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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
Files No. 3-17883

In the Matter of **Warren D. Nadel,** **Respondent.**	DIVISION OF ENFORCEMENT'S MOTION FOR SUMMARY DISPOSITION

The Division of Enforcement, relying upon the Memorandum of Law in Support of its Motion for Summary Disposition, and the Declaration of Jorge Tenreiro dated June 16, 2017 and the exhibits annexed thereto, hereby moves for summary disposition against Respondent Warren D. Nadel, pursuant to Rule 250 of the Securities and Exchange Commission's Rules of Practice, for an order permanently barring him from association with a broker, dealer or investment adviser.

Dated: June 16, 2017

Respectfully submitted,

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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
Files No. 3-17883

In the Matter of

Warren D. Nadel,

Respondent.

DECLARATION OF JORGE G. TENREIRO IN SUPPORT OF THE DIVISION OF ENFORCEMENT'S MOTIONS FOR SUMMARY DISPOSITION AGAINST RESPONDENT WARREN D. NADEL

I, Jorge G. Tenreiro, pursuant to 28 U.S.C. § 1746, hereby declare as follows:

1. I am a member of the bar of the State of New York and am employed as Senior Counsel in the Division of Enforcement (the "Division") of the Securities and Exchange Commission (the "Commission"), New York Regional Office. I submit this Declaration in support of the Division's motion for Summary Disposition against Respondent Warren D. Nadel ("Nadel"). I am fully familiar with the facts and circumstances herein.

2. Attached hereto as Exhibit 1 is a true and correct copy of the Amended Complaint filed by the Commission in *SEC v. Nadel, et al.*, No. 11-cv-0215 (E.D.N.Y.) (WFK) (the "Civil Action"), on August 25, 2011.

3. Attached hereto as Exhibit 2 is a true and correct copy of the Decision and Order granting the Commission's motion for partial summary judgment in the Civil Action on March 31, 2015, reported at *SEC v. Nadel*, 97 F. Supp. 3d 117 (E.D.N.Y. 2015).

4. Attached hereto as Exhibit 3 is a true and correct copy of the Report and Recommendation issued by Magistrate Judge Tomlinson in the Civil Action on February 11, 2016, and reported at *SEC v. Nadel*, No. 11-cv-215 (WFK) (AFT), 2016 WL 639063 (E.D.N.Y. Feb. 11, 2016).

5. Attached hereto as Exhibit 4 is a true and correct copy of Judge Kuntz's September 8, 2016 Order adopting Magistrate Judge Tomlinson's Report and Recommendation, and reported at *SEC v. Nadel*, 206 F. Supp. 3d 782 (S.D.N.Y. 2016).

6. Attached hereto as Exhibit 5 is a true and correct copy of the Final Judgment entered in the Civil Action on January 20, 2017 against Respondent Nadel.

7. Attached hereto as Exhibit 6 is a true and correct copy of a letter dated April 15, 2017 sent by Respondent Nadel to the Division.

8. Attached hereto as Exhibit 7 is a true and correct copy of Respondent Nadel's Answer, filed on May 8, 2017.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on June 16, 2017
New York, New York

Jorge G. Tenreiro

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding
File No. 3-17883

In the Matter of	
Warren D. Nadel	
Respondent.	

DIVISION OF ENFORCEMENT'S MEMORANDUM OF LAW IN SUPPORT OF ITS MOTION FOR SUMMARY DISPOSITION AGAINST RESPONDENT WARREN D. NADEL

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June 16, 2017

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PRELIMINARY STATEMENT

Pursuant to Rule 250 of the Securities and Exchange Commission's Rules of Practice, the Division of Enforcement ("Division") respectfully submits this memorandum of law in support of its motion for summary disposition against respondent Warren D. Nadel ("Nadel"), for an Order permanently barring Nadel from association with any broker, dealer or investment adviser.

The Division's motion is based on the permanent injunctions entered against Nadel on January 20, 2017, in *SEC v. Nadel, et al.*, No. 11-cv-215 (E.D.N.Y.) (WFK) (the "Civil Action"), after the Court found Nadel to have willfully violated, and permanently enjoined him from future violations of Section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a) (2009) (the "Securities Act"), Section 10(b) of the Securities Exchange of 1934, 15 U.S.C. § 78j(b) (2009) (the "Exchange Act") and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5, and Sections 206(1), 206(2) and 206(3) of the Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-6(1), 80b-6(2), 80b-6(3) (2009) (the "Advisers Act"), and also found Nadel to have willfully aided and abetted violations, and permanently enjoined him from aiding and abetting future violations, of Section 10(b) of the Exchange Act and Rule 10b-10 thereunder, 17 C.F.R. § 240.10b-10.

STATEMENT OF UNDISPUTED FACTS

I. The Commission's Allegations in the Civil Action

On August 25, 2011, the Commission filed an Amended Complaint in the Civil Action against Nadel, the broker-dealer he owned and controlled, Warren D. Nadel & Co. ("WDNC"), the registered investment adviser firm he also owned and controlled, Registered Investment Advisers, LLC ("RIA"), as well as against Relief Defendant Katherine Nadel. Ex. 1.[1] The Amended Complaint (as had the original Complaint before it) alleged that from the beginning of

[1] "Ex." refers to the exhibits annexed to the accompanying Declaration of Jorge Tenreiro, dated June 16, 2017.

2007 through 2009 (the "Relevant Period"), Nadel fraudulently induced clients of RIA to invest tens of millions of dollars in what Nadel falsely described as a liquid, cash management investment program in which RIA clients would buy and sell preferred utility securities in the open market (using WDNC as the broker-dealer), and hold them for short periods of time in order to generate either dividend income or capital appreciation (the "Strategy"). In exchange, defendants' clients paid millions of dollars in trading commissions and investment management fees. Ex. 1 at ¶¶ 1-3, 14-17. *See also* Order Instituting Proceedings ("OIP") ¶ 3. To further induce investors to join and stay in the Strategy, Nadel also knowingly overstated the amount of RIA's assets under management ("AUM"), falsely claiming that he had more than $400 million when in fact he managed less than a third of that during the Relevant Period. Ex. 1 at ¶ 37.

Contrary to Nadel's representations, however, the vast majority of the transactions in the Strategy consisted of cross-trades that Nadel secretly made between his clients' accounts, at inflated prices he also made up unilaterally. By misleading his clients in this fashion, Nadel knowingly created the false impression that there was a liquid market for these securities and that their market prices were consistent with the inflated values Nadel reported to his RIA clients. *Id.* at ¶¶ 18-36. Nadel received millions of dollars in advisory fees and commissions through this fraudulent conduct – while his clients, the Commission alleged, sustained substantial losses in what Nadel had represented was a liquid, cash management program. *Id.* at ¶ 3.

II. The District Court Concludes That Nadel Defrauded His Clients In Violation of the Securities Laws

On March 31, 2015, Judge William F. Kuntz, II of the United States District Court for the Eastern District of New York, granted the Commission's motion for partial summary judgment on its claims that Nadel (and his two entities, RIA and WDNC), violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, Section 17(a) of the Securities Act, Sections 206(1),

206(2) and 206(3) of the Advisers Act, and aided and abetted WDNC's violations of Section 10(b) of the Exchange Act and Rule 10b-10 thereunder. *See SEC v. Nadel*, 97 F. Supp. 3d 117 (E.D.N.Y. 2015) ("*Nadel I*"). Ex. 2.

The Court concluded that Nadel violated these anti-fraud provisions by knowingly misrepresenting RIA's AUM to clients and prospective clients in marketing materials and thousands of email communications. Nadel, the Court found, claimed to have AUM in excess of $300 or $400 million – overstating his actual AUM by approximately 300% to 400%. *Id.* at 122-26.[2] The Court similarly concluded that Nadel and his companies violated Section 206(3) of the Advisers Act and Rule 10b-10 of the Exchange Act by (a) conducting thousands of cross-trades (the vast majority of all the trades he executed) between his clients, and engaging in principal transactions with client accounts, without providing the required notice and obtaining the required consent for such transactions, and (b) by providing false trade confirmations with respect to those trades. *Id.* at 126-30.

Judge Kuntz directed Magistrate Judge Tomlinson to hold a hearing to determine "the appropriate relief or damages including but not limited to the determination of a permanent injunction, disgorgement, pre-judgment interest, and any civil penalties." *Id.* at 130.

III. Magistrate Judge Tomlinson Recommends Permanent Injunctions, Disgorgement, Prejudgment Interest, and a Civil Money Penalty Against Nadel

After a four-day evidentiary hearing in July 2015, at which Nadel testified extensively, as did five of his former clients, Magistrate Judge Tomlinson issued a Report and Recommendation dated February 11, 2016 (the "Report"), *see SEC v. Nadel*, No. 11-cv-215 (WFK) (AFT), 2016

[2] The Court noted that there was no dispute that Nadel had acted with scienter with respect to his AUM misrepresentations, *id.* at 122, and that "any reasonable investor would consider the accurate amount of assets under management to be a material fact to consider before investing." *Id.* at 123.

WL 639063 (E.D.N.Y. Feb. 11, 2016) ("*Nadel II*"). Ex. 3. The Report, among other things, recommended (1) that the Commission's request for permanent anti-fraud injunctions against Nadel be granted; (2) that Nadel be ordered (jointly and severally with RIA and WDNC) to pay $10,776,687.62 in disgorgement, plus pre-judgment interest; and (3) that Nadel be ordered to pay a civil money penalty in the amount of $1,000,000. *Id.* at *30.

A. Permanent Injunctions

In recommending that an injunction against Nadel be issued, Magistrate Judge Tomlinson, relying on, *inter alia*, *SEC v. Commonwealth Chem. Secs., Inc.*, 574 F.2d 90, 100 (2d Cir. 1978) and *SEC v. First Jersey Secs., Inc.*, 101 F.3d 1450, 1477 (2d Cir. 1996), considered the following factors: (1) whether Nadel had been found liable for illegal conduct; (2) the degree of scienter involved; (3) whether the infraction was an isolated occurrence; (4) whether Nadel continues to maintain that his past conduct was blameless; and (5) whether, because of his professional occupation, Nadel may be in a position where future violations could be anticipated. *Nadel II*, 2016 WL 639063 at *5. Magistrate Judge Tomlinson first noted that it was undisputed that Judge Kuntz had already determined that Nadel had violated the anti-fraud provisions of the securities laws, *id.* at *6, and then made the following findings and conclusions.

1. Degree of Scienter

Magistrate Judge Tomlinson concluded that Nadel had acted with "a high degree of scienter." *Id.* at *6. The Court concluded, first, that "for more than 18 months, Nadel . . . failed to provide accurate trading confirmations" to clients, and did not disclose that WDNC had acted as agent for both sides to the transactions, notwithstanding that being aware the confirmations were inaccurate. *Id.* Second, the Court, citing the testimony of Nadel's clients – and Nadel's continuing invocation of his Fifth Amendment privilege on this subject – observed that "the

magnitude, duration and persistent and ongoing misrepresentation concerning the amount of the [AUM], coupled with the importance placed upon that figure by Defendants' clients, further supports a finding that Defendants acted with a high degree of scienter." *Id.* at *7.

The Court emphasized in particular that Nadel persisted in his knowingly false AUM communications from January 2007 until March 2010, and he even did so for months *after* he learned that the Commission was investigating those very misrepresentations. Indeed, the Court observed, Nadel's false and misleading statements were also made to the Commission during that investigation, specifically when Nadel told the Commission (1) that he did not correspond with existing or prospective clients through email, when in fact he routinely did so; and (2) that "the claim as to [AUM] was noted and deleted" from Nadel's website, a statement that was "at best, disingenuous in as much as Defendants continued to disseminate emails misrepresenting the amount of AUM and sending these emails to prospective clients." *Id.* at *7-8, n.9.

Finally, the Court recognized that the overall scope and duration of Nadel's violations of Section 206(3) and Rule 10b-10 "evidenced a knowing disregard for Defendants' fiduciary obligations to their clients," which "further illustrates Defendants' high degree of scienter." *Id.* at *8. The Court observed that Nadel offered "evasive and conflicting testimony on this point," *id.* at 8, which nonetheless established that he understood he could only execute his Strategy by conducting 90% or more of the trades as cross-trades, and affirmatively chose not to disclose these facts to his clients. *Id.* at *8-9. For all the foregoing reasons, the Court concluded, this factor weighed in favor of granting injunctive relief. *Id.* at *9.

2. Recurring Nature of Conduct

The Court observed that (1) Defendants' unlawful cross-trading ran from at least January 1, 2007 through December 31, 2009; (2) their material misrepresentations concerning AUM ran

from January 1, 2007 through April 2010; and (3) their knowing dissemination of false trade confirmations continued from March 2008 through at least December 2009. As a result, the Court concluded that Nadel's misconduct did not involve a single isolated instance of wrongdoing, and that this factor thus weighed in favor of granting injunctive relief. *Id.*

3. **Lack of Appreciation of Wrongdoing**

The Court found that Defendants displayed "little appreciation of the wrongdoing in which they have been found to have engaged." *Id.* The Court noted that he "showed both indifference and a somewhat cavalier attitude regarding the underlying violations." *Id.* For example, with respect to his violation of Section 206(3), Nadel "appeared dismissive, stating simply that he 'felt comfortable enough with the disclosure documents' and the 'blanket expression' concerning the possibility of cross-trades," and with respect to his knowing violations of Rule 10b-10, "Nadel presented a similar lackluster attitude." *Id.* Indeed, the Court noted, Nadel initially testified that he did not review the confirmations, but then "back-pedaled" when presented with prior inconsistent testimony. *Id.*

4. **Opportunity to Commit Future Violations**

The Court, finally, noted Nadel's "long history with, and entrenchment in, the financial industry during the past 35+ years," which it recognized makes "recurrence more likely, especially since institutional investing encompasses Nadel's primary area of expertise." *Id.* at *10 (citing *SEC v. Univ. Major Indus. Corp.*, 546 F.2d 1004,1048 (2d Cir.1976) and *SEC v. Platinum Inv. Corp.*, No. 02-cv-6093, 2006 WL 2707319, at *4 (S.D.N.Y. Sept. 20, 2006)). In addition, the Court recognized, Nadel's "'fraudulent past conduct gives rise to an inference of a reasonable expectation of continued violations.'" *Id.* (quoting *SEC v. Tannenbaum*, No. 99-cv-6050, 2007 WL 2089326, at *3 (E.D.N.Y. Jul. 19, 2007) (quoting *Platinum*, 2006 WL 2707319, at *4)).

B. **Civil Money Penalties**

Magistrate Judge Tomlinson also recommended Nadel be ordered to pay a third-tier civil penalty of $1,000,000, based upon an analysis of the following factors: (1) the egregiousness of Nadel's conduct; (2) the degree of Nadel's scienter; (3) whether Nadel's conduct created substantial losses or the risk of substantial losses; (4) whether Nadel's conduct was isolated or recurrent; and (5) whether the penalty should be reduced due to Nadel's demonstrated current and future financial condition. *Id.* at *22.

The Court referenced its findings regarding injunctive relief and noted that the "scope and protracted nature of Defendants' misconduct strongly supports the conclusion that the Defendants' conduct was egregious and was executed with a high degree of scienter" – and thus that factors (1), (2) and (4) weighed in favor of imposing third-tier civil penalties. *Id.*

Magistrate Judge Tomlinson concluded, furthermore, that "not only was there a real risk of loss based upon Defendants' misconduct, but also that investors incurred actual losses." *Id.* Each of these investors learned, when exiting Nadel's strategy, that in the open market, they could sell the positions Nadel had placed them only at a substantial loss, and the Court concluded that "[t]he risk and/or actual loss was thus directly related to and resulted from each investor's reliance on Defendants' investment strategy, components of which were found to violate the securities laws." *See Id.* at *23-24.

Magistrate Judge Tomlinson ultimately concluded that Nadel's conduct was "egregious, deliberate, and resulted in the risk of significant losses and continued for a span of several years," that "'the seriousness of [his] wrongdoing justifies a serious punitive response,'" *id.* at *26 (citation omitted), and recommended a $1 million civil penalty. *Id.* at *27.[3]

[3] The Court also concluded that while Nadel's financial condition did not appear to be "robust," there were "gaps" in his presentation of inability to pay, as well as "otherwise fairly

IV. Judge Kuntz Rejects Nadel's Objections, Adopts The Report and Permanently Enjoins Nadel From Violating the Anti-Fraud Provisions of the Securities Laws

Nadel filed objections to the Report pursuant to Fed. R. Civ. P. 72. Nadel did not object to any of the Report's findings or recommendations regarding the high degree of his scienter, the recurring nature of his misconduct, his lack of appreciation for his wrongdoing, the likelihood that he would violate the law in the future, or the substantial losses his misconduct caused his clients. Nor did Nadel object to the entry of permanent injunctions, or the imposition of a third-tier civil money penalty in the amount of $1 million. *See SEC v. Nadel*, 206 F. Supp. 3d 782, 785 (E.D.N.Y. 2016) ("*Nadel III*"). Ex. 4. Nadel's objections focused on the amount of disgorgement, and the Relief Defendant objected to the recommendations the Report made with respect to her. Judge Kuntz rejected all of those objections, and adopted the Report's recommendations in their entirety. *Id.* at 789.

Pursuant to the Court's decision, on January 20, 2017, Judge Kuntz entered final judgment against Nadel (and RIA, WDNC, and the Relief Defendant), (1) permanently enjoining him from future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, Exchange Act Rules 10b-5 and 10b-10, and Sections 206(1), 206(2) and 206(3) of the Advisers Act, and from aiding and abetting future violations of Section 10(b) of the Exchange Act and Exchange Act Rule 10b-10; (2) ordering him (jointly and severally with RIA and WDNC) to pay disgorgement in the amount of $10,776,687.62 plus pre-judgment interest of $2,293,701.57; and (3) ordering him to pay a civil money penalty in the amount of $1,000,000. *See* Judgment, *SEC v. Nadel*, No. 11-cv-215 (WFK) (E.D.N.Y. Jan. 20, 2017). Ex. 5.

V. The Instant Administrative Proceeding

The Commission issued the OIP in this matter on March 16, 2017, on the basis of the

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sizable amounts of income which have thus far been unexplained." The Court found that this factor weighed "narrowly in favor of the imposition of third-tier civil penalties." *Id.* at *26.

final judgment and permanent injunctions against Nadel, pursuant to Section 15(b) of the Exchange Act, 15 U.S.C. § 78o(b) (2009), and Section 203(f) of the Advisers Act, 15 U.S.C. § 80b-3(f) (2009). The OIP alleges that, during the relevant period, Nadel was an investment adviser, was associated with WDNC, a broker-dealer, owned and controlled RIA, a registered investment adviser, *see id.* ¶ 1, and that the District Court found that Nadel willfully violated Sections 10(b) of the Exchange Act and Rule 10b-5 thereunder, Section 17(a) of the Securities Act, and Sections 206(1), 206(2) and 206(3) of the Advisers Act, and willfully aided and abetted WDNC's violations of Exchange Act Rule 10b-10, and permanently enjoined him from violating, or aiding and abetting violations of, those anti-fraud provisions. *Id.* ¶ 2.

Nadel sent a letter dated April 15, 2017 to the Division in which he, *inter alia*, continued to insist that his conduct with respect to cross-trades and false trade confirmations "were [not] the result of an attempt to defraud a client," Ex. 6 at 1, and stating his intent and hope that he could be again employed in the securities industry. *Id.* at 2. On May 8, 2017, Nadel filed an Answer to the allegations in the OIP ("Answer") (Ex. 7), in which he did not dispute any of the factual allegations of the OIP, and continued to express his desire and intention to "work in the investment industry." *See* Ex. 7 at 1.

ARGUMENT

To protect the public interest, the Division respectfully requests that the Court permanently bar Nadel from association with any broker, dealer or investment adviser. The District Court has already found that Nadel reaped more than $10 million from his clients on the basis of egregious, repetitive, fraudulent conduct (while causing substantial losses to his clients), violations over which he expressed no remorse at all before judgment was entered against him, and which even now he has attempted to minimize.

I. Summary Disposition Standard

Rule 250(a) permits a party to move for summary disposition of the OIP's allegations, and provides that such a motion should be granted if there is "no genuine issue with regard to any material fact and the party making the motion is entitled to a summary disposition as a matter of law." 17 C.F.R. § 201.250(a). Summary disposition is particularly appropriate where, as here, the pertinent facts already have been litigated and determined in a prior judicial proceeding. *See, e.g., Joseph P. Galluzzi*, Rel. No. 34-46405, 2002 WL 1941502 (Aug. 23, 2002) (Commission upheld ALJ's grant of Division's motion for summary disposition where facts were determined in earlier injunctive action and criminal conviction).

No genuine dispute of material fact exists regarding the Division's requested relief. Nadel's injunction for his violations is a matter of public record, and is in any event undisputed by Nadel. Thus, the Court should grant the Division summary disposition.

II. Nadel's Violations and the Permanent Injunctions Establish the Basis for Administrative Relief

As noted above, no genuine dispute exists that Nadel was found to have willfully violated and was enjoined from future violations of the anti-fraud provisions of the federal securities laws, within the meaning of Sections 15(b)(4)(C), 15(b)(4)(D), 15(b)(4)(E), and 15(b)(6)(A)(i) and (iii) of the Exchange Act, 15 U.S.C. §§ 78o(b)(4)(C), 78o(b)(4)(D), 78o(b)(4)(E), 78o(b)(6)(A)(i) and (iii), and of Sections 203(e)(4), (5) and (6), and 203(f) of the Advisers Act, *id.* §§ 80b-3(e)(4), 80b-3(e)(5), 80b-3(e)(6), and 80b-3(f) . Indeed, in his Answer, Nadel admitted (as he must) the existence of the injunctions, and did not dispute any factual allegation in the OIP. Ex. 7. Moreover, it is undisputed that at the time of the conduct at issue Nadel: (1) was an investment adviser, and was associated with RIA, which he owned and controlled, pursuant to Sections 203(e) and 203(f) of the Advisers Act, *id.* §§ 80b-3(e), 80b-3(f) ; and (2)

was associated with WDNC, his broker-dealer, as required for a bar under Section 15(b)(6)(A) of the Exchange Act, *id.* § 78o(b)(6)(A).

