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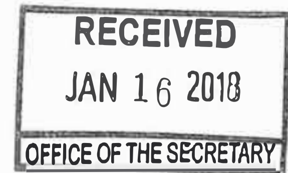
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



In the Matter of **BIOELECTRONICS CORPORATION,** **IBEX, LLC,** **ST. JOHN'S, LLC,** **ANDREW J. WHELAN,** **KELLY A. WHELAN, AND** **ROBERT P. BEDWELL,** Respondents.	File No. 3-17104

RESPONDENTS' RESPONSE TO COMMISSION'S RATIFICATION ORDER AND JUDGE CAMERON ELLIOT'S NOTICE AND ORDER

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Respondents, BioElectronics Corporation, Ibex, LLC, St. John's, LLC, Andrew J. Whelan and Kelly Whelan (collectively, "Respondents") submit this response to the Order of the Commission (the "Commission's Ratification Order") and Notice to Parties and Order Following Ratification of Judge Cameron Elliot ("Notice and Order" and, with the Commission's Ratification Order, the "Reconsideration Orders").

A. This Proceeding Violates the Appointments and Due Process Clauses.

The Commission's Ratification Order purports to ratify the appointments of five Administrative Law Judges ("ALJs"), but not their decisions. That Order mandates that Your Honor: "… Reconsider the record, including all substantive and procedural actions…"; "grant parties until January 5, 2018 to submit any new evidence the parties deem relevant …"; [and] "Determine… whether to ratify or revise in any respect all prior actions taken by an administrative law judge in the proceedings…." *Id.*, pp. 1-2. Your Honor's Notice and Order adds that each party may submit a brief explaining the relevance of its new evidence; identifying any challenged rulings, findings, or conclusions; and addressing the effect of any relevant changes to controlling law, including *Kokesh v. SEC*, 137 S.Ct. 1635 (2017) ("*Kokesh*").

Respondents are joined by the Solicitor General, and the Tenth Circuit, concluding that Your Honor was not properly appointed under the Appointments Clause. Commission's Ratification Order, p. 1, citing Solicitor General's brief in *Raymond J. Lucia v. SEC* (No. 17-130); and *Bandimere v. United States Securities and Exchange Commission*, AP# 15-9586, 844 F.3d 1168 (10th Cir. 2016) ("*Bandimere*").

A violation of the Appointments Clause constitutes a structural error requiring automatic reversal of the Initial Decision. *Bandimere at* 1181, citing *Plaut v. Spendthrift Farm, Inc.*, 514 U.S. 211, 239 (1995); *Rivera v. Illinois*, 556 U.S. 148, 161 (2009); *Intercollegiate Broad. Sys.*,

Inc. v. Copyright Royalty Bd., 796 F.3d 111, 123 (D.C. Cir.2015); *United States v. Solon*, 596 F.3d 1206, 1211 (10th Cir. 2010).

For the reasons detailed below, the purported ratifications failed and, consequently, any ruling in these proceedings by Your Honor violates the Appointments Clause and is null and void.

Even if Your Honor's appointment had been valid, which it was not, the due process required by the U.S. Constitution, and implied in the Commission's Ratification Order, was stymied by Your Honor's subsequent order in this proceeding refusing to allow adequate time to prepare Respondents' brief and disallowing a reasonable length for the brief to be filed. While Respondents were notified of a broad range of permissible new arguments and an opportunity to present new evidence, Your Honor undermined the due process ostensibly offered by the Commission when it denied Respondents' motion to allow a 50-page limit and an extra 30 days to prepare Respondents' papers, instead permitting only a 3000-word brief and a 1-week extension (one week was already lost between the date of the Commission's Reconsideration Order (November 30, 2017) and this Court's Notice and Order (December 6, 2017).

B. Post-Hearing Briefing And Evidence Relevant to Reexamination.

Respondents offer the Post Hearing Evidence And Briefs filed herewith ("Post-Hearing Evidence"), Exhibits 1 through 13, pursuant to this Court's Notice and Order, and incorporate them by this reference.

