**UNITED STATES OF AMERICA**
**Before the**
**SECURITIES AND EXCHANGE COMMISSION**


**ADMINISTRATIVE PROCEEDING**
**File No. 3-17104**

**In the Matter of**

**BIOELECTRONICS CORP.,**
**IBEX, LLC,**
**ST. JOHN'S, LLC,**
**ANDREW J. WHELAN,**
**KELLY A. WHELAN, CPA, AND**
**ROBERT P. BEDWELL, CPA,**

**Respondents.**

# THE DIVISION OF ENFORCEMENT'S POST-HEARING BRIEF

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## INTRODUCTION

Since its inception in April 2000, BioElectronics Corp. ("BioElectronics" or "BIEL") has struggled to make ends meet. During the years leading up to the events in this case, BioElectronics lost over 10 and a half million dollars, and over its lifetime, BioElectronics has accumulated losses of 27 million dollars. At the same time, the number of shares of BioElectronics stock in the market has exploded—going from 750 million shares authorized in June 2009, to 7 billion shares authorized at the end of 2014, and 15 billion shares authorized today (11 billion outstanding)—all reaching the hands of public investors in unregistered transactions.

As the Division has shown, BIEL—through the actions and efforts of Andrew Whelan, Kelly Whelan, IBEX, LLC ("IBEX"), and St. John's, LLC ("St. John's")—has dumped billions of shares of stock into the market in illegal unregistered transactions, repeatedly violating Section 5 of the Securities Act of 1933 (the "Securities Act"). BIEL also overstated nearly one half of its sales revenue in the first and only Form 10-K that it ever filed, by falsely recording $366,000 in revenue on two so-called "bill and hold" transactions, which BIEL and Andrew Whelan have since conceded were not bill and hold transactions at all. At the hearing, the Division proved that these transactions were not recordable as bill and hold sales *or* traditional sales, and BIEL and Andrew Whelan therefore violated Section 13 of the Securities Exchange Act of 1934 (the "Exchange Act") and related rules by issuing a materially false and inaccurate annual report and making materially false statements to BIEL's auditors.

Respondents do not dispute much of the Division's evidence, nor could they. Indeed, the parties have stipulated that IBEX made millions of dollars in loans to BIEL, while

simultaneously selling millions of dollars' worth of BIEL securities to third-party purchasers.[1] Respondents concede that IBEX was BIEL's primary lender, responsible for "keeping the lights on" and BIEL's ability to make payroll, and that without IBEX's financing, BIEL may well have gone out of business. Respondents admit that Kelly Whelan had a close relationship with BIEL. They also admit that IBEX, under Kelly Whelan's control, had the ultimate power to bankrupt BIEL when its loans came due, but that it was a "friendly lender," that chose not to do so. Respondents also concede that IBEX serially returned proceeds from its sales of BIEL securities back to the issuer, BIEL, to fund new loans, and that, on many occasions, the third-party buyers paid BIEL directly, completely bypassing IBEX, the alleged seller. Respondents do not contest that *billions* of shares of BIEL have entered the public market without a single registration statement being filed, or that BIEL's Board of Directors voted to authorize those shares, at least in part to fund conversions of notes by IBEX's purchasers. Respondents also do not credibly contest that BIEL's 2009 10-K included $366,000 in revenue from two transactions that never should have been characterized as bill and hold transactions at all.

This is not a close case. The Division presented overwhelming evidence that Respondents violated Section 5 of the Securities Act, and that Respondents Andrew Whelan and BIEL violated Section 13 of the Exchange Act and related rules. The Division has further established that Andrew and Kelly Whelan's violations were willful. Respondents have repeatedly cut corners, comingled interests and loyalties, misstated critical facts, evaded legal requirements, and flouted the SEC's rules and regulations to avoid the expense and inconvenience of Section 5's registration requirements. Respondents have benefitted greatly from BIEL's status as an SEC-reporting public company and have taken full advantage of being

[1] Joint Stipulations of Fact (Sept. 17, 2016) ("Joint Stip.") [DX 1], Exs. A & B.

able to reach investors through the SEC's EDGAR system and OTC Markets—raising many millions of dollars through their efforts. Yet Respondents have failed to comply with the critical duties and responsibilities that they voluntarily undertook when joining the ranks of other public reporting companies. This simply is not how a legitimate company runs its business when soliciting public investment. This Court should therefore find all Respondents liable and impose (a) a cease-and-desist order for each violation; (b) orders of disgorgement and prejudgment interest; (c) maximum civil monetary penalties for each of Respondents' violations; and (d) permanent penny stock bars against Andrew and Kelly Whelan.

## THE EVIDENCE

### I. RESPONDENTS DISTRIBUTED BILLIONS OF SHARES OF BIEL SECURITIES IN UNREGISTERED TRANSACTIONS

#### A. Respondents IBEX and Kelly Whelan Were the Financing Arm of BIEL

Kelly Whelan founded IBEX sometime before 2005 with money raised by taking funds from her personal savings, a home equity loan, credit card advances, and withdrawals from an ERISA 401K account.[2] Ms. Whelan formed IBEX to invest in her father's company, BioElectronics,[3] and, since its creation, IBEX's sole business has been to finance BioElectronics through sales of BIEL convertible notes and shares to third parties. As Kelly Whelan testified, "IBEX is not anything. It is where I sometimes hold investments."[4] Sometime between 2003

[2] Tr. 449:4-450:5 (K. Whelan); Tr. 534:13-19 (M. Whelan); Tr. 1230:20-1231:5 (K. Whelan); Joint Stip. [DX 1] ¶¶ 22-23.

[3] Tr. 443:17-18 (K. Whelan).

[4] Tr. 1048:13-15 (K. Whelan); *see also* Tr. 878:3-16 (A. Whelan); Tr. 1048:16-1049:14 (K. Whelan); Tr. 1049:15-16 (K. Whelan: "IBEX doesn't do anything in the securities market. IBEX doesn't do anything.").

and 2005, Kelly Whelan made her first investment in BIEL.[5] Thereafter, Kelly Whelan and IBEX made frequent loans to BIEL to finance BIEL's operations.[6]

IBEX quickly became BIEL's primary source of financing.[7] Kelly Whelan estimated that IBEX made "in the neighborhood of 100" loans to BIEL just between 2010 and 2014, and admitted that she could not "remember a time when [she] refused to make a loan to BioElectronics Corporation."[8] During the Relevant Period (August 2009 to November 2014) alone, IBEX loaned BIEL over $5.4 million, providing 16 percent of BIEL's *total* financing over its 16-year lifetime.[9]

Initially, IBEX's loans to BIEL were not memorialized through any formal loan or promissory note agreements or otherwise documented individually.[10] Sometime in 2009, IBEX and BIEL entered into a back-dated revolving and convertible promissory note agreement, intended to memorialize the terms of the loans made by IBEX to BIEL prior to that date.[11] Although the Loan Agreement and Revolving Convertible Promissory Note are dated January 1,

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[5] Tr. 1054:6-17 (K. Whelan).

[6] Joint Stip. [DX 1], Ex. A.

[7] OTC Markets Annual Report Dec. 31, 2010 [RX 194B] at 14 ("Our primary source of financing over the last several years has been loans provided to us by IBEX LLC, whose principal, Kelly Lorenz, is the daughter of Andrew Whelan, our president."); OTC Markets Annual Report Dec. 31, 2011 [RX 194C] at 13 (same); Tr. 243:13-23 (A. Whelan); Tr. 538:10-25 (M. Whelan) (discussing IBEX as BIEL's primary source of financing and stating that "there have been periods, obviously, when IBEX was critical to making the company whole and keeping the lights on.").

[8] Tr. 1065:17-20 (K. Whelan); *see also* Tr. 448:24-449:3, 452:1-12 (K. Whelan).

[9] Order Instituting Administrative Cease-and-Desist Proceedings ¶ 1 (Feb. 5, 2016) ("OIP"); Joint Stip. [DX 1], Ex. A; Tr. 537:12-19 (M. Whelan) (stating that total capitalization is approximately 33 million over BIEL's lifetime); Tr. 1279:7-1280:3 (Staelin).

[10] Tr. 469:17-470:3 (K. Whelan); Tr. 1113:1-13 (K. Whelan); Tr. 1116:25-1117:12 (K. Whelan) (testifying that IBEX did not have an accounting system or ledger).

[11] Tr. 405:5-10 (A. Whelan); Tr. 470:21-471:12 (K. Whelan); Tr. 1065:20-1066:24 (K. Whelan); Loan Agreement [DX 43]; Revolving Convertible Promissory Note [DX 44].

2005, they were not, in fact, drafted or executed until August 2009.[12] These documents provide that IBEX could make loans of up to $2,000,000 to BIEL "to finance working capital commitments,"[13] and receive in exchange the "Revolving Convertible Promissory Note,"[14] convertible into shares of BIEL common stock pursuant to the terms set forth in the back-dated note.[15]

The form of the Revolving Convertible Promissory Note did not match the intent and practice of the signatories. Although the back-dated Note was executed in August 2009, BIEL did not borrow and IBEX did not lend under that note following its execution.[16] Instead, BIEL began borrowing from IBEX pursuant to separate Convertible Promissory Notes, executed in connection with each borrowing, bearing interest at the rate of 8 percent per year.[17] In connection with the first two of these separate notes, BIEL granted IBEX a security interest in all of BIEL's personal and intellectual property.[18] Kelly Whelan subsequently agreed to subordinate IBEX's security interest in all of BIEL's personal and intellectual property to another lender (EXIM Bank)'s lien, seemingly without compensation or reward.[19]

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[12] Loan Agreement [DX 43]; Revolving Convertible Promissory Note [DX 44]; Tr. 471:17-472:10 (K. Whelan).

[13] Loan Agreement [DX 43].

[14] Revolving Convertible Promissory Note [DX 44].

[15] Loan Agreement [DX 43]; Revolving Convertible Promissory Note [DX 44]; Tr. 471:13-475:15 (K. Whelan).

[16] BIEL OTC Markets Annual Report Dec. 31, 2011 [RX 194C] at 002362 ("BIEL FY2011 Unaudited Report").

[17] BIEL FY2011 Unaudited Report [RX 194C] at 002362.

[18] BIEL FY2011 Unaudited Report [RX 194C] at 002362; UCC Filing Perfecting IBEX Lien [DX 7]; Tr. 302:13-305:17 (A. Whelan); Tr. 498:15-500:9 (K. Whelan); Tr. 891:20-892:4 (A. Whelan).

[19] Tr. 480:1-3, 500:18-21 (K. Whelan); Tr. 638:9-11 (M. Whelan: "And IBEX subordinated their loan to the EXIM Bank when we took the EXIM Bank loan. It was one of the requirements.").

IBEX's loans to BIEL were financed through IBEX's distributions of BIEL shares and convertible notes in unregistered transactions. Respondents' Exhibit 1F, a compilation of checks, bank records, and transaction journals gathered by Kelly Whelan in connection with litigation,[20] contains 19 third-party checks,[21] each of which reflects a sale by IBEX to a third party where the third party paid the proceeds *directly to the issuer*, BIEL, at Kelly Whelan's direction:

> Q . . . . Why is it that other people were providing the funds that were credited to you as having made a loan to BIEL?
>
> A ***I had sold my shares of BioElectronics stock to that third party and directed them to make the check payable to BioElectronics Corporation.***
>
> * * * *
>
> Q So, in effect, if I'm understanding correctly, BIEL received precisely the amount of the loan proceeds, correct, that you—from your sale of the shares or the note?
>
> A In some instances in that time period, yes.
>
> Q And that would be the case whenever there were direct payments to BIEL in connection with your sale of shares or a note to another entity?
>
> A Correct. ***I would have directed that person to make their payment to BIEL as opposed to directly to me, correct.***
>
> Q I count, just roughly, trying to keep up with you as you were going through this, ***at least 20 instances*** in which that occurred.

[20] Tr. 1110:20-1111:10 (K. Whelan).

[21] *See* Checks; Bank Statements; Transaction Journals re: Revolver [RX 1F], at 000051-52, 000056, 000090, 000092, 000095 (two checks), 000097-98, 000100, 000104 (two checks), 000105, 000108-109, 000111-114.

A ***That's—that is possible, yes.***[22]

Kelly Whelan similarly instructed third parties who purchased BIEL securities from her to wire funds directly to BIEL.[23]

Although IBEX and BIEL improved their paperwork in the fall of 2009, the *pattern* of IBEX's using its sales of BIEL shares and convertible notes to third parties to fund BIEL's operations continued throughout the Relevant Period. As Richard Staelin, BIEL's Chairman of the Board and sole member of the Audit Committee testified during his investigative testimony and affirmed at the hearing:

> Q So, Mr. Staelin, you said you knew that Kelly had made a lot of money. She had made a lot of money by selling BioElectronics stock, correct?
>
> * * * *
>
> Q Let's take a look at your testimony [DX 107] again. . . . . At line 9, you were asked: "Did you ever ask anyone on the board?
>
> 'A. ***Well, I understand that and understood that IBEX would at times go to the open market or to another investor and sell some unrestricted shares.*** . . .
>
> ***'So I imagine she would raise money by selling some stock that she owned in BioElectronics on the open market or to an investor.*** . . .
>
> * * * *
>
> Q But you believed that at times Kelly Whelan was going to the market and selling unrestricted shares of BioElectronics?
>
> A ***What I understood was that she had notes and that those notes she could sell to some other—some other third party if she wanted to. And she could get cash for that if she wanted to. And she sold it at whatever price she negotiated to some***

[22] Tr. 1223:7-1224:18 (K. Whelan) (emphasis added); Tr. 1215:8-24, 1222:17-1223:6, 1224:19-1225:8 (K. Whelan).

[23] Tr. 1225:9-1226:23 (K. Whelan); RX 1F at 000071 (instructing Mazuma Holding Corporation to wire payment for shares purchased from IBEX directly to BIEL); *id.* at 000073 (similar instruction to another purchaser).

> ***third party.***
>
> ***That was not part of my job to understand what was going on, but, yes, I knew that IBEX was disposing of selling some of her assets, which were notes, to a third party.***[24]

The evidence confirms Mr. Staelin's assumption that IBEX was funding its loans to BIEL directly through sales of BIEL securities. Not only did some third-party purchasers make payments directly to BIEL, but IBEX also provided funds directly to BIEL in "dribs and drabs,"[25] often in the precise (or very similar) amount of the proceeds that IBEX received from its contemporaneous sales of BIEL securities to third parties.[26] These loans by "dribs and drabs" reflect the fact that IBEX was funding BIEL's daily operations, including by paying BIEL creditors and consultants for bills due and outstanding, using proceeds of its BIEL sales.[27] This is hardly the role of a traditional, independent, arms' length lender.[28]

### B. IBEX is Part of the BIEL Control Group and an Affiliate of BIEL

[24] Tr. 1281:5-1283:8 (Staelin) (emphasis added).

[25] Tr. 396:10-11 (A. Whelan).

[26] Joint Stip. [DX 1], Exs. A & B; Expert Report of William D. Park (Aug. 26, 2016) ¶ 63 ("Park Report") [DX 137] (noting that approximately 25 of the loans made to BIEL during the 2013-14 period were for the same amount that IBEX had just received from the Liquidating Entity for the sale of shares); Tr. 295:8-302:11, 395:8-396:4 (A. Whelan).

[27] Tr. 394:17-401:7 (A. Whelan) (together with two members of the Board of Directors, Kelly Whelan funded BIEL settlement with a judgment creditor); Tr. 892:5-13 (A. Whelan: "The chairman badgered me and Kelly to kick in a third [to pay the settlement], and he kicked in a third, and we just paid him in cash."); Tr. 401:11-402:12 (A. Whelan) (IBEX gave Simon Jacobson stock for investor relations services to BIEL); Tr. 460:18-461:4 (K. Whelan); Tr. 538:23-25, 665:7-20 (M. Whelan); Tr. 1275:24-1277:9 (Staelin) (Kelly Whelan funded BIEL payroll and operations).

[28] IBEX's payments to third parties to whom BIEL owed money included Joseph Noel, the CEO of YesDTC Holdings, Inc. ("YesDTC"), who performed investment relations and strategic consulting work for BIEL and other consultants who assisted BIEL in its daily operations. Tr. 452:13-459:4, 459:8-460:9 (K. Whelan); Letter from K. Whelan to J. Noel for Payment for Services Rendered to BIEL (Feb. 12, 2010) [DX 85].

BIEL *preferred* to borrow from IBEX rather than other lenders. Andrew Whelan testified that Kelly Whelan was a family member who could be trusted, in contrast to other lenders, who the BIEL Board believed damaged the company through short selling.[29]

BIEL understood that Kelly Whelan was a "friendly investor"[30] who could be trusted not to exercise her power to foreclose on the assets of BioElectronics,[31] even though BIEL did not have sufficient cash to pay IBEX's notes if called.[32] BIEL also believed that the cost of capital from other independent lenders was too high.[33] In contrast to an arms' length transaction with an independent lender, through BIEL's transactions with IBEX, the company was able to fund its operations "hand to mouth"—with no cash on hand.[34] Kelly Whelan and IBEX also never refused to make a loan, unlike an arms' length, independent, lender.[35] Although BIEL had an "insatiable appetite for capital," and tried to raise capital in every imaginable way, it struggled to obtain other financing.[36]

Kelly Whelan's relationship to BIEL was that of a company insider, and she was privy to all aspects of BIEL's business. Indeed, at various times she was a valued member of BIEL's staff,[37] performing bookkeeping services,[38] and communicating with potential customers using a

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[29] Tr. 477:22-478:1 (K. Whelan); Tr. 645:12-646:3 (M. Whelan: describing loan from independent lender, LH Capital, as "the biggest mistake" in "the history of BioElectronics").

[30] Tr. 1255:16-20 (Staelin).

[31] Tr. 332:19-334:18 (A. Whelan); Tr. 542:10-25 (M. Whelan); Tr. 881:14-25 (A. Whelan); Tr. 1066:16-1067:14 (K. Whelan); Tr. 1255:6-8 (Staelin).

[32] Tr. 484:18-485:7 (testimony of Kelly Whelan re: insufficient cash available to pay).

[33] *See, e.g.*, Tr. 1046:18-1047:16 (A. Whelan: "I believe the company's drastically undervalued now, so the cost of capital is very high. So I want to delay financing until we can get the cost of capital down."); Tr. 867:11-868:5 (A. Whelan).

[34] Tr. 867:11-872:24 (A. Whelan).

[35] Tr. 481:7-17 (K. Whelan: "I can't think of a time that I refused.").

[36] Tr. 308:2-311:10 (A. Whelan); Tr. 1273:20-1275:23 (Staelin).

[37] Tr. 241:20-242:3 (A. Whelan); Tr. 434:9-435:11, 438:4-439:3, 441:9-442:6 (K. Whelan).

BIEL email address.[39] Kelly Whelan attended BIEL Board meetings and was included in BIEL Board communications at which her investments were discussed.[40] She received both cash and securities as compensation for her work at BIEL.[41] Indeed, even today, Kelly Whelan maintains a close relationship to BIEL as a distributor of BIEL products in Canada.[42] In sum, as Mary Whelan testified when asked whether Kelly Whelan played a vital role in the company, "She's been exceedingly helpful to making it real, yes."[43]

### C. IBEX Sold for the Issuer, BioElectronics

The unrebutted testimony of William D. Park—a Senior Director in the Enforcement Department of the Financial Industry Regulatory Authority ("FINRA"), with over 19 years' experience conducting hundreds of complex investigations and analyses of thousands of securities transactions—makes clear that IBEX's sales of BIEL convertible notes and shares were for the issuer, BIEL.[44] Mr. Park testified regarding his review of dozens of IBEX loans to BIEL and sales to third parties (whom Mr. Park terms "Liquidating Entities") during the Relevant Period.

Mr. Park explained that during the Relevant Period, BIEL received a substantial amount of its operating funds through the public resale of purportedly restricted securities, primarily by

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[38] Tr. 438:6-9 (K. Whelan).

[39] Tr. 340:9-343:17 (A. Whelan); Tr. 435:12-436:2 (K. Whelan); Tr. 887:10-888:9 (A. Whelan); Tr.1071:22-1073:10 (K. Whelan); Emails Among A. Whelan, M. Whelan, and R. Staelin re: Default Notes (June 5, 2012) [DX 30].