Accordingly, each individual provision that Nadel was enjoined from violating, or from aiding and abetting future violations of, alone is a sufficient basis upon which the Commission may impose remedial sanctions in this case, because each violation (1) "involves the purchase or sale of any security" and/or "arises out of the conduct of the business of a broker [or] dealer." 15 U.S.C. § 78o(b)(4)(C); and/or (2) arises out of his violations of Sections 206(1), (2) and (3) of the Advisers Act. *See* Sections 203(e)(4), 203(e)(5), 203(e)(6) and 203(f) of the Advisers Act, §§ 80b-3(e)(4), 80b-3(e)(5), 80b-3(e)(6), and 80b-3(f).[4]

III. The Public Interest Requires that Nadel Be Permanently Barred from Association with a Broker, Dealer, or Investment Adviser

In determining what sanction to impose, the Court should be guided by the following factors, which overlap with the factors considered in the Report:

> (a) the egregiousness of the defendant's actions; (b) the isolated or recurrent nature of the infraction; (c) the degree of scienter involved; (d) the sincerity of the defendant's assurances against future violations; (e) the defendant's recognition of the wrongful nature of his conduct; and, (f) the likelihood that the defendant's occupation will present opportunities for future violations.

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[4] Collateral estoppel would bar any attempt by Nadel to attack either the legal or factual basis for the injunctions entered against him. *See John W. Lawton*, Rel. No. 3513, 2012 WL 6208750, at *5 (Dec. 13, 2012) (holding that respondent could not collaterally attack allegations in the Commission's federal complaint against him where he had consented to the entry of an injunction) *vacated in part on other grounds by John W. Lawton*, Rel. No. 4402, 2016 WL 3030847 (May 27, 2016); *Phillip J. Milligan*, Rel. No. 61790, 2010 WL 1143088, at *4 (Mar. 26, 2010) (affirming initial decision imposing a permanent bar on a respondent who had been enjoined from future violations of the securities laws: "We have repeatedly held that a respondent in a follow-on proceeding may not challenge the findings made by the court in the underlying proceeding and we consider those findings in determining the appropriate sanction."); *Michael Pattison*, Rel. No. 67900, 2012 WL 4320146, *7, nn. 38-39 (Sept. 20, 2012) (affirming initial decision imposing a bar under Rule 102(e) and noting that "[c]ourts have repeatedly upheld [the] principle" that a respondent charged under Exchange Act Section 15(b)(6)(A) is "not permitted to collaterally attack the underlying injunction or findings of the court" and collecting cases).

Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981), (citing *SEC v. Blatt*, 583 F.2d 1325, 1223 n.29 (5th Cir. 1978) (internal quotations omitted)). The *Steadman* factors should be used to determine whether a bar is appropriate. *See Lawton*, 2012 WL 6208750 at *10-13; *see also Tzemach David Netzer Korem*, Rel. No. 70044, 2013 WL 3864511, at *7, nn. 56-57 (July 26, 2013) (reiterating *Lawton*); *Alfred Clay Ludlum, III*, Rel. No. 3628, 2013 WL 3479060, at *5, n. 49 (July 11, 2013) (same).

Here, no genuine dispute can exist that the *Steadman* factors weigh heavily in favor of permanent bars, because Magistrate Tomlinson considered the same factors to determine that a permanent injunction and third-tier civil penalties were warranted, and these findings were not challenged by Nadel, and were adopted in their entirety by Judge Kuntz. *See David A. Zwick*, I.D. Rel. No. 336, 2007 WL 3119764, at *3 (Oct. 25, 2007) ("The District Court's conclusions following consideration of factors almost identical to those in *Steadman* are persuasive") (imposing bar).

First, the Report concluded that Nadel's conduct was egregious, and in particular that while Nadel was reaping millions of dollars in trading commissions and advisory fees through his deceit, he risked his clients' money, and caused them substantial losses when they sought to liquidate their holdings in the market. *Nadel II*, 2016 WL 639063 at *22-24. *Second*, the Report concluded that Nadel's conduct recurred over a period of more than three years and over thousands of communications and thousands of cross trades, *id.* at *8-9, 26. *See Richard J. Daniello*, 50 S.E.C. 42, 46 (1989) (four months of misappropriating employer's funds was not isolated). *Third*, the Report concluded that Nadel acted with a "high degree of scienter" both with respect to his lies about AUM but also with respect to the violative cross-trades and the false trade confirmations. *Nadel II*, 2016 WL 639063, *6-8.

Fourth, having observed Nadel's demeanor throughout his testimony, Magistrate Tomlinson concluded that Nadel "showed both indifference and a somewhat cavalier attitude regarding the underlying violations," *id.* at *9, "appeared dismissive," *id.*, "presented a similar lackluster attitude," and "back-pedaled" with respect to his prior sworn testimony. *Id.* at *10. Moreover, it is apparent even as late at the instant proceeding that Nadel continues to seek to minimize his egregious conduct, insisting, for example, that he did not intend to defraud his clients with respect to his unlawful cross-trading, *see* Ex. 6 at 2, despite the Report's conclusions to the contrary. *Nadel II*, 2016 WL 639063 at *6-9.

Fifth, the Report concluded that Nadel would be presented with an opportunity to repeat his misdeeds given his long history of involvement with the securities industry. *See id.* at *10. Indeed, given that Nadel has vowed in this proceeding to reenter the securities industry, Ex. 6 at 2; Ex. 7 at 1, it is clear that there is a danger that he will repeat his violations. This danger is particularly acute in the instant matter, given the belated, grudging and incomplete acknowledgment by Nadel of his wrongdoing, and his demonstrated willingness to attempt to deceive the Commission itself when acting in its regulatory oversight role: Nadel, after all, did not merely engage in a years-long fraud against his clients and prospective clients, but, as the Report also expressly found, sought to conceal his fraud, and its ongoing nature, from the Commissioner's examiners. *Nadel II*, 2016 WL 639063, at *7.

The securities industry presents many opportunities for abuse and overreaching, and its survival depends upon the integrity of its participants. The public interest is therefore best served by permanently barring from association with a broker, dealer or investment adviser those individuals whose honesty and integrity have been seriously impugned. In *Milligan*, for example, the Commission affirmed the ALJ's Initial Decision to enter permanent bars against a

respondent, based in part on a Magistrate Judge's Report and Recommendation that made "strongly negative credibility findings with respect to Milligan's overall testimony based on the magistrate judge's personal observation of Milligan," 2010 WL 1143088 at *3, and concluded that "fidelity to the public interest requires a severe sanction when a respondent's misconduct involves fraud because the securities business is one in which opportunities for dishonesty recur constantly." *Id.* at *5 (internal quotation marks and citations omitted); *see also Ahmed M. Soliman*, Rel. No. 34-35609, 1995 WL 237220 (Apr. 17, 1995).

The same result is warranted here. Nadel's willful violation of the anti-fraud provisions of the securities laws reflects strongly against his fitness to associate again with a broker, dealer or investment adviser, and a bar against him is necessary to protect the investing public. Because no genuine dispute of fact exists regarding this matter, summary disposition is proper.

CONCLUSION

For the foregoing reasons, the Division respectfully requests that its motion for summary disposition be granted and that the Court issue an order permanently barring Nadel from association with any broker, dealer or investment adviser.

Dated: June 16, 2017
New York, New York

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EXHIBIT 1

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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	
Plaintiff,	
-against-	
	11 Civ. 0215 (DRH) (AKT)
WARREN D. NADEL,	
WARREN D. NADEL & CO., and	
REGISTERED INVESTMENT ADVISERS, LLC	
Defendants	
-and-	
	JURY TRIAL DEMANDED
KATHERINE NADEL,	
Relief Defendant.	

AMENDED COMPLAINT

Plaintiff Securities and Exchange Commission, as and for its Complaint against defendants Warren D. Nadel ("Nadel"), Warren D. Nadel & Co. ("WDNC") and Registered Investment Advisers, LLC ("RIA") (collectively, the "Defendants"), and Relief Defendant Katherine Nadel, alleges as follows:

SUMMARY

1. From the beginning of 2007 at the latest through 2009 (the "Relevant Period"), Defendants fraudulently induced clients of RIA, an investment advisory firm, to invest tens of mil-

lions of dollars in what Defendants described as a liquid, cash management investment program in which RIA clients would buy and sell preferred utility securities in the open market and hold them for short periods of time in order to generate either dividend income or capital appreciation, depending on the client's goal (the "Strategy"). In exchange, Defendants' clients were required to pay trading commissions and investment management fees, which amounted to over $8 million in total during the Relevant Period alone.

2. Defendants' conduct was fraudulent. In numerous communications with clients and prospective clients, Defendants deliberately overstated the value and liquidity of client holdings in the Strategy. They succeeded in doing so by concealing critical information about the way they were supposedly executing the Strategy. For example, Defendants informed clients repeatedly (orally and in writing) that they were executing open-market transactions on the clients' behalf. The vast majority of transactions, however, were not executed on the open market. Most simply consisted of trades between advisory client accounts controlled by Defendants at inflated prices made up by Nadel himself. By shuffling securities back and forth between advisory client accounts at inflated prices, Defendants created the false impression that there was a liquid market for these securities and that the market prices for the securities were consistent with the inflated values that Defendants reported to RIA clients. To further induce investors to join and stay in the Strategy, Defendants also deliberately overstated (by more than twice) the amount of assets that RIA had under management.

3. By means of these misrepresentations and omissions, Defendants attracted and maintained RIA clients, and obtained from them, more than $6 million in commissions and at least $2.4 million in advisory fees during the Relevant Period. Meanwhile, RIA's clients suffered

substantial losses on what Defendants had falsely represented to be a liquid, cash management program.

VIOLATIONS

4. Based on the conduct alleged in this Complaint:

   a. Defendant Nadel violated Section 17(a) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. § 77q(a)], Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. §§ 240.10b-5]; aided and abetted violations of Section 17(a) of the Exchange Act [15 U.S.C. § 78q] and Rules 10b-10 and 17a-4 thereunder [17 C.F.R. §§ 240.10b-10 and 204.17a-4]; violated Sections 206(1), (2) and (3) and 207 of the Investment Advisers Act of 1940 ("Advisers Act") [15 U.S.C. § 80b-6 and 80b-7]; and aided and abetted violations of Section 204 [15 U.S.C. § 80b-4] and Rule 204(2)-(a)(3) thereunder [17 C.F.R. § 204-2(a)(3)];

   b. Defendant WDNC violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Sections 10(b) and 17(a) of the Exchange Act [15 U.S.C. § 78j(b) and 78q] and Rules 10b-5, 10b-10 and 17a-4 thereunder [17 C.F.R. §§ 240.10b-5, 240.10b-10 and 204.17a-4]; and

   c. Defendant RIA violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. §§ 240.10b-5]; and Sections 204, 206(1), (2), and (3) and 207 of the Advisers Act [15 U.S.C. § 80b-4, 80b-6 and 80b-7] and Rule 204(2)-(a)(3) thereunder [17 C.F.R. § 204-2(a)(3)].

JURISDICTION AND VENUE

5. The Commission brings this action pursuant to the authority conferred by Section 20 of the Securities Act [15 U.S.C. § 77t], Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)] and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9] seeking permanent injunctions against Nadel, WDNC and RIA.

6. The Commission also seeks final judgments requiring the Defendants to disgorge any ill-gotten gains and to pay prejudgment interest thereon and ordering the Defendants to pay civil money penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)] and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9].

7. This Court has jurisdiction pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 77u(e) and 78aa] and Section 214 of the Advisers Act [15 U.S.C. § 80b-14].

8. Defendants, directly or indirectly, singly or in concert, made use of the means or instruments of transportation or communication in, or the means or instrumentalities of, interstate commerce, or of the mails, or of any facility of any national securities exchange, in connection with the transactions, acts, practices, and courses of business alleged herein.

9. Venue lies in this District pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Section 27 of the Exchange Act [15 U.S.C. § 78aa] and Section 214 of the Advisers Act [15 U.S.C. § 80b-14]. Defendants reside and transact business in the Eastern District of New York.

THE DEFENDANTS

10. **Nadel**, age 59, is a resident of Upper Brookville, New York. Nadel controls both WDNC and RIA. He is and at all relevant times was the president, chief executive officer and

chief compliance officer of WDNC and the president of RIA. Nadel holds Series 1, 3, 7, 24 and 63 licenses.

11. **WDNC** is and at all relevant times was a broker-dealer registered with the Commission since October 29, 1987, with a principal place of business Glen Cove, NY. Nadel used WDNC to execute trades as part of his fraudulent scheme, and charged customers commissions for these trades.

12. **RIA** is and at all relevant times was an investment adviser, registered with the Commission since January 5, 2004, with a principal place of business Glen Cove, NY. Nadel lured clients into becoming and remaining Strategy investors, and charged them monthly asset management fees.

RELIEF DEFENDANT

13. **Katherine Nadel,** age 61, is Nadel's wife, a resident of Upper Brookville, New York, and has been identified by Defendants as the Chief Operating Officer of Warren D. Nadel & Co. From January 1, 2007 through December 31 2009, Defendants diverted more than $711,000 of the commissions and advisory fees they fraudulently obtained from their clients to Katherine Nadel in the form of salary and profit distributions. Katherine Nadel has no legitimate claim to retain these ill-gotten proceeds.

FACTS

14. Nadel represented the Strategy to existing and prospective clients as one that consisted of investing in preferred utility stocks, traded either on over-the-counter markets or on exchanges such as the NYSE, AMEX and NASDAQ. Nadel offered Strategy investors three purported investment options: (i) to invest for capital appreciation by buying and selling preferred utility securities before their ex-dividend date; (ii) to invest for dividend income by buying be-

fore and selling after the ex-dividend date at a capital loss that could be used to offset a company's existing capital gains; or (iii) to invest for both of these objectives.

15. Nadel falsely touted the Strategy to prospective and existing advisory clients in written materials and oral communications as a conservative and liquid cash management investment program that was "tax advantaged [and] low risk."

16. Nadel marketed the Strategy as an alternative to CDs, Treasury Bills and Eurobonds primarily to corporate treasurers or CFOs seeking "enhanced treasury department performance." In a marketing document that Defendants disseminated to investors during the Relevant Period, for example, Defendants described the Strategy as follows:

> [T]his unique concept in cash management provides a competitive alternative to fully taxable investments such as CDs, Treasury Bills and Eurobonds. Close and effective management of a three-part portfolio plan strives to achieve a superior return on short term preferred stock investments, *without sacrificing liquidity. By carefully timing entry into and departure from the marketplace*, qualifying corporations are currently able to capture seven or eight quarterly dividends each year, while benefitting from a 70% Federal tax exclusion on such income. (Emphasis added).

17. RIA's Form ADV also assured investors that the Strategy was liquid, representing that it required no minimal period of commitment and that clients "will be entitled to withdraw from an account at any time." In other written materials, Nadel assured clients that "90 day liquidity is available."

18. In order to work, Defendants' Strategy required that the market have sufficient liquidity to permit frequent purchases and sales of substantial quantities of preferred utility stocks. By 2007 at the latest, however, Nadel knew that the market for the preferred utility stocks underlying the Strategy was not sufficiently liquid to allow for execution of the Strategy, at attractive prices, in the manner Nadel was representing to clients and prospective clients.

19. Nadel fraudulently concealed these market conditions by avoiding the market almost

entirely and instead cross-trading securities between his advisory clients' accounts at prices that Nadel determined himself and that almost always substantially exceeded the actual market price. Using his control over advisory client accounts, Nadel effectuated these cross-trades either by causing one advisory client account to sell securities to another advisory client account (with his broker-dealer WDNC acting as agent to both of the clients involved in the trade) or by causing one advisory client account to sell securities to WDNC and then having WDNC re-sell them to another advisory client account. This scheme was extensive and long-lasting: Between 2007 and 2009, of at least 11,250 trades for Strategy clients, approximately 90% of them were cross-trades back and forth between Strategy clients, rather than open-market transactions.

20. By avoiding the open market and shuffling securities back and forth between advisory client accounts, Nadel was able to dictate the prices for the trades and create the illusion that there was a genuine and liquid market for the securities at these artificially inflated prices. In so doing, Defendants were able to induce Strategy clients to join and stay with RIA and bilk them out of millions of dollars in brokerage commissions and advisory fees.

21. One of the reasons that Nadel was able to accomplish this fraudulent scheme was that he and RIA used the broker-dealer he also owned and controlled, WDNC, to execute transactions for the Strategy clients. In RIA's Form ADV and in other written materials he provided to clients, Nadel represented that he and RIA would use WDNC as the broker because WCNC would "deal with such other brokers or dealers as can provide the best execution for the orders on behalf of the accounts," and that WDNC provided the "best combination of services provided for costs levied."

22. As Nadel well knew, these statements were false. Nadel and RIA did not use WDNC to obtain "best execution" from other brokers or because WDNC provided the "best

combination" of services. In fact, Nadel almost never dealt with other brokers or dealers. Indeed, almost all of the transactions that Nadel executed on behalf of Strategy clients consisted of internal cross-trades between the various advisory clients at prices determined by Nadel himself. Nadel's true reason for using WDNC was to generate brokerage commissions for the Defendants' benefit and to conceal from his clients that these transactions were not executed either on the open market or at prevailing market prices.

23. Defendants never told RIA clients that virtually all Strategy transactions were between and among the RIA clients. This is so even though Nadel and RIA were under fiduciary and statutory obligations to notify clients in writing before the completion of *each* transaction in which an affiliate of RIA acted as broker and to obtain the clients' consent before the completion of *each* such transaction.

24. As noted above, Defendants also deceived RIA clients through explicit misrepresentations in marketing and registration materials that falsely described how the Strategy was liquid, and involved transacting with the marketplace using WDNC's expertise in dealing with other brokers.

25. Defendants also deceived RIA clients through trade confirmations sent to clients on the thousands of trades executed during the Relevant Period. These trade confirmations were prepared using information reported by Defendants to WDNC's clearing firm, and Defendants regularly reviewed those confirmations when they were disseminated to their clients.

26. Almost all of the trade confirmations sent to RIA Strategy clients during the Relevant Period misleadingly reported that the trades were executed with the market. In some cases, the trade confirmations falsely reported that WDNC had acted as clients' agent in "over the counter" transactions, without disclosing that the other party was another advisory client of RIA

(or even that the other party was another WDNC customer). In other cases, trade confirmations falsely indicated only that the other party to the transaction was a *WDNC* customer and did not report that the WDNC customer was also an RIA advisory client.

27. Defendants falsely reported that WDNC acted as agent on transactions for which WDNC in fact acted as principal, buying securities directly from the client or selling securities directly to the client.

28. These misrepresentations and omissions were material. They were all designed to, and did, create the illusion for RIA clients that the Strategy was being executed, and its price and liquidity tested, by the open market. These misrepresentations and omissions were essential to Nadel's scheme: Had Nadel properly disclosed the nature of each cross-trade and sought client consent, clients would have learned that this supposedly conservative, short term and liquid cash management investment Strategy was essentially a sham because there was, in fact, no liquid market for most of these securities at the reported prices, and actual market prices, as reflected in actual market transactions, were in most instances significantly less than the prices Defendants were claiming.

29. By misrepresenting to advisory clients that he was executing market transactions, Nadel materially misrepresented to these clients the value and liquidity of their holdings. In RIA's Form ADV, Defendants represented that RIA would provide clients each month with a "Monthly Cumulative Performance Report," in which each stock position would be "marked to market," and in any transactions with either WDNC as a principal-counterparty, or with another brokerage customer of WDNC as the counterparty, the securities would be priced "at the then prevailing market value."

30. In other communications with clients, Nadel claimed that he was able to arrive at

valuations of these stock positions by using an expertise he had gained in more than 20 years of experience in the market. Nadel claimed that he would contact market makers in the various security positions as of months' end to obtain the so-called "inside market" (highest bid and lowest offer), which enabled him to compute the mid-point value for the security in question.

31. These were all lies. Nadel did not set the prices or values of RIA clients' holdings based on the "prevailing market value," or on his computations of mid-market values after contacting market makers. On the contrary, Nadel himself set these generally inflated prices and values, for the purpose of keeping his clients invested in the Strategy, so that he could perpetuate his scheme and continue to receive his commissions and fees.

32. To Defendants' clients, Nadel's valuations appeared to be supported by what Nadel represented were market prices on transactions he executed in their portfolios. The prices at issue – those reported on the misleading trade confirmations, and those stated in Nadel's monthly reports – were fictitious and designed to perpetuate Defendants' false scheme.

33. Indeed, on occasions when his clients questioned him about the difference between his valuations and those contained in the clearing firm's monthly statements or in independent pricing service reports, Nadel purported to justify his prices and values by touting his expertise and his contacts with market makers. As Nadel wrote to one client in an email dated July 10, 2008, his prices were validated "by the subsequent transactions that occur at or about these prices in our client portfolios." This email was a lie. Nadel of course knew that his transactions were not market transactions and thus did not provide any independent verification of the values he reported to his clients.

34. Nadel's misrepresentations -- including the written marketing materials and false trade confirmations discussed above -- also materially misled his clients about the Strategy's li-

quidity. Each false trade confirmation that purported to report a market transaction, and each monthly performance report that purported to be based on prevailing market prices (and substantiated by market transactions), falsely conveyed that there was a liquid market for those quantities of securities at those prices. Defendants thereby provided clients with false assurance of the value of their securities and the false impression that the securities could readily be sold for the reported values.

35. These false statements were consistent with Nadel's marketing materials, which characterized the Strategy as a short-term, liquid cash management investment. In reality, however, by 2007 at the latest, Nadel knew that the market for the securities he used in the Strategy had become illiquid at the inflated prices Nadel had set and reported to clients.

36. The *only* times Nadel revealed the illiquidity of the Strategy to his clients were when they tried to exit it. Then and only then would Nadel tell such clients that exiting the Strategy at prices equivalent to those he had been reporting to them all along would take an extended period of time.

37. Nadel also intentionally misled clients about RIA's assets under management by representing in written marketing materials that he managed over $400 million in assets. In fact, as Nadel knew, Defendants managed less than a third of this amount during the Relevant Period, and Nadel knew this when he misrepresented this fact to his clients.

38. Throughout the Relevant Period, Defendants also failed to maintain any contemporaneous records of the manner in which they purportedly valued their clients' holdings, and failed to maintain any order tickets reflecting the transactions executed on behalf of their Strategy clients.

39. For the period January 1, 2007 through December 31, 2009, Defendants diverted

more than $315,000 of the commissions they fraudulently obtained from their clients to Katherine Nadel, in the form of salary. Although Defendants have reported Katherine Nadel to be the Chief Operating Officer of Warren D. Nadel & Co., she provided no substantive role in the operations of Warren D. Nadel & Co.'s securities business, and has no legitimate claim to any of these funds.

40. In addition, although Defendants did not disclose any ownership interest on the part of Katherine Nadel in RIA in its Form ADV for the period January 1, 2007 through December 31, 2009, Defendants diverted approximately 40% of the profits RIA fraudulently earned from their clients during this period to her, in an amount exceeding $396,000. Katherine Nadel has no legitimate claim to any of these funds.