In addition, Respondents re-submit evidence improperly excluded at the hearing:

1. Evidence of A. Whelan's character. RT 1194-1196, 1256-1257; Post-Hearing Evidence, Exhibit 7, pp. 4-6; Exh. 10, pp. 39-41;
2. Testimony of Three of Respondents' experts. Initial Decision, p. 31, § II.G.3; BioElectronics Corp., Admin. Proc. Rulings Release No. 4127, 2016 SEC LEXIS

3340 (ALJ Sept. 6, 2016); RX 201, 202 and 205; Post-Hearing Evidence, Exh. 7, pp. 18-20; Exh. 10, pp. 41-42.

3. Evidence of good faith reliance on counsel. Post-Hearing Evidence, Exh. 7, pp. 2-3, 16-18, 20; Exh. 10, 37-38; Exh. 11, p. 19-20

C. Elements of Ratification Are Not Satisfied.

Faced with hundreds of structurally invalid rulings from 5 unconstitutionally appointed ALJs, the Commission hopes that by purporting to ratify the appointment of all 5 ALJs, and then having the ratified ALJs ratify their rulings, it can erect valid proceedings from the wreckage of structurally invalid proceedings. This novel approach to a novel problem cannot survive Constitutional scrutiny.

The Commission's Ratification Order proposes two ratifications, neither of which satisfies the requirements for ratification: (1) the Commission's blanket ratification of appointments of its five ALJs; and (2) Your Honor's proposed ratification of its Initial Decision.

There are three pre-requisites to ratification: "First, the ratifier must, at the time of ratification, still **have the authority to take the action to be ratified.** Second, the ratifier must have full knowledge of the decision to be ratified. Third, the ratifier must **make a detached and considered affirmation** of the earlier decision." *Advanced Disposal Servs. E. v. NLRB,* 820 F.3d 592, 602 (3d Cir. 2016).

The Commission cannot satisfy the first and third pre-requisites. First, ALJs are appointed pursuant to statutory authority – which statutes do not vest unilateral appointment authority in the Commission. 5 U.S.C. § 556(b)(3); *Mullen v. Bowen*, 800 F.2d 535, 540 n.5 (6th Cir. 1986) ("[T]he ALJ's position is not a creature of administrative law; rather, it is a direct creation of Congress under the [APA]."). Because the Commission never had authority unilaterally to appoint ALJs, it also never had unilateral authority to ratify such appointments.

Under 5 U.S.C. § 3105, the Commission may "appoint as many administrative law judges as are necessary." But, the Commission's discretion to make such appointments is far from unfettered. Agencies hire ALJs through a merit-selection process administered by the United States Office of Personnel Management ("OPM"), which places ALJs within the civil service. 5 U.S.C. § 1302; 5 C.F.R. § 930.201. For example, ALJ applicants must be licensed attorneys with at least seven years of litigation experience. 5 C.F.R. § 930.204; see OPM, Qualification Standard for Administrative Law Judge Positions, https://perma.cc/2G7J-X5BW. OPM administers an exam and uses the results to rank applicants. 5 C.F.R. § 337.101.

The OPM is not the agent of the Commission and the Commission is not the principal of the OPM. The Commission has no authority to ratify or override OPM decisions and regulations, as a principal would its agent. Thus, the Commission could not ratify any ALJ's appointment unilaterally, as it purports to do.

The Commission could not and did not make a "detached affirmation" of such appointments. Such ratifications were not considered on their merits after a detached analysis, but instead reflect a legal strategy on how best to resurrect structurally invalid proceedings. Because the purported ratifications were not detached, but instead were designed specifically to fix the *Bandimere* problem, the Commission's blanket ratification of all five ALJs was invalid.

Separately, the proposed ratification by Your Honor of your own rulings would be invalid because the first and third requirements of ratification cannot be met. Because the Commission's ratification of Your Honor's appointment is invalid, Your Honor still lacks authority to ratify. Moreover, because Your Honor cannot make a **detached** affirmation, any ratification would be invalid.