[40] Tr. 344:8-348:23 (A. Whelan); Tr. 436:11-23 (K. Whelan); Board Minutes (June 18, 2009) [DX 92]; Board Communications (June 5, 2012) [DX 30].

[41] Tr. 434:9-13, 439:4-441:8 (K. Whelan).

[42] Tr. 417:7-17 (K. Whelan); Tr. 884:8-16 (A. Whelan); Tr. 1062:2-1063:1 (K. Whelan).

[43] Tr. 544:8-11 (M. Whelan).

[44] *See generally* Park Report [DX 137].

IBEX.[45] After accumulating significant inventory of convertible BIEL notes in exchange for funds loaned to the issuer, IBEX sold tranches of those notes to a small group of investors. Those Liquidating Entities in turn almost immediately converted the notes into unrestricted BIEL shares that they then sold into the public market in unregistered transactions. IBEX returned almost all the funds it received from these sales to BIEL immediately or very shortly after the sales were completed. Neither BIEL nor IBEX took any steps to ensure that the Liquidating Entities were acquiring BIEL notes and shares with investment intent.[46] Presumably, this is because the Liquidating Entities had no intention of holding onto the securities. Rather, the whole point of the Liquidating Entities' purchases was to acquire notes that were already due, negotiate a favorable conversion price—below market price and immediately sell the stock for an instant, virtually guaranteed, profit.[47] The Liquidating Entities were acquiring stock to sell, and Respondents were happy to oblige through letters (falsely) certifying that IBEX was not an affiliate and that the securities acquired by the Liquidating Entities could be resold without registration.

Overall, from January 2010 through February 9, 2015, IBEX facilitated the sale of approximately 3.5 billion shares of BIEL. Ninety-five percent of this amount (approximately 3.3 billion shares), was sold between January 2013 and November 2014. By November 2014, IBEX had facilitated the sale of over 50 percent of BIEL's total shares outstanding.[48] On a quarterly

[45] Park Report [DX 137] ¶¶ 19-21.

[46] Tr. 264:18-24 (A. Whelan); Tr. 1082:6-12 (K. Whelan).

[47] Park Report [DX 137] ¶¶ 42, 44.

[48] Park Report [DX 137] ¶¶ 19-21, 42-43. Between January 2013 and November 2014, IBEX sold convertible debt to eight Liquidating Entities. *Id.* ¶¶ 43-44. These parties typically purchased the debt usually at a significant discount to the market price that would allow them to profit from immediate resales, and would immediately convert the debt to shares and liquidate those shares into the public market. As IBEX received funds from the Liquidating Entities, IBEX sent most of these sums to BIEL. *Id.*

basis during this period, IBEX's total sales often amounted to more than one percent of the total shares outstanding. For instance, the sales in three quarters alone were at least ten percent of the total shares outstanding, with one of them (1Q 2014) representing 25 percent. Overall, from January 2010 through February 9, 2015, IBEX received approximately $4 million from the Liquidating Entities and sent approximately $5 million to BIEL. During the January 2013 through November 2014 time frame, IBEX received approximately $2.7 million from Liquidating Entities and sent approximately $2.5 million to BIEL, or over 90 percent of the amount it received from the unregistered sales.[49]

Mr. Park's testimony is confirmed by Respondents' own testimony. Kelly Whelan testified at length about her purchase and "disposal" of BIEL notes and shares and her return of the proceeds of these "disposals" to the issuer, BIEL.[50] Ms. Whelan also described how she was "looking to sell shares," but when it became too difficult to convert and sell shares herself (purportedly because of a deposit transaction restriction (or "chill") placed on transactions in BIEL's stock by the Depository Trust Company ("DTC")), she used Redwood Management's superior access to the public markets to make sales to investors.[51]

### D. BIEL was Involved in the Distributions

IBEX's distributions of BIEL's shares into the market via the Liquidating Entities would not have been possible without the knowledge and participation of BIEL. When IBEX sold BIEL convertible notes to third-party purchasers, some purchasers required an Assignment and Assumption Agreement, in which IBEX assigned its interest in the convertible note to the

[49] Park Report [DX 137] ¶¶ 19-21, 56.

[50] Tr. 1201:11-1220:12 (K. Whelan); *see also* Tr. 1222:17-21 (K. Whelan) (confirming that when she says she "disposed of the loan" she sold or converted it).

[51] Tr.491:6-492:9 (K. Whelan); BIEL Press Release, "Depository Trust Company (DTC) Lifts Chill on BioElectronics Shares" (Mar. 20, 2014) [DX 3] ("Press Release").

purchaser.[52] Andrew Whelan, as BIEL's CEO, then signed a certification in the Assignment and Assumption Agreement, in which he "agree[d] and confirm[ed]" that the Agreement's statements as to the nature of the Debt and relationship with IBEX were "true and correct."[53] Mr. Whelan confirmed IBEX's representations that it was not a 10 percent or greater shareholder of BIEL and was not an affiliate of BIEL.[54]

Andrew Whelan wrote *dozens* of letters to BIEL's transfer agent on behalf of BIEL, instructing the transfer agent to issue certificates for millions of shares of BIEL stock to purchasers without restrictive legends.[55] Mr. Whelan's representation that IBEX was not an affiliate of BIEL was critical to this process.[56] Most of IBEX's purchasers sold almost immediately upon acquiring BIEL securities,[57] evidencing that the commercial viability of these transactions depended on the purchasers' receiving securities without restrictive legends. Between April 12, 2013 and March 11, 2014, an 11-month period, Andrew Whelan wrote 19 letters to BIEL's transfer agent relating to IBEX's sales of convertible notes to Redwood, instructing BIEL's transfer agent to issue 1.47 billion shares of BIEL, all without restrictive

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[52] Tr. 249:13-251:4 (A. Whelan); Exhibits to K. Whelan Declaration (May 26, 2016) [DX 138] at 000822-825 ("K. Whelan Decl. Exs.").

[53] Tr. 253:20-254:25 (A. Whelan); K. Whelan Decl. Exs. [DX 138] at 000825.

[54] K. Whelan Decl. Exs. [DX 138] at 000822. Andrew Whelan and BIEL also entered into Securities Settlement Agreements directly with the third-party purchasers. *Id.* at 000826-836; Tr. 257:20-260:18 (A. Whelan).

[55] Tr. 231:20-232:14, 263:5-264:24 (A. Whelan); K. Whelan Decl. Exs. [DX 138] at 000815.

[56] Issuer securities acquired privately from affiliates of the issuer are restricted. 17 C.F.R. § 230.144(a)(3)(i). Thus, the issuance of unrestricted securities by BIEL's transfer agent to entities that purchased from IBEX required a justification for removing the restrictive legend. Here, IBEX and BIEL incorrectly relied on Rule 144's safe harbor for sales by non-affiliates.

[57] Park Report [DX 137] ¶¶ 43-44.

legends.[58] Mr. Whelan wrote these letters during the period of time that the DTC had in place its purported "chill" on BIEL's stock.[59] Between March 25, 2014 and September 23, 2014, a six-month period following the lifting of the purported DTC chill, Andrew Whelan wrote an additional 18 letters to BIEL's transfer agent instructing the transfer agent to issue certificates for 866 million shares of BIEL stock to Redwood without a restrictive legend.[60] Andrew Whelan knew that in so instructing the transfer agent, it made it possible for Redwood to make sales of BIEL stock to the public market:

> Q [Y]ou instructed the transfer agent to issue the shares to Redwood without a restrictive legend?
>
> A Yes.
>
> Q Which meant that Redwood was free to sell those shares into the public market?
>
> A They could do whatever they wanted to.[61]

In some instances, Andrew Whelan also wrote letters directly to third-party purchasers' broker-dealers, in which he certified that (i) IBEX was not an affiliate of BIEL or part of a control entity with BIEL; and (ii) there was no agreement by or among IBEX, the third-party purchaser, and BIEL to remit any portion of the proceeds of the resale of securities to the public to BIEL.[62] Mr.

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[58] Compilation of Letters from A. Whelan to Transfer Agent re: Redwood Sales [DX 2]; Summary of A. Whelan Letters to Transfer Agent re: Redwood Sales During DTC Chill [DX 2A]; Tr. 997:20-1007:3 (A. Whelan).

[59] *Id.*; Press Release [DX 3].

[60] Compilation of Letters from A. Whelan to Transfer Agent re: Redwood Sales [DX 2]; Summary of A. Whelan Letters to Transfer Agent re: Redwood Sales Following DTC Chill [DX 2B]; Press Release [DX 3]; Tr. 1007:4-1011:11 (A. Whelan).

[61] Tr. 264:18-24 (A. Whelan).

[62] Olde Monmouth Transfer Agent Records and Correspondence [DX 132] at SEC-OMST-E-0000919.

Whelan knew that the broker-dealers were relying on these certifications in accepting shares of BIEL for resale to the public market.[63]

Mr. Whelan and BIEL's Board also knew that IBEX's sales of BIEL convertible notes to the Liquidating Entities required the Board to authorize new shares of BIEL to meet the inevitable conversion and sale of BIEL securities by the Liquidating Entitles.[64] BIEL's Board voted to increase the number of shares of BIEL stock available from 750 million shares to 1 billion shares in 2009, to 1.5 billion shares in 2010, to 2 billion shares in 2011, to 3 billion shares in 2012, to 4 billion shares in 2013, to 7 billion shares in 2014, and 15 billion shares in 2015.[65] These increases were necessitated by "the continued requirement to cover the potential issuance of common stock resulting from the conversion of debt to equity,"[66] and because BIEL could not afford to pay off the notes' principal plus interest.[67] As IBEX continued to provide funds to BIEL and obtain new convertible debt, BIEL continued to increase its estimates of the number of shares it would need to reserve to meet future conversions by IBEX or the Liquidating Entities.[68] As of the end of 2013, BIEL estimated it would need to issue 9.9 billion shares in the future to

[63] Tr. 323:3-328:13 (A. Whelan). Among other requirements, Rule 15c2-11 imposes upon broker-dealers the obligation to ensure that shares are free-trading before posting a quotation for the stock for resale into the market. 17 C.F.R. § 240.15c2-11.

[64] *See, e.g.*, Tr. 272:5-277:3 (A. Whelan); Olde Monmouth Transfer Agent Records and Correspondence [DX 132] at SEC-OMST-E-0000931 (email exchange with transfer agent re: need to vote to increase the number of shares).

[65] BIEL OTC Markets Annual Disclosure Dec. 31, 2015 [RX 171Q] ("BIEL FY2015 Unaudited Annual Report").

[66] BIEL FY2015 Unaudited Annual Report [RX 171Q].

[67] Tr. 246:13-249:12 (A. Whelan); Tr. 1284:11-1287:22 (Staelin); *see also, e.g.*, Board Unanimous Consent (June 27, 2013) [DX 35] (increasing number of authorized shares because "the Corporation does not have cash to pay the Notes and wishes to avoid being in default and the note holders wish to avoid having the Corporation in default . . .").

[68] Park Report [DX 137] ¶ 32.

meet the anticipated demand for shares under the convertible notes. As of the end of 2014, BIEL's estimate increased to 11.7 billion.[69]

Many of Mr. Whelan's letters to BIEL's transfer agent, broker-dealers, and clearing houses contain direct misrepresentations. For example, Mr. Whelan represented that IBEX was not an affiliate of BIEL and that there was no agreement to remit the proceeds of sales back to BIEL.[70] And, in a letter dated March 19, 2014 to Chris Cervino of COR Clearing, Andrew Whelan falsely certified that "the above-referenced shares are fully registered. . . ."[71] They were not.

### E. St. John's is an Affiliate of BIEL, and Did Not File Forms 144 in Connection with its Sales of BIEL Securities

BIEL also distributed shares to the public markets through St. John's, LLC, a company owned by Andrew Whelan's wife, Patricia Whelan, of which Kelly Whelan is a one percent owner and registered agent.[72] The parties stipulated to the following relevant facts with regard to St. John's investments in BIEL and affiliated sales of BIEL securities:

Patricia Whelan formed St. John's LLC in 2009.[73] Since its formation in 2009, St. John's has loaned BIEL approximately $2.9 million, and has received in exchange convertible notes.[74]

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[69] Park Report [DX 137] ¶ 32 (citing BIEL quarterly and annual disclosure documents on otcmarkets.com).

[70] Olde Monmouth Transfer Agent Records and Correspondence [DX 132] at 0000919.

[71] Tr. 1019:12-1020:8 (A. Whelan); Olde Monmouth Transfer Agent Records and Correspondence [DX 132] at 0000211.

[72] Tr. 502:18-24 (K. Whelan); Joint Stip. [DX 1] ¶ 3. It is unclear whether Ms. Whelan also served as the "Manager" of St. John's. Although Division Exhibit 120 contains a document signed by Kelly Whelan as the "Manager" of St. John's, Ms. Whelan testified that she did not recall being the Manager. *See* World Trade Financial Documents [DX 120] at 19; Tr. 502:6-503:7 (K. Whelan). It is clear, however, that Ms. Whelan had a legal role and ownership interest in St. John's and "believed [she] could sign [the document] on behalf of [St. John's] because [she] had a 1 percent ownership …." Tr. 502:6-503:7 (K. Whelan).

[73] Joint Stip. [DX 1] ¶ 29.

[74] Joint Stip. [DX 1] ¶¶ 30-31.

Two of these convertible notes were issued on June 30, 2010 (in the amount of $95,794.67) and August 31, 2010 (in the amount of $61,108.82).[75] On June 20, 2012, St. John's converted these two convertible notes, and BIEL issued 91,808,086 shares to St. John's.[76] St. John's subsequently sold 81 million of these 91 million shares in 17 separate transactions between March 26, 2013 and March 6, 2014.[77] At the time of these sales, St. John's and BIEL did not file any Forms 144 providing notice to the Commission of their intent to sell BIEL's stock.[78] Rather, the sole Form 144 filed for these transactions is dated May 26, 2016, two to three *years* after the time of St. John's sales.[79] And, even this late-filed Form 144 only includes 14 of St. Johns'17 sales of BIEL shares and omits sales on March 5 and 6, 2014.[80]

### F. Andrew Whelan, BIEL, Kelly Whelan, and IBEX Benefitted at the Expense of Investors

Andrew and Kelly Whelan have benefitted from Respondents' distributions of unregistered BIEL securities, at the expense of an uninformed public. BIEL filed a registration statement in February 2006 because it was a requirement of its agreement with one of its lenders.[81] When it became too financially onerous to comply with the registration requirements,[82] BIEL pulled its registration and paid a settlement to the lender.[83] Thereafter, BIEL became gun-shy of dealing with arms' length lenders and was unable to generate interest

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[75] Joint Stip. [DX 1] ¶ 32.

[76] Joint Stip. [DX 1] ¶ 33.

[77] Joint Stip. [DX 1] ¶¶ 34-35; Sales Sheet of St. John's Sales of BIEL [RX 172H].

[78] Tr. 905:8-11 (A. Whelan); Declaration of Thomas B. Rogers [DX 122].

[79] Joint Stip. [DX 1] ¶ 36.

[80] St. John's Form 144 (May 26, 2016) [RX 176].

[81] Form SB-2 [RX 188]; Tr. 640:10-641:6 (M. Whelan).

[82] Tr. 665:21-666:3 (M. Whelan).

[83] Tr. 641:7-18 (M. Whelan).

from venture capitalists, and decided instead to finance BIEL's operations primarily through IBEX and Kelly Whelan, "friendly" lenders (which, in contrast to arms' length lender, LH Capital, did not require BIEL to register).[84] Kelly Whelan sold BIEL stock and notes, sending back monies received to BIEL in the form of "new investments."[85]

Kelly Whelan personally became wealthy at the expense of uninformed public shareholders. After initially financing IBEX with her own limited assets,[86] Kelly Whelan "bec[a]me very liquid" in 2009 by selling BIEL stock.[87] In 2010, Kelly Whelan had $3.8 million in the bank, "most of" which was the result of sales of BIEL shares.[88] Kelly Whelan used the proceeds of her sales of BIEL convertible notes and shares to fund further monies made available to BIEL,[89] and continued to make loans because the accrual of interest at eight percent and the sales of BIEL securities were profitable to her.[90] Other than her initial (undocumented and nominal) investment, Kelly Whelan never took on any additional investment risk; She simply took the proceeds of sales of BIEL securities and immediately reinvested them in BIEL, effectively replacing the shares sold, with an ability to obtain shares in the future.[91]

Despite profiting personally from her sales of BIEL shares and using those sales to fund BIEL's operating expenses—all while BIEL's share value was plummeting—Kelly Whelan

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[84] *See, e.g.,* Tr. 665:4-666:3 (M. Whelan).

[85] Joint Stip. [DX 1], Ex. B.

[86] Joint Stip. [DX 1] ¶¶ 22-23; Tr. 1230:20-1231:5 (K. Whelan).

[87] Tr. 416:24-417:1 (K. Whelan: "The stock price of BioElectronics Corporation went up significantly in July of 2009, and I was able to become very liquid at that point"); Tr. 448:21-23 (K. Whelan: "And in 2009, the stock price went up significantly and I was able to then become very liquid."); Tr. 487:4-6 (K. Whelan) (again confirming she made a substantial amount of money from sale of BIEL shares in 2009); Tr. 1061:23-1062:1 (K. Whelan).

[88] Tr. 1229:14-1230:19, 1233:10-13 (K. Whelan).

[89] Tr. 487:14-19 (K. Whelan).

[90] Tr. 485:8-12 (K. Whelan).

[91] Park Report [DX 137] ¶ 27.

exhibited no concern for BIEL's public shareholders, whose interest were being diluted every time BIEL authorized additional shares to provide for IBEX's conversion rights.[92] Indeed, in the face of the purported DTC chill, Ms. Whelan's solution was not to *stop* distributing shares to the public market until the issue was resolved. Instead, she significantly *increased* the volume of her sales of BIEL convertible notes to Redwood Management, a company that she knew was in the business of buying debt, converting it into shares, and immediately selling to the public market.[93] Despite the fact that Redwood Management could not have sold BIEL shares to investors without her participation in the chain of distribution, Ms. Whelan expressed *no* concern whatsoever for the impact of this conduct on the investing public, or her own role in getting BIEL shares to the market without registration statements.[94]

Andrew Whelan and BIEL's Board of Directors were equally unconcerned about the impact of their actions on the investing public.[95] Although BIEL's Board paid lip service to concern about the diminution in shareholder value resulting from conversions and sales of BIEL's notes to the public markets,[96] they justified this *immediate* harm to BIEL's shareholders by suggesting that "all ships would rise, as the saying goes, with the success of the firm" and FDA approval.[97] Thus, BIEL concluded "as a business decision," that "it was [BIEL's] best

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[92] Tr. 497:4-498:3 (K. Whelan: "I didn't see any reason for me to have a concern about that.").

[93] Tr. 490:11-14 (K. Whelan: "I sold primarily to Redwood Management. They are an accredited investor and this is what they do. They buy debt and they convert it.").

[94] Tr. 1082:6-12 (K. Whelan: "IBEX has nothing to do with that transaction. *Once I've sold the note to Redwood, what Redwood does with that note from that point has nothing to do with IBEX.*") (emphasis added).

[95] Tr. 877:3-12 (A. Whelan: "I'm not distraught by it because it's not unusual in the type of business that we're in, and I believe that the shareholders will get a good return. That when we dilute, we're bringing in additional capital."); *see also* Tr. 1017:22-1018:3, 1024:25-1025:20 (A. Whelan); Tr. 341:17-21 (A. Whelan); *see also* Tr. 1284:11-1287:19 (Staelin).

[96] Tr. 1253:13-1254:9 (Staelin).