FIRST CLAIM FOR RELIEF

Violations of Section 17(a) of the Securities Act
(Defendants Nadel, RIA and WDNC)

41. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

42. Nadel, RIA and WDNC, directly and indirectly, singly and in concert, knowingly or recklessly, by the use of the means or instruments of transportation or communication in, and the means or instrumentalities of, interstate commerce, or by the use of the mails, in the offer or sale of securities: (a) have employed devices, schemes or artifices to defraud; (b) have obtained money or property by means of untrue statements of material fact, or omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (c) have engaged in transactions, acts, practices and courses of business which operated or would operate as a fraud or deceit upon purchasers of securities or other persons.

43. As described in the paragraphs above, Nadel, RIA and WDNC have violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

SECOND CLAIM FOR RELIEF

Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder
(Defendants Nadel, WDNC and RIA)

44. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

45. Nadel, WDNC and RIA, directly or indirectly, singly or in concert, knowingly or recklessly, by use of the means or instrumentalities of interstate commerce, or of the mails, or of the facilities of a national securities exchange, in connection with the purchase and sale of securities: (a) have employed devices, schemes and artifices to defraud; (b) have made untrue statements of material fact, and have omitted state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; or (c) have engaged in transactions, acts, practices and courses of business which operated or would operate as a fraud or deceit upon purchasers of securities.

46. As described in the paragraphs above, Nadel, WDNC and RIA, directly or indirectly, singly or in concert, have violated, are violating, and unless enjoined will again violate, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] thereunder.

THIRD CLAIM FOR RELIEF

Violations of Sections 206(1) and (2) of the Advisers Act
(Nadel and RIA)

47. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

48. As described above, Nadel and RIA directly and indirectly, singly and in concert, knowingly or recklessly, (1) have employed a device, scheme or artifice to defraud clients or prospective clients; and (2) have engaged in a transaction, practice or course of business which operates as a fraud upon clients or prospective clients.

49. As described in the paragraphs above, Nadel and RIA, directly or indirectly, singly or in concert, have violated, are violating, and unless enjoined will again violate, Section 206(1) and 206(2) of the Advisers Act [15 U.S.C. § 80b-6].

FOURTH CLAIM FOR RELIEF

Violations of Section 206(3) of the Advisers Act
(Nadel and RIA)

50. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

51. As described above, Nadel and RIA directly and indirectly, singly and in concert, knowingly or recklessly, have acted as a principal for their own account knowingly to sell a security or to buy a security from a client, or have acted as a broker for a person other than such client, knowingly to effect a sale or purchase of a security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which they are acting and obtaining the consent of the client to such transaction.

52. As described in the paragraphs above, Nadel and RIA, directly or indirectly, singly or in concert, have violated, are violating, and unless enjoined will again violate, Section 206 (3) of the Advisers Act [15 U.S.C. § 80b-6].

FIFTH CLAIM FOR RELIEF

Violations of Section 207 of the Advisers Act
(Nadel and RIA)

53. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

54. As described above, Nadel and RIA directly and indirectly, singly and in concert, knowingly or recklessly, made false statements of material fact in a report, Form ADV, filed with the Commission.

55. As described in the paragraphs above, Nadel and RIA violated Section 207 of the Advisers Act [15 U.S.C. § 80b-7].

SIXTH CLAIM FOR RELIEF

Violations of and Aiding and Abetting Violations of Rule 10b-10 of the Exchange Act
(Defendants WDNC and Nadel)

56. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

57. As described above, WDNC directly and indirectly, singly and in concert, knowingly or recklessly, provided confirmations to customers that did not reflect WDNC's role in the transaction as principal or as the agent of both parties to transactions between advisory clients from at least March 2008 forward.

58. As described in the paragraphs above, WDNC violated Rule 10b-10 under the Exchange Act [17 C.F.R. §§ 240.10b-10].

59. By reason of the activities herein described, Nadel knowingly or recklessly aided and abetted WDNC's violations of Rule 10b-10 under the Exchange Act [17 C.F.R. §§ 240.10b-10].

SEVENTH CLAIM FOR RELIEF

Violations of and Aiding and Abetting Violations of Section 204 of the Advisers Act and Rule 204-2 Thereunder
(Nadel and RIA)

60. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

61. As described above, RIA directly and indirectly, knowingly or recklessly, failed to make and/or keep true, accurate, complete, and current books and records, and to maintain certain other records for a period of five years, including memoranda concerning certain transaction details for the purchase and sale of any security. RIA failed to make and/or keep memoranda concerning certain transaction details for the purchase and sale of securities for the required five year period.

62. As described in the paragraphs above, RIA violated Section 204 of the Advisers Act [15 U.S.C. § 80b-4] and Rule 204(2)-2 [17 C.F.R. § 204-2(a)(3)] thereunder.

63. By reason of the activities herein described, Nadel knowingly or recklessly aided and abetted WDNC's violations of Section 204 of the Advisers Act [15 U.S.C. § 80b-4] and Rule 204(2)-2 [17 C.F.R. § 204-2(a)(3)] thereunder.

EIGHTH CLAIM FOR RELIEF

Violations and Aiding and Abetting Violations of Section 17(a) of the Exchange Act and Rule 17a-4 Thereunder
(WDNC and Nadel)

64. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

65. As described above, WDNC directly and indirectly, knowingly or recklessly, failed to maintain, make and keep for proscribed periods such records and reports as the Commission,

by rule, prescribes as necessary. Rule 17a-3(a)(6) under Section 17(a) of the Exchange Act requires a broker-dealer to make and keep current memorandums of brokerage orders. Rule 17a-4(b)(1) under Section 17(a) of the Exchange Act requires broker-dealers to preserve these records for three years. WDNC failed to make and/or keep memoranda concerning transaction details for the purchase and sale of each security for the required three year period.

66. As described in the paragraphs above, WDNC violated Section 17(a) of the Exchange Act [15 U.S.C. § 78q] and Rule 17a-4 thereunder [17 C.F.R. § 204.17a-4].

67. By reason of the activities herein described, Nadel knowingly or recklessly aided and abetted WDNC's violations of Section 17(a) of the Exchange Act [15 U.S.C. § 78q] and Rule 17a-4 thereunder [17 C.F.R. § 204.17a-4]

NINTH CLAIM FOR RELIEF

(Disgorgement from Relief Defendant Katherine Nadel)

68. The Commission realleges and incorporates by reference the allegations contained in paragraphs 1 through 40.

69. In the manner described above, Relief Defendant Katherine Nadel received ill-gotten gains for which she gave no consideration, and to which she has no legitimate claim.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff respectfully requests a Final Judgment:

I.

Permanently enjoining Nadel, his agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from future direct or indirect violations of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15

U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. §§ 240.10b-5]; aiding and abetting violations of Section 17(a) of the Exchange Act [15 U.S.C. § 78q] and Rules 10b-10 and 17a-4 thereunder [17 C.F.R. §§ 240.10b-10 and 204.17a-4]; violating Sections 206(1), (2) and (3) and 207 of the Investment Advisers Act of 1940 ("Advisers Act") [15 U.S.C. § 80b-6 and 80b-7]; and aiding and abetting violations of Section 204 [15 U.S.C. § 80b-4] and Rule 204(2)-(a)(3) thereunder [17 C.F.R. § 204-2(a)(3)].

II.

Permanently enjoining WDNC, its agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from future direct or indirect violations of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Sections 10(b) and 17(a) of the Exchange Act [15 U.S.C. § 78j(b) and 78q] and Rules 10b-5, 10b-10 and 17a-4 thereunder [17 C.F.R. §§ 240.10b-5, 240.10b-10 and 204.17a-4].

III.

Permanently enjoining RIA, its agents, servants, employees and attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise, and each of them, from future direct or indirect violations of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. §§ 240.10b-5]; and Sections 204, 206(1), (2), and (3) and 207 of the Advisers Act [15 U.S.C. § 80b-4, 80b-6 and 80b-7] and Rule 204(2)-(a)(3) thereunder [17 C.F.R. § 204-2(a)(3)].

IV.

Ordering Defendants to disgorge their ill-gotten gains and to pay prejudgment interest

thereon.

V.

Ordering Relief Defendant Katherine Nadel to disgorge her ill-gotten gains and to pay prejudgment interest thereon.

VI.

Ordering the Defendants to pay civil penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)] and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9].

VII.

Such other and further relief as the Court deems appropriate.

Dated: New York, New York
August 25, 2011

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EXHIBIT 2

97 F.Supp.3d 117
United States District Court,
E.D. New York.

SECURITIES & EXCHANGE COMMISSION, Plaintiff,
v.
Warren D. **NADEL**; Warren D. **Nadel** & Co.; and Registered Investment Advisers, LLC, Defendants,
and
Katherine **Nadel**, Relief Defendant.

No. 11–CV–215 (WFK)(AKT).
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Signed April 2, 2015.
|
Filed March 31, 2015.

Synopsis
Background: Securities and Exchange Commission (SEC) brought action alleging that broker-dealer, investment adviser, and their principal fraudulently induced broker-dealer's clients to invest millions of dollars in investment strategy by misrepresenting to clients and to prospective clients amount of assets they had under management and by failing to provide written notice and to obtain consent for cross-trade transactions amongst clients, in violation of Securities Exchange Act, Securities Act, and Investment Advisers Act. Parties filed cross-motions for summary judgment.

Holdings: The District Court, William F. Kuntz, II, J., held that:

[1] defendants' misrepresentations were sufficiently material to constitute securities fraud;

[2] misrepresentations violated Investment Advisers Act's anti-fraud provisions;

[3] principal was acting as broker when he made misrepresentations;

[4] clients' blanket consents did not exempt defendants from liability under Investment Advisers Act; and

[5] broker-dealer violated rule requiring it to "disclose material information."

SEC's motion granted.

West Headnotes (10)

[1] **Securities Regulation**
⇦ Manipulative, Deceptive or Fraudulent Conduct

To establish securities fraud claim under § 10(b) and Rule 10b–5, Securities and Exchange Commission (SEC) must plead that defendant (1) made material misrepresentation or material omission as to which he had duty to speak, or used fraudulent device; (2) with scienter; (3) in connection with purchase or sale of securities. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5.

Cases that cite this headnote

[2] **Securities Regulation**
⇦ Scienter;knowledge or intention

Securities Regulation
⇦ Nature and grounds of injunction in general

Same elements required to establish § 10(b) violation and Rule 10b–5 violation suffice to establish fraud in connection with offer or sale of security under Securities Act, with exception that scienter is not required for Securities and Exchange Commission (SEC) to enjoin violations under subsection making it unlawful to obtain money or property by means of any untrue statement of material fact or any omission to state material fact necessary in order to make statements made, in light of circumstances under which they were made, not misleading or under subsection making it unlawful to engage in any transaction, practice, or course of business which operates or would operate as fraud or deceit upon purchaser. Securities Act of 1933, § 17(a), 15 U.S.C.A. § 77q(a);

Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5.

Cases that cite this headnote

[3] **Securities Regulation**
⇦ Materiality of violation

False statement is sufficiently material to support securities fraud claim under § 10(b) if there is substantial likelihood that reasonable investor would consider information important in his or her decision-making process. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5.

Cases that cite this headnote

[4] **Securities Regulation**
⇦ Materiality of violation

While, to support securities fraud claim, false statement must have been one that would have assumed actual significance in reasonable shareholder's decision-making process, there is no requirement that fact would have been outcome determinative, and thus fact may be material even if it would not have changed investor's ultimate decision. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5.

Cases that cite this headnote

[5] **Securities Regulation**
⇦ Materiality and causation

Securities Regulation
⇦ Materiality of violation

Misrepresentations by broker-dealer, investment adviser, and their principal to clients and prospective clients regarding amount of assets they had under management were sufficiently material to constitute securities fraud under Securities Act and Securities Exchange Act, even though accurate amount of assets under management was disclosed in publicly-available documents; any reasonable investor would need accurate disclosures about assets under management to correctly evaluate asset manager's performance, and clients believed misstatements about assets under management to be material. Securities Act of 1933, § 17(a), 15 U.S.C.A. § 77q(a); Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5.

1 Cases that cite this headnote

[6] **Witnesses**
⇦ Effect of refusal to answer

Asset manager's affidavit opposing summary judgment motion in Securities and Exchange Commission's (SEC) civil enforcement action suit would not be considered by district court, where manager had repeatedly invoked his Fifth Amendment privilege against self-incrimination to avoid providing testimony and discovery on issue of assets under management. U.S.C.A. Const.Amend. 5.

Cases that cite this headnote

[7] **Securities Regulation**
⇦ Investment Advisers

Misrepresentations by broker-dealer, investment adviser, and their principal to clients and prospective clients regarding amount of assets they had under management were sufficiently material to violate Investment Advisers Act's anti-fraud provisions. Investment Advisers Act of 1940, § 206(1, 2), 15 U.S.C.A. § 80b–6(1, 2).

Cases that cite this headnote

[8] **Securities Regulation**
⇦ Investment Advisers

Investment adviser's principal was acting as broker when he misrepresented to clients and prospective clients amount of assets they had under management, in violation of Investment Advisers Act, even though principal had separate broker-dealer entity, where brokerage fees were not comprised of commissions but rather were based on percentage of assets under management.

Investment Advisers Act of 1940, § 206(3), 15 U.S.C.A. § 80b–6(3).

1 Cases that cite this headnote

[9] **Securities Regulation**
⇐ Investment Advisers

Investment adviser and its principal were required to provide their clients with written notice and to obtain transaction-specific consent prior to engaging in cross-trade activity, and thus could not rely on clients' blanket consents to escape liability under Investment Advisers Act for conducting thousands of cross-trades among their clients and engaging in principal transactions with client accounts. Investment Advisers Act of 1940, § 206(3), 15 U.S.C.A. § 80b–6(3); 17 C.F.R. § 275.206(3)–2.

Cases that cite this headnote

[10] **Securities Regulation**
⇐ Nondisclosure or misrepresentation

Broker-dealer violated rule requiring it to "disclose material information" when it failed to disclose it was acting as either agent for both sides to transaction or as principal in some transactions, even though clients signed blanket consents for cross-trading, where consents were not publicly filed with Securities and Exchange Commission (SEC), and trade confirmations disclosed to customers that transactions were handled by broker in agency capacity, not principal capacity. 17 C.F.R. § 240.10b–10.

1 Cases that cite this headnote

Attorneys and Law Firms

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DECISION & ORDER

WILLIAM F. KUNTZ, II, District Judge.

The Securities and Exchange Commission ("SEC") brings this action against Defendants Warren D. Nadel ("Nadel"), Warren D. Nadel & Co. ("WDNC"), and Registered Investment Advisers, LLC ("RIA") (collectively "Defendants"), and Relief Defendant Katherine Nadel. The SEC alleges Defendants fraudulently induced clients of RIA to invest millions of dollars in an investment strategy by misrepresenting to clients and to prospective clients the amount of assets Defendants had under management and by failing to provide written notice and to obtain consent for cross-trade transactions amongst clients. Currently before the Court is the SEC's motion for partial summary judgment on its claims under Section 10(b) of the Securities Exchange Act of 1934 ("1934 Exchange Act") and Rules 10b–5 and 10b–10 thereunder, Section 17(a) of the Securities Act of 1933 ("1933 Securities Act"), and Sections 206(1), (2), and (3) of the Investment Advisers Act of 1940 ("Advisers Act"). Also before this Court is Defendants' cross-motion for summary judgment. Dkt. 81. For the reasons that follow, the SEC's motion for partial summary judgment is GRANTED. Because the Court grants the SEC's motion for summary judgment in its entirety, Defendants' motion is DENIED. *See e.g., Walker v. City of New York,* 63 F.Supp.3d 301, 308–09, 12–CV–2535, 2014 WL 6883049, at *4 (E.D.N.Y. Dec. 5, 2014) (Kuntz, J.).

BACKGROUND

The following facts are either undisputed or described in the light most favorable to Defendants, the non-moving party. *See Capobianco v. City of New York,* 422 F.3d 47, 50 n. 1 (2d Cir.2005).

Defendant Nadel is a resident of Upper Brookville, New York. Dkt. 82 (Defendants' Local Rule 56.1 Statement of Disputed Facts in Opposition to Plaintiff's Motion for Partial Summary Judgment) ("SDF") at ¶ 1. At all relevant times, Nadel *120 was the President, Chief

Executive Officer, and Chief Compliance Officer of WDNC and the President of RIA. *Id.* RIA was an investment adviser, registered with the SEC since January 5, 2004, with a principal place of business in Glen Cove, New York. *Id.* at ¶ 2. RIA held itself out as providing continuous investment advice to clients in exchange for a fee, which was based upon assets under management. *Id.* WDNC was a broker-dealer registered with the Financial Industry Regulatory Authority ("FINRA") with a principal place of business in Glen Cove, New York. *Id.* at ¶ 3.

The Investment Strategy

Defendants engaged in an investment strategy known as a Preferred Stock Dividend Capture Strategy ("Investment Strategy"), which required a high volume of transactions in preferred utility stocks to maximize tax-preferred income while minimizing loss exposure on the open marketplace. *Id.* at ¶ 4; Dkt. 77 (Defendants' Memorandum of Law in Opposition to Plaintiff's Motion for Partial Summary Judgment) ("Defs.' Br.") at 2. The purpose of the Investment Strategy was to "generate tax-favored dividend income from short-term holdings of preferred stocks while hedging positions to preserve capital." SDF Ex. 1 ("Program Package") at CGC–SEC 297. The Investment Strategy was marketed as "particularly suited to corporations subject to United States federal income tax as 'C' corporations that wish to invest at least $500,000 short-term for income. Under the [Investment] Strategy, long positions in preferred stocks [would] be turned over approximately every 45 days, and the entire portfolio [would] be turned over seven or eight times in any 12 month period." *Id.*

While the Investment Strategy focused on preferred stock transactions occurring in the open marketplace, the Program Package stated that "[m]any such stocks are thinly traded. That is, many such stocks are not abundantly available in the over-the-counter markets where they trade, and, as a consequence relatively small changes in supply or demand can cause disproportionately large changes in then available bid and offered prices for such stocks." *Id.* Nonetheless, "[i]t is anticipated that most transactions in a client's account will be effected over-the-counter, not on a national exchange[.]" *Id.*

By late 2007, Defendants began conducting cross-trades between RIA's own advisory clients instead of executing trades on the open marketplace. SDF at ¶ 8. According to Nadel, uncertainty in the marketplace made preferred utilities securities illiquid, making it difficult to carry out the Investment Strategy by buying and selling securities in the marketplace. *Id.* at ¶ 9.

Marketing Materials

As part of the Investment Strategy, Defendants also distributed marketing materials, such as brochures, power point presentations, firm overviews, and quarterly performance updates, to clients and to prospective clients which represented that RIA managed over $400 million in investor assets. SDF at ¶ 13. However, RIA's Form ADV[1] Part I filings with the SEC revealed that Defendants overstated the actual amount of assets under management. *Id.* at ¶¶ 13, 15. Specifically, RIA's assets under management were only $147.28 million in January 2007; $147.37 million in January 2008; $127.63 million in January 2009; and $54.84 million in January 2010—not the over $400 million that RIA claimed in its marketing materials, a fact undisputed by Defendants. *Id.* at 15.

121** ***SEC Action

Based on the above facts, the SEC filed a complaint against Defendants on January 13, 2011. Dkt. 1 ("Complaint"). On August 25, 2011, the SEC filed an amended complaint against Defendants alleging violations of 17(a) of the 1933 Securities Act, 10(b) of the 1934 Exchange Act and Rule 10b–5 thereunder, Sections 206(1),(2), and (3) of the Advisers Act, Section 207 of the Advisers Act, Section 204 of the Advisers Act and Rule 204–2 thereunder, and aiding and abetting under 10b–10 of the 1934 Exchange Act and Section 17(a) of the 1934 Exchange Act and Rule 17a–4 thereunder. Dkt. 11 ("Amended Complaint") at 12–17.

Currently before this Court is the SEC's motion for partial summary judgment on its claims under Section 10(b) of the 1934 Exchange Act, Rules 10b–5 and 10b–10 thereunder, Section 17(a) of the 1933 Securities Act, and Sections 206(1), (2), and (3) of the Investment Advisers Act. Dkt. 71 (Memorandum of Law in Support of the SEC's Motion for Partial Summary Judgement) ("SEC Br.") at 1. With respect to these claims, the SEC seeks summary judgment on two grounds.

"*First,* the SEC seeks judgment on its claims that Defendants misrepresented to clients and prospective clients the amount of assets they had under management.

Although Defendants managed between $55 to $147 million in assets during the relevant period, they routinely told investors (in over one thousand communications) that they managed more than $300 or $400 million in client assets, overstating the truth by approximately 300% to more than 600%." *Id.* (emphasis in original).

"*Second,* the SEC seeks summary judgment on its claims that Nadel and RIA violated Section 206(3) of the Advisers Act and 1934 Exchange Act Rule 10b–10 by conducting thousands of cross-trades among their clients, and engaging in principal transactions with client accounts, without providing required notice, and obtaining client consent, prior to each transaction. Defendants represented to investors RIA's [Investment Strategy] as a liquid 'cash management' program that utilized WDNC's expertise in dealings with broker-dealers in the market, thereby enhancing best execution for RIA's clients." *Id.* at 2. (emphasis in original).

DISCUSSION

I. Legal Standard

Summary judgment is appropriate when the pleadings, depositions, interrogatories, admissions, and affidavits demonstrate that there are no genuine issues of material fact in dispute and that one party is entitled to judgment as a matter of law. *See* Fed.R.Civ.P. 56; *Celotex Corp. v. Catrett,* 477 U.S. 317, 322–23, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). A genuine issue of material fact exists "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986).

On a motion for summary judgment, "[t]he role of the court is not to resolve disputed issues of fact but to assess whether there are any factual issues to be tried. In determining whether summary judgment is appropriate, this Court will construe the facts in the light most favorable to the non-moving party and must resolve all ambiguities and draw all reasonable inferences against the movant." *Brod v. Omya, Inc.*, 653 F.3d 156, 164 (2d Cir.2011) (internal quotation marks and citations omitted). Once the movant has demonstrated that no genuine issue of material fact exists, then "the nonmoving party must come forward with 'specific facts showing that there is a *genuine issue for trial.*' " ***122** *Matsushita Electric Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 587, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986) (quoting Fed.R.Civ.P. 56(e)) (emphasis in original). The non-moving party must present "concrete evidence from which a reasonable juror could return a verdict in his favor." *Anderson,* 477 U.S. at 256, 106 S.Ct. 2505.

