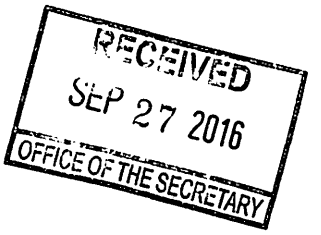
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-17387



In the Matter of

DONALD F. ("JAY") LATHEN, JR., EDEN ARC CAPITAL MANAGEMENT, LLC, and EDEN ARC CAPITAL ADVISORS, LLC

Respondents.

DIVISION OF ENFORCEMENT'S MOTION TO PRECLUDE RESPONDENTS' ADVICE OF COUNSEL DEFENSE AND TO ISSUE SUBPOENAS AND MEMORANDUM OF LAW IN SUPPORT

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September 26, 2016

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The Division of Enforcement ("Division") moves to preclude Respondents from asserting a defense of good-faith reliance on advice of counsel and respectfully requests that the Court issue the attached subpoenas.

INTRODUCTION

This case is about whether Respondents misled bond issuers when they disclosed that Lathen and certain terminally individuals ("Participants") were "owners" of the bonds at issue without also disclosing the relevant side agreements—among Lathen, his hedge fund, and the Participants—that explicitly disclaimed those same ownership rights.

During the September 12, 2016 prehearing conference, Respondents stated that they may interpose a reliance on advice of counsel defense, a defense that they had declined to assert throughout the investigation. (Ex. A (Sept. 12, 2016 Pre-Hearing Conference Tr.) at 18:1-17.) Given that Respondents demanded that the Hearing be held by October 17, the Division expressed its concern that—instead of fully and quickly waiving the privilege and producing the required information (including the names of all consulted attorneys and the relevant communications and documents), as they are required to do as a prerequisite to asserting the defense—Respondents would attempt to game their disclosures to make it difficult (if not impossible) for the Division and the Court to determine the validity of their proposed defense. (Id. at 19:24 - 20:14.) In response, the Court ordered Respondents (if they chose to assert the defense) to make a full and complete disclosure by September 23, 2016. (Id. at 20:15-25 (ordering "disclosure by the 23rd of September").) As feared, however, Respondents have chosen to ignore the foundational requirements for interposing a reliance on advice of counsel defense, and instead have made only selective disclosures, and the disclosures they have made concern irrelevant advice. As such, the Court should preclude Respondents from raising the advice of counsel defense.

BACKGROUND

I. The Prehearing Conference

On September 12, 2016, the Court held a prehearing conference. (Id.) At that conference, Respondents indicated that they may raise an advice of counsel defense. (Id. at 18:1-17.) In response, the Division requested a date certain for them to make that determination and to produce (1) all relevant documents; (2) the names of all attorneys consulted; and (3) a representation that those attorneys had been notified of the privilege waiver and given permission to speak to the Division. (Id. at 19:24 – 20:5.) In addition, the Division expressed its concern that Respondents—in order to gain a tactical advantage—would not make a complete and full disclosure on September 23, 2016, but rather drag out the necessary disclosures. (Id. at 20:6-14 ("My concern is that this is going to end up being a death by 1,000 cuts and we'll get a little information, then there will be a little more, then there will be a little more. And, practically speaking, we won't have time to bottom out the facts prior to the October 17th date . . . .").)[1] The Court granted Respondents' request to make the determination and disclosures by September 23, 2016. (Id. at 20:15-25.) However, the Court also noted that—if there was delay in making the required disclosures—the Court would grant the Division sufficient time to explore the validity of the defense:

> To the extent the Division finds that the disclosure or feels the disclosure is not sufficient then you can make an appropriate filing. And if that means we're going to have to hold the hearing a little bit longer than expected then that's what will happen.

(Id. at 20:20-24.)

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[1] This concern seemed warranted, given that Respondents counsel candidly acknowledged that, "[o]bviously it serves our interests the later they get it, the better it is for us." (Id. at 19:10-11.)