[97] Tr. 1284:11-1287:19 (Staelin).

opinion that this was the only option available to [BIEL] for financing, to get the capital to stay alive and meet our obligations to pay off the notes."[98] Although Mr. Whelan expressly admitted that when Redwood converts its notes and sells shares of BIEL into the market, it shifts risk onto the investing public, he expressed no concern for his own responsibility for that shift.[99] Mr. Staelin was similarly nonplussed. Mr. Staelin began his testimony by professing that his "primary role as an independent Board member is to look out for the shareholders and shareholder value,"[100] but during the time that Mr. Staelin has served on BIEL's Board, BIEL's share price has gone from a high of 12 cents per share in 2009,[101] to just eight one-thousandths of a cent today.[102]

BIEL's "only option" to get capital through distributions of shares to the market in unregistered transactions came at the expense of public shareholders, who never received a standard registration disclosure document that disclosed the shares to be sold and the purpose of any distribution, including the use of sales proceeds,[103] much less that BIEL was financing its operations through the distribution of shares to the market via affiliated entities without registration.[104] As Mr. Park testified, those buying shares from the Liquidating Entities "would not have known, because it wasn't disclosed, that those shares that you are actually buying

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[98] Tr. 1287:1-5 (Staelin); Tr. 315:5-7 (A. Whelan) ("I have a long term view of the company. . . . . I don't get excited day to day."); *see also* Tr. 314:3-322:23 (A. Whelan); Emails Among A. Whelan, M. Whelan, and R. Staelin re: Convertible Notes [DX 29].

[99] Tr. 302:6-11 (A. Whelan).

[100] Tr. 1246:19-21 (Staelin).

[101] BIEL Form 10-K for Fiscal Year Ended Dec. 31, 2009 [DX 51] at 16.

[102] Tr. 1031:9-1032:20 (A. Whelan). This Court may take judicial notice of BIEL's stock quote, as reported on BIEL's corporate website (http://www.bielcorp.com/category/news/) and OTC Markets (http://www.otcmarkets.com/stock/BIEL/quote). *See, e.g., Ieradi v. Mylan Lab., Inc.*, 230 F.3d 594, 600 n.3 (3d Cir. 2000) (taking judicial notice of reported stock prices).

[103] Tr. 147:7-148:2 (Park).

[104] Tr. 152:23-25 (Park).

were—part of those proceeds are going right back to the issuer."[105] Thus, Respondents' actions deprived public investors who were purchasing billions of shares of BIEL of the knowledge that "they [we]re helping to support the issuer by the passing of the proceeds right back to BIEL. If they had known that they might not have bought it."[106]

### G. Respondents' Testimony Regarding IBEX's "Holding Periods" and Placement at "Investment Risk" is Not Credible

As discussed below, IBEX cannot show that it is entitled to an exemption to Section 5 or to Rule 144's safe harbor by pointing to holding periods that are applicable only to non-affiliates. *See* Law & Argument §§ I.B.1.d, I.B.2 and note 182, *infra*. But even if holding periods were relevant, Respondents' have not met their burden to establish holding periods by a preponderance of the evidence.

First, Respondents' expert, Mr. Flood testified that he relied on a document provided to him by Kelly Whelan's tax accountant for the dates of certain loans by IBEX, which Mr. Flood then tied to the Revolving Convertible Promissory Note.[107] Mr. Flood had no idea, however, that the Revolving Convertible Promissory Note was not written or executed until the fall 2009, long-after IBEX supposedly made many of its loans to BIEL.[108] Moreover, Mr. Flood did not include all IBEX loans in his analysis, notably omitting a $519,000 note from August 2009 entirely from his holding period calculation.[109] Mr. Flood's testimony is also problematic because Mr. Flood

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[105] Tr. 197:19-24 (Park); *see also* Tr. 152:23-25 (Park: "So in other words, it [BIEL's OTC filings] didn't say that shares were—that loans were being converted and sold and these proceeds going back to BIEL.").

[106] Tr. 161:16-162:6 (Park).

[107] Tr. 1143:18-1144:21 (Flood).

[108] Tr. 1148:5-1149:8 (Flood).

[109] Tr. 1170:23-1172:23 (Flood). Mr. Flood suggested that this is because IBEX has not sold that note, and that his analysis is focused on notes that have been sold or converted into shares and sold, but acknowledged that he did not undertake any independent analysis to determine whether or not that note in

of his close relationship with Andrew Whelan: Mr. Flood is BIEL's outside Chief Financial Officer and has prepared BIEL's last 15 quarterly unaudited financial reports, and his testimony revealed an improperly close relationship with Mr. Whelan.[110]

Second, Kelly Whelan's own testimony regarding holding periods makes clear that there is no reliable documentation of holding periods for loans that preceded the Revolving Convertible Promissory Note in the fall 2009. Rather, these "loans" were a series of checks and payments by IBEX of BIEL's operating expenses between 2003 and 2009, which were only subsequently "memorialized" as convertible loans through the backdated Revolver Note.[111] Since there are *no* promissory notes relating to these payments by IBEX to BIEL before the fall 2009, IBEX and Kelly Whelan cannot prove, by a preponderance of the evidence, that they obtained a "security" at the time they made the original loans.[112]

Finally, the Record does not support a finding that Kelly Whelan purchased BIEL securities with investment intent. The Liquidating Entities that purchased BIEL notes from IBEX converted and sold their shares almost immediately, demonstrating that they had no investment intent.[113] As IBEX received proceeds from the Liquidating Entities, it promptly sent most of them to BIEL. Between January 2013 and November 2014, for example, the Liquidating

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fact had been sold. Nor did Mr. Flood undertake any independent analysis to determine (and there are no contemporaneous documents reflecting) what loan activity the $519,000 note memorialized. *Id.*

[110] Tr. 1140:6-1142:10 (Flood); Tr. 1194:14-1196:1 (Flood). *Cf.* Adopting Release for Rule 102(e), Rel. Nos. 33-7593, 34-40567, 1998 WL 729201, at *8 (Oct. 19, 1998) ("Because of the importance of an accountant's independence to the integrity of the financial reporting system, the Commission has concluded that circumstances that raise questions about an accountant's independence always merit heightened scrutiny.").

[111] *See* Evidence § I.A, *supra.*

[112] 17 C.F.R. § 240.144(d)(3)(ii).

[113] Park Report [DX 137] ¶¶ 43-44. For example, between 2010 and February 2015, the Liquidating Entities resold BIEL shares within 10 calendar days of receipt *91 percent* of the time. And, on average, Redwood resold BIEL shares within three days of receipt. *Id.* ¶ 44.

Entities paid IBEX $2.7 million for 3.3 million shares of BIEL. Of the $2.7 million IBEX received from the Liquidating Entities, it sent $2.5 million to BIEL in the form of new loans for which it received convertible notes.[114] By immediately "reinvesting" in nearly identical amounts, IBEX effectively was at investment risk only for the period of *days* between the date of sale and the replacement of the divested securities.

## II. BIEL IMPROPERLY RECORDED REVENUE ON TWO BILL AND HOLD TRANSACTIONS WITH CLOSELY RELATED PARTIES

In its first and only Form 10-K, filed with the Commission on March 31, 2010, BIEL recorded revenue from two purported "bill and hold" transactions in which the products never left BIEL's warehouse.[115] These transactions, which totaled $366,000, represented 47% of BIEL's revenue in 2009.[116]

### A. The eMarkets Transaction

The first bill and hold transaction that BIEL improperly recorded in its 2009 10-K involved sales to eMarkets Group, LLC ("eMarkets"), a company owned by Andrew Whelan's sister, Mary Whelan, a member of BIEL's Board and its former Vice President of Marketing.[117]

BIEL recorded $216,000 worth of "bill and hold" sales to eMarkets in its 2009 10-K.[118] The purported sales all arose out of, and were governed by, a distribution agreement that

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[114] Park Report [DX 137] ¶ 42.

[115] *See* 2009 10-K [DX 51] at 20-21; Tr. 350-352, 377:18-25, 382:12-20 (A. Whelan: products did not leave BIEL's warehouse).

[116] 2009 10-K [DX 51] at 20-21 [$366,000/(1,145,647 – 366,000)] = 47 percent. If the bill and hold transactions are included in the denominator, they represent 32 percent of revenue as recorded. *See* Report of Albert A. Vondra (Aug. 26, 2016) ¶ 123(1) [DX 135] ("Vondra Report").

[117] *See* 2009 10-K [DX 51] at 21, 36; Joint Stip. [DX 1] ¶¶ 12-15; Tr. 351:25-352:17 (A. Whelan); Tr. 518-520:5-10, 583:10-12 (M. Whelan).

[118] 2009 10-K [DX 51] at 21 ("The specialized veterinary products sold to eMarkets include approximately $216,000 of revenues related to bill and hold transactions and for which the related product is expected to be delivered during the fourth quarter of 2010."); *see* Vondra Report [DX 135] ¶ 84.

eMarkets and BIEL signed on February 9, 2009 (the "eMarkets Agreement").[119] The eMarkets Agreement was modeled after, and "virtually identical" to standard distribution agreements that BIEL entered into with its other distributors.[120]

The eMarkets Agreement granted eMarkets the right to sell a veterinary product line for BIEL.[121] The agreement required that eMarkets make an initial purchase of 1,500 "Covered Products" @ $10.50, for a total of $15,750,[122] and listed certain "target" amounts of BIEL products that eMarkets was to attempt to sell in the following four years.[123] For all Covered Products that eMarkets wanted to purchase, the parties agreed, in paragraph 4.1 of the Agreement, that eMarkets would submit written orders to BIEL, and that only orders accepted and confirmed in writing by BIEL would be deemed valid and binding.[124]

The parties likewise agreed, in paragraph 4.2, that "Orders accepted and confirmed in writing by the Company shall be due and payable by the Distributor on net 30-day terms, FOB factory."[125] These standard provisions in the eMarkets Agreement aligned with BIEL's

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[119] eMarkets Agreement [DX 18]; *see also* Tr. 595:25-596:11, 617:23-11 (M. Whelan: acknowledging $216,000 recorded by BIEL was under eMarkets Agreement and governed by its terms).

[120] *See* Tr. 598:14-599:2 (M. Whelan); Tr. 1319:15-19 (Linsley).

[121] eMarkets Agreement [DX 18] at 1; 2009 10-K [DX 51] at 21.

[122] *See* eMarkets Agreement [DX 18] at 4 (¶ 2.3) & 12 ("Covered Products" list); Tr. 599:3-8 (M. Whelan: discussing initial order and volume targets).

[123] eMarkets Agreement [DX 18] at 4 (¶ 2.3).

[124] eMarkets Agreement [DX 18] ¶ 4.1; *see also* Tr. 367:22-368:10 (A. Whelan); Tr. 599:16-600:9 (M. Whelan) (confirming ¶ 4.1).

[125] eMarkets Agreement [DX 18] ¶ 4.2; *see* Tr. 601:1-13 (M. Whelan: acknowledging FOB payment terms). The term, "FOB factory"—freight on board—means that the items had to ship from BIEL's warehouse. There was no provision in the eMarkets Agreement allowing for indefinite storage or bill and hold treatment by BIEL.

established policies for written purchase orders and shipment of product out of BIEL's premises, before recording sales, even in bill and hold arrangements.[126]

eMarkets made three separate payments, totaling $216,000, pursuant to the terms of the eMarkets Agreement: an initial payment of $15,750 in February 2009;[127] a second payment of $90,000 in "May or June" 2009;[128] and the remaining amount of approximately $111,000 in June 2010, more than six months after BIEL recorded the sales in its financial statements.[129] eMarkets made the third payment not to BIEL, but to Jarenz, LLC, a company owned by Mary Whelan's niece, Kelly Whelan, who purchased BIEL's accounts receivable.[130] Kelly Whelan loaned eMarkets the money to make this third payment, because at the time, Mary Whelan did not want to liquidate her BIEL shares to pay the remaining amount owed.

At the time eMarkets paid BIEL $216,000, the company did not have "anything close" to $216,000 worth of orders from customers. In 2009, eMarkets sold approximately $15,000 worth of BIEL products, *in total*, of which about $10,000 were attributable to the eMarkets Agreement.[131] Mary Whelan asserted that the rest of the $216,000 that BIEL recorded in the 2009 10-K represented "advanced purchases" of discontinued stock that she was hopeful she

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[126] *See e.g.,* BIEL letter to SEC Div. of Corp. Fin. (Nov. 25, 2010) [DX 83] at 83 ("Nov. 25 Corp. Fin. Letter") ("In bill-and-hold transactions, the customer must accept the risks of ownership for goods. The customer must sign a purchase order and have a fixed commitment, enforceable in court, to purchase the goods."). *See also* Memorandum to Workpaper File (Dec. 21, 2009) at 2 [DX 78] ("Delivery has occurred once the items are shipped from the warehouse. The Company has established with each distributor and customer that the products will be shipped as FOB shipping point, which implies that the sale has occurred at the seller's shipping dock.")

[127] Tr. 604:25-6 (M. Whelan) (initial payment of $15,000).

[128] Tr. 624:18-625:4 (M. Whelan) (second payment of $90,000).

[129] *See* DX 22 at 2-3 (eMarkets checks for $108,538 and $2,958 payable to Jarenz, LLC).

[130] *See* Tr. 614:15-616:9 (M. Whelan) (describing loan from Kelly Whelan).

[131] Tr. 584:1-15, 585:17-589:24 (M. Whelan) (describing that eMarkets had about 89 total orders in 2009 worth approximately $15,000, about 75 percent of which were attributable to the eMarkets Agreement); *see also* Vondra Report [DX 135] ¶ 87 & n.99 (reviewing eMarkets' production, noting approximately 36 eMarkets purchase orders totaling less than $10,000, most in the $10-30 range).

would be able to sell to veterinarians and veterinary hospitals, though at the time, she did not have pending customers or orders.[132]

Other than a few large invoices that BIEL unilaterally issued to eMarkets in 2009 so that it could record the payments in its financial statements, and the $10,000 or so worth of purchase orders that eMarkets issued to BIEL in 2009 (many of which were comingled with unrelated drop-shipment purchases),[133] eMarkets did not issue written orders to BIEL for the products it allegedly purchased, as required by paragraph 4.1.[134] eMarkets also did not ever request, in writing, that BIEL store the products on its behalf, or that BIEL treat the transactions as bill and hold sales, a concept that was unfamiliar to Mary Whelan at the time.[135] The eMarkets Agreement did not contain a fixed delivery schedule—a necessary omission, given that eMarkets did not have customers or orders for the products at the time.[136]

The record also does not contain any correspondence, memos, shipping logs or manifests, bills of lading, merchandise receipts or receiving documents, insurance policies or riders, or any other contemporaneous documents generated or exchanged in the ordinary course of business

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[132] *See* Tr. 621:8-627:19 (M. Whelan) (describing reasoning for paying up front for discontinued products without having booked orders, and attempts to market and sell products).

[133] *See* Tr. 594:2-25 (M. Whelan) (purchase orders did not distinguish between purchases under eMarkets Agreement and drop shipment orders not covered by agreement).

[134] *See* Tr. 368:22-369:1 (A. Whelan: We didn't have a written purchase order as far as I know."); Tr. 595:8-15, 603:4-6 (M. Whelan: "Q But you didn't submit purchase orders to them? A No, I did not write purchase orders . . ."); Tr. 368:22-369:1 (A. Whelan); Tr. 595:8-15, 603:4-6 (M. Whelan); Vondra Report [DX 135] ¶ 87 & n.99.

[135] *See* Tr. 369:9-19 (A. Whelan: "Q So neither YesDTC nor eMarkets asked BioElectronics to treat these transactions as bill and hold? A No. Why would they?"); Tr. 606:9-13 (M. Whelan: "I don't remember ever committing to writing the request to keep it in the warehouse."); Tr. 606:23-607:1 (M. Whelan: "Q Let me ask you this: Have you heard the term "bill and hold transactions"? A I certainly have now. At the time, I didn't think much about it.")

[136] Tr. 672:11-24 (M. Whelan: "Q You did not have a fixed delivery schedule at the time; is that correct? A No, this was establishing a fixed delivery schedule that I was going to get them sold by then. That was my intent. Q So anticipating is not the same thing as having booked orders, correct? A Right. No. Q And did you—A I did not have booked orders."); *see also* Vondra Report [DX 135] ¶¶ 113-15.

indicating that eMarkets agreed to take delivery, or assume ownership, title, or risk of loss of $216,000 worth of BIEL products by December 31, 2009, or indeed, at any time thereafter. As Mary Whelan admitted:

> Q . . . . [Y]ou didn't issue anything in writing anywhere confirming that you accepted the risk and ownership and title of these products, isn't that correct, by the end of the year?
>
> A I don't remember saying that or being—until the auditors started to ask.[137]

This lack of contemporaneous evidence of transfer of ownership, title, or risk of loss was confirmed by the Division's accounting expert, Mr. Vondra,[138] and by Respondents' accounting expert, Dr. Linsley.[139]

Finally, it is undisputed that BIEL did not ship or deliver products to eMarkets.[140] In BIEL's 10-Q filed on August 16, 2010, the Company stated that "it has not yet delivered 43,005 units, totaling approximately $365,000 bill and hold sales recognized for the year ended December 31, 2009. The units will be shipped during 2010 to help meet the distribution 2010 purchase obligation."[141] This 2010 delivery never happened.[142] As Andrew Whelan admitted, "there was not delivery in the normal sense."[143] In fact, there was not delivery in *any* sense. Other than the few samples and orders that BIEL drop-shipped to eMarkets' customers, the vast

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[137] Tr. 608:24-5 (M. Whelan); *see also* Tr. 674:1-11 (M. Whelan).

[138] Vondra Report [DX 135] ¶¶ 96-102; Supplemental Expert Report of Albert A. Vondra (Sept. 14, 2016) ¶¶ 1, 5 [DX 9] ("Vondra Supp. Report").

[139] Tr. 1327:25-1328:9, 1340:3-10 (Linsley) (confirming he never saw anything indicating that the parties agreed to exchange title, purchase the goods, or assume the risk of loss without delivery).

[140] *See* Vondra Report [DX 135] ¶ 54 & n.50.

[141] BIEL 2010 Q2 Form 10-Q [DX 114C] at 26.

[142] *See* Tr. 351:6-24 (A. Whelan: "No units were shipped in 2010, that's correct.").

[143] Tr. 361:1-2 (A. Whelan).

majority of the products stayed in BIEL's warehouse throughout 2009 and 2010, and even years later.[144]

### B. The YesDTC Transaction

The second of BIEL's two invalid bill and hold transactions was a transaction with YesDTC, a Nevada corporation owned by Mr. Noel, a former business associate of BIEL.[145]

On December 31, 2009, the final day of BIEL's fiscal year, Mr. Noel signed a distribution agreement with BIEL (the "YesDTC Agreement").[146] BIEL did not sign the agreement.[147] The purpose of the agreement was for YesDTC to have the rights to sell BIEL human (not veterinary) products in Japan.[148] The agreement provided that YesDTC was to purchase an initial 15,000 products @ $10.00, for a total of $150,000, and set forth minimum purchase amounts for three subsequent years.[149] On December 31, 2009, BIEL issued an invoice to YesDTC. YesDTC paid BIEL $150,000 for the products—$100,000 when signing, and $50,000 in March 2010.[150] BIEL recorded $150,000 in revenue for the transaction in in the 2009 10-K.[151]

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[144] *See* Tr. 382:12-20 (A. Whelan: "Q You didn't ship $216,000 worth of product to eMarkets, correct? A Correct. Q And that product remained in BioElectronics' warehouse? A Yes."); Tr. 608:9-14 (M. Whelan: "Q You say you considered them delivered to you, but they never physically went to you, they never went to your house. Yeah, but, you know — Q They never left the building, correct? A Right."); *see also* Tr. 1336:2-8 (Linsley) (agreeing there was no physical delivery of goods).

[145] *See* 2009 10-K [DX 51] at 21 ("Revenues from international sales for the year ended December 31, 2009 included $150,000 of sales related to a bill and hold transaction."); *see also* Tr. 378:19-379:2 (A. Whelan) (describing Noel's relationship with BIEL); Joint Stip. [DX 1] ¶¶ 40-41; Nov. 15, 2010 Corp. Fin. Letter [DX 83] at 86 (as of July 2010, Noel owned 28 million shares of BIEL stock).

[146] YesDTC Agreement [DX 67]; *see also* Tr. 371:17-372:4 (A. Whelan); Joint Stip. [DX 1] ¶ 42.

[147] *See* YesDTC Agreement [DX 67] at 9; Tr. 1323:21-1324:1 (Linsley).

[148] YesDTC Agreement [DX 67] at 9; Tr. 1323:21-1324:1 (Linsley).

[149] YesDTC Agreement [DX 67] ¶¶ 5.1-5.2.