D. *Kokesh* Limits Disgorgement to 5 years and Eliminates Double Penalties.

A 5-year statute of limitations applies to the Division's claims. 28 U.S.C. § 2462. *Kokesh v. Securities and Exchange Commission*, No. 16-529, slip op. (June 5, 2017) ("*Kokesh*"). "[U]nder *Kokesh*, any ill-gotten gains received before April 17, 2010—five years before April 17, 2015—should be excluded from the disgorgement relief to be awarded." Division's Brief, Post-Hearing Evidence, Exh. 13, p. 1. [1]

Because violations of section 5 are strict liability offenses, the computation of profits to be disgorged should not exceed profits on transactions completed within the 5-year statute of limitations. Post-Hearing Evidence, Exh. 11, pp. 11-13.

In the Initial Decision, Your Honor reasoned, at page 55: "the measure of disgorgement under the facts of this case is the value of the securities sold minus their cost of acquisition." Citations omitted. The total profits from transactions within the 5-year statute of limitations was $462,532. RX 1A; and Post-Hearing Evidence, Exh. 2. If correctly limited to ill-gotten gains in 2013 and 2014, the sole and isolated period during which the Division's own expert, Mr. Park, testified that a scheme to evade the registration requirements was ongoing, the proper disgorgement would be zero. TR. 155 and 201. During that period, there was no profit. Post-Hearing Evidence, Exh. 2 (Flood Post-Hearing Decl., Exh. 1).

After *Kokesh,* "the Division reduced the aggregate sales proceeds of $4,296,266 determined by the ALJ by $813,000". Post-Hearing Evidence, Exh. 2, ¶¶7-8; Exh. 13 p. 5. Because Your Honor's calculation assigned no cost basis to the $813,000 in sales proceeds eliminated, the *Kokesh* adjustment should include no change in the $2,715,673 cost basis used by Your Honor. Initial Decision, p. 55. The proposed award of $1,580,593 (*Id.*) ($4,296,266-

[1] The OIP was published February 5, 2016. Per Tolling Agreements at Post-Hearing Exhibit 3, the February 5, 2011 start date was extended to April 17, 2010.

$2,715,673) should be reduced by at least $813,000 to $767,593. Any prejudgment interest accrued thereon should be reduced *ab initio*.

While the Division correctly reduced the aggregate sales proceeds, it mistakenly also reduced, in part, the aggregate loan principal by "$105,000, reflecting the aggregate loan principal corresponding to those ten sales of BIEL stock... RX 1A." Division Supplemental Brief, Post-Hearing Evidence, Exh. 13. But, Your Honor did **not** include that $105,000 into the $2,715,673 in the first place, explaining that the $2,715,673 cost basis "does not include the first loan listed in Flood's analysis, because the record is insufficient to determine precisely how much of the original loan should be apportioned to what was sold in 2010." Stipulation at Ex. A (line 3); RX 1A at 1, 7...." Initial Decision, p. 55; Post-Hearing Evidence, Exh. 2; Exh. 13, p. 5. It makes no sense (and would be grossly unfair) to reduce $105,000 from the cost basis number, when that $105,000 was never included in the $2,715,673 cost basis number used in Your Honor's calculation.

In addition, Your Honor should reduce the disgorgement award by the amount of lawful interest earned on the debt, $259,291. Post-Hearing Evidence, Exh. 2, ¶9. Lawful interest is not ill-gotten gains. Post-Hearing Evidence, Exh. 1, p. 15; Exh. 2, ¶9.

After *Kokesh*, which made clear that "[d]isgorgement in the securities-enforcement context is a 'penalty'" (*Kokesh*, p. 1)), any awards of pre-judgment interest would be improper because "prejudgment interest is not available on punitive damages awards." *Nance v. City of Newark*, 501 F. App'x 123, 129 (3d Cir. 2012), citing *Belinski v. Goodman*, 139 N.J. Super. 351, 354 A.2d 92, 96 (N.J. Super. Ct. App. Div. 1976); *Poleto v. Consol. Rail Corp.*, 826 F.2d 1270, 1278 n.14 (3d Cir. 1987), *abrogated on other grounds by Kaiser Aluminum & Chem. Corp. v. Bonjorno*, 494 U.S. 827, 834-35, 110 S. Ct. 1570, 108 L. Ed. 2d 842 (1990); *Nance v. City of Newark*, Civil Action No. 97-6184 (JLL), 2014 U.S. Dist. LEXIS 96494, at *14 (D.N.J. 2014).