II. Respondents Announce Their Intention to Raise an Advice of Counsel Defense

On September 23, 2016, Respondents notified the Court and the Division that they intended to assert the advice of counsel defense. (Ex. B (Letter from Harlan Protass to the Honorable James E. Grimes, Sept. 23, 2016).) Respondents separately wrote to the Division:

- Stating that they intended to waive only as to "the legal advice they received concerning and relating to the structure of, and structuring of, the Eden Arc Respondents' investment strategy." (Ex. J (Letter from Harlan Protass to Judith Weinstock, Sept. 23, 2016) at 1);
- Indicating that they relied on advice from only four attorneys, Margaret F. Farrell, Esq., Robert G. Flanders, Jr., Esq., Eric Roper, Esq. and Cherryl J. Calaguio, Esq. (Id. at 1-2); and
- Producing only 49 e-mails, but stating that they would produce more documents "during the week of September 26, 2016." (Id. at 2)

III. The September 25, 2016 Meet & Confer

On September 25, 2016, the parties held a telephonic meet and confer concerning the scope of the waiver and the date for full production.[2] (See Ex. K (e-mail from Alexander Janghorbani to Harlan Protass, Sept. 25, 2016 (summarizing telephonic meet and confer).) During that conversation, Respondents' counsel refused to confirm whether they were waiving the privilege as to any legal advice sought or received about:

- whether Respondents needed to disclose the ownership structure for their investments, including the existence and terms of the Participant Agreements and Investment Management Agreement, to issuers and other third parties; or
- their strategy's compliance with the federal securities laws.

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[2] The Division first informed the Respondents on September 24th of the many deficiencies in their purported waiver, asked Respondents to make complete production by the end the day, and asked Respondents to meet and confer immediately. Demonstrating their desire to delay their disclosures, Respondents refused to speak with the Division on September 24th or to answer its questions in writing and have not, to date, provided the Division with the additional required information. (See Exs. C and J (e-mail correspondence between counsel for the Division and Respondents).)

(Id.) Counsel confirmed their position that Respondents were not waiving privilege as to disclosures to the Commission in Respondents' Forms ADV. (Id.) Counsel also told the Division that Respondents were not waiving privilege as to communications with a number of law firms—including Katten Muchin Rosenman LLP and Seward & Kissel LLP—that Mr. Lathen testified that he spoke with concerning his investment strategy. Respondents also stated that they were waiving privilege as to communications with Kevin Galbraith—yet another attorney they consulted—but only as to the structuring of Respondents' business in 2015. (Id.) Importantly, Respondents refused to waive privilege as to communications with Mr. Galbraith as to any advice sought or received from him concerning disclosure issues. Finally, Respondents indicated that they (1) have only searched Lathen's Eden Arc e-mail accounts, but not his personal Yahoo account; (2) had not yet even searched for communications with Mr. Galbraith; and (3) could not give the Division a date certain by which they would complete their production. (Id.)

ARGUMENT

As feared, Respondents have not made (1) a full and timely production of all relevant documents; nor (2) a full and timely disclosure of all of the relevant attorneys Respondents consulted, and waiver of privilege as to each. Perhaps more worrying, Respondents refuse to tell the Division whether they are waiving the privilege as to the central relevant question: did Respondents receive advice from attorneys as to whether Respondents needed to disclose their side agreements to the notes issuers? For these reasons—and as further explained below—Respondents should be precluded from raising an advice of counsel defense at the Hearing.

I. Respondents' Assertion of Advice of Counsel Is Irrelevant and Should Be Precluded

Respondents advised the Division that—rather than waiving the privilege with respect to advice received as to the disclosure issue—they were waiving only as to "the legal advice

[Respondents] received concerning and relating to the structure of, and structuring of, the Eden Arc Respondents' investment strategy." (Ex. J at 1.) However, this case is not about whether Respondents appropriately structured their fund—from a corporate law standpoint—but about whether they disclosed their side agreements and the many caveats on Lathen's and the Participants' purported ownership to the bonds issuers. Respondents have not offered to waive privilege as to advice they received on that topic, the core issue in this case.

The elements of advice of counsel defense are straightforward. Respondents must demonstrate that they (1) made a complete disclosure of the relevant facts to counsel; (2) sought and received advice from counsel that the conduct in question was legal; and (3) relied on that advice in good faith. See Markowski v. SEC, 34 F.3d 99, 104-05 (2d Cir. 1994). The defense cannot be claimed (or shown) unless Respondents waive the privilege so that the contours of the relevant advice sought and given (if any) can be fully explored. See In re Grand Jury Proceedings, 219 F.3d 175, 182 (2d Cir. 2000) ("[A] party cannot partially disclose privileged communications or affirmatively rely on privileged communications to support its . . . defense and then shield the underyling communications from scrutiny by the opposing party."). If the rule were otherwise, a "claim of reliance on counsel would be immune from a showing that, in fact, the defendant had received overwhelming advice to the contrary," SEC v. Forma, 117 F.R.D. 516, 523 n.5 (S.D.N.Y. 1987)[3], or that the lawyer's advice was in fact based on misinformation from the client. Critically, Respondents may not—as they are attempting to do here—unilaterally set the scope of the