[150] Tr. 940:12-19 (A. Whelan).

[151] 2009 10-K [DX 51] at 21.

The YesDTC Agreement contained a material contingency that voided the buyer's commitment and negated delivery and performance obligations.[152] The parties understood, and memorialized in the Agreement, that before YesDTC was able to sell any of BIEL's products in Japan, YesDTC first had to obtain regulatory approval from Japan's food and drug regulator. The YesDTC Agreement stated:

> 1. Acceptance and Approval
>
> ***
>
> The rights granted by company to Distributor are made under the assumption that regulatory clearance to sell the Company's products in Japan can be relatively easily obtained. Should Distributor be unable to gain regulatory clearance within six months of contract execution, ***this agreement is voidable at the option of Distributor.***[153]

Under the Agreement, YesDTC had a right to cancel the Agreement for a period of six months pending Japanese regulatory approval.[154] If YesDTC was unable to obtain regulatory clearance from Japan authorities, then it could void the contract.[155]

In an email dated March 31, 2010—right before Mr. Noel made his second payment of $50,000—Mr. Noel confirmed his understanding that the funds that YesDTC paid to BIEL were refundable if he was unable to receive Japanese regulatory clearance.[156]

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[152] *See* Vondra Report [DX 135] ¶¶ 45, 49; Tr. 742:18-20 (Vondra: "It's a major cancellation contingency that . . . invalidates revenue recognition until the contingency is lifted."); Tr. 749:9-14 (Vondra: "You have a contingency that says that he is not entitled to take and sell those goods until that contingency is relieved.").

[153] YesDTC Agreement [DX 67] at 1 (emphasis added); *see also* Tr. 373:12-374:23 (A. Whelan) (confirming contingency).

[154] Tr. 375:22-376:6 (A. Whelan: "It was voidable.").

[155] Tr. 375:22-376:6 (A. Whelan).

[156] Letter from J. Noel to A. Whelan (Mar. 31, 2010) [DX 112] (Noel: "I want to make sure we do not have any disagreements relative to the refundability of these funds. Please confirm our understanding that this $50K is refundable to YesDTC should Japan approval prove more difficult than we originally envisioned—specifically, should clearance in Japan take more than 4 months.").

Not only did YesDTC have the right to void the agreement if it could not obtain Japanese regulatory approval, but such approval was a *condition for delivery.* Andrew Whelan testified that if YesDTC was unable to obtain regulatory clearance, BIEL *would not deliver* the goods to YesDTC.[157] In fact, it would have been against the law to do so.[158]

The YesDTC Agreement, like the eMarkets Agreement, also contained no fixed delivery schedule. Paragraph 4.7 of the Agreement states that products will be shipped on *"mutual future agreement."* As Mr. Noel explained to BIEL's accounting consultant in March 2010, "We will draw the inve[n]tory *as needed*."[159] Drawing inventory pursuant to a "mutual future agreement" or "as needed" is not a fixed delivery schedule.[160]

Ultimately, YesDTC was unable to obtain regulatory clearance in Japan, and BIEL never delivered the products to YesDTC.[161] They remained in BIEL's warehouse for the entire period of the contract.[162] On November 2, 2010, the parties terminated the YesDTC Agreement. BIEL kept the $150,000 paid by YesDTC, and all of the products that purportedly belonged to YesDTC, claiming that YesDTC had "abandoned" them.[163] There is no evidence of abandonment, however. A buyer cannot abandon items it never owned.

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[157] *See* Letter from BIEL to Corp. Fin. at 15 (Jan. 17, 2011) [DX 14] ("Jan. 17, 2011 Corp. Fin. Letter") ("The units would be shipped to Japan upon receipt of regulatory clearance. Therefore, YesDTC could not take delivery without Japanese approval and could not take delivery."); *see also* Tr. 374:20-23 (A. Whelan).

[158] Tr. 378:13-17 (A. Whelan: "[T]hey would not have a license to accept and distribute.").

[159] *See* Email Exchange between J. Noel and BIEL's accounting consultant, E. Ko (Mar. 18, 2010) at 4 [DX 86].

[160] Tr. 751:12-20 (Vondra: "That's not a fixed delivery schedule, as needed.").

[161] Tr. 377:13-22; Joint Stip. [DX 1] ¶ 43.

[162] Tr. 377:18-22 (A. Whelan).

[163] Jan. 17, 2011 Corp. Fin. Letter [DX 14] at 15; Tr. 744:1-4 (Vondra).

Finally, as with the eMarkets Agreement, the Record contains no documents prepared or exchanged in the ordinary course of business evidencing that YesDTC ever took delivery or possession, or assumed title, ownership, or risk of loss of BIEL products, as of December 31, 2009, or at any time thereafter.[164] In addition, as with eMarkets, there is no evidence in the Record that on or before the end of 2009, YesDTC requested in writing that BIEL store products for it, or that BIEL treat the transaction on a bill and hold basis.[165]

### C. BIEL and Andrew Whelan Made False Statements to BIEL's Auditors in Connection with the Bill and Hold Transactions

In March 2010, in connection with BIEL's audit of its 2009 financial statements, Andrew Whelan, on behalf of BIEL, sent a memorandum to the Company's independent auditors concerning the eMarkets and YesDTC transactions (the "Bill and Hold Memo").[166] In the memo, Mr. Whelan provided an explanation to BIEL's auditors concerning the facts supporting treatment of the eMarkets and YesDTC transactions as bill and hold sales for revenue-recognition purposes. Although an external consultant assisted BIEL in preparing the document, Mr. Whelan acknowledged that the memo was the collective statement of himself and the company.[167]

The Bill and Hold Memo is riddled with misstatements and omissions. Among other errors, the Memo represents that:

- There was persuasive evidence of an arrangement with both buyers, when there was not.

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[164] *See* Tr. 747:22-748:3 (Vondra); Tr. 1327:25-1328:9, 1340:3-9 (Linsley); *see also* Vondra Report [DX 135] ¶¶ 49-51.

[165] *See* BIEL Annual Report and Financial Statement (May 16, 2011) at 27 [DX 13] ("Restatement"); Tr. 744:16-18 (Vondra); Vondra Report [DX 135] ¶¶ 67-69, 72-73.

[166] Memorandum from A. Whelan to Auditor Work Paper re: Bill and Hold [DX 90] ("Bill and Hold Memo"). The memorandum is entitled "BioElectronics, Bill and Hold Memo, Audit of 2009" and is addressed, "From: Andrew Whelan, To: Workpaper."

[167] Tr. 390:9-18 (A. Whelan: "[G]enerally, the content is what we decided.").

- There was a fully executed agreement with YesDTC, when BIEL did not sign the contract.
- There was fixed pricing with YesDTC, though the contingency negated fixed pricing.
- eMarkets and YesDTC had (a) assumed risk of loss; (b) made a fixed commitment to purchase $366,000 worth of product; and (c) requested bill and hold treatment, when neither buyer had done so at the time BIEL recorded the sales.
- There was a fixed delivery schedule with both buyers.[168]

The memo also did not inform BIEL's auditors that BIEL would not deliver products to YesDTC until it obtained Japanese regulatory clearance; that neither buyer had orders from any end-users, rendering any estimate of delivery unreasonable; or that eMarkets did not submit purchase orders to BIEL (or any other form of documentation memorializing its commitment to purchase $216,000 worth of product).[169]

### D. BIEL Admitted That Both Transactions Were Not Valid Bill and Hold Transactions

Months after filing the 2009 10-K, BIEL admitted to the SEC's Division of Corporation Finance that the eMarkets and YesDTC transactions did not represent valid bill and hold arrangements, as the Company had stated in its public filing.[170] In May 2011, the Company posted its restated financial statements, expressly stating that "[t]he Company incorrectly

[168] Bill and Hold Memo [DX 90].

[169] *Id.*

[170] *See* Jan. 14, 2011 Corp. Fin. Letter [DX 14] at 13, 18 ("The Company intends to revise its terminology in the Amended Form 10-K by removing the term "bill-and-hold" since the term was used interchangeable and for convenience. The phrase *is not indicative of the accounting pronouncement definition* and was used to describe the type of agreement but the definition under accounting literature. As such, the management believes all requirements have been met for revenue recognition as a distributor agreement, *but not as "bill-and-hold"* transaction as defined in FASB ASC 605.") (emphasis added).

recognized revenues on transactions previously characterized as 'bill and hold.'"[171] Mr. Whelan likewise admitted this at trial, as did Respondent's expert, Dr. Linsley.[172]

## LAW AND ARGUMENT

The Division proved, by a preponderance of the evidence, that Respondents violated or caused violations of the securities laws at issue in the OIP, as described below.

### I. RESPONDENTS VIOLATED SECTION 5 OF THE SECURITIES ACT

#### A. The Division Proved its *Prima Facie* Section 5 Case Against all Respondents

Section 5's registration requirements are the cornerstone of the Securities Act. *Van Dyke v. Coburn Enter., Inc.*, 873 F.2d 1094, 1097 (8th Cir. 1989). The purpose of Section 5 is "to protect investors by promoting *full disclosure* of information thought necessary to make informed investment decisions." *Id.* (emphasis added); *SEC v. Ralston Purina Co.*, 346 U.S. 119, 124 (1953); *Geiger v. SEC*, 363 F.3d 481, 484 (D.C. Cir. 2004). To establish a *prima facie* case for a violation of Sections 5(a) and 5(c), the Division must prove that: (1) Respondents offered to sell or sold a security; (2) Respondents used the mails or interstate means to sell or offer to sell the security; and (3) no registration statement was filed, or in effect as to the security. *See SEC v. Continental Tobacco Co.*, 463 F.2d 137, 155-56 (5th Cir. 1972). The Division is not required to prove scienter or intent. *See Softpoint*, 958 F. Supp. at 859-60. The Division has met its *prima facie* burden.

Between 2010 and early 2015, Respondents distributed billions of shares of BIEL stock to the public markets without any registration statement filed, or in effect, as to the securities.[173]

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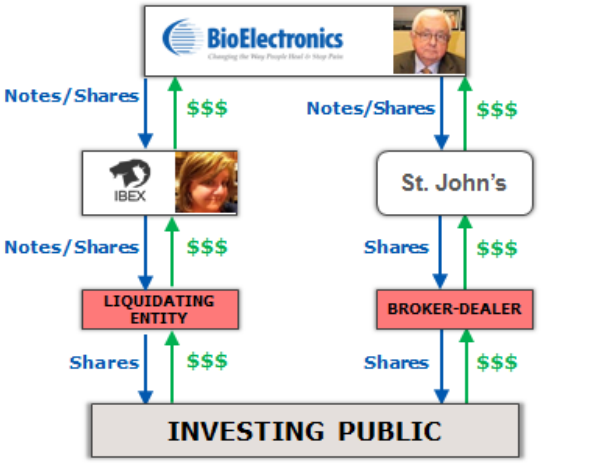
[171] *See* Restatement [DX 13] at 26-27; Tr. 364:14-20 (A. Whelan: "Q And in the May 2011 restatement that we've just been discussing, you restated the YesDTC revenue as other income, not sales revenue, correct? A Yes. Q And that's because no product had been delivered to YesDTC? A Yes."); *see also* Vondra Report [DX 135] ¶ 38, Vondra Supp. Report [DX 9] ¶ 8.

[172] Tr. 363:7-15 (A. Whelan); *see* Tr. 1315:17-16:6 (Linsley) ("Q But you also agree that they were incorrectly recorded as bill and hold transactions. A Yes.").

As illustrated by **Figure 1**, below, BIEL and IBEX engaged in dozens of distributions, whereby BIEL issued convertible notes or shares to IBEX, IBEX sold the convertible notes or shares to third parties, and the third parties then converted the notes into purportedly unrestricted shares of BIEL, and sold those shares to the market.[174] BIEL also issued convertible notes to St. John's, and St. John's converted and sold tens of millions of shares to the public between 2013 and 2014.[175] No registration statements were filed or in effect as to the securities sold by IBEX or St. John's.[176]

**Figure 1: The Distribution Chain**

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[173] *See generally* Park Report [DX 137].

[174] Park Report [DX 137] ¶¶ 19-21; Joint Stip. [DX 1], Exs. A & B.

[175] Joint Stip. [DX 1] ¶¶ 29-36.

[176] Declaration of Thomas B. Rogers [DX 122]; Tr. 432:4-8 (K. Whelan); Tr. 905:8-11, 1029:22-1030:10 (A. Whelan). There is no dispute here that the distributions of BIEL shares used the instrumentalities of interstate commerce. BIEL is a Maryland company, IBEX and St. John's are Virginia companies, and the third-party purchasers, transfer agents, attorneys, and broker-dealers involved in the final sales to investors are scattered nationwide. Joint Stip. [DX 1] ¶ 2 & Ex, B (identifying purchasers of BIEL securities from IBEX); Tr. 502:19-21 (K. Whelan). Respondents frequently used the interstate mails and email to communicate with each other, as well as with transfer agents, broker-dealers, and purchasers of BIEL securities. *See, e.g.*, DX 2; DX 132. Respondents also wired money and sent checks between various bank accounts. *See* RX 1F. These facts are sufficient to meet the Division's burden to prove interstate commerce. *See, e.g.*, *SEC v. Huff*, 758 F. Supp. 2d 1288, 1353 (S.D. Fla. 2010) (public trading, telephone calls, facsimiles, interstate wire transfers, and the negotiation of checks in other states all sufficient evidence of interstate commerce).

Where, as here, a company fails entirely to register its securities and nonetheless proceeds to sell them to the public, the entire system of mandatory public disclosure is evaded to the detriment of public investors. Absent a showing by Respondents—by a preponderance of the evidence—that these distributions of BIEL stock to the public fall within an exemption to Section 5's registration requirement, each Respondent is strictly liable under Section 5.

### B. Respondents Did Not Meet Their Burden of Showing Entitlement to an Exemption Under Section 5

Respondents have failed to prove any entitlement to an exemption to Section 5's registration requirements. *See Ralston Purina*, 346 U.S. at 124-26. Respondents seek to have it both ways—they want to take the investing public's money, while running BIEL like a closely-held family business. But through Section 5, Congress put the burden on companies that deal with the investing public to inform the public truthfully about themselves and the nature of the securities being issued through the filing of a registration statement. *SEC v. Platforms Wireless Int'l Corp.*, 617 F.3d 1072, 1085 (9th Cir. 2010). Respondents have not met this burden.

Respondents urge this Court to ignore the clear evidence that BIEL was financing its operations through sales of unregistered securities through affiliated entities, and instead break up the chain of distribution, looking at *each* sale by *each* Respondent as though it were an independent stand-alone act. This argument elevates form over function in violation of Section 5's mandate.[177] The question for this Court is whether—*in substance*—Respondents engaged in a distribution of securities to the public without a registration or exemption. *Platforms Wireless*,

[177] *SEC v. M&A West Inc.*, 538 F.3d 1043, 1053 (9th Cir. 2008) ("The Supreme Court has long instructed that securities law places emphasis on economic reality and disregards form for substance.") (internal citations omitted).

617 F.3d 1072, 1086; *see also Zacharias v. SEC*, 569 F.3d 458, 463-66 (D.C. Cir. 2009). Respondents did precisely that, and cannot rely on an exemption to Section 5.

Any way you look at the evidence in this case, it is clear that Respondents formed a chain of distribution that emanated with the issuer, BIEL, flowed through IBEX and St. John's, as nominees and surrogates, and ended with the delivery of billions of shares of BIEL stock to the hands of the investing public in unregistered transactions. Placing substance over form, as it must, this Court should find that no exemption is available to any Respondent. First, neither BIEL nor IBEX can establish an exemption under Section 4(a)(1)—BIEL, because it is the issuer, and IBEX, because it (i) sold for the issuer, (ii) is in a control relationship with the issuer, (iii) participated in transactions in which the Liquidating Entities, without investment intent, purchased securities from IBEX and immediately sold them into the market, and (iv) was a necessary and indispensable participant in a public offering, and thus directly participated in an offering. Second, neither BIEL nor IBEX can establish an exemption under Section 4(a)(2), because these were public distributions to the market, not private sales to accredited investors. Third, Rule 144 is unavailable to both IBEX and St. John's, because they are affiliates of BIEL that sold securities without meeting the stringent requirements of Rule 144. The evidence shows that Respondents engaged in a plan or scheme to circumvent registration, and no safety-net is available. Thus, any way you cut it, none of the Respondents meets its burden of showing that its distributions of securities are exempt, and they are liable under Section 5.

### 1. BIEL and IBEX Did Not Meet Their Burden of Showing That They are Entitled to the Section 4(a)(1) Exemption

Section 4(a)(1) provides that the registration requirements of Section 5 do not apply to "transactions by any person *other than* an issuer, underwriter, or dealer." 15 U.S.C. § 77d(a)(1) (emphasis added). This reflects Congress' intent that Section 4(a)(1) "exempt routine trading of

securities already issued," but not exempt distributions by issuers or others, such as underwriters and dealers, "who engage in steps necessary to such distributions." *SEC v. Holschuh*, 694 F.2d 130, 137-38 (7th Cir. 1982). "Thus, even assuming that a particular defendant is not an issuer, underwriter, or dealer, he is not protected by Section 4[(a)](1) if the offer or sale of unregistered securities in question was part of a transaction by someone who was an issuer, underwriter, or dealer." *Id.* at 138.

Here, BIEL as an issuer, by definition, cannot rely on the Section 4(a)(1) exemption. 15 U.S.C. § 77d(a)(1). But it is equally clear on examination of the evidence that IBEX likewise cannot rely on Section 4(a)(1). The question is a substantive and holistic one—was IBEX engaged in routine trading of securities that had come to rest with independent investors, intended by Congress to be exempt under the Securities Act? Or was IBEX "engage[d] in steps necessary to . . . distributions" of BIEL's stock to the market, and therefore *not* exempt? *Ackerberg v. Johnson*, 892 F.2d 1328,1328 (1989). The Division proved at trial that IBEX was a conduit for the distribution of BIEL shares to the market; its sales therefore are not exempt under Section 4(a)(1).

**(a) Section 4(a)(1)'s Governing Legal Principles**

The Section 4(a)(1) exemption is not available if there is a distribution of securities by an underwriter. *SEC v. Chinese Consol. Benevolent Ass'n, Inc.*, 120 F.2d 738, 741 (2d Cir. 1941). The term "underwriter," which was broadly defined in Section 2(a)(11), was the statutory device by which Congress subjected transactions of the issuer and its control persons and intermediaries to registration. 15 U.S.C. § 77b(a)(11). This is because "[t]he congressional intent in defining 'underwriter' [in Section 2(a)(11)] was to cover *all* persons who might operate as conduits for the transfer of securities to the public." *Ackerberg v. Johnson*, 892 F.2d 1328, 1335-36 (1989) (emphasis added) ("underwriter" is the statutory device by which Congress subjected the

transactions of the issuer and its control persons and intermediaries to registration). The definition of underwriter is generally defined in close connection with the definition and meaning of "distribution." *See G. Eugene England Found. v. First Fed. Corp.*, 663 F.2d 988, 989 (10th Cir. 1973). A distribution comprises "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public." *R.A. Holman & Co. Inc. v. SEC*, 366 F.2d 446, 449 (2d Cir. 1966) (quoting *Lewisohn Copper Corp.*, 38 S.E.C. 226, 234 (1958)); *see also SEC v. Kern*, 425 F.3d 143, 153 (2d Cir. 2005) (holding that when a putative affiliate claims a Section 4(1) exemption, the transaction is considered to include "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public").

As defined in Section 2(a)(11), an underwriter includes persons who (1) acquire the securities from the issuer "with a view to" distribution; (2) sell "for an issuer in connection with" a distribution; or (3) "participate[] or [have] a direct or indirect participation in" a distribution. 15 U.S.C. § 77b(a)(11). An underwriter is thus a person or entity that "participate[s], in some manner, in the distribution of the securities to the public." *Ackerberg*, 892 F.2d at 1336 (quoting *Ingenito v. Bermec Corp.*, 441 F. Supp. 525, 535 (S.D.N.Y. 1977)). Most relevant here is Section 2(a)(11)'s explicit clause providing that *for purposes of the underwriter definition*, an "issuer" includes not only the statutory issuer, but also "any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer." 15 U.S.C. § 77b(a)(11). The concepts of underwriter, distribution, and issuer thus all combine to require registration when securities that emanate with the issuer make their way into the public markets through the issuer's control persons or intermediaries and to exempt

from further registration any trading amongst investors once securities come to rest in their hands.