II. Analysis

A. *Defendants Violated Section 10(b) of the 1934 Exchange Act and Rule 10b–5 thereunder, and Section 17(a) of the 1933 Securities Act*

The SEC seeks summary judgment on its claims that Defendants violated Section 10(b) of the 1934 Exchange Act and Rule 10b–5 thereunder and Section 17(a) of the 1933 Securities Act because Defendants misrepresented to clients and to prospective clients the amount of assets they had under management. For the reasons set forth below, the Court agrees.

[1] [2] To establish "a claim under section 10(b) of the [Exchange] Act, 15 U.S.C. § 78j(b), and Rule 10b–5 promulgated thereunder, 17 C.F.R. § 240.10b–5, the SEC must plead that the defendant '(1) made a material misrepresentation or a material omission as to which he had a duty to speak, or used a fraudulent device; (2) with scienter; (3) in connection with the purchase or sale of securities.' " *U.S. SEC v. Landberg,* 836 F.Supp.2d 148, 153 (S.D.N.Y.2011) (Castel, J.) (quoting *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir.1999)). "The same elements required to establish a section 10(b) violation and a Rule 10b–5 violation suffice to establish a violation under sections 17(a)(1)–(3) of the [Securities] Act, with the exception that scienter is not required for the SEC to enjoin violations under subsections (a)(2) or (a)(3). The statutory language of [S]ection 17(a) is broad and bars any person in the offer of sale of any securities from directly or indirectly employing any device, scheme[,] or artifice to defraud." *Id.* (internal citations, brackets, quotations, and ellipses omitted). The Court addresses each element the SEC must prove in turn.

1. The Evidence Regarding the Elements of Scienter and In Connection with the Purchase or Sale of Securities is Undisputed

We turn first to the elements of (1) scienter and (2) in connection with the purchase or sale of securities. Here, the SEC has produced sufficient evidence to establish that

both elements have been met. SEC Br. at 7–12. Defendants neither dispute that they acted (1) with scienter and (2) in connection with the purchase or sale of securities, nor do Defendants provide any evidence to establish they did not act (1) with scienter and (2) in connection with the purchase or sale of securities. As such, there is no triable issue of fact as to the two elements of (1) scienter and (2) in connection with the purchase or sale of securities. *See Anderson*, 477 U.S. at 249, 106 S.Ct. 2505 (sufficient evidence in favor of the nonmoving party is necessary to create an issue of material fact). Therefore, the only issue left for the Court to determine is whether a genuine issue of fact exists as to whether Defendants' misrepresentations were material. For the reasons set forth below, the Court finds that Defendants' misrepresentations were material.

2. Defendants' Misrepresentations Were Material

[3] [4] A false statement is material if there is "a substantial likelihood that a reasonable investor would consider the information important in his [or her] decision-making process." *RMED Int'l, Inc. v. Sloan's Supermarkets, Inc.*, 185 F.Supp.2d 389, 399 (S.D.N.Y.2002) (Leisure, ***123** J.) (citing *Basic Inc. v. Levinson*, 485 U.S. 224, 231, 108 S.Ct. 978, 99 L.Ed.2d 194 (1988)). "In other words, there must exist a substantial likelihood that the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of information made available." *Id.* (internal quotations omitted) (citing *Basic*, 485 U.S. at 231–32, 108 S.Ct. 978). While a false statement "must have been one that would have assumed actual significance in a reasonable shareholder's decision-making process, there is no requirement that the fact would have been outcome determinative. Thus, a fact may be material even if it would not have changed an investor's ultimate decision." *Id.* (internal citations omitted).

Ultimately, "whether an alleged misrepresentation or omission is material necessarily depends on all of the relevant circumstances of the case, and materiality is a mixed question of both law and fact." *Id.* at 400 (citing *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 450, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976)). Since materiality is a fact intensive determination, "the Supreme Court has noted that materiality is particularly well suited for jury determination." *Id.* (citing *TSC Indus.*, 426 U.S. at 450, 96 S.Ct. 2126). However, summary judgment is appropriate where the alleged misstatements or omissions are so obviously important to an investor that reasonable minds could not differ on the question of their importance. *See e.g., id.; see also TSC Indus.*, 426 U.S. at 450, 96 S.Ct. 2126. Generally, "[p]rofit statements and financial reports are of particular interest to investors." *RMED Int'l, Inc.*, 185 F.Supp.2d at 400 (internal citations omitted). It is also "undisputed that investors rely on assets under management in deciding to which investment advisor to entrust their funds." *SEC v. Locke Capital Mgmt., Inc.*, 794 F.Supp.2d 355, 367 (D.R.I.2011) (Smith, J.) (citing *SEC v. K.W. Brown & Co.*, 555 F.Supp.2d 1275, 1309–10 (S.D.Fla.2007) (Johnson, J.)).

Here, the SEC argues that summary judgment is warranted because "Nadel's lies about his assets under management were unquestionably material" as a matter of law. SEC Br. at 9. The SEC claims that Nadel's statements were material because "[Nadel] gave assets under management prominent billing in [the] marketing materials as one of [the] prominent 'highlights,' " "devoted thought and energy to making his lies as persuasive as possible," and "pushed his lies on his clients relentlessly, even in the face of regulatory scrutiny [.]" *Id.* at 9–10. The SEC further argues that no genuine dispute as to the materiality of Nadel's misrepresentations exists because even "Nadel's clients have uniformly testified about the importance of Defendants' assets under management to their decisions to invest with them." *Id.* at 10–11.

Defendants argue that summary judgment is not warranted because the accurate amount of assets under management was disclosed in publicly-available documents. Specifically, Defendants argue that "Nadel disclosed [the] accurate [assets under management] in [the] publicly-filed Form ADV Part I" and "referred prospective clients ... to the S.E.C.'s public website to review [RIA's] publicly-available Form ADV Part I[.]" Defs.' Br. at 15. As such, Defendants claim that "the truth was staring these sophisticated clients in the face at the time they invested." *Id.* at 16.

[5] Summary judgment is appropriate in this case for several reasons. First, as established above, any reasonable investor would consider the accurate amount of assets under management to be a material fact to consider before investing. *See Locke Capital Mgmt., Inc.*, 794 F.Supp.2d at 366. This is so because any reasonable ***124** investor would need accurate disclosures about assets under management to correctly evaluate an asset manager's performance. Without such information, an

investor would have no baseline to determine the risk for his or her investment. Moreover, Defendants themselves have demonstrated the importance they attached to the information by not only admitting they sent marketing materials containing such misstatements, but also by highlighting the fact they managed upwards of $300 million in assets under management in the marketing materials. SDF at ¶ 13–16; *see also In re Facebook, Inc. IPO Sec. & Derivative Litig.*, 986 F.Supp.2d 487, 520 (S.D.N.Y.2013) (Sweet, J.) (noting the importance defendant places on statements lends itself to materiality).

Defendants cannot attempt to circumvent the issue of materiality by arguing that the misstatements were immaterial because the accurate information was publicly disclosed in RIA's Form ADV Part I filings. In the context of securities regulation, "[a]vailability elsewhere of truthful information cannot excuse untruths[.]" *Dale v. Rosenfeld*, 229 F.2d 855, 858 (2d Cir.1956); *see also SEC v. Mozilo*, 09–cv–3994, 2010 WL 3656068, at *9 (C.D.Cal. Sept. 16, 2010) ("[I]n an action that does not involve the fraud on the market presumption, that truthful information is available elsewhere does not relieve a defendant from liability for misrepresentations in a given filing or statement.") (internal citation omitted). As a result, Defendants cannot be excused from liability by arguing that misleading information is immaterial if disclosed elsewhere in publicly available documents. To hold otherwise would not only result in a disparity of information within the market but would also allow individuals to escape liability for misstatements so long as accurate information is set forth elsewhere in publicly available documents. The Court refuses to adopt such a policy. Moreover, Defendants cannot and do not provide any case law to establish otherwise.

Defendants also cannot attempt to circumvent the issue of materiality by claiming their clients knew the truth because they were referred to the Form ADV Part I filings. According to Defendants, "Nadel referred prospective clients them [*sic*] to the S.E.C.'s public website to review his firm's publicly-available Form ADV Part I, and his conversations with them confirmed that they had accessed this document." Defs.' Brief at 15. To substantiate this argument, the only evidence Defendants provide is Nadel's own self-serving statements. Nadel testified that "[d]uring the relevant period of this action, and prior to this period, whenever a prospective client contacted me to perform diligence on the [Investment Strategy] that my firm offered [ ], I referred them to the S.E.C.'s website to review the [RIA] Form ADV Part I, which contained RIA's assets under management." Dkt. 79 ("Declaration of Warren D. Nadel") at ¶¶ 2–3. Nadel also claimed that "[i]t was my understanding from my discussions with each of my clients, who were institutional investors, that they had obtained access to RIA's Form ADV Part I before the time of their investment. Many clients ... obtained access to and referenced RIA's Form ADV Part I for use in performing due diligence on the [Investment] Strategy." *Id.* (naming one client as an example).

[6] However, Defendants' only piece of evidence, the Declaration of Warren D. Nadel, must be stricken from the record with respect to statements made about assets under management. At all times leading up to the SEC's motion for summary judgment, Nadel invoked his Fifth Amendment privilege to avoid providing testimony and discovery on the issue of *125 assets under management. For example, Nadel refused to answer questions about why he made false statements about the assets under management, to whom he made them, and whether the statements were intentionally made. *See* SDF at ¶¶ 43–46. It was not until this instant motion that Nadel attempted to provide color on these issues with respect to what information was disclosed regarding assets under management.

In *United States v. Inc. Vill. of Island Park*, 888 F.Supp. 419, 431 (E.D.N.Y.1995) (Glasser, J.), the court found this similar cat-and-mouse game to be the basis for precluding affidavits at the summary judgment stage by holding "[i]n view of [Defendants'] repeated invocation of their Fifth Amendment privilege at deposition, their 'eleventh hour' attempt to avoid the consequences of asserting that privilege by submitting affidavits in opposition to the government's summary judgment motion constitutes an abuse of the discovery procedure which should not be permitted." Here, Nadel should not be allowed to "utilize[ ] the Fifth Amendment in an abusive or manipulative fashion by asserting and waiving the privilege when convenient and by persistently asserting his Fifth Amendment rights throughout the pendency of this proceeding and then seeking to waive or deny the existence of the privilege on the eve of [this motion for summary judgment]." *United States v. Certain Real Prop. & Premises Known as 4003–4005 5th Ave., Brooklyn, N.Y.*, 55 F.3d 78, 85–86 (2d Cir.1995) (internal citations, quotations, and brackets

omitted). Therefore, the Declaration of Warren D. Nadel must be precluded with respect to testimony concerning assets under management for purposes of this summary judgment motion. As a result and without any additional evidence, Defendants cannot argue that the misrepresentations about the assets under management were immaterial because Defendants referred prospective clients to the SEC's website to review the Form ADV Part I filings and had conversations with prospective clients to confirm they accessed the documents.

Second, summary judgment is also warranted because the evidence in the record establishes Defendants' clients believed the misstatements about assets under management to be material. SDF at ¶ ¶ 23–30. Although Defendants attempt to suggest their clients did not think the misstatements about the assets under management were material, the testimony Defendants rely on is not only taken out of context but is also misconstrued. For example, Defendants argue that "Mr. Donabedian of Winston Wade Capital has stated that the 'precise number of assets under management in the [Investment] Strategy' was not one of his 'primary concerns in investing in the [Investment] Strategy.' " Defs.' Brief at 16 (internal citations omitted). However, just because Mr. Donabedian may not have believed it to be a primary concern does not mean he found it to be immaterial. Something that is considered primary is not necessarily considered material without more.

Defendants also attempt to argue that the amount of assets under management was not relevant to Patricia Canning of LWCC because it was not on her list of due diligence questions. Defs.' Brief at 16–17. This, however, is wrong. When directly asked "[f]ocusing on the assets under management of over $370 million, is that something you focused on when doing diligence for the [Investment Strategy] [,]" Ms. Canning responded "[i]t was.... assets under management ... was always a criteria that we looked at when hiring any manager. We didn't want to be a big fish in a little pond. We wanted to make sure that there were enough assets under management so that if one client left, we wouldn't be the only one left. It was just ***126** a due diligence and a criteria that we had[.]" Dkt. 82–7, SDF Ex. 5 ("Deposition Transcript of Patricia Canning") at 207–208.

Similarly, Defendants also claimed that Blyth, one of its corporate clients, found the accurate amount of assets under management to be immaterial. Defs.' Brief at 17. However, Blyth's corporate representative, Jane F. Casey, testified to the opposite. When asked "if you had learned that in fact the assets under management that Nadel had was something more like a hundred to $120 million at that time, would that have been significant for you to know [,]" Ms. Casey responded "Yes." Dkt. 82–6, SDF Ex. 4 ("Deposition Transcript of Jane Casey") at 134. As such, there is no evidence in the record to suggest a single one of Defendants' clients found the misstatements about the amount of assets under management to be immaterial.

Based on the foregoing, the evidence is sufficient to establish that the misrepresentations about the amount of assets under management were so obviously important to investors that reasonable minds could not differ on the question of their importance. As a result, summary judgment is appropriate on the SEC's claims that Defendants violated Section 10(b) of the 1934 Exchange Act and Rule 10b–5 thereunder, and Section 17(a) of the 1933 Securities Act.

B. *Defendants Violated Sections 206(1) and (2) of the Advisers Act*

[7] The SEC also seeks to hold Defendants liable for their misrepresentations about the amount of assets under management under Sections 206(1) and (2) of the Advisers Act. SEC Br. at 4–5. For the reasons set forth below, summary judgment is appropriate on this issue as well.

Section 206 of the Advisers Act, as codified by 15 U.S.C. § 80b–6, provides in pertinent part:

> It shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly—(1) to employ any device, scheme, or artifice to defraud any client or prospective client; (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client[.]

15 U.S.C. § 80b–6.

It has been established that "[f]acts showing a violation Section 17(a) or 10(b) by an investment adviser will also support a showing of a Section 206 violation." *SEC v. Haligiannis,* 470 F.Supp.2d 373, 383 (S.D.N.Y.2007) (Holwell, J.) (citing *SEC v. Berger,* 244 F.Supp.2d 180, 188–89 (S.D.N.Y.2001) (Cote, J)). Because the Court has found summary judgment to be appropriate on the SEC's claims that Defendants violated Section 10(b) and 17(a), it follows that summary judgment is also appropriate on the SEC's claims that Defendants violated Sections 206(1) and (2) of the Advisers Act.

C. *Defendants Violated Section 206(3) of the Advisers Act*

The SEC also seeks summary judgment on its claims that Nadel and RIA violated Section 206(3) of the Advisers Act by conducting thousands of cross-trades among their clients and engaging in principal transactions with client accounts without providing required notice and obtaining client consent prior to each transaction. SEC Br. at 2. For the reasons that follow, the Court grants summary judgment on this issue.

Section 206(3) of the Advisers Act, as codified by 15 U.S.C. § 80b–6, provides in pertinent part:

> It shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate *127 commerce, directly or indirectly —(3) acting as principal for his own account, knowingly to sell any security to or purchase any security from a client, or acting as broker for a person other than such client, knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transaction. The prohibitions of this paragraph shall not apply to any transaction with a customer of a broker or dealer if such broker or dealer is not acting as an investment adviser in relation to such transaction[.]

15 U.S.C. § 80b–6. Unlike Section 206(1) and (2) of the Act, Section 206(3) "can be violated without a showing of fraud." *In the Matter of Geman,* SEC Release No.1924, Exchange Act Release No. 43,963, 74 SEC Docket 852, 2001 WL 124847, at *8 (Feb. 14, 2001), *aff'd sub nom. Geman v. SEC,* 334 F.3d 1183 (10th Cir.2003).

Here, the parties do not dispute that Defendants engaged in cross-trades. The parties only dispute (1) whether Nadel can be considered a broker within the meaning of Section 206(3), and (2) whether a general or blanket consent is sufficient to satisfy the conditions of Section 206(3). Therefore, these are the only issues for the Court to consider for purposes of summary judgment. The Court considers each issue in turn.

1. *Nadel is a Broker Under Section 206(3) of the Advisers Act*

Defendants argue that Nadel's actions did not violate Section 206(3) of the Advisers Act because he was not acting as a broker within the meaning of Section 206(3). To support their argument, Defendants rely on the SEC's Interpretation of Section 206(3) which states "[w]e have concluded that if an investment adviser receives no compensation (other than its advisory fee), directly or indirectly, for effecting a particular agency transaction between advisory clients, the adviser would not be 'acting as broker' within the meaning of Section 206(3)." *Interpretation of Section 206(3) of the Inv. Advisers Act of 1940,* SEC Release No. 1732, 67 SEC Docket 1344, 1998 WL 400409, at *5 (July 17, 1998). According to Defendants, Nadel was not acting as a broker within the meaning of Section 206(3) because "[Nadel] received no compensation besides his advisory fee for effecting the cross-trading pursuant to the strategy." Defs.' Br. at 10.

At the heart of Defendants' argument is the contention that since WDNC and RIA were acting as one business enterprise, the management and brokerage functions were not separate. As such, Nadel's compensation was comprised of trading commissions, and any brokerage fees would therefore be characterized as advisory fees, precluding Nadel from being deemed a broker for purposes of Section 206(3) liability. Defs.' Br. at 13.

[8] However, Defendants present conflicting testimony on whether or not Nadel should not be considered a broker for purposes of Section 206(3) liability. On the one hand, Defendants represented in the Program Package that WDNC and RIA were acting as one business enterprise by stating the Company has "not separated the management and brokerage functions." Program Package at CGC–SEC 298. However, in motion practice, Defendants have claimed that "[Section] 206(3) does not apply, because Nadel's broker-dealer *was a separate entity* 'not acting as an investment adviser.' " Defendants' Motion for Summary Judgment at 24 (emphasis added). Without any other evidence to suggest Nadel was not acting as a broker ***128** within the meaning of Section 206(3) of the Advisers Act (*i.e.* evidence to suggest that brokerage fees should be characterized as advisory fees), the Court cannot agree that Nadel was not acting as a broker.

Moreover, for purposes of summary judgment, the SEC has produced sufficient evidence to suggest that Nadel was acting as a broker for purposes of Section 206(3) liability. For example, the evidence suggests that Defendants' brokerage fees were not comprised of commissions but rather based on a "percentage of assets under management." Dkt. 73–27 ("Declaration of Richard G. Primoff") at Ex. AA. As such, Nadel's fees cannot be considered "advisory fees" because they would not be based off commissions, but rather based off a percentage of assets under management. Therefore, the Court concludes that Nadel was acting as a broker for purposes of Section 206(3) liability.

2. *Blanket Consent is Insufficient Under the Circumstances*

The SEC argues that a general or blanket consent is not sufficient to satisfy the requirements of Section 206(3). Rather, the SEC claims one must obtain transaction-specific written notice and consent prior to engaging in cross-trade activity. SEC Br. at 13–14. To support its argument, the SEC relies on its Interpretation of Section 206(3), which states "[b]y enacting [Section 206(3)], Congress recognized that self-dealing transactions pose particular risks for abuse by investment advisors. Rather than ban them, Congress imposed a strict transaction-by-transaction disclosure and consent regiment." *Id.* at 13; *see also Interpretation of Section 206(3) of the Inv. Advisers Act of 1940,* 1998 WL 400409, at *4. As such, the SEC claims Defendants were required to receive transaction-specific consent and written notice before engaging in any cross-trading.

In contrast, Defendants claim they satisfied the written notice and consent requirement of Section 206(3) by obtaining blanket consent for all cross-trades between clients and providing significant warnings that clients would be subject to cross-trades. As part of their argument, Defendants claim the SEC cannot rely on the SEC's Interpretation of Section 206(3)—the same source of authority Defendants relied on to argue that Nadel was not a broker for purposes of Section 206(3)—because "this informal interpretation is entitled to respect only to the extent it has the power to persuade, and is thus entitled to no deference, because it was not promulgated as a formal rule through notice-and-comment rulemaking and codified in the [Code of Federal Regulations]" Defs.' Br. at 11 (internal citations and quotations omitted).

Defendants should not be allowed to use the SEC's Interpretation of Section 206(3) as a sword in some instances (*i.e.* to find Nadel was not a broker for purposes of Section 206(3) liability) and then attack its opponents for using the same sword in other instances (*i.e.* that its interpretation that blanket consents are not sufficient has no power to persuade). What is sauce for the goose is sauce for the gander. Since Defendants have already conceded the authoritative and persuasive nature of the SEC's Interpretation of Section 206(3)—something uncontested by the SEC—this Court need not reach the issue of whether or not deference should be granted to the SEC's Interpretation of Section 206(3). The Court construes each party's reliance on the SEC's Interpretation of Section 206(3) as controlling for purposes of this motion.

[9] Because general consents are not sufficient as a matter of law under the SEC's Interpretation of Section 206(3), Defendants cannot escape liability for violating ***129** Section 206(3) by relying on blanket and general consents. *Interpretation of Section 206(3) of the Inv. Advisers Act of 1940,* 1998 WL 400409, at *4; *see also* Barry P. Barbash & David N. Solander, Am. L. Inst. Am. Bar. Assoc., Moving Toward A Functional Regulation of Broker–Dealers and Investment Advisers: What's on the Horizon, SR029 ALI–ABA 57, 67 (2009) ("Under a long-standing SEC position, the notice and consent must be given on a transaction-by-transaction basis and cannot be blanket consent."). Additionally, Defendants have not provided any case law to establish otherwise.

Defendants also attempt to argue that because the SEC has allowed global consents in certain situations to satisfy Section 206(3), the use of global consents in this case would not violate Section 206(3). Defs.' Br. at 12. Defendants' position is meritless. For example, Defendants claim that "17 C.F.R. § 275.206(3)–2 permits the use of global consent to prospectively authorize agency cross transactions in writing, where two different investment advisers are involved. The S.E.C.'s Interpretation of Section 206(3) provides that 17 C.F.R. § 275.206(3)–2 is a *non-exclusive* safe harbor for certain ... transactions[.]"[2] *Id.* at 12 (internal quotations omitted; emphasis in original). However, Defendants do not meet the necessary requirements to trigger 17 C.F.R. § 275.206(3)–2. Under Section 275.206(3)–2(a)(3), Defendants were required to "send[ ] to each such client, at least annually, and with or as part of any written statement or summary of such account from the investment adviser or such other person, a written disclosure statement identifying the total number of such transactions during the period since the date of the last such statement or summary, and the total amount of all commissions or other remuneration received or to be received by the investment adviser or any other person relying on this rule in connection with such transactions during such period." Here, Defendants have presented no evidence to suggest they provided clients with either (1) an annual statement of the number of cross-transactions, or (2) the total amount of commissions received in connection with the number of cross-transactions. Although Defendants claim that certain trade confirmations sent to clients advised them that 90% of transactions were cross-trades, this is simply not the case. *See e.g.*, SDF at ¶ 68; Dkt. 83–4, Ex. 11 at CGC–SEC 00001867. Nothing in the documents suggests that 90% of the transactions were cross-trades. As a result, having failed to meet these requirements, Defendants cannot avail themselves of Section 275.206(3)–2's safe harbor.

