit cards (over $6,000 in December 2016 alone and at least $3,000 in January 2017), and unexplained checks totaling thousands of dollars (checks totaling $7,300 in January of 2017).

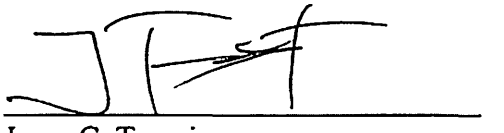
Again, while Osborn's financial condition may not be robust, there are sufficient gaps in his avowal of poverty to dissuade the Court from considering his inability to pay as a defense. And, even if considered, the available evidence shows that Osborn has access to funds that would enable him to pay civil penalties here.

CONCLUSION

In sum, both Respondent Middlebury and Respondent Osborn have failed to provide sufficient evidence of their respective inabilities to pay. To the contrary, both have submitted documents that show access to at least some assets. The Court should, therefore, grant the Division summary disposition and order that Osborn and Middlebury pay disgorgement and prejudgment interest jointly and severally, and that Respondents pay civil penalties as requested in the Division's opening brief.

Dated: January 20, 2017
New York, New York

DIVISION OF ENFORCEMENT



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