### (b) IBEX Cannot Rely on Section 4(a)(1) Because it Sold For the Issuer

IBEX cannot rely on Section 4(a)(1), first and foremost, because it sold *for the issuer*, BIEL, in a distribution, and was thus acting as an underwriter on that basis. Here, IBEX made dozens of sales of convertible notes to third parties that immediately converted and sold the securities to the market, while simultaneously returning the overwhelming majority of its sales proceeds back to BIEL.

There can be no legitimate debate that IBEX was distributing BIEL shares to the public *for* BIEL. By Kelly Whelan's own admission, she purchased BIEL convertible notes and shares and sold them to third parties, who distributed them to the market.[178] IBEX then returned the vast majority of the proceeds of these resales back to BIEL, the issuer.[179] Indeed, by November 2014, IBEX was responsible for 50 percent of the BIEL shares in the public markets.[180] Further, Ms. Whelan testified that when it became difficult for her to place shares with her own broker-dealer for distribution to the market, she *increased* her sales to Redwood Management, a company that she knew was in the business of buying debt, converting it, and selling to the market.[181] In so doing, Ms. Whelan provided Redwood with access to purportedly unrestricted securities that it otherwise would not have had, making IBEX an indispensable participant in the chain of distribution of BIEL securities to the public. Further, Kelly Whelan's deliberate "work around" to the purported DTC chill shows, contrary to her testimony, that she did not acquire

[178] Tr. 420:14-20, 447:9:23,490:3-492:9, 495:10-496:5 (K. Whelan).

[179] Park Report [DX 137] ¶¶ 19, 27-28, 33, 40, 64-65.

[180] Park Report [DX 137] ¶¶ 19, 42-43.

[181] Tr.491:6-492:9 (K. Whelan).

BIEL securities with investment intent and *never* intended that the BIEL securities "rest" with her.[182] To the contrary, she sought out and secured a means to ensure that she was able to get BIEL securities into the hands of purchasers, even when her own broker-dealers refused to accept BIEL securities for resale into the market.

Thus, IBEX sold for the issuer and is a statutory underwriter as defined in Section 4(a)(1), ineligible for that exemption. 15 U.S.C. § 77b(a)(11). As a statutory underwriter, IBEX may not rely on the Section 4(a)(1) exemption.

**(c) IBEX Cannot Rely on Section 4(a)(1) Because it is an Affiliate of BIEL and Part of the Issuer's Control Group**

Section 4(a)(1)'s exemption is also unavailable to IBEX because IBEX is an affiliate of BIEL, forming part of a single control group under Section 5. Thus, any broker-dealers selling shares acquired from IBEX were "selling for an issuer" (*i.e.*, underwriters) and the Liquidating Entities who immediately resold shares acquired from IBEX were likewise underwriters because they acquired from an issuer with the intent to distribute into the market. *See SEC v. Cavanagh*, 445 F.3d 105, 111 n.12 (2d Cir. 2006) ("'affiliates' are outside the coverage of Section 4[(a)](1)"); *see also, e.g.*, *SEC v. Culpepper*, 270 F.2d 241, 245-46 (2d Cir. 1959). IBEX is also

[182] The failure of BIEL's securities to "come to rest" in IBEX's hands is why Respondents' reliance here on so-called "holding periods" is a red-herring. BIEL's pattern of transactions with IBEX are a chain of distribution, in which the securities do not "come to rest" until they land in the hands of the investing public.

At trial, IBEX failed to meet its burden to establish that it intended to hold onto BIEL's notes until they reached maturity. IBEX has *never* received payment of principal and interest on one of its notes. *See* Tr. 246:13-247:2 (A. Whelan: "As far as I know, we've never liquidated a note."). IBEX's investment levels have remained steady at approximately $5 million, because it has continuously sold BIEL securities, and then effectively replaced the securities sold through new "investments." Park Report [DX 137] ¶ 33 ("BIEL's notes payable inventory remained relatively constant because as convertible debt was sold by IBEX to various Liquidating Entities, new debt was created as IBEX returned the sale proceeds to BIEL."); Tr.153:1-7 (Park).

an "affiliate" as defined in Rule 144 and cannot take advantage of Rule 144's safe harbor, having failed to comply with its terms.[183]

As the Second Circuit held in its first *Cavanagh* decision:

> A control person, such as an officer, director, or controlling shareholder, is an affiliate of an issuer and is ***treated as an issuer*** when there is a distribution of securities. Thus, an affiliate ordinarily may not rely upon the Section 4[a](1) exemption—he must either re-register his shares or qualify for a different exemption before undertaking to sell them.

*SEC v. Cavanagh*, 155 F.3d 129, 134 (2d Cir. 1998) (emphasis added) (internal citations omitted). This makes logical sense: An issuer cannot do through entities under common control what it cannot do itself. *See, e.g.*, *SEC v. Int'l Chem. Dev. Corp.*, 469 F.2d 20, 27-28 (10th Cir. 1972); *see also Platforms Wireless*, 617 F.3d at 1090 ("Strictures placed on transactions involving 'affiliates' prevent those possessing superior access to information and the power to compel registration from abusing their privileged position to foist unregistered securities on an unwitting public.").

Thus, a primary inquiry here, is whether IBEX and Kelly Whelan are controlled or controlling persons, and therefore affiliates, within the meaning of the Act. The evidence that IBEX is part of BIEL's control group is overwhelming:

- IBEX had no independent corporate purpose other than to facilitate the public distribution of BIEL securities;
- Without IBEX's sales into the market and funneling of sale proceeds into new loans, BIEL would have gone bankrupt;

[183] Section 2(a)(11) defines "issuer" for purposes of the underwriter definition as "any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer." Rule 144 captures the same concept in its use of the terms "affiliate," defining an affiliate as "a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such issuer."

- IBEX had the power to force BIEL's Board to take action (*e.g.*, to authorize new shares or register its shares) and to put BIEL into bankruptcy; even if Kelly Whelan did not exercise that power, she had the ability to do so;

- Andrew Whelan had the power to influence Kelly Whelan; Kelly Whelan and IBEX have made loans "pretty much whenever they have been requested," and have never demanded repayment in cash;

- Andrew Whelan was "fair" to Kelly Whelan, and Kelly Whelan was not "greedy" in dealing with BIEL, evidencing the symbiotic control relationship between BIEL and IBEX;

- Respondents did not observe corporate formalities; notes were back-dated, loans were not individually documented, Andrew Whelan did not consistently consult with the Board, and Andrew Whelan had blanket authority to accept loans from IBEX;

- IBEX subordinated its security interest in EXIM for no apparent benefit to IBEX;

- Kelly Whelan maintained a presence at BIEL, had a BIEL email address, and was intimately familiar with BIEL's day-to-day goings on;

- Kelly Whelan attended Board meetings and was on Board communications, including critical communications concerning her own investments; and

- IBEX compensated BIEL consultants and paid off a judgment creditor of BIEL (together with Andrew Whelan and Richard Staelin, both members of the Board).

*See* Evidence § I.B, *supra.* Accordingly, this Court should find that IBEX and BIEL formed a single control group for purposes of Section 4(a)(1)'s analysis.

Respondents will protest, though, that Kelly Whelan was not an officer, director, or controlling shareholder of BIEL, did not make hiring and firing decisions, and did not have authority to enter into agreements on behalf of BIEL, and therefore is not part of the BIEL control group.[184] This argument, once again, elevates form over substance. It is not necessary that one be an officer, director, manager, or even *shareholder*, to be a controlling person. *Pennaluna & Co. v. SEC*, 410 F.2d 861, 866 (9th Cir. 1969). Rather, as the United States Supreme Court held in *Rochester Telephone Corp. v. United States*, 307 U.S. 125 (1939), control

[184] Tr. 1069:12-25 (K. Whelan).

is not to be determined by artificial tests, but is an issue to be determined from the special circumstances of the case. 307 U.S. at 145-46 (1939). "The term 'control' (including the terms 'controlling', 'controlled by' and 'under common control with') means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." *SEC v. Franklin Atlas Corp.*, 154 F. Supp. 395, 400 (S.D.N.Y. 1957) (quoting 17 Code of Fed. Reg. § 230.405(f)).[185]

Kelly Whelan indisputably had the power to direct the management and policies of BIEL. She was BIEL's primary lender, had the power to put the Company out of business, was involved in publicity, marketing, and distribution for BIEL, attended Board meetings and participated in Board communications concerning her investments, and was a valued BIEL employee. *Compare Franklin Atlas*, 154 F. Supp. at 400-01 (holding that although defendant was not a director, officer, or stockholder of the issuer, he was part of the control group because "[h]e was a manager and he did exercise control over the operations, publicity . . . and the issuance of stock . . . .").

Moreover, Respondents have not met their burden of showing that Kelly Whelan and IBEX could not have required BIEL to seek registration—the practical test for control. *See* 1 L. Loss, Securities Regulations 557 (2d ed. 1961) ("In the light of this purpose a practical test for control has been suggested: 'Is a particular person in a position to obtain the required signatures of the issuer and its officers and directors on a registration statement?'"); *see also Pennaluna*,

[185] *Franklin Atlas*, 154 F. Supp. at 400 ("The question of 'control' is a factual question. 'Control' is not synonymous with the ownership of 51 percent of the voting stock of a corporation. Where power exists to direct the management and policies of a corporation, 'control' within the meaning of Section 2(11) exists even though the persons who possess that power do not own a majority of the corporation's voting stock.") (quoting *Thompson Ross Securities Co.*, 6 S.E.C. 1111, 1119).

410 F.2d at 865.[186] As BIEL's primary lender, IBEX could have demanded that BIEL's Board seek registration in order to protect IBEX's collateralized interest in BIEL.[187] At all times, IBEX had the ability to require BIEL's Board to renegotiate the terms of its notes[188] and to force the Board to create new shares of BIEL stock in order to fund IBEX's (and its purchasers') conversions of debt to equity. *See* Evidence § I.B, I.D, *supra*. IBEX also, at times, held a lien on all of BIEL's assets, which it could have leveraged in negotiations to induce BIEL to register.[189] Significantly, another lender, LH Capital, required BIEL to register as a condition of its loan, showing that IBEX could have done the same.[190] Finally, Kelly Whelan assisted in preparation of BIEL's SB-2 filing,[191] further evidencing her close link to the inner workings of BIEL, and her ability to compel registration. *See SEC v. Int'l Chem.*, 469 F.2d at 30 ("[H]is ability to compel registration is demonstrated through his aiding and abetting the others in filing the defective Form 10 statement with the SEC."). The fact that IBEX had the power to require BIEL to register, but did not exercise it, underscores the close control relationship between IBEX and BIEL.

Because IBEX and Kelly Whelan were affiliates of BIEL (standing in the shoes of the issuer), any broker selling securities to the market on behalf of IBEX and Kelly Whelan was an underwriter ("selling for an issuer") and no participant in the chain of distribution may claim the Section 4(a)(1) exemption. As the Second Circuit held in *SEC v. Kern*, 425 F.3d 143 (2d Cir.

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[186] *Pennaluna*, 410 F.2d. at 865 ("[I]t is not unreasonable, in our judgment, to impose upon the seller the burden of establishing his inability to secure the necessary corporate action.").

[187] Tr. 460:18-461:4 (K. Whelan); Tr. 538:23-25, 665:7-20 (M. Whelan); Tr. 1275:24-1277:9, 1279:21-1280:3 (Staelin).

[188] Tr. 478:18-479:2, 507:5-18 (K. Whelan); Tr. 564:8-567:14, 574:16-575:3 (M. Whelan); Emails Among K. Whelan, M. Whelan, and R. Staelin re: Board Resolution (Nov. 20, 2009) [DX 31].

[189] Tr. 1286:16-1287:18 (Staelin).

[190] Tr. 912:12-23 (A. Whelan).

[191] Tr. 443:24-444:6 (K. Whelan).

2005), "if *any* person involved in a transaction is a statutory underwriter, then none of the persons involved may claim exemption under Section 4[(a)](1)." 425 F.3d at 452 (emphasis added).[192] IBEX sold BIEL notes to the Liquidating Entities, and the Liquidating Entities were underwriters that acquired securities from the issuer control group with a view to immediate distribution—No exemption is available.

IBEX likewise cannot rely on Rule 144's safe harbor, because it was an affiliate at the time of the sales, and did not satisfy Rule 144's stringent criteria for sales by affiliates. 17 C.F.R. § 230.144(a)-(h); *Platforms Wireless*, 617 F.3d at 1090. IBEX did not consistently sell through registered broker-dealers, never filed a single Form 144 providing notice of its intent to sell shares of BIEL, and grossly exceeded Rule 144's volume limitations for sales by affiliates of an issuer.[193]

**(d) Section 4(a)(1) is Unavailable to IBEX, Because IBEX Participated in a Public Distribution**

In the alternative, IBEX "consciously engaged in steps necessary to the consummation of the public distribution of shares by the issuer [BIEL] and . . . cannot invoke the exemption provided by Section 4[(a)](1)." *Culpepper*, 270 F.2d at 247. This is because Section 4(a)(1) "does not in terms or by fair implication protect those who are engaged in steps necessary to the distribution of security issues." *Chinese Consol. Benevolent*, 120 F.2d at 741. Respondents do not dispute that IBEX sold to numerous third parties that sold their shares to the public market.[194] Indeed, Kelly Whelan expressly acknowledged that Redwood Management was in the business

[192] *See also United States v. Wolfson*, 405 F.2d 779, 782 (2d Cir. 1968) (holding that where control persons sold securities through brokers, control persons could not claim exemption because brokers were underwriters under Section 2(a)(11)).

[193] Tr. 423:19-424:1, 430:14-25 (K. Whelan); Tr. 1058:22-1059:14 (K. Whelan); Joint Stip. [DX 1], Ex. B; Park Report [DX 137] ¶¶ 19, 28, 52-53.

[194] Respondents' Schedule of Acquisition and Sales [RX 1A]; Joint Stip. [DX 1], Ex. B.

of buying debt, converting it, and selling to the market.[195] Mr. Park's expert report details the sales into the market by the Liquidating Entities that purchased convertible notes from IBEX.[196] The Liquidating Entities are underwriters, and IBEX therefore is not entitled to an exemption under Rule 4(a)(1), because it participated in violations by underwriters. *Pennaluna*, 410 F.2d at 868.

IBEX's participation in the chain of distribution was a vital part of the steps necessary to the distribution of BIEL's shares to the public market. *See SEC v. Int'l Chem.*, 469 F.2d at 28. IBEX therefore cannot rely on Section 4(a)(1) because it was unquestionably "one who 'participate[d] or ha[d] a direct or indirect participation in [the] undertaking." *Culpepper*, 270 F.2d at 246 (quoting Section 4(a)(1)); *see also Chinese Consol. Benevolent Ass'n*, 120 F.2d at 740 (holding that defendant violated Section 5 by soliciting offers to buy securities "for value" and thereby participated in the distribution).

### 2. BIEL and IBEX Did Not Meet Their Burden of Showing That They are Entitled to the Section 4(a)(2) and 4(a)(1½) Exemption

Respondents seemingly argued at the hearing that their sales should be exempt under Section 4(a)(2), because they were private sales to accredited investors, not involving any public offering.[197] This argument fails. Respondents' sales were public distributions, *not* private sales.

#### (a) IBEX Did Not Establish Entitlement to an Exemption for Private Sales

IBEX cannot rely on the Section 4(a)(2) private offering exemption, because that exemption is only available to statutory issuers—*i.e.*, BIEL. 15 U.S.C. § 77d(a)(2). To the extent IBEX is seeking exemption under the so-called Section 4(a)(1½) exemption—a "'hybrid

[195] Tr.491:6-492:9 (K. Whelan).

[196] Park Report [DX 137] ¶¶ 43, 48.

[197] Tr. 420:14-421:12, 494:3-25 (K. Whelan); Tr. 1025:23-1027:1 (A. Whelan) (Witness responded "yes" at same time as objection); Tr. 1030:11-1031:3 (A. Whelan).

exemption' not specifically provided for in the Securities Act" that, in essence, "allows affiliates to make private sales of securities held by them [as] long as some of the established criteria for sales under both Section 4[(a)](1) and Section 4[(a)](2) of the Act are satisfied," *Zacharias*, 569 F.3d at 464—that exemption is not available to IBEX, because its distributions of BIEL securities involved underwriters. *See* Law & Argument § I.B.1.c, *supra*. Where, as here, an affiliate of the issuer uses an underwriter to make a what amounts to a distribution, the Section 4(a)(1½) exemption will not apply. *Zacharias*, 569 F.3d at 464. As the D.C. Circuit Court of Appeals stated in *Zacharias*:

> This is because, although the term 4(1½) exemption adequately expresses the relationship between § 4[(a)](1) and § 4[(a)](2), the actual basis for private resales of restricted securities is § 4[(a)](1). Section 4[(a)](1), in turn, exempts transactions by any person other than an issuer, underwriter, or dealer. Thus, if an underwriter is present, the § 4[(a)](1) exemption, and by extension the 4[(a)](1 ½) exemption, cannot apply.

*Id.* (internal citations and quotation marks omitted) (alterations added); *see also Kern*, 425 F.3d at 152. Here, both the Liquidating Entities that purchased from IBEX and IBEX's broker-dealers were underwriters that sold the securities purchased from IBEX to the public in a distribution. *See* Law & Argument § I.B.1.c, *supra.* Accordingly, IBEX's sales cannot be exempt under Section 4(1½).

**(b) BIEL Did Not Establish an Exemption for Private Sales**

Nor can BIEL rely on Section 4(a)(2)'s private offering exemption. Section 4(a)(2) is construed narrowly in furtherance of the Securities Act's purpose, and the issuer bears the burden of proof. *SEC v. Murphy*, 626 F.2d 633, 641 (9th Cir. 1980) (citing *SEC v. Blazon Corp.*, 609 F.2d 960, 968 (9th Cir. 1979)). BIEL has not met its burden.

BIEL's reliance on Section 4(a)(2) is misplaced for several reasons. First, BIEL participated in a public offering. The transactions at issue involved distributions to the public

market. *Geiger*, 363 F.3d at 487 ("[D]istribution refers to the *entire process* in a public offering through which a block of securities is dispersed and ultimately comes to rest in the hand[s] of the investing public.") (emphasis added); *see also Ackerberg*, 892 F.2d at 1335 (Congress intended "to cover all persons who might operate as conduits for the transfer of securities to the public").

The transactions at issue here are one, continuous, indirect primary public offering. *See* **Figure 1** and argument, p. 35, *supra*. This chain is a distribution that ended with the public, *not* a private offering that ended with IBEX. *See* SEC Release 33-4552 (Nov. 6, 1962) ("[A]n important factor to be considered [under Section 4(a)(2)] is whether the securities offered have come to rest in the hands of the initial informed group or whether the purchasers are merely conduits for a wider distribution."). Securities BIEL issued to St. John's likewise ended up in the hands of the investing public.[198]

Second, the touchstone of any inquiry under Section 4(a)(2) is whether the ultimate purchasers need the protection afforded by registration.[199] Neither BIEL nor IBEX provided *any* evidence that public investors had access to the information that they would have received in a registration statement. *See Sorrell v. SEC*, 679 F.2d 1323, 1326 (9th Cir. 1982) ("The offeree's access to financial information about the investment, similar to what would be found in a registration statement, is crucial."); *M&A West*, 538 F.3d at 1053 (when the investing public has relatively little information about the former private corporation, "the investor protections provided by registration requirements are especially important"). Indeed, neither Andrew nor Kelly Whelan took any steps to determine whether the Liquidating Entities were acquiring BIEL

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[198] Joint Stip. [DX 1] ¶¶ 29-36.

[199] *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 125 (1953) ("[T]he applicability of § 4[(a)](2) should turn on whether the particular class of persons affected needs the protection of the Act. An offering to those who are shown to be able to fend for themselves is a transaction 'not involving any public offering'.").

securities with investment intent or whether they planned to immediately sell into the market. *See* Evidence § I.C-D & I.F, *supra*.