Based on the foregoing, summary judgment is appropriate on the SEC's claims that Defendants violated Section 206(3) of the Advisers Act.

C. *Defendants Violated Rule 10b–10 of the 1934 Exchange Act*

The SEC also seeks summary judgment on its claims that Nadel and WDNC violated Rule 10b–10 of the 1934 Exchange Act by falsely disclosing the capacity in which WDNC was acting. For the reasons set forth below, the Court grants summary judgment on this issue.

Rule 10b–10 requires "that the broker or dealer disclose the date, time, and price of the transaction; the broker's or dealer's role as either agent or principal; and other information based on whether the broker or dealer is an agent or principal." ***130** *Press v. Chem. Inv. Servs. Corp.*, 166 F.3d 529, 534 (2d Cir.1999) (citing 17 C.F.R. § 240.10b–10). Defendants may either disclose this information directly to the customers, or may "rely on the fund prospectuses and other documents *publicly* filed with the SEC to satisfy their Rule 10b–10 disclosure obligations." *Press v. Quick & Reilly, Inc.*, 218 F.3d 121, 128–29 (2d Cir.2000) (emphasis added).

Here, the SEC argues that Nadel and WDNC violated Rule 10b–10 of the 1934 Exchange Act for the period of March 1, 2008 to December 31, 2009 by "falsely stat[ing] that WDNC had acted as agent solely for the client in an over-the-counter market transaction—they did not disclose either that WDNC had acted as agent for both sides to the transaction, or as principal in some of the transactions[.]" SEC Br. at 18.

Defendants claim that no violation of Rule 10b–10 occurred because "Nadel satisfied Rule 10b–10 by having each client sign a blanket 'Consent and Trading Authorization' for cross-trading in Nadel's Program Package." Defs.' Br. at 18–19. However, Defendants' argument misses the mark as there is no evidence in the record to suggest that Nadel's "Consent and Trading Authorization" form was *publicly* filed with the SEC. *See Quick & Reilly, Inc.*, 218 F.3d at 128–29.

[10] Summary judgment is warranted because the SEC has presented sufficient evidence to establish that WDNC failed to disclose it was acting as either an agent for both sides to the transaction or as a principal in some of the transactions as required by Rule 10b–10. To support its argument, the SEC relies on the Declaration of Michael Fioribello who states that "[f]or the 334 transactions identified.... I retrieved 257 trade confirmations (the remainder were apparently not produced). All of the trade confirmations were marked either with the code #08,' '08P,' #61,' '61P,' or, in one instance, '31P,' all of which, I understand, disclose to the customer that the transaction was handled by the broker in an 'agency' capacity, not

a principal capacity." Dkt. 76 ("Declaration of Michael Fioribello") at ¶ 16. Other documents provided by the SEC confirm the same. *See e.g.*, Declaration of Richard G. Primoff at Ex. DD (trade confirmation from June 2008 revealed a code of 61, which meant that WDNC solely acted as an "agent" as opposed to "principal" during relevant period).

Defendants do not even attempt to dispute that trade confirmations during this period failed to acknowledge that WDNC acted as either an agent or both sides to the transaction or as a principal in some of the transactions. *See* SDF at ¶ 63. As a result, no genuine issue of material fact exists. See *Matsushita Electric Indus. Co., Ltd.*, 475 U.S. at 587, 106 S.Ct. 1348 (once the moving party demonstrates that no genuine issue of material fact exists, the non-moving party must come forward with specific facts to establish a genuine issue for trial). Therefore, summary judgment is appropriate on the SEC's claims that Defendants violated 10b–10 of the 1934 Exchange Act.

D. *Resolution of Relief*

At this stage, the Court will not determine what, if any, relief or damages the SEC is entitled to receive. Accordingly, the Court respectfully directs Magistrate Judge Tomlinson to hold a hearing to determine the appropriate relief or damages including but not limited to the determination of a permanent injunction, disgorgement, pre-judgment interest, and any civil penalties. *See e.g., SEC v. Renaissance Capital Mgmt., Inc.*, 09–CV–01848, 2003 WL 23353464, at *1 (E.D.N.Y. Aug. 25, 2003) (Wall, Mag. J.), *report and recommendation adopted,* No. 00–CV–1818, 2003 WL 23353490 (E.D.N.Y. Oct. 31, 2003) ***131** (Platt, J.) *aff'd sub nom. SEC v. Andrescu,* 117 Fed.Appx. 160 (2d Cir.2004).

CONCLUSION

For the reasons stated above, Plaintiff's motion for partial summary judgment, Dkt. 71, is GRANTED in its entirety. Accordingly, Defendants' motion for summary judgment, Dkt. 81, is DENIED in its entirety. Magistrate Judge Tomlinson is respectfully directed to hold a hearing on damages consistent with this opinion.

SO ORDERED.

All Citations

97 F.Supp.3d 117

Footnotes

1 A Form ADV is a required submission to the SEC by a professional investment advisor that specifies the investment style, assets under management, and key officers of the firm.

2 This is yet another example where Defendants attempt to use the sword of the SEC's Interpretation of Section 206(3) to avoid liability.

End of Document

EXHIBIT 3

2016 WL 639063
United States District Court,
E.D. New York.

Securities and Exchange Commission, Plaintiff,
v.
Warren D. Nadel, Warren D. Nadel & Co., and Registered Investment Advisers, LLC, Defendants,
and
Katherine Nadel, Relief Defendant.

CV 11–0215 (WFK) (AKT)
|
Signed February 11, 2016

Attorneys and Law Firms

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REPORT AND RECOMMENDATION

A. KATHLEEN TOMLINSON, U.S. Magistrate Judge

I. *PRELIMINARY STATEMENT*

*1 Plaintiff Securities and Exchange Commission ("Plaintiff" or "the Commission"), brought this civil enforcement action against Defendants Warren D. Nadel ("Nadel"), Warren D. Nadel & Co. ("WDNC") and Registered Investment Advisers, LLC ("RIA") (collectively, "the Defendants"), and Relief Defendant Katherine Nadel, seeking damages and injunctive relief for alleged violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), Sections 204, 206(1), (2) and (3) and 207 of the Investment Advisers Act of 1940 ("Advisers Act") as well as the applicable rules promulgated thereunder. *See generally* Amended Complaint ("Amend.Compl.") [DE 11].

On March 31, 2015, Judge Kuntz issued a Decision and Order granting Plaintiff's motion for partial summary judgment and denying Defendants' cross-motion for summary judgment. *See* DE 100. In rendering his decision, Judge Kuntz further directed this Court to "hold a hearing to determine the appropriate relief or damages including but not limited to the determination of a permanent injunction, disgorgement, pre-judgment interest, and any civil penalties." *Id.* at 21.

In accordance with Judge Kuntz's directive, this Court conducted an evidentiary hearing on the issue of damages over four days, from July 20, 2015 through July 23, 2015. *See* DE 102. The Findings of Fact and Conclusions of Law, set forth below and as required by Rule 52(a) of the Federal Rules of Civil Procedure, constitute this Court's Report and Recommendation to Judge Kuntz.

II. *BACKGROUND*

A. Judge Kuntz's Summary Judgment Decision

1. Violation of Section 10(b) of the Exchange Act and Rule 10b–5 thereunder, and Section 17(a) of the Securities Act

In his decision, Judge Kuntz first addressed Plaintiff's claims that Defendants' violated Section 10(b) of the Exchange Act, Rule 10b–5 thereunder and Section 17(a) of the Securities Act which focused on whether "Defendants misrepresented to clients and to prospective clients the amount of assets they had under management." *See S.E.C. v. Nadel,* 97 F.Supp.3d 117, 122 (E.D.N.Y.2015). [1] In that regard, Judge Kuntz enumerated the requisite elements giving rise to these violations, namely, that a defendant "(1) made a material misrepresentation or a material omission as to which he had a duty to speak, or used a fraudulent device; (2) with scienter; (3) in connection with the purchase or sale of securities." *Id.* (internal quotations and citation omitted). Judge Kuntz further pointed out that these same elements "suffice to establish a violation under sections 17(a)(1)-(3) of the [Securities] Act, with the exception that scienter is not required to enjoin violations under subsections (a)(2) or (a)(3)." *Id.* (alteration in original).

*2 Turning to the second element ("scienter") and the third element ("in connection with the purchase or sale of securities"), Judge Kuntz found that "the SEC has produced sufficient evidence to establish that both

elements have been met." *Id.* Specifically, Judge Kuntz held that "no triable of issue of fact [existed] as to the[se] two elements" since "Defendants neither dispute that they acted (1) with scienter and (2) in connection with the purchase or sale of securities, nor do Defendants provide any evidence to establish they did not act(1) with scienter and (2) in connection with the purchase or sale of securities." *Id.*

Having found no triable issue of fact with respect to elements (2) and (3), Judge Kuntz next focused on whether a triable issue of fact existed regarding the first element – *i.e.*, whether Defendants' misrepresentations were material. *Id.* In this regard, Judge Kuntz determined that no triable issue of fact existed and that

> [s]ummary judgment is appropriate in this case for several reasons. First, as established above, any reasonable investor would consider the accurate amount of assets under management to be a material fact to consider before investing. This is so because any reasonable investor would need accurate disclosures about assets under management to correctly evaluate an asset manager's performance. Without such information, an investor would have no baseline to determine the risk for his or her investment. Moreover, Defendants themselves have demonstrated the importance they attached to the information by not only admitting they sent marketing materials containing such misstatements, but also by highlighting the fact they managed upwards of $300 million in assets under management in the marketing materials.
>
> * * *
>
> Second, summary judgment is also warranted because the evidence in the record establishes Defendants' clients believed the misstatements about assets under management to be material.

Nadel, 97 F.Supp.3d at 123–25 (internal citation omitted). In light of these findings, Judge Kuntz determined that "the misrepresentations about the amount of assets under management were so obviously important to investors that reasonable minds could not differ on the question of their importance. As a result, summary judgment is appropriate" with respect to those claims. Id. at 126.

2. Violation of Sections 206(1) and 206(2) of the Advisers Act

Similar to their claims under Section 10(b) of the Exchange Act, Rule 10b–5 thereunder and Section 17(a) of the Securities Act, Plaintiff also sought to "hold Defendants liable for their misrepresentations about the amount of assets under management under Sections 206(1) and (2) of the Advisers Act." *Id.* After reviewing the language of the controlling section of the Advisers Act, Judge Kuntz noted that "[i]t has been established that '[f]acts showing a violation [of] Section 17(a) or 10(b) by an investment adviser will also support a showing of a Section 206 violation.' " *Id.* (internal citation omitted) (second alteration in original). As such, Judge Kuntz determined that "because the Court has found summary judgment to be appropriate on the SEC's claims that Defendants violated Section 10(b) and 17(a), it follows that summary judgment is also appropriate on the SEC's claims that Defendants violated Sections 206(1) and (2) of the Advisers Act." *Id.*

3. Violation of Section 206(3) of the Advisers Act

Judge Kuntz next addressed the Commission's allegation that "Nadel and RIA violated Section 206(3) of the Advisers Act[2] by conducting thousands of cross-trades among their clients and engaging in principal transactions with client accounts without providing required notice and obtaining client consent prior to each transaction." *Id.* at 126. Since neither party disputed the fact that "Defendants engaged in cross-trades" in the first instance, Judge Kuntz determined that the only issues before the Court were "(1) whether Nadel can be considered a broker within the meaning of Section 206(3), and (2) whether a general or blanket consent is sufficient to satisfy the conditions of Section 206(3)." *Id.* at 127.

*3 Turning to the first issue of whether Nadel could be considered a broker within the meaning of Section 206(3), Judge Kuntz pointed out Defendants' "conflicting testimony on whether or not Nadel should not be considered a broker for purposes of Section 206(3) liability." Coupled with the fact that Defendants did not provide "any other evidence to suggest Nadel was not acting as a broker within the meaning of Section 206(3) of the Advisers Act," Judge Kuntz did not agree that "Nadel

was not acting as a broker." *Id.* at 128. Further, Judge Kuntz determined that the Commission

> produced sufficient evidence to suggest that Nadel was acting as a broker for purposes of Section 206(3) liability. For example, the evidence suggests that Defendants' brokerage fees were not comprised of commissions but rather based on a "percentage of assets under management." As such, Nadel's fees cannot be considered "advisory fees" because they would not be based off commissions, but rather based off a percentage of assets under management.

Id. Based upon Defendants' conflicting testimony and Nadel's own lack of evidence in light of the Commission's affirmative evidence, Judge Kuntz concluded that "Nadel was acting as a broker for purposes of Section 206(3) liability." *Id.*

The next issue addressed by Judge Kuntz was whether the Defendants' obtaining blanket consents prior to engaging in cross-trading was sufficient for compliance with Section 206(3) of the Advisers Act. *Id.* Relying on the Commission's interpretation of Section 206(3)—an interpretation which was "controlling for purposes of this motion"—Judge Kuntz found that "general consents are not sufficient as a matter of law under the SEC's Interpretation of Section 206(3)" and, consequently, "Defendants cannot escape liability for violating Section 206(3) by relying on blanket and general consents." *Id.* 128–29. Despite this finding, Defendants asserted that "because the SEC has allowed global consents in certain situations to satisfy Section 206(3), the use of global consents in this case would not violate Section 206(3)." *Id.* Although recognizing that the Commission's "Interpretation of Section 206(3) provides that 17 C.F.R. § 275.206(3)–2 is a *non-exclusive* safe harbor for certain ... transactions," *id.* at 129 (emphasis and ellipses in original), Defendants did not present any evidence establishing that they met the criteria needed to take advantage of the safe harbor provision. *Id.*

In light of the above information, Judge Kuntz determined that "summary judgment is appropriate on the SEC's claims that Defendants violated Section 206(3) of the Advisers Act." *Id.*

4. Violation of Rule 10b–10 of the Exchange Act

The Commission also sought summary judgment on its claim that Nadel and WDNC violated Rule 10b–10[3] of the Exchange Act based upon "falsely disclosing the capacity in which WDNC was acting." *Id.* Specifically, the Commission claimed that "Nadel and WDNC violated Rule 10b–10 of the 1934 Exchange Act for the period of March 1, 2008 to December 31, 2009 by 'falsely stat[ing] that WDNC had acted as agent solely for the client in an over-the-counter market transaction—they did not disclose either that WDNC had acted as agent for both sides to the transaction, or as principal in some of the transactions[.]' " *Id.* at 130. (internal citation omitted) (alterations in original). In enumerating the criteria necessary to satisfy Rule 10b–10, Judge Kuntz noted that "Defendants may either disclose this information directly to the customers, or may 'rely on the fund prospectuses and other documents *publicly* filed with the SEC to satisfy their Rule 10b–10 disclosure obligations.' " *Id.* (internal citation omitted) (emphasis in original).

*4 In finding that summary judgment was appropriate on the Rule 10b–10 violation, Judge Kuntz found that "the SEC has presented sufficient evidence to establish that WDNC failed to disclose it was acting as either an agent for both sides to the transaction or as a principal in some of the transactions as required by Rule 10b–10." *Id.* Further, Judge Kuntz pointed out that Defendants never disputed the fact that "trade confirmations during this period failed to acknowledge that WDNC acted as either an agent [f]or both sides to the transaction or as a principal in some of the transactions" and that, as a result, "no genuine issue of material fact exists." *Id.*

B. Relevant Procedural History

Following Judge Kuntz's decision, which granted Plaintiff's motion for partial summary judgment, and which further directed this Court to hold a hearing on damages, *see* DE 100, this Court scheduled a telephone conference for April 10, 2015 in order to set a date for the damages hearing. *See* April 6, 2015 Electronic Order. During the re-scheduled conference, the Court set the

damages hearing for the week of July 20, 2015. *See* DE 102.

The hearing was conducted over four days, from July 20–23 2015. The Court heard testimony from the following witnesses: (1) Richard Anderson; (2) William Hedges; (3) Michael Fioribello; (4) Jane Casey; (5) Walter Boilieu; (6) Patricia Canning; (7) Warren Nadel; and (8) Katherine Nadel. At the conclusion of the hearing, the Court set a schedule for post-hearing briefs. *See* DE 124; DE 126.

III. *FINDINGS OF FACT AND CONCLUSIONS OF LAW*

The Commission seeks to "deter future violations of the securities laws, and to deprive Defendants of the illicit proceeds of their fraud. To that end, the Commission seeks: (1) permanent injunctions; (2) disgorgement and prejudgment interest, jointly and severally, on Defendants' ill-gotten gains; and (3) third-tier civil penalties." *See* Plaintiff Securities and Exchange Commission's Pre–Hearing Brief on Remedies ("Pl.'s Pre–Hearing Br.") [DE 107], at 2. The Court will address each of these forms of relief in turn.

A. Injunctive Relief

1. Applicable Law

Section 20(b) of the Securities Act, 15 U.S.C. § 77t(b), Section 21(d)(1) of the Exchange Act, 15 U.S.C. § 78u(d)(1), and Section 209(d) of the Advisers Act, 15 U.S.C. § 80b–9(d), authorize injunctive relief for violations of the securities laws. Specifically, Section 20(b) of the Securities Act provides that

> [w]henever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this subchapter, or of any rule or regulation prescribed under authority thereof, the Commission may, in its discretion, bring an action in any district court of the United States, or United States court of any Territory, to enjoin such acts or practices, and upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond.

15 U.S.C. § 77t(b). Section 21(d) of the Exchange Act similarly provides that

> [w]henever it shall appear to the Commission that any person is engaged or is about to engage in acts or practices constituting a violation of any provision of this chapter, the rules or regulations thereunder, the rules of a national securities exchange or registered securities association of which such person is a member or a person associated with a member, the rules of a registered clearing agency in which such person is a participant, the rules of the Public Company Accounting Oversight Board, of which such person is a registered public accounting firm or a person associated with such a firm, or the rules of the Municipal Securities Rulemaking Board, it may in its discretion bring an action in the proper district court of the United States, the United States District Court for the District of Columbia, or the United States courts of any territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond.

*5 15 U.S.C. § 78u(d)(1). Likewise, Section 209(d) of the Adviser's Act states that

> [w]henever it shall appear to the Commission that any person has engaged, is engaged, or is about to engage in any act or practice constituting a violation of any provision of

> this subchapter, or of any rule, regulation, or order hereunder, or that any person has aided, abetted, counseled, commanded, induced, or procured, is aiding, abetting, counseling, commanding, inducing, or procuring, or is about to aid, abet, counsel, command, induce, or procure such a violation, it may in its discretion bring an action in the proper district court of the United States, or the proper United States court of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this subchapter or any rule, regulation, or order hereunder. Upon a showing that such person has engaged, is engaged, or is about to engage in any such act or practice, or in aiding, abetting, counseling, commanding, inducing, or procuring any such act or practice, a permanent or temporary injunction or decree or restraining order shall be granted without bond

15 U.S.C. § 80b–9.

"The Supreme Court has viewed injunctive relief as necessary in [securities] actions for the basic protection of the investing public." *S.E.C. v. Bonastia,* 614 F.2d 908, 913 (3d Cir.1980); *see S.E.C. v. China Energy Sav. Tech., Inc.,* No. 06–CV–6402, 2008 WL 6572372, at *7 (E.D.N.Y. Mar. 28, 2008). In addition, in an "action involving 'remedial statutes,' such as the federal securities laws, a district court has broad discretion to enjoin future violations of law where past violations have been shown." *S.E.C. v. U.S. Environmental, Inc.,* No. 94 Civ. 6608, 2003 WL 21697891, at *24 (S.D.N.Y. Jul. 21, 2003).

In determining whether injunctive relief is warranted in a particular case, courts must make a determination whether there exists "a substantial likelihood of future violations of illegal securities conduct." *S.E.C. v. Tavella,* 77 F.Supp.3d 353, 359 (S.D.N.Y.2015); *S.E.C. v. Cavanagh,* 155 F.3d 129, 135 (2d Cir.1998) ("*Cavanagh I* ") (recognizing that injunctive relief is appropriate where the "SEC makes a substantial showing of likelihood of success as to both a current violation and the risk of repetition"); *but see U.S. Environmental, Inc.,* 2003 WL 21697891, at *24 (finding injunctive relief warranted upon a showing of "reasonable likelihood of future violations"); *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *7 (recognizing that "[i]njunctive relief is appropriate when there is a 'realistic likelihood of recurrence' of the violations") (internal citation omitted). In order to make a finding of "substantial likelihood of future violations," courts consider the following factors: (1) that the defendant has been found liable for illegal conduct; (2) the degree of scienter involved; (3) whether the infraction is an isolated occurrence; (4) whether defendant continues to maintain that his past conduct was blameless; and (5) whether, because of his professional occupation, the defendant might be in a position where future violations could be anticipated. *Tavella,* 77 F.Supp.3d at 359; *S.E.C. v. Commonwealth Chem. Secs., Inc.,* 574 F.2d 90, 100 (2d Cir.1978); *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *7; *S.E.C. v. Wyly,* 56 F.Supp.3d 394, 407 (S.D.N.Y.2014). Further, a permanent injunction is "particularly within the court's discretion where a violation was founded on systematic wrongdoing rather than an isolated recurrence." *S.E.C. v. First Jersey Secs., Inc.,* 101 F.3d 1450, 1477 (2d Cir.1996) ("*First Jersey* ") (internal quotations omitted); *Tavella,* 77 F.Supp.3d at 359; *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *8.

2. Application to the Facts

i. Liability for Illegal Conduct

*6 There is no dispute that Judge Kuntz found the Defendants violated the securities laws. Specifically, Judge Kuntz determined that Defendants violated Section 10(b) of the Exchange Act, Rule 10b–5 thereunder, Section 17(a) of the Securities Act, Sections 206(1), 206(2) and 206(3) of the Advisers Act and Rule 10b–10 of the Exchange Act. *See Nadel,* 97 F.Supp.3d at 117. As such, this factor weighs in favor of granting injunctive relief.

ii. Degree of Scienter

Defendants acted with scienter. At the summary judgment phase of this case, Judge Kuntz noted that Defendants "neither dispute[d] that they acted [ ] with scienter ... nor [did they] provide any evidence to establish they did not act [ ] with scienter." *Nadel*, 97 F.Supp.3d at 122. Although Judge Kuntz did not make a finding as to the degree of scienter involved, the Court finds for the reasons which follow that Defendants acted with a high degree of scienter.