E. Ratification Only Applies To Actions That Are Not Time-Barred.

In *Fec v. Nra Political Victory Fund*, 513 U.S. 88, 98, 115 S. Ct. 537, 543 (1994), the Supreme Court invalidated the Solicitor General's attempt to ratify the FEC's filing of a petition for certiorari because such ratification came after the deadline to file that petition had lapsed. Although the petition was filed timely by the FEC, its lack of authority to do so could not be cured by ratification after the deadline to file had passed.

Here, the Commission's Ratification Order can only ratify that which is not time barred. Because it was entered on November 30, 2017, more than five years after all profitable transactions occurred and more than five years after the alleged Section 13(a) violations, the Division can no longer proceed on those claims. 28 U.S.C. § 2462; *Kokesh,* Flood Post-Hearing Decl., Exh. 1. Among other things, because all profitable transactions fall outside of the statute of limitations, all disgorgement and interest must be eliminated from the award.

F. There Were No Violations of Section 5.

Section 4 exempts the transactions in this case. Post-Hearing Evidence, Exh. 7, pp. 20-24; Exh. 10, pp. 14-23; Exh. 11, pp. 14-18.

G. Section 13(a) Is Not Applicable After BioElectronics' 2006 and 2007 Withdrawals of its Registration – No Violations Occurred.

The reporting requirements upon which the OIP is based under Section 13(a) do not apply because BioElectronics' 2006 and 2007 withdrawal from registration was effective under Section 12(g) of the Securities Act. 15 USC §78m. Post-Hearing Evidence, Exh. 7, pp. 25-28; Exh. 10, pp. 42-44. In any event, the technical accounting issues at play in connection with such violation do not justify penalties. Post-Hearing Evidence, Exh. 11, p. 19.

H. The Penalties Violate the Eighth Amendment.

Because the *Kokesh* decision holds that disgorgement is a penalty, the disgorgement awards against each of the Respondents are limited by the Excessive Fines Clause of the Eighth Amendment: "Excessive bail shall not be required, nor excessive fines imposed, nor cruel and unusual punishments inflicted." U.S. Const., Amendment 8. "[A] punitive forfeiture violates the Excessive Fines Clause if it is grossly disproportional to the gravity of a defendant's offense." *United States v. Bajakajian*, 524 U.S. 321, 334, 118 S. Ct. 2028, 141 L. Ed. 2d 314 (1998).

Courts consider a variety of factors when evaluating whether a fine is excessive under the Eighth Amendment, including (1) the extent of the harm caused; (2) the gravity of the offense; and (3) whether the violation was related to other illegal activity and the nature and extent of that illegal activity. *United States v. 3814 NW Thurman St., Portland, Or.*, 164 F.3d 1191, 1197-98 (9th Cir. 1999) (citing *Bajakajian*, 524 U.S. at 336-39).

Respondents caused no harm. Their violations, if any, were technical non-scienter violations of securities laws and rules governing the timing of income recognition under complex accounting standards. The violations, if any, were committed after consultation with lawyers and accountants. The section 5 violations, if any, were crimes arising out of excessive and dedicated reinvestment by IBEX, not crimes involving the taking of moneys away from investors. All moneys reported received were, in fact, received and no such funds were refunded. Only the characterization and timing of recordation were questioned.

The misstatements, if any, were not made in conjunction with illegal activity. Just the opposite. They were made as part of BioElectronics' laudable efforts made to develop an innovative drug free pain relieving device that would benefit a world plagued with opioid addiction. Under these circumstances, imposing devastating disgorgement and other civil penalties far beyond each Respondent's ability to pay would be grossly disproportionate to the

offenses in violation of the Eighth Amendment. Post-Hearing Evidence, Exh. 7, pp. 13-18; Exh. 10, pp. 28-31.[2]

The civil penalties against St. John's are extraordinarily excessive, unpayable and not remotely supported by St. John's conduct. Post-Hearing Evidence, Exh. 1, pp. 2-3, 25-29, Exh. 11, p. 18.

Your Honor's assessment of third-tier penalties, a cease and desist order and a penny stock bar were not supported by the evidence or the Order Instituting Proceedings. Post-Hearing Evidence, Exh. 7, pp. 14-18; Exh. 10, pp. 31-34.