Although BIEL argued that the unaudited financial reports on the OTC Markets website provided substantial information about the Company, these after-the-fact periodic disclosures are no substitute for the information that would have been provided about *each sale* of BIEL's securities in a contemporaneously-filed registration statement. The information required in a registration statement is extensive. *See Murphy*, 626 F.2d at 647. Schedule A of the Securities Act lists 32 categories of information that should be included in a registration statement. *Id.* (citing 15 U.S.C. § 77aa). The information required is designed to protect the investor by furnishing him with detailed knowledge of the company and its affairs to make possible an informed investment decision. *Id.* Included in this information is the use of investor funds, the amount of direct and indirect commissions, and *accurate financial statements. Id.*

BIEL provided almost none of this required information to purchasers of BIEL securities through IBEX. Most glaringly, BIEL did not tell public investors that it was financing BIEL's operations by selling shares of BIEL stock to the public via its affiliates, IBEX and St. John's. Nor did BIEL tell public investors that a significant percentage of the proceeds from sales to the public was being returned to BIEL via IBEX and being used to "keep the lights on." Investors did not know that BIEL's ability to finance its day-to-day operations depended on the funds raised via IBEX's sales to third parties and the third parties' sales to the public. In the absence of any registration statement, investors likely assumed that shares being offered in the market were part of ordinary trading in the secondary market; but, in fact, newly authorized shares were emanating from the issuer, BIEL, to fund its struggling business. *Compare, e.g., id.* ("[T]hus offerees did not know that because of [the issuer's] large short-term debt obligations, the

continued viability of [the issuer] depended upon a consistent influx of new capital. These omissions contrast sharply with the Act's requirements for provision of information."). Section 4(a)(2) is unavailable to BIEL.

### 3. St. John's Did Not Meet its Burden of Showing That it Complied with Rule 144's Requirements for Affiliated Sales and Therefore Is Not Within Rule 144's Safe Harbor

Rule 144 imposes stringent requirements on affiliates of issuers that deal in an issuer's stock, to prevent precisely the type of misconduct we see here. The safe harbor "is precisely limited to its terms." *Kern*, 425 F.3d at 147. As the Ninth Circuit stated in *Platforms Wireless*, "[s]trictures placed on transactions involving 'affiliates' prevent those possessing superior access to information and the power to compel registration from abusing their privileged position to foist unregistered securities on an unwitting public." 617 F.3d at 1090. Here, as in *Platforms*, St. John's relationship with BIEL (and Patricia Whelan's relationship with Andrew Whelan), put St. John's in the position to sell large quantities of unregistered BIEL stock through St. John's. St. John's did so.[200] Because St. John's did not comply with Rule 144's strictures for sales by affiliated entities, its sales of tens of millions of shares of BIEL stock are not within Rule 144's safe harbor.

Among its other requirements,[201] Rule 144 requires that the seller provide concurrent notice to the Commission of each proposed sale by filing a Form 144. 17 C.F.R. § 230.144(h).[202]

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[200] Joint Stip. [DX 1] ¶¶ 29-36.

[201] Rule 144 also requires that: (i) affiliates hold securities for a minimum of one year before they may resell such securities without registration, 17 C.F.R. § 230.144(d); (ii) the issuer be current in its periodic filings with the Commission, *id.* § 230.144(c); (iii) the sales be made through a broker, market maker, or as a riskless transaction, *id.* § 230.144(f); and (iv) affiliates comply with certain volume limitations on the resale of restricted securities, *id.* § 230.144(e)). St. John's did not introduce evidence at trial with regard to these requirements.

[202] Subsection (1) of Rule 144(h) states that, "[i]f the amount of securities to be sold in reliance upon this rule during any period of three months exceeds 5,000 shares or other units or has an aggregate sale price in excess of $50,000, three copies of a notice on Form 144 . . . shall be filed with the Commission. If

There is no dispute that St. John's did not comply with the requirements of Rule 144. *See* Evidence § I.E, *supra*. St. John's made 17 sales to the public of shares of BIEL stock between March 2013 and March 2014, but failed to file any Forms 144 at the time of these sales,[203] as Mr. Whelan admitted.[204] Moreover, even the late-filed Form 144 that St. John's and BIEL submitted in connection with summary disposition omits four of St. John's sales and 20 million shares of BIEL.[205] St. John's has failed to carry its burden to establish its entitlement to the Rule 144 safe harbor.

### C. Respondents BIEL, Andrew Whelan, IBEX, and Kelly Whelan Also Engaged in a Plan or Scheme to Evade the Registration Requirements

Regulation D (Rule 500(f)) and Rule 144 both explicitly state that the exceptions and safe harbors to the registration requirements in those provisions are not available, "to any issuer for any transaction or chain of transactions that, although in technical compliance . . . is part of a plan or scheme to evade the registration provisions of the Act. In such cases, registration under the Act is required." Respondents incorrectly suggest that in order to prevail on its Section 5 claims, the Division must prove a scheme to evade Section 5's registration requirements. This is false. First, the plain language of the above Rules indicates that a "plan"—as opposed to a "scheme"—disqualifies the transactions from the safe harbors. One does not need malicious or deceitful intent to devise a plan. Second, unless Respondents meet *their* burden of showing an exemption to Section 5, the Division is entitled to a finding of liability. Thus, and to be clear, the

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such securities are admitted to trading on any national securities exchange, one copy of such notice also shall be transmitted to the principal exchange on which such securities are admitted," 17 C.F.R. § 230.144(h)(1), while subsection (2) requires that notice be signed and filed concurrently, *id.* § 230.144(h)(2).

[203] Joint Stip. [DX 1] ¶ 35; Declaration of Thomas B. Rogers [DX 122].

[204] Tr. 905:8-11 (A. Whelan).

[205] St. John's Form 144 (May 26, 2016) [RX 176].

Division's showing that all Respondents are liable under Section 5 does *not* require a finding by this Court that Respondents engaged in a plan *or* scheme to evade registration requirements. Nor does it require a finding by this Court of intent or scienter.

That said, if ever a case cried out for a finding that Respondents willfully circumvented Section 5's registration requirements, it is this one. This Court should consider the following facts, among others, in assessing whether or not Respondents engaged in a plan or scheme to evade Section 5's registration requirements, and whether Andrew and Kelly Whelan's Section 5 violations were willful, warranting enhanced civil penalties:

- Respondents' planned and executed their distributions over a period of years in an attempt to disguise the manner in which BIEL was financing its operations;
- Respondents' misconduct involved dozens of transactions, over a period of five years, which caused billions of shares of BIEL to enter the market;
- Respondents have exhibited no remorse whatsoever for their actions or the impact on the investing public, and repeatedly have disavowed any responsibility to the investing public;
- BIEL provided convertible notes in exchange for "investments" by IBEX, rather than standard loan documentation, enabling IBEX to sell BIEL notes and shares to return proceeds to BIEL to fund its operations;
- BIEL's Board of Directors passed a resolution capping IBEX's (but no other investor's) ownership percentage of the Company at 9.9%, to ensure that IBEX would not be deemed an affiliate as a matter of law;
- After being burned by another investor's purported short sales of BIEL stock and the investor's insistence on registration of its shares, BIEL decided to rely on investments by IBEX as a "friendly" investor instead, financing BIEL's operations through non-transparent sales to the public markets;
- Because it was too difficult and financially taxing to meet the SEC's requirements for registration (including the provision of audited financial reports and the 30-plus pieces of information required by registration statements), BIEL used non-transparent distributions to the market through IBEX to generate public capital, without the disclosures required of companies that deal with the investing public;
- When the purported DTC chill caused IBEX's broker-dealers to refuse to accept BIEL shares for distribution to the market, Kelly Whelan and IBEX identified a work-around,

using Redwood's superior access to the public markets to ensure that this source of financing remained available to BIEL; and

- Respondents engaged a distribution over a period of years, resulting in billions of shares reaching the hands of the investing public, all without registration statements. This generated millions of dollars in capital for BIEL.

*See* Evidence § I.A-D & I.F, *supra.*

For all of these reasons, the Record supports a finding that Respondents purposefully planned and orchestrated transactions that had the effect of circumventing the registration requirements. These facts also support a finding by this Court that Andrew and Kelly Whelan's Section 5 violations were willful.

## II. BIEL AND ANDREW WHELAN VIOLATED SECTION 13 OF THE EXCHANGE ACT AND RELATED RULES

The Division has proven that BIEL improperly recorded $366,000 worth of revenue in its 2009 10-K from the eMarkets and YesDTC so-called "bill and hold" transactions. The transactions did not comply with GAAP, as either traditional or bill and hold sales.[206] The Division's accounting expert, Albert Vondra, an experienced public auditor and forensic accountant from PricewaterhouseCoopers, showed that the transactions failed at least three of the four elements of traditional sales, and at least five of the seven elements of bill and hold sales. The Division also proved that the transactions were qualitatively and quantitatively material to reasonable investors. Respondents' sole evidence to the contrary, the testimony of Dr. Linsley defending the transactions and finding them immaterial, is not supported by either the facts or well-established accounting principles, and therefore should be rejected.

By misstating revenue from the eMarkets and YesDTC transactions in its 2009 10-K, BIEL violated the reporting provisions of the Exchange Act, as detailed in Section 13(a) and

[206] Vondra Report [DX 135] ¶¶ 6, 36, 42.

Rule 13a-1, and the books and records and internal controls provisions set forth in Section 13(b)(2)(A) and (B). Andrew Whelan caused BIEL to violate these Section 13 provisions, in violation of Exchange Act Section 21C, and independently violated Rule 13a-14 by issuing a false Sarbanes-Oxley Certification and Rules 13b2-1 and 13b2-2 by making false statements in BIEL's books and records, and to BIEL's auditors.

### A. Requirements For Recording The eMarkets And YesDTC Transactions

For BIEL to record revenue from the eMarkets and YesDTC transactions as revenue in its 2009 10-K, the transactions had to qualify under GAAP as either (1) traditional sales; or (2) bill and hold sales, as set forth in Staff Accounting Bulletin (SAB) 101 and SAB 104 (hereinafter, "SAB 104").[207] There is no other applicable accounting method for these transactions.[208]

#### 1. Requirements of a Traditional Sale

To qualify as a traditional sale, all of the following four criteria must have been met *at the time* that BIEL recorded the sales—on or before December 31, 2009:[209]

1. Persuasive evidence of an arrangement exists;
2. Delivery has occurred or services have been rendered;
3. The seller's price is fixed or determinable, and
4. Collectability is reasonably assured.

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[207] *See* Vondra Report [DX 135] ¶¶ 17-24 (describing applicable GAAP for sales transactions).

[208] *See* Tr. 361:13-18 (A. Whelan: "There's two alternative accounting methods: You can report income as generally recognized income or you can report it as a bill and hold."); Tr. 697:24-698:16 (Vondra: "Now, if there is no delivery, then that automatically kicks over to bill and hold. There is no other accounting model that would account for that."); *see also* Vondra Report [DX 135] ¶¶ 23-24.

[209] *See* SAB 104 at 10-11; *see also* Vondra Report [DX 135] ¶ 23; Tr. 697:25-6 (Vondra); 2009 10-K [DX 51] at 26.

### 2. Requirements of a Bill and Hold Sale

In limited situations when a seller has not delivered its products, it may recognize revenue prior to delivery under a "bill and hold" transaction. Such transactions are unusual and subject to stringent accounting criteria, as they have "long been associated with indicia of fraud."[210] To qualify as bill and hold transactions, *all* of the following seven criteria must have been met, again, *at the time* the transactions were recorded:[211]

> 1. The risks of ownership must have passed to the buyer;
>
> 2. The customer must have made a fixed commitment to purchase the goods, preferably in written documentation;
>
> 3. The buyer, not the seller, must request that the transaction be on a bill and hold basis. The buyer must have a substantial business purpose for ordering the goods on a bill and hold basis;
>
> 4. There must be a fixed schedule for delivery of the goods. The date for delivery must be reasonable and must be consistent with the buyer's business purpose (e.g., storage periods are customary in the industry);
>
> 5. The seller must not have retained any specific performance obligations such that the earning process is not complete;
>
> 6. The ordered goods must have been segregated from the seller's inventory and not be subject to being used to fill other orders, and
>
> 7. The product must be complete and ready for shipment.

## B. The eMarkets and YesDTC Transactions Did Not Comply with GAAP

The evidence conclusively establishes that the eMarkets and YesDTC transactions violated GAAP. As Mr. Vondra testified, the transactions did not comply with at least three of

[210] *See* Vondra Report [DX 135] ¶¶ 24, 27-30.

[211] *See* SAB 104 at 20-21; *see also* Vondra Report [DX 135] ¶ 26; 2009 10-K [DX 51] at 27 (quoting bill and hold criteria).

the four revenue recognition criteria for traditional sales, and at least five of the seven criteria for bill and hold transactions.[212]

### 1. The eMarkets and YesDTC Transactions Are Not Valid Traditional Sales Agreements

The eMarkets and YesDTC transactions failed at least three of the four revenue recognition criteria for traditional sales under GAAP, as set forth in SAB 104. There was no persuasive evidence of a binding arrangement and no delivery for both transactions. The YesDTC transaction did not have fixed pricing, due to the Japanese regulatory contingency. Collectability was not reasonably assured for the eMarkets transaction due to the lack of evidence that the buyer could timely pay the amount owed.

#### (a) There is No Persuasive Evidence of a Binding Sales Arrangement with Either eMarkets or YesDTC

"Persuasive evidence" under GAAP means that the parties exchanged written sales documentation in the ordinary course of business memorializing the terms of their agreement.[213] An "arrangement" means "the final understanding between the parties to the specific nature and terms of the agreed-upon transaction."[214] A seller thus violates this first element of GAAP if it "recognize[s] revenue before binding agreements existed and before contract requirements were complete." *Provenz* v. *Miller*, 102 F.3d 1478, 1485 (9th Cir. 1996). Both the eMarkets and YesDTC Agreements failed this requirement, because the parties did not submit or exchange documentation in the ordinary course of business evidencing binding, enforceable sales arrangements.[215]

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[212] *See* Tr. 737:10-25 (Vondra); *see also* Vondra Report [DX 135] ¶¶ 6, 36, 47, 85, and Table 3.

[213] Vondra Report [DX 135] ¶ 48 (citing SAB 104 at 12).

[214] Vondra Report [DX 135] ¶ 48 (citing SAB 104 at 10 n.3).

[215] Vondra Report [DX 135] ¶¶ 49-51 (YesDTC); *id.* ¶¶ 86-89 (eMarkets).

BIEL's standard policies require written orders and written confirmations prior to recording sales with distributors.[216] Evidence § II.A, *supra*. Here, there is no evidence establishing that eMarkets agreed to buy $216,000 worth of products from BIEL in the ordinary course of business.[217] Rather, both Mary Whelan and Andrew Whelan both admitted that eMarkets did not submit written orders to BIEL covering "anything close" to $216,000 worth of products.[218] And, although the Division issued comprehensive subpoenas to BIEL and eMarkets covering their entire business relationship,[219] neither company produced any form of documentation representing transfer of ownership, title, or risk of loss in the ordinary course of business.[220]

The YesDTC transaction also fails the "persuasive evidence" test, for at least three reasons. First, the YesDTC Agreement was not signed by BIEL.[221] Second, the transaction, like the eMarkets transaction, lacks supporting documentation establishing that YesDTC took title to any BIEL product.[222] Third, and most critically, the transaction was subject to a material contingency that negated the sale.[223] The YesDTC Agreement was voidable by YesDTC if it

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[216] Vondra Report [DX 135] ¶ 51; Vondra Supp. Report [DX 9] ¶¶ 4-5.

[217] *See* Vondra Report [DX 135] ¶ 87; Vondra Supp. Report [DX 9] ¶¶ 1, 4-5; *see also* Tr. 608:24-5 (M. Whelan); Tr. 674:1-11 (M. Whelan); Tr. 1340:3-10, 1327:25-1328:9 (Linsley).

[218] *See* Tr. 368:22-369:1 (A. Whelan: We didn't have a written purchase order as far as I know."); Tr. 595:8-15 (M. Whelan: "I didn't issue purchase orders."); Tr. 603:4-6 (M. Whelan: "Q But you didn't submit purchase orders to them? A No, I did not write purchase orders . . .").

[219] *See* SEC Investigative Subpoenas [DX 131] at 66, 85; *see also* Tr. 516:20-517:20 (M. Whelan) (discussing eMarkets production pursuant to subpoena).

[220] *See* Tr. 608:24-5 674:1-11 (M. Whelan); Tr. 1327:25-1328:9, 1340:3-10 (Linsley).

[221] YesDTC Agreement [DX 67] at 9; *see* also Vondra Report [DX 135] ¶ 50; Tr. 1323:21-1324:1 (Linsley).

[222] *See* Vondra Report [DX 135] ¶¶ 51, 67-69, 72-73; Tr. 1340:3-9 (Linsley).

[223] *See* YesDTC Agreement [DX 67] at 1; *see* Vondra Report [DX 135] ¶¶ 45, 49; Tr. 742:18-20 (Vondra: "It's a major cancellation contingency that … invalidates revenue recognition until the contingency is lifted."); Tr. 749:9-14 (Vondra: "You have a contingency that says that he is not entitled to take and sell those goods until that contingency is relieved.").

was unable to obtain regulatory clearance from Japanese authorities in six months.[224] BIEL *would not deliver* the products to YesDTC, unless and until YesDTC obtained such regulatory clearance.[225] Mr. Noel himself understood that his funds (at least $50,000 worth) were refundable, "should Japan approval prove more difficult than we originally envisioned."[226]

This unsatisfied material contingency defeats revenue recognition under GAAP.[227] Material contingencies in a sales contract must be satisfied before a company may recognize revenue.[228] *Provenz*, 102 F.3d at 1484; *see also* SAB 104 at 12-13 (if arrangement is subject to subsequent approval or execution of another agreement, revenue recognition is inappropriate until subsequent approval or agreement is complete). BIEL could only have recorded revenue with YesDTC after the buyer obtained regulatory clearance, which it never did.[229]

**(b) BIEL Did Not Deliver Products to eMarkets or YesDTC**

"Delivery" has a precise definition under GAAP:

> Delivery generally is not considered to have occurred unless the customer has taken title and assumed the risks and rewards of ownership of the products specified in the customer's purchase order or sales agreement. Typically this occurs when a product is delivered to the customer's delivery site (if the terms of the sale are "FOB destination") or shipped to the customer (if the terms are "FOB shipping point)."[230]

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[224] *See* Tr. 373:12-374:23, 375:22-376:6 (A. Whelan: "The document speaks for itself. It was voidable."); Jan. 17, 2011 Corp. Fin. Letter [DX 14] at 17 ("The Contract was voidable but not voided by the terms of the agreement.").

[225] *See* Tr. 374:20-23 (A. Whelan); Tr. 1336:9-13 (Linsley); *see also* Jan. 17, 2011 Corp. Fin. Letter [DX 14] at 15 ("The units would be shipped to Japan upon receipt of regulatory clearance. Therefore, YesDTC could not take delivery without Japanese approval and could not take delivery.").

[226] Letter from J. Noel to A. Whelan (Mar. 31, 2010) [DX 112].

[227] Vondra Report [DX 135] ¶¶ 45, 48-49; Vondra Supp. Report [DX 9] ¶ 2.

[228] Vondra Report [DX 135] ¶¶ 45, 48-49; Vondra Rebuttal Report [DX 9] ¶ 2.

[229] Tr. 377:13-25 (A. Whelan); Vondra Report [DX 135] ¶¶ 48-49, 60; Vondra Rebuttal Report ¶ 2.

[230] SAB 104 at 20.