First, for more than 18 months, Nadel and WDNC failed to provide accurate trading confirmations. *Id.* at 130. They did not disclose that WDNC had acted as agent for both sides to the transaction or as principal in some of the transactions. *Id.* The fact that they did so, notwithstanding their awareness of the inaccuracy, illustrates that the Defendants acted with a high degree of scienter.[4] Nadel testified at the hearing that despite the change in the format of trade confirmations as of March 1, 2008 (which ceased to include transaction codes reflecting that Nadel was acting as the agent for both the buyer and the seller), Nadel nevertheless failed to alert his clients as to the inaccuracy. *See* Testimony of Warren Nadel at July 2015 Damages Hearing at 558:17–559:1.[5] Indeed, when asked whether it was important to "look at the capacity in which the trade confirmation was report[ed]," Nadel answered "no." *Id.* at 570:3–6. The testimony further demonstrates that Nadel's failure to alert his clients to the inaccuracy of these confirmations continued for an extended period of time and was never corrected. For example, Nadel testified:

> Q: [Y]ou also knew for an extended period of time, from March 2008 to at least September of 2009 or perhaps later, you actually knew the trade confirmations that were going out were incorrectly reporting your capacity in which you were acting on behalf of your clients, correct?
>
> A: Yes.
>
> Q: And you never alerted your advisory clients to that fact, right?
>
> A: No.

Hrg. Tr. at 570:7–16. Nadel also testified that after an audit was performed by the Commission in late 2009, he got a call from the back office people at RBC and was provided with an "alpha code" that would enable him "to correct the situation by creating the information in English on the front of the confirm," which Nadel says he "implemented immediately." *Id.* at 565. However, when asked whether he was "aware of any trade confirmation that has th[e] correction that [he] referred to for any date prior to late March 2010," Nadel was unable to provide a direct response, stating only that "well, *I have no idea* when it actually was implemented." When pressed further, Nadel simply stated "I have no recollection as to when it was [implemented.]" *Id.* at 565:25–566:7 (emphasis added).

*7 Second, the magnitude, duration and persistent and ongoing misrepresentation concerning the amount of the Assets Under Management ("AUM"), coupled with the importance placed upon that figure by Defendants' clients, further supports a finding that Defendants' acted with a high degree of scienter.[6] Testimony from Defendants' clients revealed that the amount of AUM was an important criterion in determining whether to invest in Defendants' investment strategy. For example, Richard Anderson, former Treasurer of the Continental Grain Company ("CGC"), testified that AUM was an important benchmark because he "wanted to get an idea of the size of the firm ... so that [he] didn't have to worry about [his company's] investment ... [constituting] 25 percent of [Defendants'] assets under management." Hrg. Tr. at 45:18–21. Similarly, Jane Casey, Chief Financial Officer of Blyth, Inc., testified that the total amount of Defendants' AUM was an important investment consideration because that AUM figure would directly impact how much her company would have invested with Defendants. *Id.* at 248:4–10. According to Casey, if the AUM figure was "significantly less" than the amount Defendants represented, she would have been concerned in light of her company's $10 million investment. *Id.* at 248:2–10. Likewise, Patricia Canning, Assistant Vice President and Senior Portfolio Manager of the Louisiana Worker's Compensation Corporation ("LWCC"), testified that based upon the $370 million AUM figure proffered by Defendants, she "thought it would be an acceptable type of strategy for LWCC" to invest in. *Id.* at 364: 7–16.

Although Nadel refused to answer any questions during the hearing pertaining to AUM—instead invoking his rights under the Fifth Amendment—*id.* at 532:5–7; 585;12–13, a description of Defendants' investment strategy, as provided to Blyth, Inc. in 2007, highlights that Defendants were touting their AUM to be $404.93

million.[7] *Id.* at 532:5–7; 585:12–13; Pl.'s Hrg. Ex. 22 at 17[8]; Hrg. Tr. at 241:23–24 (noting that Blyth, Inc. invested with Defendants in September 2007). Moreover, these same inflated AUM claims were made to other potential clients via email during this same time period. *See* Pl.'s Hrg. Ex. 111 at 37 (Defendants' investment strategy brochure provided by email to Oregon Mutual Insurance Company ("Oregon Mutual") in 2007 highlighting AUM as $404.93 Million); Pl.'s Hrg. Ex. 112 at 1–2 (additional marketing materials provided by Defendants to Oregon Mutual by email in late 2007 identifying AUM as $411.63; million); Pl.'s Hrg. Ex. 113 at 1–2 (marketing materials sent to Oregon Mutual in early 2008 identifying the amount of AUM as $414.79 million); *see also* Hrg. Tr. at 109:20113:12 (William Hedges testimony).

Even an investigatory inquiry by the Commission on October 28, 2009—which sought substantiation for the statement on Defendants' website claiming that Defendant WDNC was managing over $400 million—did not dissuade Defendants from continuing to misrepresent AUM to clients.[9] *See* Pl.'s Hrg. Ex. 35 (investigatory inquiry from the Commission regarding Defendants' AUM representation); Pl.'s Hrg. Ex. 25 at 1–3 (email dated January 22, 2010 from Nadel to Hal Pasetsky and Adam Feldman concerning a revised brochure containing an AUM figure of $308.70 million); Pl.'s Hrg. Ex. 36 (email dated February 3, 2010 from WDNC to Brandon Dees at Goldman Sachs representing AUM at "[o]ver $300 Million"); Hrg.Tr. at 585:18–589:20; Pl.'s Hrg. Ex. 19 (chart denoting numerous emails misrepresenting Defendants' AUM after October 2009); Pl.'s Hrg. Ex. 135 (underlying emails referenced in Pl.'s Hrg. Ex. 19).

*8 Further, despite the numerous emails sent by Defendants to clients and prospective clients between January 2007 and March 2010 misrepresenting Defendants' AUM, *see* Pl.'s Hrg. Ex. 19, Nadel was not truthful in written correspondence to the Commission dated September 14, 2009 in which he stated

> [t]his is to serve as my written confirmation that the above firm does not correspond via email to any existing or prospective clients. Correspondence of this nature occurs via telephone conversations or face-to-face meetings or in writing. In the event that there is any business related email correspondence, the firm policy is to print a copy and retain in a designated file if deemed to be of significance of to be deleted if determined to be otherwise.

Pl.'s Hrg. Ex. 161; Hrg. Tr. at 581:21–582:8. During the hearing, when confronted with this correspondence, Nadel confirmed that he did in fact routinely communicate with existing and prospective clients via email and when pressed as to why he made this false statement, his only response was that he had no recollection as to his reasoning. *See* Hrg. Tr. at 583:21–23; 584:15–17.

Third, the overall scope and duration of Defendants' failure to provide proper transaction-by-transaction notice and consent with respect to the cross-trading of client accounts evidenced a knowing disregard for Defendants' fiduciary obligations to their clients. This factor further illustrates Defendants' high degree of scienter.[10] Nadel's testimony at the hearing establishes that at least as of 2007, executing 90 percent or more of trades as cross-trades between client accounts was necessary to the functioning of Nadel's investment strategy. However, despite this fact, Defendants never properly apprised clients, through transaction-by-transaction notice and consent, that cross-trading would encompass the primary means of investment execution. For instance, the following portion of the hearing transcript illustrates these facts:

> Q: Did there come no point during th[e] period from January 1, 2007, to February 29, 2008, when you were aware that [cross-trading] had been the mainstay of your strategy for a period of time?
>
> A: I realized we were doing a predominant amount of our trading amongst clients. Yes.

Hrg. Tr., at 527:3–8.

* * *

> Q: Don't you think the switch in your strategy from the 2005–2006 period, from executing trades in the marketplace to executing 90 percent or more of

them only between your clients at prices you set, was a significant-enough change to include in your account disclosure forms, your program packages, your brochures, or your form ADV Part 2?

A: I believe I felt comfortable enough with the disclosure in the documents, themselves that indicated that there was a distinct possibility that there would be cross-trading amongst clients, and it was a blanket expression to that effect. I did not specify a percentage in that statement that was signed off on by each client.

Id. at 522:21–523:8. In addition, although Nadel stated that engaging in such rampant cross-trading provided "a better alternative than other options that were available ... in the marketplace," he had no recollection as to why this information was not included in any brochures distributed to prospective clients. *Id.* at 523:23–524:6. Indeed, even when Nadel testified that he alone was engaging in the cross-trading, *see id.* at 527:7–11; 536:5–7, he refused to concede that as of March 2009 more than 90 percent of the trades executed were cross-trades, despite having agreed in a Stipulation dated July 17, 2015 to that overall figure. *See id.* at 535:23–536:11; July 17, 2015 Stipulation at ¶ 2; Hrg. Tr. at 3:24–5:13 (parties verbally enter the Stipulation into the record). Nadel offered only evasive and conflicting testimony on this point, claiming simply that he knew "it was over 50 percent" and contradicting his prior sworn testimony where he testified to the "over 90 percent" figure. *See* Hrg. Tr. at 536:8–17; Pl.'s Hrg. Ex. 140, at 40 (sworn investigatory testimony of Warren Nadel before the Commission on March 23, 2010).

***9** Further, Defendants' clients Anderson, Hedges, Casey, Boilieu and Canning indicated at the hearing that the overall amount of cross-trades conducted constituted an important figure which would have determined, in part, whether they would have invested assets with the Defendants. *See* Hrg. Tr. at 47:16–48:6; 115:19–116:24; 245:9–246:3; 330:12–23; 366:6–367:18. Despite this testimony, when Nadel was asked "[w]ell isn't it a fact, sir, that you knew that if you disclosed to clients [the amount of cross-trades] before they invested, that they never would have invested with you," he responded "[n]ot really." *Id.* at 524:7–10.

In light of the foregoing information, the Court finds that Defendants acted with a high degree of scienter. This factor weighs in favor of granting injunctive relief.

iii. Recurring Nature of Conduct

The evidence offered at the damages hearing establishes that: (1) Defendants' cross-trading occurred at least from January 1, 2007 through December 31, 2009, *see id.* at 180:14181:7 (Michael Fioribello testimony); Pl.'s Hrg. Ex. 9 (summary of Defendants' cross-trading activity from January 1, 2007 to February 29, 2008); Pl.'s Hrg. Ex. 10 (summary of Defendants' cross-trading activity from March 1, 2008 through December 31, 2008); (2) Defendants' material misrepresentations concerning their overall AUM occurred from January 2007 through April 2010, *see* Pl.'s Hrg. Exs. 19, 135; and (3) from March 2008 to at least December 2009 Defendants knew that the trade confirmations being sent to clients were inaccurate, but failed to alert clients or correct the inaccuracy. *See* Hrg. Tr. at 570:7–16. As such, the Court finds that Defendants' misconduct was ongoing and did not involve a single isolated incident. Consequently, this factor also weighs in favor of injunctive relief.

iv. Appreciation of Wrongdoing

Based upon the testimony and evidence adduced at the hearing, the Court finds that Defendants have little appreciation of the wrongdoing in which they have been found to have engaged. During his testimony, Nadel showed both indifference and a somewhat cavalier attitude regarding the underlying violations. For example, with respect to his failure to provide clients with transaction-by-transaction notification and consent to engage in cross-trades, Nadel appeared dismissive, stating simply that he "felt comfortable enough with the disclosure documents" and the "blanket expression" concerning the possibility of cross-trades—despite the fact that this approach failed to comply with Section 206(3) of the Advisers Act. As to the inaccurate trading confirmations, Nadel presented a similar lackluster attitude. Indeed, Nadel testified that he did not alert clients to the inaccuracy of the confirmations. *See* Hrg. Tr. at 567: 3–7. And although he initially testified that he "did not review the confirm[ations]" because his assistant completed this job, *id.* at 567:12–13, when he was

presented with his prior sworn testimony, *see* Pl.'s Hrg. Ex. 140, which showed that he did in fact review the trading confirmations, Nadel back-pedaled, stating that he "didn't look at the codes" because he "was under the assumption that the codes were reflecting that [the broker was acting as agent for both sides of the transaction]." *See* Hrg. Tr. at 569:25–570:1. Moreover, when presented with the false statement made to the Commission that the Defendants did not communicate with clients via email, *id.* at 581:21–582:8—despite acknowledging that there "seem to be quite a few emails," *id.* at 583:21–23—Nadel had no recollection as to why he made the false statement. In any event, he continued to send out numerous emails to prospective clients containing inflated AUM claims. *See id.* at 584:15–17; 586:8–17; Pl.'s Hrg. Ex. 19.

v. Opportunity to Commit Future Violations

***10** Nadel has a Bachelor of Science degree in Administrative and Management Sciences from Carnegie-Mellon University and a Masters in Business Administration from New York University. Pl.'s Hrg. Ex. 22 at 27. He has worked in the financial industry over 35 years – since 1977. *Id.* at 15. Prior to starting WDNC and RIA he worked for firms such as Lehman Bros., Oppenheimer & Company and Jefferies & Company. *Id.* This long history with, and entrenchment in, the financial industry during the past 35+ years makes recurrence more likely, especially since institutional investing encompasses Nadel's primary area of expertise. See *S.E.C. v. Univ. Major Indus. Corp.*, 546 F.2d 1004, 1048 (2d Cir.1976) (recognizing as a factor the "likelihood, because of defendant's professional occupation, that future violations might occur"); *S.E.C. v. Platinum Inv. Corp.*, No. 02 CV 6093, 2006 WL 2707319, at *4 (S.D.N.Y. Sept. 20, 2006) (same). In addition, Nadel's "fraudulent past conduct gives rise to an inference of a reasonable expectation of continued violations." *S.E.C. v. Tannenbaum*, No. 99–CV–6050, 2007 WL 2089326, at *3 (E.D.N.Y. Jul. 19, 2007) (quoting *Platinum Inv. Corp.*, 2006 WL 2707319, at *4); see First Jersey, 101 F.3d at 1477. As such, the Court finds that this factor also weighs in favor of granting injunctive relief.

In light of the above findings, the Court respectfully recommends to Judge Kuntz that the Commission's request for permanent injunctive relief against the Defendants be GRANTED.

B. Disgorgement

1. Applicable Law

"Once the district court has found federal securities law violations, it has broad equitable power to fashion appropriate remedies, including ordering that culpable defendants disgorge their profits." *First Jersey*, 101 F.3d at 1474; *China Energy Sav. Tech., Inc.*, 2008 WL 6572372, at *10. Disgorgement thus functions as an equitable remedy, imposed to "forc[e] a defendant to give up the amount by which he was unjustly enriched." *FTC v. Bronson Partners*, 654 F.3d 359, 372 (2d Cir.2011) (quoting *S.E.C. v. Commonwealth Chem. Sec., Inc.*, 574 F.2d 90, 102 (2d Cir.1978)). To that end, disgorgement serves to remedy securities law violations by depriving violators of the fruits of their illegal conduct. *See S.E.C. v. Fischbach Corp.*, 133 F.3d 170, 175 (2d Cir.1997); *see S.E.C. v. Tome*, 833 F.2d 1086, 1096 (2d Cir.1987) ("The paramount purpose of enforcing the prohibition against insider trading by ordering disgorgement is to make sure that wrongdoers will not profit from their wrongdoing."); *see also S.E.C. v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1104 (2d Cir.1972) ("The deterrent effect of an SEC enforcement action would be greatly undermined if securities law violators were not required to disgorge illicit profits."). As such, by forcing wrongdoers to give back the fruits of their illegal conduct, disgorgement also "has the effect of deterring subsequent fraud." *S.E.C. v. Cavanagh*, 445 F.3d 105, 117 (2d Cir.2006) ("*Cavanagh II* "); *First Jersey*, 101 F.3d at 1474. Indeed, without the availability of this equitable enforcement mechanism, "the deterrent effect of an SEC enforcement action would be greatly undermined[.]" *China Energy Sav. Tech., Inc.*, 2008 WL 6572372, at *10 (quoting *Manor Nursing Ctrs., Inc.*, 458 F.2d at 1104).

"The district court has broad discretion not only in determining whether or not to order disgorgement but also in calculating the amount to be disgorged." *First Jersey*, 101 F.3d at 1474–75; *see S.E.C. v. Contorinis*, 743 F.3d 296, 301 (2d Cir.2014), *cert. denied*, 136 S.Ct. 531 (2015); *see also S.E.C. v. Posner*, 16 F.3d 520, 522 (2d Cir.1994) (affirming district court's order of disgorgement since "[t]he [district] court has broad discretion to tailor the sanction to the wrongful conduct involved"). Such a calculation "need only be a reasonable approximation

of profits causally connected to the violation ... any risk of uncertainty [in calculating disgorgement] should fall on the wrongdoer whose illegal conduct created that uncertainty." *First Jersey,* 101 F.3d at 1475 (quoting *S.E.C. v. Patel,* 61 F.3d 137, 139–40 (2d Cir.1995)) (alteration in original); *see Tavella,* 77 F.Supp.3d at 359; *S.E.C. v. McCaskey,* 98 Civ. 6153, 2002 WL 850001, at *4 (S.D.N.Y. Mar. 26, 2002); *S.E.C. v. Haligiannis,* 470 F.Supp.2d 373, 384 (S.D.N.Y.2007) ("The amount of disgorgement ordered by a court for violation of the securities laws need not be an exact calculation of the defendant's profits, but only "a reasonable approximation of profits causally connected to the violation."); *see also Cavanagh II,* 445 F.3d at 116 & n. 25 (noting that since disgorgement "is remedial rather than punitive, the court may not order disgorgement above" "the amount of money acquired through wrongdoing ... plus interest"). "Thus, once the Commission shows the existence of a fraudulent scheme in violation of federal securities laws, the burden shifts to the defendant to 'demonstrat[e] that he received less than the full amount allegedly misappropriated and sought to be disgorged.' " *S.E.C. v. Rosenfeld,* No. 97 CIV.1467, 2001 WL 118612, at *2 (S.D.N.Y. Jan. 9, 2001) (quoting *S.E.C. v. Benson,* 657 F.Supp. 1122, 1133 (S.D.N.Y.1987)); *S.E.C. v. Grossman,* 87 Civ. 1031, 1997 WL 231167, at *8 (S.D.N.Y. May 6, 1997) ("The SEC bears the burden of persuasion that its proposed disgorgement figure reasonably approximates the amount of unjust enrichment ... once the SEC has established that the proposed amount is reasonable, the burden shifts to the defendant to demonstrate that the amount requested is not a reasonable approximation of the unlawfully obtained profits."), *aff'd, in part, vacated, in part,* 173 F.3d 846 (2d Cir.1999).

2. Application to the Facts

i. The Commission's Disgorgement Figure Represents a Reasonable Approximation of Defendants' Profits

*11 The Commission seeks to disgorge a total of $10,959,714.30 in illicit profits which the Commission claims are causally connected to Defendants' violations. Pl.'s Hrg. Ex. 213 at 1. Specifically, the Commission seeks to have Defendants disgorge the following streams of income received by them from January 1, 2007 through December 31, 2009:(1) $3,432,140.85 in advisory fees charged by Defendants to clients to participate in Defendants' investment strategy, *see* Pl.'s Hrg. Ex. 213 at 1; 15 (Table 8 Amended showing the breakdown of advisory fees charged to Defendants' clients from 2007 through 2009); Hrg. Tr. at 202:17–20; (2) $5,384,443.70 constituting trading commissions paid on 5,615 unlawful cross-trades, *see* Pl.'s Hrg. Ex. 213 at 1, 9, 10[11]; and (3) $2,143,129.75 representing profits from the 71 groups of unlawful principal trades. *See* Pl.'s Hrg. Ex. 213 at 1.

In addition to the hearing testimony elicited from Michael Fioribello, the Commission's Senior Specialized Examiner, *see* Hrg. Tr. at 179:23–24, and the exhibits introduced by the Commission substantiating the amounts noted above, the parties also entered into a Stipulation confirming the above referenced amounts of advisory fees, commissions and profits received from Defendants' illicit activities between January 1, 2007 and December 31, 2009. *See* Hrg. Tr. at 3:7–5:7. The language of the Stipulation also provided that during this same period, the Defendants "executed 120 other groups of principal trades against their Corporate Advisory Clients on which they incurred $2,256,644.54 in losses." *Id.* at 4:24–5:2.

In light of the Defendants' underlying violations, as determined by Judge Kuntz, *see* Section 2. A. *supra,* along with the fact that the Commission's calculations concerning Defendants' profits appear to reasonably approximate those profits causally connected to Defendants' underlying violations, *see First Jersey,* 101 F.3d at 1475, the Court finds that disgorgement in the amount of $10,959,714.30 is warranted since that figure reasonably approximates the amount of Defendants' unjust enrichment. *See Grossman,* 1997 WL 231167, at *8.

ii. Defendants' Entitlement to Deductions

Although the Court finds that the Commission's figure of $10,959,714.30 constitutes a reasonable approximation of the Defendants' illicit profits, Defendants have asserted that this amount should be offset by: (1) trading losses incurred; (2) payments made to Hal Pasetsky and two other outside individuals; (3) payment of clearing charges; and (4) payment made to Polycom. *See* Defendants' Post–Hearing Memorandum Regarding Damages ("Defs.' Post–Hearing Mem.") at 1. "Because the [Commission's] disgorgement calculation is 'reasonable,' the burden shifts to [Defendants] to demonstrate that they received less

than the full amount sought to be disgorged." *S.E.C. v. Svoboda,* 409 F.Supp.2d 331, 344–45 (S.D.N.Y.2006). The Court will address each category in turn to determine if Defendants have met their burden.

1. Trading Losses

*12 Defendants claim that "the $2,256,644.54 in principal trading losses should be used to offset any disgorgement in this action, because such losses 'were incurred incidental to, and as part and parcel of, the intended scheme.' " Defs.' Post–Hearing Mem. at 4 (quoting *McCaskey,* 2002 WL 850001, at *8). For the reasons that follow, the Court finds that Defendants have not met their burden and thus have failed to establish that any perceived trading losses should be deducted from the total amount of disgorgement.

With respect to the 71 groups of principal trades [12] for which the Commission is seeking the profits, the record establishes that any losses actually incurred by Defendants in executing these trades were already accounted for—the Commission netted the profitable and unprofitable individual transactions which occurred within each group of the 71 groups of principal trades. This calculation is illustrated in Michael Fioribello's testimony where he explains the purpose behind "grouping" the trades comprising each principal trading transaction and the internal as well as overall calculation regarding each principal group of trades. For example, when asked why the trades were grouped together, Michael Fioribello stated:

> A: All of the trades are grouped together in one group to give a complete picture of all of the pieces of this principal trade example; the proprietary account and the corporate advisory account, in this case.