I. Other Errors Made At The Hearing.

1. At all times, there were less than 500 shareholders of record of BioElectronics. Post-Hearing Evidence, Exh. 1, pp. 2, 20-25; Exh. 4, ¶¶3, 4; RX 194, 194B at 2242, 2293, 2313; and TR 642-643; 910-911.
2. Any disgorgement award should be reduced by the 15% capital gains taxes paid, $193,096. Post-Hearing Evidence, Exh. 2, ¶¶8, 9. The federal government cannot double-dip; retaining capital gains taxes paid and disgorgement of the same funds. Post-Hearing Evidence, Exh. 1, p. 4.
3. IBEX should not be ordered to disgorge funds it no longer holds, never received or received and immediately reinvested. Post-Hearing Evidence, Exh. 1, pp. 16-17.
4. The Initial Decision unfairly misconstrues and discounts Mr. Flood's testimony. Post-Hearing Evidence, Exh. 1, pp. 17-20; Exh. 2, ¶¶10-20.
5. Joint and several liability is unwarranted because gains can be apportioned. Post-Hearing Evidence, Exh. 10, pp. 34-37.

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[2] Respondents incorporate by reference all financial documents and Form D-A's submitted under seal in this proceeding.

6. Your Honor had no authority to award restitution at law, by simply mischaracterizing such relief as "disgorgement." Because Respondents no longer have the proceeds of the transactions at issue, the award is one at law for money, not one in equity for disgorgement. Post-Hearing Evidence, Exh. 11, pp. 6-10.

J. Conclusion.

In summary, Respondents ask that Your Honor reject all claims asserted in the OIP, as amended, and award nothing, or substantially modify the Initial Decision, for the reasons stated above and in the briefs incorporated by reference. Among other things:

1. This Court decisions and rulings violate the Appointments Clause;
2. The structural defects from violation of the Appointments Clause are not curable;
3. A superficial review conducted by the initial unauthorized decision maker based on extremely limited briefing does not afford the Respondents Constitutionally mandated due process;
4. The ratifiers lack authority to ratify;
5. The ratifications fail because the ratifiers cannot make a ***detached*** decision;
6. *Kokesh* limits disgorgement to a 5-year statute of limitations;
7. *Kokesh* makes clear that disgorgement is a penalty – there is no need for duplicative penalties where a disgorgement award wipes out Respondents' assets;
8. The five-year statute of limitations counts back from the date of ratification, eliminating all disgorgement claims and Section 13(a) violations;
9. No interest should accrue on pre-judgment disgorgement because disgorgement is a penalty under *Kokesh* and no interest can run on penalties;
10. All transactions were exempt from registration under Section 5;
11. Proposed penalties violate the Eighth Amendment of the U.S. Constitution.

12. The exclusion of key Respondents' experts, including testimony establishing IBEX's investments as being based on and motivated by commercially reasonable terms for both parties, mandates a new trial.

13. BioElectronics' FDA and UK NHS approvals establish IBEX's investments as valid long-term investments, not part of any scheme to evade.

Dated: West Los Angeles, California
January 11, 2018

Respectfully submitted,
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CERTIFICATION TO WORD COUNT

I, Brian T. Corrigan, that the number of words in the foregoing brief is less than 3000 words, excluding the cover page, signature block and tables of contents and authorities, based on the word-count report generated by the Microsoft Word computer software program.

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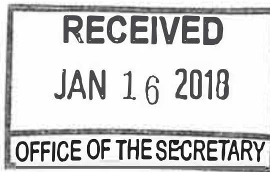

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I hereby certify that on January 11, 2018, I caused to be served a true and correct copy of the following documents on the date and in the manner indicated below.

RESPONDENTS' POST-HEARING EVIDENCE AND BRIEFS

RESPONDENTS' RESPONSE TO COMMISSION'S RATIFICATION ORDER AND JUDGE CAMERON ELLIOT'S NOTICE AND ORDER

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I declare under penalty of perjury that the foregoing documents were served as described above from West Los Angeles, California on January 11, 2018.

Brian T. Corrigan