Here, there is no dispute that BIEL did not deliver $366,000 worth of products to YesDTC or eMarkets, by December 31, 2009, or thereafter.[231] Evidence, § II.A (at pp. 27-28, 31), *supra*. As Andrew Whelan admitted, "there was not delivery in the normal sense."[232] Dr. Linsley likewise confirmed there was no delivery and that the items remained in BIEL's warehouse.[233]

**(c) There Was no Fixed Price for the YesDTC Transaction**

The YesDTC transaction also fails the requirement that the price to the buyer be fixed or determinable. GAAP defines a *"fixed fee"* as a "fee required to be paid at a set amount *that is not subject to refund or adjustment."*[234] The contingency in the YesDTC Agreement made the funds paid by YesDTC "subject to refund or adjustment." As Mr. Vondra opined, "the transaction was not recognizable as revenue by BIEL due to the outstanding obligation for the distributor [YesDTC] to obtain regulatory clearance in Japan that was never obtained."[235]

**(d) Collectability Was Not Reasonably Assured from eMarkets**

The eMarkets transaction also fails the collectability requirement. BIEL has not shown that eMarkets had sufficient funds to pay the $216,000 it owed BIEL by the end of 2009, or within thirty days of delivery, per paragraph 4.2 of the eMarkets Agreement.[236] Mary Whelan testified that she sold less than $10,000 worth of BIEL products attributable to the eMarkets

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[231] *See* BIEL 2010 Q2 Form 10-Q [DX 114C] at 26; *see also* Tr. 351:6-24, 377:18-25, 382:12-20 (A. Whelan); Tr. 1336:2-13 (Linsley); *see also* Vondra Report [DX 135] ¶¶ 54-55 (YesDTC); *id.* ¶¶ 90-91 (eMarkets).

[232] Tr. 361:1-2 (A. Whelan).

[233] *See* Tr. 1336:2-13 (Linsley); *see also* Tr. 377:18-25, 382:12-20 (A. Whelan); Tr. 608:9-14 (M. Whelan).

[234] Tr. 1328:13-1329:4 (Linsley) (quoting SAB 104 at 11, n.5) (emphasis added); Vondra Report [DX 135] ¶ 56.

[235] Vondra Report [DX 135] ¶¶ 56-57 (quoting SAB 101 at paragraph 4 (Fixed or Determinable Sales Price)).

[236] *See* eMarkets Agreement [DX 18] ¶ 4.2; *see also* Vondra Report [DX 135] ¶¶ 93-94.

Agreement in 2009.[237] eMarkets thus could not rely on payments from its end-users to pay BIEL. Respondents also did not establish that eMarkets had sufficient assets of its own to pay BIEL in 2009. Respondents did not submit evidence that Mary Whelan or eMarkets had sufficient liquid assets, or the ability to receive alternative funding, prior to June 2010 when Mary Whelan was able to secure a favorable loan from her niece, Kelly Whelan. *See* Evidence § II.A, *supra*.

### 2. The Transactions Are Not Valid Bill and Hold Transactions

Because BIEL did not deliver product to YesDTC or eMarkets, BIEL's only hope to record the transactions in its 2009 10-K was as bill and hold agreements.[238] There was no other available accounting method for the transactions.[239]

As set forth above in Evidence § II.D, however, the Respondents and their expert have conceded that BIEL made a mistake, and that the Company improperly recorded the transactions as bill and hold.[240] The evidence supports and confirms Respondents' admissions. The eMarkets and YesDTC transactions failed at least five of the seven GAAP requirements.[241] There is no contemporaneous evidence that risk of ownership passed to either buyer.[242] There were no fixed commitments from the buyers to purchase even a fraction of the $366,000 that

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[237] Tr. 584:1-15 (M. Whelan); Tr. 588:20-592:24 (M. Whelan: estimating she had approximately $15,000 worth of orders in 2009, 75 percent of which were attributable to the $216,000 recorded by BIEL).

[238] *See* SAB 104 at 20-22; *see also* Vondra Report [DX 135] ¶¶ 23-30.

[239] *See* Tr. 361:13-18 (A. Whelan); Tr. 697:24-698:16 (Vondra).

[240] Even if the characterization of these transactions as bill and hold was "a mistake," as Respondents claim, this is not a valid defense to liability under Section 13, particularly when the transactions constituted such a large portion of BIEL's revenue.

[241] *See* Vondra Report [DX 135] ¶¶ 66-83 (YesDTC); Tr. ¶¶ 96-117 (eMarkets).

[242] *See* Tr. 608:24-5, 674:1-11 (M. Whelan); Tr. 747:22-748:3 (Vondra); Tr. 1340:3-10, 1327:25-1328:9, 1340:3-9 (Linsley); *see also* Vondra Report [DX 135] ¶¶ 49-51, 67-69 (YesDTC); Tr. 96-102 (eMarkets); Vondra Supp. Report [DX 9] ¶¶ 1, 4-5.

BIEL recorded.[243] The YesDTC Agreement included a material contingency that voided the contract.[244] There were no written requests from either buyer asking that BIEL to treat the transactions on a bill and hold basis.[245] The agreements did not have fixed delivery schedules.[246] Finally, the Record contains no contemporaneous evidence that BIEL segregated the eMarkets and YesDTC products in its warehouse from other products.[247] In fact, BIEL's auditors noted to the contrary in their work papers.[248]

### 3. Dr. Linsley's Opinion that the Transactions Complied With GAAP is Not Reliable

Dr. Linsley, though conceding the transactions were not bill and hold sales, opined that they nevertheless were valid traditional sales under GAAP. His opinion is not reliable for a number of reasons:

(1) Dr. Linsley's opinion is unsupported by any industry experience as an auditor or public accountant.[249]

(2) Dr. Linsley only examined a very limited pool of evidence, hand-selected by the Respondents,[250] and took their factual representations at "face value."[251] Accordingly, he did not

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[243] *Id.* *See also* Tr. 368:22-369:1 (A. Whelan); Tr. 595:8-15, 603:4-6 (M. Whelan).

[244] *See* Vondra Report [DX 135] ¶¶ 45, 49, 70 (citing YesDTC Agreement [DX 67] at 1; *see also* Tr. 742:18-20, 749:9-14 (Vondra).

[245] *See* Tr. 369:9-19 (A. Whelan); Tr. 606:9-13, 606:23-607 (M. Whelan); *see also* Vondra Report [DX 135] ¶¶ 71-75 (YesDTC); *id.* ¶¶ 105-12 (eMarkets).

[246] *See* Tr. 672:11-24 (M. Whelan); Vondra Report [DX 135] ¶¶ 76-79 (YesDTC); *id.* ¶¶ 113-15 (eMarkets).

[247] Vondra Report [DX 135] ¶¶ 81-83 (YesDTC); *id.* ¶ 117 (eMarkets).

[248] Vondra Report [DX 135] ¶¶ 81-83 (YesDTC); *id.* ¶ 117 (eMarkets); *see also* BIEL Audit Program for Inventory Observation (Jan. 25, 2010) at 3 [DX 88] ("Inquire of the management . . . whether inventory held by the company for others is segregated . . . . As of 1/25/10, no such transactions identified or disclosed.").

[249] *See* Tr. 1296:1-25, 1345:21-1346:3 (Linsley: no auditing or public accounting experience).

[250] *See* Tr. at 1304:1-18 (Linsley); *see also* Linsley Rep. [RX 203] at 3.

examine or consider the wealth of transcripts, correspondence, and business records that contradicted his factual assumptions and conclusions.

(3) For the *persuasive evidence of an arrangement* element, Dr. Linsley failed to consider BIEL's standard policies for documenting sales transactions, as provided in SAB 104, so he had no baseline on which to assess the adequacy of documentation supporting the transactions.[252] He also failed to identify any contemporaneous documentation evidencing an enforceable agreement;[253] and he did not consider the effects of the contingency in the YesDTC Agreement that negated the buyer's commitment.[254]

(4) For the *delivery* element, Dr. Linsley's opinion that delivery occurred within the four walls of BIEL's warehouse, is belied by the evidence and GAAP.[255] Again, neither buyer submitted contemporaneous documents indicating that they accepted title to BIEL products.[256] And, even if they had, a critical requirement of GAAP's revenue recognition rules is that the products must leave the premises.[257] Dr. Linsley did not support his novel theory of "in-house delivery" with any citation to accounting standards. Dr. Linsley's opinion on this critical element is thus a clear example of expert conjecture and *ipse dixit*—"because he said so"—and should be disregarded by this Court. *See SEC v. Tourre*, 950 F. Supp. 2d 666, 678 (S.D.N.Y. 2013) ("The law is clear that mere *ipse dixit* is not appropriate expert testimony.").

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[251] *See* Tr. at 1311:18-1312:3 (Linsley).

[252] *See* Tr. 1317:10-14, 1318:5-8 (Linsley).

[253] *See* Tr. 1310:15-21, 1327:25-1328:9, 1340:3-10 (Linsley).

[254] *See* Vondra Supp. Report [DX 9] ¶ 5.

[255] *See* Vondra Report [DX 135] ¶¶ 54, 91; Vondra Supp. Report [DX 9] ¶¶ 5-6.

[256] *See* Tr. 608:24-5, 674:1-11 (M. Whelan); Tr. 747:22-748:3 (Vondra); Tr. 1340:3-10, 1327:25-1328:9, 1340:3-9 (Linsley); *see also* Vondra Report [DX 135] ¶¶ 49-51, 67-69 (YesDTC), 96-102 (eMarkets); Vondra Supp. Report [DX 9] ¶¶ 1, 4-5.

[257] *See* Vondra Supp. Report [DX 9] ¶ 6 ("Shipping product from the seller's premises is essential for demonstrating delivery.").

(5) For the *pricing is fixed* element, Dr. Linsley's opinion did not consider the meaning of a "fixed fee" under GAAP, nor how the contingency in the YesDTC Agreement negatively affected the requirement.[258]

(6) For the *collectability* element, Dr. Linsley did not consider whether eMarkets had sufficient assets or funding to pay for the inventory, nor the lack of proof submitted by Respondents for this element.[259]

### C. The Improperly Recognized Revenue from the Bill and Hold Transactions Was Material

Because BIEL misstated the bill and hold transactions in the 2009 10-K, the sole remaining question is whether the misstatements were material. *See Huntington Bancshares,* 2005 WL 1307747, *10 (issuer's obligation to file periodic reports includes the obligation that they be complete and accurate in all material respects). A fact is material if there is a substantial likelihood that a reasonable investor would have viewed it as significantly altering the total mix of information made available. *Mitchell H. Fillet,* Release No. 75054 (May 27, 2015), 2015 WL 3397780, *8 (citing *Basic Inc. v. Levinson,* 485 U.S. 224, 231 (1988)). "[M]ateriality depends on the significance the reasonable investor would place on the withheld or misrepresented information." *S.W. Hatfield,* Release No. 3602, 2014 WL 6850921, *7 (Dec. 5, 2014). Materiality under GAAP is determined under both qualitative and quantitative factors.[260] Here, the Division has established that the eMarkets and YesDTC transactions were both qualitatively and quantitatively material to reasonable investors.

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[258] Tr. 1329:12-1330:4 (Linsley: "I don't know if SAB 104 is using that definition. They are quoting that definition…What I relied on with regards to the fixed fee is that, in all for the documentation that I saw, there was no dispute between any of the parties over the amounts involved.").

[259] Tr. 1334:23-1335:6 (Linsley: "I had no information regarding their ability to pay.").

[260] *See* Vondra Report [DX 135] ¶¶ 119-24 (discussing quantitative and qualitative materiality) (citing SAB No. 99).

First, by restating the revenue from these transactions in May 2011, BIEL acknowledged that they were material.[261] Second, as both Mr. Vondra and the Division's expert statistician and econometrician, Benjamin Sacks, testified, the transactions are clearly quantitatively material: (i) $366,000 was nearly one half of BIEL's annual revenue,[262] 66 percent of its 2009 fourth quarter sales,[263] and 85 percent of its increase in revenue from operations from the prior year;[264] (ii) the eMarkets transaction was 80% of 2009 veterinary revenue;[265] and (iii) the YesDTC transaction was 25% of 2009 international revenue.[266] A typical numerical benchmark for materiality is anything over five percent of revenue. *See Ganino v. Citizens Util. Co.*, 228 F.3d 154, 163 (2d Cir. 2000)) ("The use of a percentage as a numerical threshold, such as 5%, may provide the basis for a preliminary assumption [of materiality].") (citing SAB 99—Materiality, at 3). The eMarkets and YesDTC transactions were nearly ten times this standard benchmark. Third, the transactions are unquestionably *qualitatively* material.[267]

The SEC and courts recognize a presumption of materiality for information concerning the financial condition of a company. *See Albert Glenn Yesner, CPA*, 75 SEC Docket 156, 2001 WL 587989, *24 (May 22, 2001) (*"Yesner")* (citations omitted). Investors are particularly interested in earnings because they are highly relevant to investment decisions. *Id.* (citing *Ganino*, 228 F.3d 154, 164 (2d Cir. 2000)). In addition, the eMarkets and YesDTC transactions concerned segments of BIEL's business that the Company "identified as playing a significant

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[261] *See* Vondra Report [DX 135] ¶ 123(7); Vondra Supp. Report [DX 9] ¶ 8.

[262] *See* 2009 10-K at 20 [DX 51] ($366,000/1,145,647-366,000 = 47 percent).

[263] Vondra Report [DX 135] ¶ 123(2).

[264] *Id.* ($366,000/$429.000) = 85 percent).

[265] *Id.* ($216,000/271,047 = 80 percent).

[266] *Id.* ($150,000/$610,785 = 25 percent).

[267] *See* Vondra Report [DX 135] ¶ 123(4-6).

role in the registration's operations or profitability." SAB 99 at 4. BIEL highlighted these distribution agreements when touting the growth of its "domestic and international distribution channels."[268] Investors also would be concerned that BIEL's improper recording of revenue, at year-end, with closely related parties, when the items never left the company's warehouse, represented management's attempt to "manage" earnings.[269]

Respondents have argued that a holistic reading of the 2009 10-K rendered the misstatements immaterial. This argument is misplaced. None of the Company's statements in the 2009 10-K told investors that it had made a "mistake," or improperly recorded nearly one half of its revenue. In fact, BIEL—to this day—falsely contends that the transactions were correctly recorded.[270] Respondents, through Dr. Linsley, also contend that the misstated earnings were immaterial to investors because the Company was in poor financial shape.[271] This argument defies logic. *See* July 26, 2016 Order denying MSJ at 8-9 ("The fact that BIEL "was a start-up company, had suffered millions of dollars in losses, and was almost entirely dependent on outside funding for its past and immediate future survival" is at best irrelevant, and at worst it makes a $366,000 increase in 2009 revenue more material, not less."). Given BIEL's status as an emerging start-up company, which quite often are burdened with debt and struggling to turn a profit, a reasonable investor absolutely would be very interested in the company's revenue

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[268] *See* 2009 10-K at 17 [DX 51] ("During 2009, our focus was on developing product, obtaining additional domestic and international distribution channels . . ."); *id.* at 19 ("BioElectronics has made steady, significant progress in building an international distribution network . . ."); *id.* at 20 ("International sales increased by approximately $149,000 or 32% in 2009 from 2008 as a result of new distributorship agreements signed in 2009. . . Revenue from international sales for the year ended December 31, 2009 include $150,000 of sales related to a bill and hold transaction . . .Veterinary revenues of $271,047 were recorded in connection with a distribution agreement signed on February 9, 2009 with eMarkets . . . .").

[269] *See* SAB 99 at 5; *see also* Vondra Report [DX 135] ¶ 123(4).

[270] Tr. 363:25-364:5 (A. Whelan).

[271] Expert Report of Colin Linsley [RX 203] at 13-14.

stream and earnings reports. *See Ganino*, 228 F.3d at 164 (earnings reports are among the pieces of data that investors find most relevant to their investment decisions).[272]

### D. BIEL and Andrew Whelan Violated Section 13 of the Exchange Act and Related Rules

For the reasons stated below, because BIEL's recognition of revenue from the two bill and hold transactions in its 2009 10-K was improper, it is liable under Section 13 of the Exchange Act and related rules.

#### 1. BIEL Was Required to Comply with Section 13 of the Exchange Act

As an initial matter, BIEL was required to comply with the books and records requirements of Section 13 and its related rules. BIEL's argument to the contrary misstates the law.

Once BIEL filed a Form 8A-12g registration under the Exchange Act, on February 12, 2006, it had 60 days to withdraw the registration before it became effective. Once effective, the company *from that point forward* had a class of securities registered under Section 12(g) of the Exchange Act. As the Commission staff explained in external guidance to registrants (Compliance and Disclosure Interpretations (CDI)), at Question 116.06:[273]

> A registration statement on Form 10, Form 20-F, or Form 8-A to register a class of equity securities under Section 12(g) becomes automatically effective 60 days after the date of filing . . . . The

[272] Respondents' final attack on materiality, based on the event study prepared by their expert, Robert Hills, is likewise unavailing. First, as a matter of law "[t]he SEC does not have to show a stock drop to plead or prove materiality." *SEC v. Mudd*, 885 F.Supp.2d 654, 667 (S.D.N.Y. 2012). Second, even if this Court were to give evidentiary weight to the event study, the Hills study is not the correct tool to attempt to prove lack of materiality, as the Division's expert statistician and econometrician, Benjamin Sacks, showed [DX 8, 136]: (1) there was never a legitimate curative disclosure of the misinformation here, so an event study is not an appropriate vehicle for testing materiality, or lack thereof, of the disclosures; (2) Mr. Hills erroneously assumes that if a stock price movement is *not* statistically significant then an event is *not* material; and (3) when Mr. Sacks adjusted Mr. Hills' methodology to use the appropriate event window and date, he noted a spike in BIEL's stock price of nearly 10%—clearly material.

[273] *Available at* https://www.sec.gov/divisions/corpfin/guidance/exchangeactsections-interps.htm.

> only way to delay or prevent effectiveness is to withdraw the Section 12(g) registration statement before the effective date.

And *from that point forward*, once BIEL had a class of securities registered under Exchange Act, the Company was required to comply with Section 13 and related rules. As the Commission further explained: "Once the Section 12(g) registration statement becomes effective, the company is subject to Exchange Act reporting obligations, including the filing of periodic and current reports." *Id.* BIEL's reporting status existed until the company filed a Form 15 in April 2011, voluntarily deregistering its class of securities.

BIEL has mistakenly conflated the filing of a SB-2 registration statement seeking to register a securities offering under the Securities Act, with the registration of a class of securities under the Exchange Act. They are completely different regulatory provisions and standards. A company can file any number of registration statements under the Securities Act, without having registered a class of securities under the Exchange Act. Once an issuer has registered a class of securities under Exchange Act Section 12(g) (whether by filing a Form 8-A, Form 10, or Form 20-F), and once that registration statement becomes effective, the registration bell cannot be unrung, except by filing a Form 15 under the Exchange Act, which BIEL did not accomplish until April 2011.[274]

BIEL thus was required to comply with the registration, books and records, and internal control provisions mandated by Section 13. Having voluntarily opted to become a reporting company, and having taken full advantage of the benefits of such status—able to raise millions in

[274] Nor is it any surprise to BIEL that withdrawing its SB-2 registration statement did not eliminate its obligations to comply with Section 13. In a December 9, 2010 letter, the Division of Corporation Finance informed BIEL that "Your response to prior comment 15 regarding voluntary filers appears to be irrelevant because you have a class of securities registered under Section 12(g) of the Exchange Act and therefore have reporting obligations under Section 13 of the Exchange Act; therefore we reissue the comment." *See* Letter from Corp. Fin. to BIEL (Dec. 9, 2010) [DX 83] at 65, ¶ 26; *see also* Jan. 11, 2011 Corp. Fin. Letter [DX 14] at 23 (responding to comment).

capital and publicize its prospects and accomplishments to the world through public filings, BIEL may not shirk the serious responsibilities incumbent upon a reporting company, as Section 13 requires.

### 2. BIEL Violated Section 13(a) and Rule 13a-1 of the Exchange Act by Improperly Recording Revenue on the Bill and Hold Transactions

Section 13(a) of the Exchange Act requires issuers registered under Section 12 (like BIEL) to file annual and quarterly reports, and other documents and information as provided in the Exchange Act and related rules. Issuers must file annual reports as required by Exchange Act Rule 13a-1. *Yesner*, 2001 WL 587989 at *30. An issuer violates these provisions if it files a report that contains materially false or misleading information. *SEC v. Yuen*, No. CV 03-437, 2006 WL 1390828, at *41 (C.D. Cal. Mar. 16, 2006); *see also SEC v. Blackburn*, No. 15-2451, 2015 WL 9459976, *10 (E.D. La. Dec. 28, 2015) ("The reporting provisions of the Exchange Act are 'clear and unequivocal,' and satisfied only by the filing of complete, accurate, and timely reports.") (citation omitted).