Hrg. Tr. at 191:1–4. In addition, when describing the mechanics of principal trade number 16 (which resulted in a net profit) on Plaintiff's Hearing Exhibit 4 (chart showing commissions on principal trades from 1/1/2007 – 2/29/2008), the testimony demonstrates that internal losses within this trading group were netted out and therefore already accounted for when determining whether the trade represented an overall profit or loss. The following testimony is illustrative of this point as it concerns principal trade number 16:

> Q: So did the proprietary account make or lose money on those two buys?
>
> A: The proprietary account lost money on those two buys.
>
> Q: And over on the right you show a positive difference of 35 cents in the average price of the buys and sells.
>
> A: Yes.
>
> Q: Does that reflect that overall for that group the Nadel accounts made money on that example?
>
> A: Yes.
>
> Q: Okay. Does that number take into account that on the last two buys in that example Mr. Nadel lost money?
>
> A: Yes.
>
> Q: And how so?
>
> A: For this group, for this example, regardless of whether any individual made or lost money with respect to the proprietary account, I took a straight weighted average buy price and a straight weighted average sell price, and I took the difference between those prices.

Id. at 193:19–194:13.

In addition, as to those groups of principal trades which resulted in an overall *net loss,* the Commission is not seeking disgorgement of any of the profitable internal individual transactions and has therefore not included that profit in any of its disgorgement calculations. As such, offsetting these amounts from the overall disgorgement figure would be improper since these internal profits were never accounted for in the first instance. Michael Fioribello illustrated this point during his hearing testimony when he was asked:

> *13 Q: Can you look at Exhibit 4 please. And specifically the top of page 3. And Example No. 26. Do you see that Mr. Fioribello?
>
> A: Yes.

Q: And you see, over on the right, the difference in average price of buy and sells and that is in red?

A: Yes.

Q: So in that example, did Mr. Nadel's proprietary account make money or lose money?

A: Lose money.

Q: And were there any transactions within that group on which Mr. Nadel made money?

A: Yes.

Q: Can you explain that?

A: With respect to the bottom three rows each for Warren D Nadel & Company proprietary account, there is one sell only at 90.625. There is each a buy at 90.45 and a buy at $90.8125. One of those two trades is the buy, at $90.45, was lower than the sell at a price of 90.625 so that particular buy resulted in a profit to the proprietary account.

Q: And did you include that profit in any of the disgorgement figures that were calculated in your other tables?

A: No.

Q: Why not?

A: I based disgorgement on examples where the weighted average price and the weighted sell to the Warren D Nadel & Company proprietary account was net positive or profit.

Q: So is it fair to say there that profit was netted out against the other transactions in this group that were losses.

A: Yes.

Id. at 225:14–226:22.

In light of the evidence presented at the hearing, it is evident that Defendants' reliance on *S.E.C. v. McCaskey* is misplaced. In *McCaskey*, the court rejected the Commission's disgorgement theory which was "based solely on McCaskey's sales on sixteen days, ignoring all other transactions during the more than six-month manipulation scheme." *McCaskey*, 2002 WL 850001, at *7. On that basis, the Court in *McCaskey* determined that losses during the balance of the manipulation period "should be considered in determining whether to order disgorgement." *Id.* However, in deciding that issue, the court was careful to highlight that the rejection of the Commission's theory was based solely on the "Particular *Facts of this Case*." *Id.* at *6 (emphasis in original). Unlike *McCaskey* – where the Commission ignored transactions during the manipulation period that resulted in losses and otherwise did not take those into account in calculating the overall amount of disgorgement – in the case at bar, the Commission expressly considered all principal trades that occurred from January 1, 2007 through December 31, 2009. However, as explained above, the Commission only calculated the amount of disgorgement based upon the 71 groups of principal trades that resulted in an overall net profit. Therefore, any principal trades which included an internal profit but resulted in an overall net loss were not charged against Defendants in the first instance, nor were they factored into the Commission's calculation of disgorgement. Consequently, such losses were netted out and in that sense were already credited to Defendants and thus should not be double-counted by offsetting these losses from the overall disgorgement figure.

In light of the above analysis, the Court respectfully recommends to Judge Kuntz that Defendants are not entitled to an offset of the $2,256,644.54 in trading losses.

2. Payments to Hal Pasetsky

*14 Defendants also seek an offset from the total disgorgement figure for payments which Defendants characterize as "brokerage commissions" paid to Hal Pasetsky ("Pasetsky") in the amount of $2,666,486.25. *See* Defs.' Post–Hearing Mem. at 5. The hearing testimony establishes that Hal Pasetsky worked at WDNC, purportedly as a broker, and was paid "a percentage of brokerage commissions." *See* Hrg. Tr. at 726:2–727:2. Specifically, Pasetsky was paid "35 percent of commissions on a transaction-by-transaction basis and a percentage, 35 percent of the management fee." *Id.* at 727:10–12. In order to determine Pasetsky's monthly payment, Nadel "would add up all the commissions on each transaction and for each client, and then [Nadel] would add up the management fees upon receipt, and the summation of all of those numbers would be

multiplied by 35 percent, and that was his monthly brokerage commission to be received." *Id.* at 727:4–8. In addition, the trading confirmations received by clients listed Pasetsky as the financial consultant. *Id.* at 735:12–738:15. Nadel testified that the confirmations also contained "the brokerage commission portion that was due to Mr. Pasetsky." *Id.* at 739:2–3.

Despite Nadel's direct testimony at the hearing concerning Pasetsky's role as a broker, Nadel testified on cross-examination that only he and RBC Correspondent Services were involved in executing the cross-trades and that it was RBC which ultimately executed, processed and cleared the transactions. *Id.* at 726:21–23; 783:21–784:11. When questioned concerning Pasetsky's actual role in the execution of the cross-trades, Nadel testified as follows:

> Q: Was Mr. Pasetsky involved in any of the steps you described in the execution of the cross-trades?
>
> A: Of the actual transactions, no.
>
> Q: He didn't negotiate any of those trades?
>
> A: No.
>
> Q: He didn't broker any of the cross-trades, did he?
>
> A: No.
>
> Q: Well, what happened is you were getting the commission income from RBC, and then at some point you would break out his share of that as well as his share of the management fees from RIA, and then he would be paid. Is that fair to say?
>
> A: As is typical of a managed account at any broker firm in the country.

Id. at 785:6–19.

Based upon the testimony and evidence adduced at the damages hearing, the Court is not convinced that any of the payments made by Nadel to Pasetsky should be deducted from the total amount of disgorgement. It is true that "a court may, in its discretion, deduct from the disgorgement amount any direct transactions costs, such as brokerage commissions." *S.E.C. v. Univ. Express, Inc.*, 646 F.Supp.2d 552, 564 (S.D.N.Y.2009); *see Svoboda*, 409 F.Supp.2d at 345. However, courts have also "taken care to distinguish such costs from 'general business expenses, such as overhead expenses, which should not reduce the disgorgement amount.' " *Univ. Express, Inc.*, 646 F.Supp.2d at 564 (quoting *McCaskey*, 2002 WL 850001, at *4 n. 6); *see S.E.C. v. U.S. Envt'l, Inc.*, No. 94 Civ. 6608, 2003 WL 21697891, at *28 (S.D.N.Y. Jul. 21, 2003); *Svoboda*, 409 F.Supp.2d at 345. Further, where courts have deducted brokerage commissions, the deduction is generally based upon the direct execution of trades and the expenses incurred as a result of such trade executions. *See Litton Inuds., Inc. v. Lehman Bros. Kuhn Loeb Inc.*, 734 F.Supp. 1071, 1077 (S.D.N.Y.1990) ("[T]ransaction costs such as brokerage commissions incurred by [defendant] in *executing* trades in [the company's] securities should be deducted from any fees and commissions disgorged as profit.") (emphasis added); *S.E.C. v. East Delta Res. Corp.*, No. 10–CV–310, 2012 WL 3903478, at *7 (E.D.N.Y.2012).

Although Defendants attempt to characterize Pasetsky's payments as brokerage commissions in the traditional sense, the testimony instead establishes that these payments were not made to Pasetsky for executing the cross-trades on behalf of Defendants since Nadel was solely responsible for trade execution. *See* Hrg. Tr. at 527:9–11; 536:4–7. The testimony further shows that Nadel himself executed the trades, received the commission income from the trades and then parsed out Pasetsky's share based upon the fee arrangement which was in place. *See* Hrg. Tr. at 785:6–19. Considering these facts, it would be illogical and contrary to the purpose behind the remedy of disgorgement to permit Defendants to offset the payments made to Pasetsky which are closer to a general business expense than a direct transaction cost. In short, any payments made to Pasetsky, which were more akin to a profit-sharing arrangement, were at best ancillary to Defendants' violations – as opposed to constituting a direct transaction cost derived from Defendants' wrongdoing. Such payments, therefore, should not be deducted. *See McCaskey*, 2002 WL 850001, at *8 (noting that expenses which are "ancillary to the fraudulent scheme" should not serve to reduce the overall amount of disgorgement).

***15** Furthermore, "it is irrelevant for disgorgement purposes, how the defendant chose to dispose of the ill-gotten gains ... [and therefore] payment [s] to co-conspirators are not deductible from the gross profits subject to disgorgement." *Univ. Express, Inc.*, 646 F.Supp.2d at 564 (internal quotations and citation omitted); *see Rosenfeld*, 2001 WL 118612, at *2; *S.E.C.*

v. Benson, 657 F.Supp. 1122, 1134 (S.D.N.Y.1987) ("The manner in which [defendant] chose to spend his misappropriations is irrelevant as to his objection to disgorge. Whether he chose to use this money to enhance his social standing through charitable contributions, to travel around the world, or to keep his co-conspirators happy is his own business."). The testimony demonstrates that Defendants opted to funnel payments to affiliates such as Pasetsky. That Defendants chose to do so is their own business. However, having made that choice, they cannot now seek to offset such ancillary payments – which do not constitute direct transaction costs – in order to reduce the overall amount of disgorgement. Thus, it is of no moment that the funds may have been procured for a third-party. *See Contorinis,* 743 F.3d at 307 (recognizing that "when third parties have benefitted from illegal activity, it is possible to seek disgorgement from the violator, even if that violator never controlled the funds."). Indeed, labeling someone a broker and categorizing such payments as direct transaction costs does not make them so.

Based upon the foregoing, this Court respectfully recommends to Judge Kuntz that the $2,666,486.25 in payments made to Hal Pasetsky *not* be deducted from the total amount of disgorgement. [13]

3. Clearing Charges

The Defendants next seek to offset the "$301,201.90 [14] in clearing charges that Defendants paid to RBC and MF Global for clearing trades in executing the transactions at issue." Defs.' Post–Hearing Mem. at 8. Defendants again cite *S.E.C. v. McCaskey* for the proposition that these clearing charges are " 'direct transaction costs' that should be reduced from disgorgement because they 'plainly reduce the wrongdoer's profit.' " *Id.* at 8 (quoting *McCaskey,* 2002 WL 850001, at *4).

With respect to the clearing charges, Nadel testified these were "charges for processing transactions associated with RBC with any trades that were performed." Hrg. Tr. at 751:1–2. In addition to clearing trades processed through RBC, Nadel testified that Defendants "utilized MF Global for hedging purposes of the preferred portfolio which utilized treasury bonds, futures and put options." *Id.* at 767:24–768:1. Specifically, Nadel stated that MF Global was the clearing firm used with respect to the options portion of Defendants' investment strategy. *Id.* at 751:4–7.

As noted above, the parties have stipulated that the total amount of clearing charges paid by Defendants from 2007 through 2009 is $301,201.90. *See* Defs.' Hrg. Ex. 103 at 1. The hearing testimony discloses that Defendants did indeed pay this amount to their clearing brokers. The amounts were allocated as follows: $183,026.68 to RBC, $76,411.90 to Man Financial and $41,763.32 to MF Global. *Id.*; *see* Hrg. Tr. at 765:16–767:25.

"Courts in this circuit consistently hold that a court may, in its discretion, deduct from the disgorgement amount any direct transaction costs, such as brokerage commissions, that plainly reduce the wrongdoer's actual profit." *McCaskey,* 2002 WL 850001, at *4 (citing cases); *Svoboda,* 409 F.Supp.2d at 345; *Univ. Express,* 634 F.Supp.2d at 564; *but see Bronson Partners, LLC,* 654 F.3d at 375 ("[I]t is well established that defendants in a disgorgement action are "not entitled to deduct costs associated with committing their illegal acts."); *S.E.C. v. Cavanagh,* No. 98 CIV. 1818, 2004 WL 1594818, at *30 (S.D.N.Y. July 16, 2004), *aff'd on other grounds,* 445 F.3d 105 (2d Cir.2006) ("Defendants are not entitled to deduct costs associated with committing their illegal acts."); *S.E.C. v. Amerindo Inv. Advisors Inc.,* No. 05 CIV. 5231, 2014 WL 2112032, at *5 (S.D.N.Y. May 6, 2014) (same).

***16** In light of the fact that there is some disagreement within this Circuit as to whether the direct costs associated with a defendant's illegal acts should be deducted from the overall amount of disgorgement, it is necessary to briefly review the purpose behind this remedy. "[D]isgorgement is an equitable remedy that prevents unjust enrichment" and is therefore unlike a criminal forfeiture which constitutes "a statutory legal penalty imposed as punishment." *Contorinis,* 743 F.3d at 306. As such, "disgorgement is designed to equitably deprive those who have obtained ill-gotten *gains* of enrichment ... [and thus operates] not to punish, but to ensure illegal actions do not yield unwarranted enrichment...." *Id.* at 306–07. (emphasis added); *see S.E.C. v. Lorin,* 869 F.Supp. 1117, 1121 (S.D.N.Y.1994) (noting that the court would "not label disgorgement as a fine, penalty, or forfeiture in light of the operation of disgorgement, which merely deprives one of wrongfully obtained proceeds") (internal quotations and citation omitted).

Since the over-arching purpose of disgorgement is the prevention of a defendant's unjust enrichment by requiring the relinquishment of his "ill-gotten gains," this Court finds the cases holding that direct transaction costs may, in the court's discretion, be deducted from the total amount of disgorgement represent the correct approach since such direct costs do not constitute "gains" to a defendant. Factoring such direct costs into a disgorgement calculation would operate as a penalty, thus failing to achieve disgorgement's ultimate purpose and intent. *See S.E.C. v. Shah,* No. 92 Civ.1952, 1993 WL 288285, at *5 (S.D.N.Y. Jul. 28, 1993); *Litton Indus., Inc.,* 734 F.Supp. at 1077.

In this case, the Commission is seeking to have Defendants disgorge, in part, $5,384,443.70 in commissions which Defendants received by engaging in 5,615 illicit cross-trades. *See* Hrg. Tr. at 4:8–15 (Stipulation). These cross-trades, which encompassed only the preferred utility stocks, were cleared solely by RBC. *See* Hrg. Tr. at 751:1–3. As such, the direct costs associated with Defendants clearing these cross-trades *i.e.* – $183,026.68, Defs.' Hrg. Ex. 103 at 1 – should be deducted from the total amount of disgorgement sought since these charges constituted direct expenses associated with the wrongdoing which reduced Defendants' actual profit. *See Univ. Express,* 634 F.Supp.2d at 564; *Svoboda,* 409 F.Supp.2d at 345. However, the $76,411.90 paid to Man Financial and the $41,763.32 paid to MF Global should not be deducted from the overall amount of disgorgement. *See* Defs.' Hrg. Ex. 103 at 1. The rationale is that although "hedging" may have constituted a portion of the Defendants' investment strategy, none of these "hedging" trades – consisting of treasury bonds, future or put options – involved conduct that was found to have violated the securities laws. *See* Hrg. Tr. at 767:25768:1. Therefore, any profits Defendants may have made from these separate trades is not otherwise included in the $5,384,443.70 disgorgement total for the cross-trading commissions received. A deduction for clearing charges incurred on these trades, then, would be is improper since any profits garnered on such trades would not have been illegal in the first instance since the underlying trades themselves did not violate the law. *See Rosenfeld,* 2001 WL 118612, at *2 ("A court may in its discretion, deduct from the defendant's gross profits certain expenses incurred while garnering the *illegal profits* ....") (emphasis added); *S.E.C. v. Thomas James Associates, Inc.,* 738 F.Supp. 88, 94 (W.D.N.Y.1990) ("In determining the proper amount of restitution, a Court may consider as an offset the sums which a defendant paid to effect a *fraudulent transaction.*") (emphasis added).

For these reasons, this Court respectfully recommends to Judge Kuntz that (1) Defendants be permitted a deduction solely for the $183,026.68 in clearing charges paid to RBC to effectuate the illicit cross-trades but (2) Defendants not be permitted a deduction for the clearing charges incurred in executing the "hedging" trades.

4. Payment to Polycom

*17 Defendants next assert that the $553,063.37 payment made by them to Polycom, one of Defendants' investors, should serve as an offset to the total amount to be disgorged. Defendants maintain that "where a defendant 'can establish that he has repaid' alleged ill-gotten gains to an investor, 'such payments will offset his disgorgement obligation.' " Defs.' Post–Hearing Mem. at 8 (quoting *Disraeli v. S.E.C.,* 334 F. App'x 334, 335 (D.C.Cir.1998)).

The evidence introduced at the damages hearing established that a payment of $553,063.37 was in fact made by RIA to Polycom. *See* Hrg. Tr. at 341.21:7–23 (Boilieu testimony); Defs.' Hrg. Ex. 63. Further evidence established that with respect to Polycom's investment,

> in the September 2008 time frame we became aware that the portfolio was—the Nadel portfolio was out of compliance with Polycom's investment policy, and due to that noncompliance, there was approximately—and that's probably a rounded number, but there was approximately $1.5 million worth of loss that was on those instruments due to the fact that they were out of compliance. And by out of compliance, as to duration, meaning they had no longer the 90 days, and as to quality of instrument.

See Pl.'s Hrg. Ex. 209, October 28, 2011 Michael Kourey [CFO of Polycom] Deposition Transcript ("Kourey Dep."), at 45–46; Hrg. Tr. at 321:22–323:5. The testimony supplied by Walter Boilieu at the hearing corroborated

Michael Kourey's rationale concerning the promissory note issued by RIA. When asked "what was the purpose of the note, again?," Boilieu responded that to his recollection "it had something to do with losses [Polycom] incurred to get the portfolio back into compliance with [Polycom's] investment policy, and I guess we extracted a note from [Nadel] to make us whole for some of those losses." Hrg. Tr. at 341.11:14–20 (Boilieu testimony).

In light of this evidence, the Court finds that the promissory note issued by Defendants to Polycom for approximately $1.5 million, of which $553,063.37 was repaid, was entered into as a result of Defendants' non-compliance with Polycom's investment policy – not due to losses incurred by Polycom directly relating to or resulting from Defendants' underlying misconduct which was found by Judge Kuntz to have violated the securities laws. Thus, Defendants' attempts to characterize these funds as a repayment of an "ill-gotten gain" rings hollow.

The two cases cited by Defendants are inapposite since neither one reflects the scenario encountered here. For example, in *Disraeli,* the court specifically limited its holding to those funds which the petitioner "transferred from Lifeplan's bank account to his own" – in other words, ill-gotten gains – and determined that in such instance, these "payments will offset his disgorgement obligation." *Disraeli,* 334 F. App'x at 335. Further, the Second Circuit case cited by *Disraeli* (and noted in Defendants' Post-Hearing Memorandum) dealt with a circumstances in which the court determined that "to the extent that [defendant] pays or has paid *restitution* as ordered in the criminal judgment, such payments will offset his disgorgement obligation under the present judgment." *S.E.C. v. Palmisano,* 135 F.3d 860, 864 (2d Cir.1998) (emphasis added). Neither of these decisions is on-point. Since Defendants' repayment to Polycom pursuant to the promissory note did not involve repayment of ill-gotten gains – but rather repayment due to non-compliance with Polycom's investment parameters – a deduction of this payment from the total disgorgement amount is not warranted.

C. Prejudgment Interest

1. Applicable Law

***18** Whether prejudgment interest should be awarded in a case involving violation of the securities laws is "confided to the district court's broad discretion, and will not be overturned on appeal absent an abuse of that discretion." *Contorinis,* 743 F.3d at 307 (quoting *Endico Potatoes, Inc. v. CIT Group/Factoring, Inc.,* 67 F.3d 1063, 1071–72 (2d Cir.1995)); *see First Jersey,* 101 F.3d at 1476; *Tavella,* 77 F.Supp.3d at 360; *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *12. Thus, the decision whether to award prejudgment interest is "governed by the equities, reflecting 'considerations of fairness' rather than 'a rigid theory of compensation ... and [ ] the failure of securities law violators to enjoy a profit 'does not standing alone, make it inequitable to compel them to pay interest.' " *Contorinis,* 743 F.3d at 308 (internal citations omitted).

The primary purpose behind awarding prejudgment interest is "to deprive the wrongdoer of the benefit of holding the illicit gains over time by reasonably approximating the cost of borrowing such gain from the government." *Id.*; *see First Jersey,* 101 F.3d at 1476; *Tavella,* 77 F.Supp.3d at 360. Therefore "[r]equiring the payment of interest prevents a defendant from obtaining the benefit of what amounts to an interest free loan procured as a result of illegal activity." *S.E.C. v. Moran,* 944 F.Supp. 286, 295 (S.D.N.Y.1996); *see China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *12.

In determining whether to award prejudgment interest, courts consider the following factors "(i) the need to fully compensate the wronged party for actual damages suffered, (ii) considerations of fairness and the relative equities of the award, (iii) the remedial purpose of the statute involved, and/or (iv) such other general principles as are deemed relevant by the court". *First Jersey,* 101 F.3d at 1476; *see China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *13; *U.S. Envt'l, Inc.,* 2003 WL 21697891, at *30. "In an enforcement action brought by a regulatory agency, the remedial purpose of the statute takes on special importance." *First Jersey,* 101 F.3d at 1476; *see U.S. Envt'l, Inc.,* 2003 WL 21697891, at *30; *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *13. Notwithstanding the four factors enumerated above, "the amount on which a violator must pay prejudgment interest usually tracks the amount the party is ordered to disgorge [and][w]hether or not a party personally enjoyed the gains from the illegal action does not alter this principle." *Contorinis,* 743 F.3d at 308.

In calculating the rate of prejudgment interest to be awarded, "the Second Circuit has approved the calculation ... at the [Internal Revenue Service] underpayment rate, which 'reflects what it would have cost to borrow the money from the government and therefore reasonably approximates one of the benefits the defendant derived from its [illegal conduct].' " *Tavella,* 77 F.Supp.3d at 360 (quoting *First Jersey,* 101 F.3d at 1476); *see U.S. Envt'l, Inc.,* 2003 WL 21697891, at *30 ("The district court generally calculates prejudgment interest by using the IRS rates for underpayment of taxes under 26 U.S.C. § 6621(a)(1)"); *S.E.C. v. Spongetech Del. Sys., Inc.,* No. 10–CV–2031, 2015 WL 5793303, at *9 (E.D.N.Y. Sept. 30, 2015) (noting that the Second Circuit has "approved" the use of the IRS underpayment rate when calculating a prejudgment interest award).