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[3] Integral to the inquiry of whether Respondents relied in good faith on the advice that they received is a full disclosure of all attorneys they consulted and the advice that each of them offered. Thus, Respondents claiming the defense must also identify and waive the privilege between themselves and all lawyers they consulted on these questions. In re Gaming Lottery Secs. Litig., No. 96 Civ. 5567(RPP), 2000 WL 340897, at *2 (S.D.N.Y. Mar. 30, 2000). Respondents have not done so. Their list of the four relevant attorneys omits the many other attorneys that Lathen testified he consulted on various topics. (Ex. F, Lathen Tr. at 312-315; 329-30.)

privilege waiver. Glendmede Trust Co. v. Thompson, 56 F.3d 476, 486 (3d Cir. 1995) ("There is an inherent risk in permitting the party asserting a defense of its reliance on advice on counsel to define the parameters of the waiver of the attorney-client privilege as to that advice. That party should not be permitted to define selectively the subject matter of the advice of counsel on which it relied in order to limit the scope of the waiver of the attorney-client privilege and therefore the scope of discovery. To do so would undermine the very purpose behind the exception to the attorney-client privilege at issue here—fairness").

Here, Respondents are engaging in just such an effort to "define the parameters" of their waiver. Id. While the central question here is whether Respondents received advice about their *disclosures* (and their disclosure obligations) to the issuers, they have not waived privilege as to that issue. Instead, they are waiving as to the chimerical issue of how they organized their corporate structure and the *drafting* of the side agreements. Thus, as the Division has been blocked from collecting evidence about the relevant advice, Respondents should not be able to make out the defense.

Indeed, what Respondents appear to be asserting is not a cognizable advice of counsel defense at all, but rather an argument that because there were lawyers involved with some facets of their business organization, Respondents' scienter is somehow diminished as to the disclosure issue (about which they do not even appear to be claiming that they received advice). Courts explicitly bar such a "lawyers in the room" defense. In SEC v. Tourre, for example, the Court barred just such an attempt:

> [T]he fact that a lawyer was present at a meeting suggests that he or she must have implicitly "blessed" the legality of all aspects of a transaction . . . This misunderstanding would give the defendant all of the essential benefits of an advice of counsel defense without having to bear the burden of proving any of the elements of the defense.

950 F. Supp. 2d 666, 683 (S.D.N.Y. 2013). So it is here. Because Respondents are refusing to waive privilege as to any advice they received (or did not receive) as to the relevant disclosure issues, they cannot demonstrate that they sought and received advice from counsel that the conduct in question was legal, nor can the Division explore whether Respondents made a complete disclosure of the relevant facts to counsel or relied on that advice in good faith. Markowski, 34 F.3d at 104-05 (emphasis added). The Court should reject Respondents' attempt to set the parameters of their own waiver and, thus, to hide information relevant to central issue in this case from the Division.

Moreover, given the lateness of the hour, the Division simply does not have time to meet Respondents' claimed defense even if they were to make a full waiver as to the actual relevant issues (which they have not). Thus, the only adequate remedy here is to preclude Respondents from putting on an advice of counsel defense or, at a minimum, to delay the proceedings to allow the Division to collect *all* of the relevant documents (not just those that speak to Respondents' overly-narrow waiver) and speak with *all* of Respondents' attorneys who purportedly gave advice relating to Respondents' scheme (and not just those who purportedly gave advice on the "structuring" of Respondents' "investment strategy").

II. Respondents Have Refused to Produce the Relevant Communications

On September 23, 2016, Respondents (1) produced only 49 e-mails, many of them entirely irrelevant to this case; and (2) identified only four attorneys as to which they were waiving the privilege.[4] (Ex. J.) This disclosure is deficient for a host of reasons.