In particular, Section 13(a) and Rule 13a-1 require the filing of financial statements that are prepared in conformity with GAAP. *Huntington Bancshares, Inc.*, 85 SEC Docket 1433, 2005 WL 1307747, *10 (June 2, 2005); *see also Ponce v. SEC*, 345 F.3d 772, 735 (9th Cir. 2003). Financial reports that are not in accordance with GAAP are presumed to be misleading. *Yesner*, 2001 WL 587989, *31 (citing 17 C.F.R. § 210.4-01(a)(4)). It is misleading to anyone trying to analyze an issuer's financial statements when they are published if those financial statements do not comply with GAAP. *Id.* (citing *In re Baan Securities Litigation*, 103 F. Supp. 2d 1, 14-15 (D.D.C. 2000)).

Scienter is not an element under Section 13 or Rule 13a-1. *See Yesner*, 2001 WL 587989, *30, citing *SEC v. McNulty*, 137 F.3d 732, 740-41 (2d Cir. 1998); *see also Left Behind*

*Games, Inc.*, 107 SEC Docket 2404, 2014 WL 117593, *5 (Jan. 13, 2014); *Huntington Bancshares,* 2005 WL 1307747, *10.

As set forth in Law and Argument § IIB, *supra*, BIEL improperly recorded $366,000 worth of revenue for the bill and hold transactions in violation of GAAP.[275] Because the transactions did not comply with GAAP, and because the transactions were material, it was improper and misleading for BIEL to record them in its financial statements and in the 2009 10-K. *Yesner*, 2001 WL 587989, *3. By doing so, BIEL violated Section 13(a) and Rule 13a-1 as a matter of law.

### 3. BIEL Violated Exchange Act Section 13(b)(2)(A) by Filing False and Misleading Financial Statements

Exchange Act Section 13(b)(2)(A) requires registrants to make and keep books, records and accounts which, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets. Proof of a violation does not require scienter, materiality, or that the transactions are above a specific dollar amount. *Yesner*, 2001 WL 587989, *32.

The evidence establishes that BIEL improperly recorded $366,000 in revenue attributable to the eMarkets and YesDTC transactions its 2009 10-K and accompanying financial statements. The Company thus violated Section 13(b)(2)(A) as a matter of law, as BIEL's financial statements are a critical component of the company's "books, records, and accounts," and required to be included in the company's public filings.

### 4. BIEL Violated Exchange Act Section 13(b)(2)(B) by Failing to Devise and Maintain Adequate Internal Controls

Section 13(b)(2)(B) of the Exchange Act requires all reporting companies to devise and maintain a system of internal controls sufficient to provide reasonable assurances that

[275] *See* 2009 10-K [Ex. 51] at 20-21.

transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP. *Yesner,* 2001 WL 587989, *33.

BIEL admittedly did not implement or maintain adequate internal controls. BIEL stated in its 2009 10-K and 2010 Form 10-Qs that, "our disclosure controls and procedures were not effective due to the existence of several weaknesses in our internal control over financial reporting, as discussed below."[276] The Company then listed several internal control deficiencies, including "lack of review over the financial reporting process that would likely result in a failure to detect errors in [documents] used to compile the financial statements and related disclosures with the SEC."[277]

The Company also did not maintain adequate controls to ensure that it properly documented and recorded its sales transactions, as evidenced by the lack of documentation in BIEL's files concerning the bill and hold transactions. *See SEC v. e-Smart Tech., Inc.*, 82 F. Supp. 3d 97, 109-10 (D.D.C. 2015), *appeal dismissed* (Oct. 27, 2015) ("Examples of internal controls include manual or automated review of records to check for completeness, accuracy and authenticity; a method to record transactions completely and accurately; and reconciliation of accounting entries to detect errors.").

### 5. Andrew Whelan Caused BIEL to Violate Sections 13(a), 13(b), and Rule 13a-1

The Division proved that Andrew Whelan caused BIEL to violate the above-described reporting, books and records, and internal controls provisions, under Section 21C of the Exchange Act. To "cause" a securities law violation, the Division must establish: (1) a primary violation; (2) an act or omission by the respondent that was a cause of the violation; and (3) the

[276] 2009 10-K [DX 51] at 31-33.

[277] *See, e.g.*, BIEL 2010 Q1 10-Q at 26-27 [DX 114A].

respondent knew, or should have known, that his conduct would contribute to the violation. *Navistar Int'l Corp.*, Release No. 3165, 2010 WL 3071892, *13 (Aug. 5, 2010). The Division need not show that Mr. Whelan's conduct was a proximate cause of the primary violations. *Id.* Negligence is sufficient to establish liability for causing a primary violation that does not require scienter, which include the violations at issue in this case. *Id.* (citations omitted).

Here, the Division has established all three elements. BIEL engaged in the primary violations of Sections 13(a), 13(b), and Rule 13a-1. Andrew Whelan's acts and omissions were undeniably a cause of the Company's violations. As BIEL's founder, President, CEO, CFO, and member of the Board, Andrew Whelan was responsible for the Company's operations, sales, financial reporting, and internal controls.[278] His wrongful acts included negotiating and signing the invalid bill and hold transactions; submitting the inaccurate Bill and Hold Memo to BIEL's auditors;[279] and signing the 2009 10-K that contained materially false financial information. Mr. Whelan's omissions included failing to prevent the Company from improperly recording revenue from the bill and hold transactions; failing to hire and train sufficient accounting staff; and failing to appoint a financial expert on the audit committee. *See e-Smart Tech.*, 82 F. Supp. 3d 97, 112 (company CEO and CFO "bore special responsibilities with respect to the company's internal controls").

As for Andrew Whelan's negligence, the evidence shows that he did not act reasonably or prudently under the circumstances. Given Andrew Whelan's in-depth knowledge of, and control over, the Company, and his hands-on involvement negotiating the bill and hold

[278] As Mr. Whelan stated in his Sarbanes-Oxley Certification accompanying the 2009 10-K, "I am the sole officer responsible for establishing and maintaining disclosure controls and procedures and internal controls over financial reporting." Sarbanes-Oxley Certification (Mar. 31, 2010) [DX 113]; *see also* Tr. 387:7-10 (A. Whelan); Tr. 980:8-984:8 (A. Whelan).

[279] *See* Bill and Hold Memo [DX 90] at 2-3.

transactions, his acts and omissions, were, at best, unreasonable and careless. For example, Andrew Whelan knew, or should have known, that: (i) BIEL did not deliver products to either eMarkets or YesDTC;[280] (ii) there was no fixed delivery schedule with either buyer;[281] (iii) the YesDTC Agreement had a contingency requiring Japanese regulatory approval; (iv) BIEL would not deliver the products to YesDTC without such approval;[282] (v) Mr. Noel understood the agreement to mean what it said;[283] (vi) eMarkets and YesDTC did not submit any documents evidencing transfer of title or risk of loss;[284] (vii) the buyers did not have even a fraction of $366,000 worth of orders by the end of the year, and thus could not possibly take delivery in a reasonable amount of time; and (viii) neither buyer requested in writing that BIEL hold or store the goods for them, or treat the transactions on a bill and hold basis.[285] Finally, from a big-picture perspective, Mr. Whelan knew, or should have known, that it was not a proper business purpose for buyers to store products indefinitely in his warehouse, in the vague hopes of one day being able to receive regulatory approval (for YesDTC), and market and sell the products to unknown and unidentified buyers, at some unknown point in the future.[286]

#### 6. Andrew Whelan Violated Exchange Act Rules 13a-14, 13b2-1, and 13b2-2

The OIP also charges Andrew Whelan for his personal misconduct. It alleges that Whelan signed false Sarbanes-Oxley certifications, in violation of Rule 13a-14; made or directed

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[280] *See* Tr. 377:13-25, 351-352 (A. Whelan).

[281] eMarkets Agreement [DX 18]; YesDTC Agreement [DX 67]; *see also* Tr. 672:11-24 (M. Whelan).

[282] Tr. 373:12-374:23 (A. Whelan).

[283] *See* Letter from J. Noel to A. Whelan (Mar. 31, 2010) [DX 112]; Tr. 379:3-17 (A. Whelan).

[284] *See* Tr. 368:22-369:2 (A. Whelan).

[285] *See* Tr. 369:9-19 (A. Whelan).

[286] *See* Vondra Report [DX 135] ¶¶ 108-10 (discussing proper business purposes for bill and hold transactions).

the making of false statements in the company's books and records, in violation of Rule 13b2-1; and made false statements to BIEL's auditors, in violation of Rule 13b2-2.

The Division proved these claims. Andrew Whelan violated Rule 13a-14 by knowingly and/or negligently signing false Sarbanes-Oxley certifications misrepresenting that the company had accurately recorded its revenue in compliance with GAAP, and that the Company had in place adequate internal controls.[287] These representations were false. Mr. Whelan violated Rules 13b2-1 and 13b2-2 by, *inter alia*, knowingly or negligently signing the false Sarbanes-Oxley certification; directing the preparation of inflated revenue statements that accompanied the 2009 10-K; and sending the Bill and Hold Memo to BIEL's auditors that misrepresented and omitted material facts.[288]

Facts establishing the falsity of these representations and omissions, Andrew Whelan's knowledge and/or negligence as to the falsity, and the materiality of the misstatements, are set forth at length above.

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In sum, the Record contains ample evidence that Respondents are liable for all of the charges set forth in the OIP.

## THIS COURT SHOULD IMPOSE REMEDIES IN THE PUBLIC INTEREST

In determining whether sanctions should be imposed in the public interest, this Court may consider the egregiousness of the actions; the isolated or recurrent nature of the infractions; the degree of scienter involved; the sincerity of Respondents' assurances against future violation; Respondents' recognition of the wrongful nature of their conduct; and the likelihood that Respondents' occupation will present opportunities for future violations. *See Steadman v. SEC*,

[287] Sarbanes-Oxley Certification (Mar. 31, 2010) [DX 113].

[288] Bill and Hold Memo [DX 90]; *see also* Evidence § II.C-D, *supra*.

603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981); *Flannery and Hopkins*, AP File No. 3-14081, 2014 SEC LEXIS 4981, *138 (Dec. 15, 2014). The Court also may consider the extent to which a sanction will have a deterrent effect. *See Schield Mgmt. Co.*, AP File No. 3-11762, 58 S.E.C. 1197, 1217 (Jan. 31, 2006); *Flannery*, 2014 SEC LEXIS 4981, at *151.

Respondents' misconduct was egregious, involved willfulness, and occurred for *at least* five years (and very likely both precedes that date and continues to present). Neither Andrew nor Kelly Whelan has offered *any* assurances against future violations or acknowledged the wrongful nature of their conduct. To the contrary, Respondents do not believe that there is anything improper about the way in which BIEL has systematically financed its operations through distributions to the public market in unregistered transactions or BIEL's improper revenue recognition. *See* Evidence § I.F, *supra.* Absent an appropriate sanction, there is no question that Respondents will continue to commit future violations of Sections 5 and 13 in a misguided effort to keep BIEL afloat at the expense of investors.

### A. This Court Should Enter a Cease-and-Desist Order

Section 21C of the Exchange Act authorizes the Commission to issue a cease-and-desist order against any person who "has violated" the statute or rules thereunder. Respondents' violations of Sections 5 and 13 raise a sufficient risk of future violations to support the entry of such an order. In making this determination, the Commission may appropriately issue a cease-and-desist order upon a showing "significantly less than that required for an injunction." *KPMG Peat Marwick LLP*, 54 S.E.C. 1135, 1191 (Jan. 19, 2001). Moreover, "[e]vidence of a past violation ordinarily suffices to establish a risk of future violations" for purposes of a cease-and-desist order. *Flannery and Hopkins*, AP File No. 3-14081, 2014 SEC LEXIS 4981, *138, *145

(Dec. 15, 2014); *see also KPMG*, 54 S.E.C. at 1185 ("[E]vidence showing that a respondent violated the law once probably also shows a risk of repetition that merits our ordering him to cease and desist."). Given Respondents' repeated and flagrant violations of Section 5's registration requirements, the issuance of billions of shares of BIEL stock in unregistered transactions over a five-year period, and Andrew Whelan's insistence—to this day—that the misstatement of revenue in BIEL's 2009 10-K was a mere question of "timing" or nomenclature—this Court should impose cease-and-desist orders for each violation charged in the OIP.

### B. This Court Should Order Disgorgement and Prejudgment Interest

Exchange Act Section 21C also authorizes this Court to order disgorgement, plus reasonable interest. "[D]isgorgement need only be a reasonable approximation of the profits causally connected to the violation," and "the well-established principle is that the burden of uncertainty in calculating ill-gotten gains falls on the wrongdoers who create the uncertainty." *Zacharias*, 569 F.3d at 473.

Here, during the Relevant Period, IBEX realized $2,606,425 in proceeds from sales of BIEL convertible notes, and $1,639,841 in proceeds from sales of BIEL stock to third parties, a total of $4,246,266.[289] Meanwhile, IBEX made loans during this same time period to BIEL of at least $5,438,675.[290] In 2013 and 2014, St. John's sold 81 million shares of BIEL worth $397,196.70 in 17 separate transactions, none of which was noticed by a contemporaneous Form

[289] Joint Stip. [DX 1], Ex. B.

[290] Joint Stip. [DX 1], Ex. A.

144.[291] None of the proceeds of these transactions would have been realized absent Respondents' repeated violations of Section 5.

As a matter of law, the Court should order Respondents to disgorge the full amount of the proceeds they realized from their sales of BIEL shares in unregistered transactions, $4,643,462.70, plus prejudgment interest, to be paid on a joint and several basis. *See Platforms Wireless*, 617 F.3d at 1096-97 (affirming disgorgement under Section 5 of total "proceeds obtained from the illegal sale of . . . unregistered securities," where company was thinly-traded and, like BIEL, "did not have any source of income or assets" besides investor proceeds); *SEC v. StratoComm Corp.*, 89 F. Supp. 2d 357, 367-70 (N.D.N.Y. 2015) (ordering disgorgement of total proceeds obtained from investors for violations of Section 5 and Section 10(b), plus prejudgment interest, to be paid joint and severally).

### C. This Court Should Impose Maximum Civil Penalties

Respondents should also be directed to pay significant civil penalties pursuant to Securities Act § 20 and Exchange Act § 21(d). In considering whether to impose civil penalties, the factors to consider include: (1) whether the violations involved fraud, deceit, manipulation, or reckless disregard of a regulatory requirement; (2) the harm caused to others; (3) the extent to which any person was unjustly enriched; (4) prior violations by Respondents; (5) the need for deterrence; and (6) such other matters as justice may require. 15 U.S.C. §§ 77t(d)(2)(C), 78u(d)(3)(B)(iii); *StratoComm*, 89 F. Supp. 3d at 371; *SEC v. One or More Unknown Traders*, 825 F. Supp. 2d 26, 33-34 (D.D.C. 2010).

Respondents' repeated and multiyear violations of Section 5 qualify for the maximum civil penalties provided by the Securities Act and Exchange Act[292]:

[291] Joint Stip. [DX 1] ¶¶ 34-36; Sales Sheet for St. John's Sales of BIEL [RX 172H]; St. John's Form 144 (May 26, 2016) [RX 176].

- Respondents' misconduct involved the deliberate and egregious disregard of regulatory requirements, BIEL's responsibilities as a public company, and Andrew Whelan's responsibilities as a public company CEO;

- Respondents' violations were made willfully and with reckless disregard to Section 5's registration requirements;

- Respondents' violations created a substantial risk of loss to BIEL and its investors, and, in fact, harmed the investing public by diluting BIEL's share value;

- BIEL failed to tell the investing public that BIEL was financing itself through IBEX's sales of BIEL stock to third parties that immediately liquidated their shares, with proceeds returning to BIEL via IBEX;

- Long after BIEL and IBEX were fully aware that Redwood Management was purchasing convertible notes with the intent to immediately convert them and sell to the market, Respondents continued to sell to Redwood. Indeed, Kelly Whelan sold to Redwood specifically because she knew that Redwood had access to the public markets that she did not during the period of the purported DTC chill;

- There is a high degree of unjust enrichment; Kelly Whelan became wealthy through sales of BIEL stock in 2009;

- Respondents' misconduct spans years, continued throughout the Division's investigation, and likely continues to the present; and

- Respondents' show no remorse for their misconduct or concern for investors.

These facts warrant the imposition of maximum civil penalties against all Respondents. *See, e.g.*, *StratoComm*, 89 F. Supp. 3d at 371-73; *SEC v. Kenton Capital, Ltd.*, 69 F. Supp. 2d 1, 17 (1998).

Maximum civil penalties are also warranted against BIEL and Andrew Whelan for each of the five quarters between the issuance of BIEL's 2009 10-K on March 31, 2010 and BIEL's Restatement on May 16, 2011.[293] Furthermore, because BIEL's unaudited financial reports following the May 16, 2011 Restatement continue to maintain (incorrectly) that revenue could

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[292] Maximum penalties under Securities Act Section 20(d) and Exchange Act Section 21(d)(3) may be for an amount not to exceed either the greater of $650,000 per violation for an entity and $130,000 for an individual. Adjustment of Civil Money Penalties—2005, 17 C.F.R. § 201.1004 (2009) & Table IV.

[293] 2009 10-K [DX 51]; Restatement [DX 13].

properly have been recognized under standard revenue recognition criteria,[294] there is a sound basis for maximum penalties against BIEL and Andrew Whelan for their Section 13 violations through the present.

### D. Andrew Whelan and Kelly Whelan Should Be Subject to Permanent Penny Stock Bars

Under both the Securities Act and the Exchange Act, the Court may impose a penny stock bar on any person who violated the securities laws while participating in an offering of penny stock. *See* 15 U.S.C. §§ 77t(g); 78u(d)(6); *SEC v. Jean-Pierre*, No. 12-cv-8886, 2015 WL 1054905, *12-13 (S.D.N.Y. Mar. 9, 2015). The factors to be considered in imposing a penny stock bar include the: (1) egregiousness of the underlying securities law violations; (2) Respondents' repeat offender status; (3) Respondents' role or position at the time of the misconduct; (4) Respondents' degree of scienter; (5) Respondents' economic stake in the violation; and (6) likelihood that misconduct will recur. *Jean-Pierre*, 2015 WL 10540905, at *12; *see also SEC v. Patel*, 61 F.3d 137, 141 (2d Cir. 1995).

Andrew and Kelly Whelan's misconduct warrants permanent penny stock bars. Their conduct was egregious, recurrent, and not isolated. Both Andrew and Kelly Whelan acted willfully, and they refuse to acknowledge the wrongful nature of their conduct or its impact on investors. BIEL has profited greatly from its Section 5 violations by financing its operations, nearly since inception, through distribution of securities in unregistered transactions. Kelly Whelan has become personally wealthy from the violations. Under the circumstances, absent a permanent bar, it is likely that Andrew and Kelly Whelan will continue to finance BIEL in the future through sales of BIEL securities in unregistered transactions. *Siris v. SEC*, 773 F.3d 89,

[294] *E.g.*, BIEL FY2015 Unaudited Annual Report [RX 171Q] at 001714 ("The Company also believes that it properly accounted for the sales transactions in 2009, which were validated by an independent auditor.").

93-94, 97-98 (D.C. Cir. 2015) (upholding permanent penny stock bar where conduct was repeated, egregious, and involved scienter); *Jean-Pierre*, 2015 WL 10540905, at *13 (similar).

## CONCLUSION

For these reasons, this Court should find all Respondents liable under Section 5 and impose: (i) cease-and-desist orders; (ii) permanent penny stock bars against Andrew and Kelly Whelan; (iii) an order of disgorgement of $4,246,266, plus prejudgment interest, to be paid joint and severally by Andrew Whelan, BIEL, Kelly Whelan, and IBEX; (iv) an order of disgorgement of $397,196.70, plus prejudgment interest, to be paid joint and severally by Andrew Whelan, BIEL, and St. John's; and (v) maximum civil monetary penalties. This Court should also find Andrew Whelan and BIEL liable under Section 13 and related rules and regulations and impose: (i) cease-and-desist orders; and (ii) maximum civil monetary penalties.

Dated: October 28, 2016

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## CERTIFICATE OF SERVICE

I hereby certify that true copies of the foregoing were served on the following, this 28th day of October 2016, in the manner indicated below:

**By hand and email:**

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