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[4] Respondents may, in any event, have waived privilege through their repeated failures to correct their claimed inadvertent production of privileged documents to the Commission during the investigation. It is well established that litigants lose privilege protection for any documents "inadvertently" produced where they failed to take "reasonable steps to prevent disclosure" and to "rectify the error" when they learn of it. Fed. R. Evid. 502(b); Clarke v. J.P. Morgan Chase & Co., 08 Civ. 02400 (CM) (DF), 2009 WL 970940, at *5 (S.D.N.Y. Apr. 10, 2009). Respondents

First, by their own admission, Respondents have not complied with the Court's order that they make a full waiver by September 23. Respondents admit that they have not produced all relevant communications, telling the Division only that they intend to "supplement the attached production of attorney-client privileged correspondence and/or documents consistent with the invocation of the advice of counsel defense detailed above during the week of September 26, 2016," but that they could give no date certain by which their production would be completed. (Ex. J.) It is exactly this type of gamesmanship that the Division flagged for the Court at the prehearing conference. Given that there are now three weeks until the Hearing, Respondents' refusal to produce all documents when due plainly prejudices the Division, making it impossible to meet their purported defense.

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have been on notice of serious issues with their production and, to date, have refused to correct them.

On September 13, 2016, the Division notified Respondents that it had discovered what appeared to "a draft Wells submission" in Respondents' production. (See Ex. L (e-mail from Judith Weinstock to Harlan Protass, Sept. 13, 2016).) Respondents did not respond. Again, on September 18, 2016, the Division notified Respondents that it had found "three additional documents" that appeared to be privileged. (Ex. M at 1-2 (e-mail from Judith Weinstock to Harlan Protass, Sept. 18, 2016).) The Division further notified Respondents that "given the length of time that you have had notice that these documents were produced to us and have not requested their return, it appears that you may have intended to waive any privilege attached to these documents." (Id. at 2) Instead of notifying the Division of any additional documents over which they were claiming privilege and inadvertent production, Respondents merely replied that "[w]e . . . are still investigating" and would "endeavor to conclude the matter of the inadvertent production of privileged documents by the close of business on September 19." (Id. at 1) On September 20, Respondents wrote to the Division and, instead of identifying additional privileged documents, asked the Division to undertake, on their behalf, a search of their production to determine if any additional privileged documents were produced. (Ex. N (letter from Harlan Protass to Judith Weinstock, Sept. 20, 2016).) On September 21, the Division wrote to Respondents (1) that the Division was willing to sequester all privileged documents that Respondents identified; (2) that it would be inappropriate for the Division to undertake Respondents' requested search on their behalf; and (3) asking Respondents to identify all purportedly-privileged documents for sequester by Bates number. (Ex. O (e-mail from Nancy Brown to Harlan Protass, Sept. 21, 2016); see also Ex. P (letter from Harlan Protass to Nancy Brown, Sept. 22, 2016).) Respondents have, to date, failed to identify such documents to the Division.

Second, as discussed above, the communications they did produce do not go to the critical issue of whether Respondents obtained advice about disclosing their side agreements to the bond issuers. Indeed, there is evidence to believe that any advice Respondents received on this issue—the critical question—they ignored. For example, Respondents received an opinion from the law firm of Hinckley Allen Snyder LLP on December 20, 2012.[5] (Ex. D.) Most of that opinion is concerned with whether Respondents' business is similar to that of Joseph Caramadre, an individual who was criminally convicted for a fraudulent scheme involving survivor's options. (Ex. D at 2.) However, near the end of the opinion, the attorney advised Lathen that:

> Representations to third parties . . . must not misrepresent the nature of the relationship between Participants and you . . . . Further, such representations should not misrepresent the nature or intent of the Program.

(Ex. D at 6.) However, there is no real dispute that after December 20, 2012, Lathen continued to hide his side agreements as well as the true nature of his investment scheme from the issuers (the parties who most needed to understand it in order to be able to evaluate the legitimacy of his redemptions).

Third, it is readily evident from the documents they have produced, as well as from Lathen's investigative testimony, that Respondents have neither turned over all relevant documents, nor identified all relevant attorneys. Even a quick perusal of Respondents' 52-page privilege log demonstrates that Lathen began receiving advice as early as April 2009 concerning "Survivors Option." (Ex. E at 1 (privilege log).) Moreover, the log identifies communications with a number of attorneys as to whom Lathen does not now purport to waive privilege. (See, e.g., id.) For example, during the investigation, Respondents produced an "Attorney List," identifying more than 40 attorneys (and their agents) that Respondents consulted. (Ex. H.) In testimony,

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[5] Because Respondents provided this opinion to prospective investors, the document is not privileged and was produced to the Commission during the investigation.

Lathen pointed to the law firms of Katten Muchin Rosenman LLP (whom he consulted as early as 2009), as well as Seward & Kissel LLP, as firms with which he consulted. (Ex. F (Lathen Tr. at 311:25-312:19, 329:1-22).) Moreover, Lathen told investors, as early as April 2011, that "[p]rior to launching business, Eden Arc received advice from counsel that the strategy is legal." (Ex. Q at SEC-EDENARC-E-0038739 (excerpt of Eden Arc investor presentation).) He testified that that advice came from Katten Muchin Rosenman LLP. (Ex. F (Lathen Tr. at 196:16-197:10).) Thus, Respondents touted advicethey purported to receive about Respondents' business, but now (inexplicably) claim that advice is irrelevant to their current advice of counsel defense, and have blocked the Division from speaking with the relevant attorneys at Katten Muchin Rosenman LLP.

Tellingly, Lathen also testified that "[t]here were maybe a handful of firms that I pursued conversations to varying degrees around exploring whether or not they could be a candidate to render an opinion" in "early 2014." (Id. at 312:20-313:9.) However, Respondents' recent production of privileged communications is entirely from 2012 and includes nothing from Katten Muchin Rosenman LLP, Seward & Kissel LLP, or Kevin Galbraith, Esq., an attorney whom Lathen hired to press his case with bond issuers who rejected redemptions (while he was continuing to put in misleading redemption requests to other issuers). (See, e.g., Ex. G (Oct. 20, 2014 Letter from Corey Chivers to Kevin Galbraith).)

Finally, a review of even the small amount of communications that Respondents did produce shows communications with at least one other attorney, Stephen Derosa, as to which Respondents have not agreed to waive privilege. During the September 25th meet-and-confer, Respondents' counsel informed the Division that Mr. Derosa worked on preparing Respondents' Forms ADV and that counsel did not think that a relevant area for their waiver. However, Respondents' disclosures to the Commission on their Form ADV—relating to asset ownership and

custody—is exactly the type of issue on which one would expect to see advice requested and provided and as to which Respondents would be likely to waive given the central focus of this case on those issues. .

Respondents' efforts to use the privilege as a sword and shield are foreclosed by the law. Moreover, given that there is only three weeks until the Hearing (a date that Respondents alone chose), the Division simply does not have the time or resources to meet Respondents' unsupported defense. This appears to have been Respondents' plan all along.[6] Such gamesmanship should not be tolerated. Respondents should be precluded from asserting an advice of counsel defense. In the alternative, the Court should move the hearing date back at least one month to allow the Division to collect and review the relevant documents and interview all of the attorneys Lathen consulted.

III. The Court Should Issue the Attached Subpoenas

While the Court considers this motion, the Division also respectfully requests that it issue subpoenas (attached hereto as Ex. R) directed to the attorneys Respondents have identified as subject to their privilege waiver so that the Division can at least begin the process of collecting the new evidence. These subpoenas seek all documents concerning (1) the structure of, and structuring of, Respondents' investments; (2) the disclosure of Respondent's investment strategy to issuers (including disclosure of the relevant side agreements); and (3) billing records concerning work done for Respondents. The requested documents are relevant to the advice of counsel

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[6] Indeed, Respondents have been playing games with whether to assert an advice of counsel defense for at least a year. In 2015, Mr. Lathen testified to a number of communications he had with lawyers. (See, e.g., Ex. F at 311:25-312:19, 329:1-22). However, Respondents repeatedly refused to waive privilege to allow the Commission to investigate the validity of Lathen's claims, and at the same time indicated that they might do so at some future date. (See id. at 109:16-110:18; see also Ex. I (correspondence between the Commission staff and Respondents' attorneys concerning advice of counsel).)

defense. Moreover, it would be highly unfair to require the Division to rely on Respondents' productions in this case, particularly given their facial incompleteness.

CONCLUSION

For the reasons discussed above, the Division respectfully requests that the Court (1) preclude Respondents from asserting a defense of good-faith reliance on advice of counsel; and (2) issue the attached subpoenas while the Court considers the Division's current motion.

Dated: September 26, 2016
New York, New York

DIVISION OF ENFORCEMENT

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Respondents.

Certificate of Service

I hereby certify that I served (1) the Division of Enforcement's Motion to Preclude Respondents' Advice of Counsel Defense and to Issue Subpoenas and Memorandum of Law in Support, dated September 26, 2016; and (2) the Declaration of Alexander Janghorbani, dated September 26, 2016, and all exhibits attached thereto on this 26th day of September, 2016, on the below parties by the means indicated:

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