2. Application to the Facts

The evidence presented at the hearing illustrated that throughout the duration of the wrongdoing, which lasted for at least two years, Defendants acted with a high degree of scienter. *See* Hrg. Tr. at 3:24–5:7 (Stipulation); Section III. A. 2., *supra* (discussing Defendants' degree of scienter in the context of awarding injunctive relief); *see also Svoboda,* 409 F.Supp.2d 331 (noting that "courts have routinely awarded prejudgment interest in SEC enforcement actions where the defendant's scheme evidences a high degree of scienter"); *S.E.C. v. Musella,* 748 F.Supp. 1028, 1042–43 (S.D.N.Y.1989); *S.E.C. v. Sekhri,* No. 98 Civ. 2320, 2002 WL 31100823, at *18 (S.D.N.Y. Jul. 22, 2002); *Shah,* 1993 WL 288285, at *6. There is another factor to be considered in addition to the duration of the wrongdoing and high degree of intent involved in the underlying violations. Because this action has been brought by the Commission – a regulatory agency – "the remedial purpose of the statute takes on special importance" and this fact, therefore, weighs in favor of awarding prejudgment interest. *Svoboda,* 409 F.Supp.2d at 346. Likewise, Defendants enjoyed the use of the illicit funds for the period between the wrongdoing and the entry of judgment, and, as a result, it would be inappropriate to effectively reward Defendants with "an interest free loan procured as a result of [their] illegal activity." *S.E.C. v. Stone,* No. 06 CIV 6258, 2009 WL 82661, at *6 (S.D.N.Y. Jan. 13, 2009); *see S.E.C. v. Roor,* No. 99 Civ. 3372, 2004 WL 1933578, at *10 (S.D.N.Y. Aug. 30, 2004); *Univ. Express,* 646 F.Supp.2d at 566–67 ("Because a defendant has use of the unlawful profits from the time of the wrongdoing until entry of judgment, prejudgment interest is necessary to capture the full measure of defendant's ill-gotten gains."). For these reasons, the Court, in its discretion, finds that the award of prejudgment interest is warranted.

***19** The S.E.C.'s examiner, Michael Fioribello, testified that in calculating the amount of prejudgment interest, the Commission "uses the IRS underpayment rate." Hrg. Tr. at 205:8. "The Second Circuit has endorsed the use of the IRS underpayment rate in actions brought before the SEC" since the rate "reflects what it would have cost to borrow the money from the government and therefore reasonably approximates one of the benefits the defendant[s] derived from [their] fraud." *Svoboda,* 409 F.Supp. at 346 (citing *First Jersey,* 101 F.3d at 1476). As such, the Court finds that the Commission's use of the IRS underpayment rate in calculating the total amount of prejudgment interest is proper.

The total amount of prejudgment interest sought by the Commission is $2,372,401.11. *See* Pl.'s Hrg. Ex. 213 at 1; Hrg. Tr. at 205:1. This sum was calculated "by using the [Commission's] prejudgment interest calculator ... [which requires the user to] input the disgorgement amount and the begin and end dates of the prejudgment interest period." Hrg. Tr. at 205:3–6. In addition to Fioribello's testimony, the evidence produced by the Commission demonstrates that prejudgment interest was calculated on a categorical basis which was further broken down by "Quarter Range," "Annual Rate," "Period Rate," "Quarter Interest," and "Principal + Interest." Pl.'s Hrg. Ex. 213 at 2–5 (illustrating the breakdown, by category, of the Commission's prejudgment interest calculation). The Court takes no issue with the Commission's raw calculations. However, because the Commission based its overall calculations on a total disgorgement amount of $10,959,714.30, and since the Court has determined that Defendants' clearing charges paid to RBC in the amount of $183,026.68 should be deducted from the total amount of disgorgement, the Commission's prejudgment interest figure will need to be revised to reflect that deduction. *See* Defs.' Hrg. Ex. 103 at 1; *East Delta Res. Corp.,* 2012 WL 3903478, at *7 (requiring the Commission to recalculate the amount of prejudgment interest to be awarded based upon the Court's deduction of broker's commissions from total amount of disgorgement).

The Court therefore respectfully recommends to Judge Kuntz that: (1) an award of prejudgment interest is appropriate in this case; and (2) the Commission should be required to submit a revised prejudgment interest calculation based upon the deduction of $183,026.68 in clearing charges paid by Defendants to RBC to execute the cross-trades during the period January 1, 2007 through December 31, 2009.

D. Joint & Several Liability

1. Applicable Law

"Courts have held that joint-and-several liability is appropriate in securities cases when two or more individuals or entities collaborate or have close relationships in engaging in the illegal conduct." *S.E.C. v. Hughes Capital Corp.*, 124 F.3d 449, 455 (3d Cir.1997) (citing *First Jersey*, 101 F.3d at 1475); *Sekhri*, 2002 WL 31100823, at *17 (citing cases). The burden falls upon the wrongdoer to "establish that the liability is capable of being apportioned." *Hughes Capital Corp.*, 124 F.3d at 455 (citing *U.S. v. Alcan Aluminum Corp.*, 964 F.2d 252, 269 (3d Cir.1992)). In this regard, the district court has wide latitude in levying disgorgement on a joint-and-several basis. *Hughes Capital Corp.*, 124 F.3d at 455; *China Energy Sav. Tech., Inc.*, 2008 WL 6572372, at *14. Indeed, the imposition of this burden upon the defendant is appropriate since

> [a]lthough in some cases, a court may be able easily to identify the recipient of ill-gotten profits and apportionment is practical, that is not usually the case. Generally, apportionment is difficult or even practically impossible because defendants have engaged in complex and heavily disguised transactions. Very often defendants move funds through various accounts to avoid detection, use several nominees to hold securities or improperly deprived profits, or intentionally fail to keep accurate records and refuse to cooperate with investigators in identifying the illegal profits. Hence, the risk of uncertainty should fall on the wrongdoer whose illegal conduct created that uncertainty.

*20 *Hughes Capital Corp.*, 124 F.3d at 455 (internal quotations and citations omitted); *see also S.E.C. v. Boock*, No. 09 CV 8261, 2012 WL 3133638, at *3 (S.D.N.Y. Aug. 2, 2012) (finding that joint and several liability is "particularly appropriate" when apportionment between defendants "is difficult or even practically impossible because ... defendants have engaged in complex and heavily disguised transactions in an effort to conceal their fraud") (internal quotations and citation omitted). In this regard, "[t]he SEC is not required to trace every dollar of proceeds or identify misappropriated monies which have been commingled." *Spongetech Del. Sys., Inc.*, 2015 WL 5793303, at *8.

2. Application to the Facts

The evidence presented at the hearing illustrates that Nadel acted as President and Chief Executive Officer of both WDNC, his broker-dealer, and RIA, his investment advising affiliate. *See* Pl.'s Hrg. Ex. 111 at 18, 49 (biographical data of Warren D. Nadel noting that Nadel "[f]ounded the firm, a securities Broker–Dealer and Registered Investment Advisor...."). In addition, during her hearing testimony, Relief Defendant Katherine Nadel, who purportedly worked for WDNC and RIA, was asked whether "Warren D. Nadel & Company and Registered Investment Advisers ... work[ed] together at all T" – to which Katherine Nadel answered "[y]es." Hrg. Tr. at 601:2–5 (Katherine Nadel testimony). Later in her testimony, Katherine Nadel confirmed that WDNC and RIA functioned as a unitary enterprise by claiming to be responsible for the "written supervisory procedures of both firms, the RIA and the WDNC[ ]" and that she kept "[m]inutes of both the IRA [*sic*] and Warren D. Na[d]el Company." *Id.* at 602:2–3; 606:21–607:2. Moreover, Judge Kuntz noted in his summary judgment decision that: (1) Defendants themselves, in arguing against a finding of liability predicated upon Section 206(3) of the Advisers Act, asserted that "WDNC and RIA were acting as one business enterprise [and that] the management and brokerage functions were not separate;" and (2) Defendants represented "in the Program Package that WDNC and RIA were acting as one business enterprise by stating the Company has 'not separated the management

and brokerage functions.' " *Nadel,* 97 F.Supp.3d at 127 (internal citation omitted).

In light of these facts, the Court finds that imposition of joint-and-several liability upon all Defendants is warranted since it is clear that a close relationship existed among Nadel, WDNC and RIA in engaging in the illegal conduct. *See Hughes Capital Corp.*, 124 F.3d at 455 (citing *First Jersey,* 101 F.3d at 1475); *Sekhri,* 2002 WL 31100823, at *17; *Spongetech Del. Sys., Inc.*, 2015 WL 5793303, at *8. Likewise, Defendants have not shown through testimony at the damages hearing or otherwise that the amounts are capable of being apportioned. *See Hughes Capital Corp.*, 124 F.3d at 455 (citing *Alcan Aluminum Corp.*, 964 F.2d at 269); *China Energy Sav. Tech., Inc.*, 2008 WL 6572372, at *14 (recognizing that the burden is on the tortfeasor to establish that liability is capable of being apportioned and finding imposition of joint-and-several liability to be appropriate where "[d]efendants have not refuted the SEC's allegations as to the relationship between them").

Based on these factors, the Court respectfully recommends to Judge Kuntz that Defendants be found jointly-and-severally liable for the total amount of disgorgement and prejudgment interest to be awarded.

E. Civil Penalties

1. Applicable Law

***21** Pursuant to Section 20(d) of the Securities Act, 15 U.S.C. § 77t(d); Section 21(d) of the Exchange Act, 15 U.S.C. § 78u(d); and Section 209(e) of the Advisers Act, 15 U.S.C. § 80b–9(e), the Commission is empowered to pursue civil monetary penalties in addition to an award of disgorgement. The imposition of civil monetary penalties is designed "to punish the individual violator and deter future violations of the securities law." *S.E.C. v. Neurotech Dev. Corp,* No. CV 04–4667, 2011 WL 1113705, at *3 (E.D.N.Y. Feb. 28, 2011) (quoting *Tannenbaum,* 2007 WL 2089326, at *6); *see Moran,* 944 F.Supp. at 296 (noting that the primary purpose behind civil monetary penalties are punishment of the violator and deterrence from future violations).

Courts are empowered to impose a monetary penalty "not to exceed the greater of (1) the gross pecuniary gain to the defendant as a result of a violation, or (2) a specified amount per violation...." *Neurotech Dev. Corp,* 2011 WL 1113705, at *4; *see Tavella,* 77 F.Supp.3d at 362. Where the Court relies upon a specified amount per violation, the maximum amount of the monetary penalty to be imposed for each distinct violation is set forth by each governing statute [15] which structures the penalty into three tiers – the third tier being the most serious. *See* Section 20(d)(2)(A)-(C) of the Securities Act, 15 U.S.C. § 77t(d)(2)(A)-(C); Section 21(d)(3)(B)(i)-(iii) of the Exchange Act, 15 U.S.C. § 78u(d)(3)(B)(i)-(iii); and Section 209(e)(2)(A)-(C) of the Advisers Act, 15 U.S.C. § 80b–9(e)(2)(A)–(C); *Tavella,* 77 F.Supp.3d at 362; *Tannenbaum,* 2007 WL 2089326, at *6. Under each of these statutes,

> a first-tier penalty may be imposed for any violation; a second-tier penalty may be imposed if the violation "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement"; a third-tier penalty may be imposed when, in addition to meeting the requirements of the second tier, the "violation directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons,"

S.E.C. v. Razmilovic, 738 F.3d 14, 38 (2d Cir.2013); *see China Energy Sav. Tech., Inc.*, 2008 WL 6572372, at *15. The maximum penalty per violation –which is periodically adjusted for inflation – for both an individual as well as a corporate entity in each tier for individual violations occurring through March 3, 2009 are: (1) First tier, $6,500 for an individual or $65,000 for a corporate entity per violation; (2) Second tier, $65,000 for an individual or $325,000 for a corporate entity per violation; (3) Third tier, $130,000 for an individual or $650,000 for a corporate entity per violation. *See* 17 C.F.R. § 201.1003, Table III. Additionally, for violations occurring after March 3, 2009 but prior to March 5, 2013, the applicable rates are as follows: $7,500 and $75,000 for first-tier violations; $75,000 and $375,000 for second-tier violations; and $150,000 and $725,000 for third-tier violations. *See id.* at § 201.1004, Table IV. Therefore, "[s]ubject only to the applicable maximum, [t]he amount of the penalty shall be determined by the court in light of the facts and [c]ircumstances." *Tavella,* 77 F.Supp.3d at 362 (internal quotations and citation omitted) (first alteration in original). In that regard, [b]eyond setting maximum penalties, the statutes leave "the actual amount of the penalty ... up to the discretion of the district court." *Razmilovic,* 738 F.3d 14, 38 (quoting *S.E.C. v. Kern,* 425 F.3d 143, 153 (2d Cir.2005)).

*22 In determining whether to impose civil penalties, and if so, what the appropriate amount should be, a court should consider the following factors, including:

> (1) the egregiousness of the defendant's conduct; (2) the degree of the defendant's scienter; (3) whether the defendant's conduct created substantial losses or the risk of substantial losses to other persons; (4) whether the defendant's conduct was isolated or recurrent; and (5) whether the penalty should be reduced due to the defendant's demonstrated current and future financial condition.

Tavella, 77 F.Supp.3d at 362–63; *see Haligiannis*, 470 F.Supp.2d at 386; *Neurotech Dev. Corp*, 2011 WL 1113705, at *4; *Tannenbaum*, 2007 WL 2089326, at *6. Despite the usefulness of these factors in "characterizing a particular defendant's actions, the civil penalty framework is of a 'discretionary nature' and each case 'has its own particular facts and circumstances which determine the appropriate penalty to be imposed.'" *S.E.C. v. Opulentica, LLC*, 479 F.Supp.2d 319, 331 (S.D.N.Y.2007) (quoting *Moran*, 944 F.Supp. at 296–97); *Tavella*, 77 F.Supp.3d at 363.

2. *Appropriateness of Third–Tier Civil Penalties*

The Commission seeks the imposition of "maximum third tier civil [monetary] penalties" based on Defendants' violation of the securities laws. Plaintiff's Opening Statement, Hrg. Tr. at 8:9–12. In response, Defendants assert that they have provided "strong evidence of their inability to pay a civil penalty" and thus, such penalties should therefore be "waiv[ed] or significantly reduc [ed]." Defs.' Post–Hearing Mem., at 10.

i. Egregious / Recurrent Nature of Conduct and Degree of Scienter

The evidence adduced at the damages hearing, which illustrated the overall scope and protracted nature of Defendants' misconduct, strongly supports the conclusion that the Defendants' conduct was egregious and was executed with a high degree of scienter. The Court's previous analysis of Defendants' conduct, *see* Section III. A. 2. *supra,* is thus equally applicable in this context, and for those reasons, the Court finds that each of these factors weigh in favor of imposing third-tier civil penalties in this case. *See Tannenbaum,* 2007 WL 2089326, at *6 (finding Defendants' conduct encompassed a high degree of scienter, was egregious and recurrent based upon prior discussion of these factors).

ii. Defendant's Conduct Resulted in the Risk of Substantial Losses

Testimony at the damages hearing from Defendants' investors establishes that not only was there a real risk of loss based upon Defendants' misconduct, but also that investors incurred actual losses. For example, Richard Anderson of the CGC stated that upon terminating his company's relationship with Defendants in September 2009, CGC incurred an overall loss when trying to liquidate its portfolio of preferred utility stocks in the open market. *See* Hrg. Tr. at 81:6–86:8 (Anderson testimony). Specifically, when asked whether CGC made or lost money on the "last batch of securities that Mr. Nadel purchased," Anderson stated that CGC "lost money." Anderson further stated that of the approximately $5.1 million held in preferred utility stocks at the time CGC exited Defendants' strategy, only about $4.7 million was able to be recouped from selling the portfolio on the open market. *See id.* at 84:14–86:8; Pl.'s Hrg. Exs. 44 at 10 and 46 at 3.

*23 William Hedges of Oregon Mutual testified that during the fourth quarter of 2008, his company's board of directors decided to terminate Oregon Mutual's relationship with Defendants and directed Hedges to "liquidate the portfolio" which was managed by Defendants. Hrg. Tr. at 127:21–128:6 (Hedges testimony). At that point, although Defendants "took back one issue [that was sold to Oregon Mutual] it was nevertheless "sold as a loss." *Id.* at 128:5–10. Additionally, because Defendants were not able to timely liquidate Oregon Mutual's holdings and expressed that "little is being accomplished," *see* Pl.'s Hrg. Ex. 120 (email from Nadel to Hedges expressing depressed nature of market and inability to liquidate the portfolio), Oregon Mutual sought to liquidate its position in the open market.

However, Hedges testified that after conferring with an independent money manager, *see* Hrg. Tr. at 129:10–17, Oregon Mutual decided not to liquidate its holdings since "it would have generated a *significant loss*." *Id.* at 131:10–19; *see also* Pl.'s Hrg. Ex. 121 (email from Douglas Clark to Hedges containing matrix summarizing current positions and probable liquidation prices on a per-share basis).

Jane Casey of Blyth testified that in "June 2008, [Blyth] requested an order of liquidation of the portfolio" and after Defendants were unable to timely liquidate Blyth's holdings at or near cost, Casey stated that Blyth "took custody of the portfolio ... in December 2008." Hrg. Tr. at 261:19–262:13 (Casey testimony). Casey noted that Blyth was not interested in liquidating "at a price well below the cost [of the securities]" and therefore Blyth approached Deutsche Bank to determine if they would be able to liquidate Blyth's portfolio "at any price 95 percent or greater than cost." *Id.* at 265:5–9; 268:24–25. Casey stated that it took Deutsche Bank until "sometime in 2012 to liquidate the entire portfolio [because] [t]hey couldn't find buyers at 95 percent of cost or higher" and, therefore, had the securities been sold in 2009, Blyth would have incurred a loss. *Id.* at 269:3–16. In addition, even while liquidating the portfolio, Casey stated that because the liquidation was "generally in the range of 95 percent or greater of cost [ ] we were generating capital losses at that point." *Id.* at 300:20–25. Furthermore, Casey testified that there existed the ongoing risk of sustaining an actual loss based upon the "capital value of the securities, and ... [the] potential depreciation of the value based on interest rates." *Id.* at 307:5–12.

Walter Boilieu of Polycom testified that the process of liquidating the portfolio which Polycom held with Defendants began during the fourth quarter of 2009. Hrg. Tr. at 341.5:2223.[16] On April 6, 2010, Polycom terminated its relationship with Defendants, *see* Pl.'s Hrg. Ex. 30, and "over the life of the portfolio [determined that they sustained] a cash loss of a million 7 on the original 50 million invested." Hrg. Tr. at 341.10:17–23; Pl.'s Hrg. Ex. 30. In addition, when asked whether Polycom incurred a "cash loss on the last set of securities that Mr. Nadel purchased" Boilieu stated:

> [y]es. Back to the amount we had written it down to, the FTID value of $6.5 million, we only were able to recover $700,000 more than that to make us whole. So we were still short the 5.7 million that would have taken us back to the cost on the Nadel portfolio as of March 2010.

Hrg. Tr., at 341.16, at 10–17; Pl.'s Hrg. Ex. 106. On cross-examination, Boilieu did state that he could not be sure whether the promissory note payment and dividends received were calculated into the $48.3 million total cash withdrawn and thus, conceded that the overall loss could have been approximately $800,000. Hrg. Tr. at 342:25–343:12.

Patricia Canning of LWCC testified that Defendants' services were terminated in May or June of 2009 and that LWCC took control of its portfolio in "late September or October of 2009." Hrg. Tr. at 371:12–15 (Canning testimony). Canning stated that if LWCC had sold its holdings as of September 30, 2009 –shortly after ending their relationship with Defendants – they would have sustained an approximate $3 million loss. *See id.* at 409:7–20. In addition, Canning highlighted the fact that LWCC incurred a $2.8 million loss on liquidation trades made from October 1, 2009 through December 31, 2009. *Id.* at 410:21–22. However, Canning clarified that "as of the date of liquidation of the portfolio in total, the amount of dollars in, received, versus the amount of dollars that was expended, turned out to be very close. About break even." *Id.* at 412:12–15; *see* Pl.'s Hrg. Ex. 93.

***24** Each of the above investors testified at the damages hearing that their investments with Defendants were either placed at risk of sustaining substantial losses or in fact did sustain substantial losses on their initial investment. The risk and / or actual loss was thus directly related to and resulted from each investor's reliance on Defendants' investment strategy, components of which were found to violate the securities laws. As such, based upon the foregoing evidence, the Court finds that at a minimum, there existed a clear and substantial risk of loss to Defendants' investors based upon the underlying statutory violations. Therefore, this factor weighs in favor of imposing third-tier civil penalties.

iii. Defendants' Financial Condition

Nadel testified at the damages hearing that he is not employed at the present, has not worked for the past five

years and has no viable source of income at present. *See* Hrg. Tr. at 669:4–9. In terms of his monthly expenses, Nadel stated that these total $8,700, including $2,150 in insurance premiums and $2,200 in medical expenses. *See id.* at 673:13–674:10; Defs.' Hrg. Ex. 89. According to Nadel, he currently has total assets of $4.4 million and total liabilities of $5,376,057, for a total net worth of negative $975,197. *See id.* at 669:688:15–17. These figures were also included on a chart prepared by Nadel in which he "listed assets and liabilities for [him]self, [his] family and any corporate entity that [he] owned." *Id.* at 688:5–9; Defs.' Hrg. Ex. 99 at 10. Further, Nadel testified that for tax years 2011, 2012 and 2013, for which he filed jointly with his wife, he earned zero taxable income and was projected to earn zero taxable income for tax year 2014. *See id.* at 677:15–680:23; Defs.' Hrg. Ex. 99 at 2841 (Nadel's joint tax return for 2012), 2981 (Nadel's joint tax return for 2013).

Tax return information was also provided with respect to Nadel's three corporate entities – RIA, WDNC and Emancipation Corporation. The testimony and exhibits presented illustrated that with respect to RIA, for calendar years, 2012 and 2013, no gross receipts were recorded and losses of $15,000 and $123,655 were sustained for these years respectively. *See id.* at 682:8–683:19; Defs.' Hrg. Ex. 99 at 2499, 2536. For calendar year 2011, RIA earned $146,504 in total income but sustained an ordinary business loss of $–70,086. *See id.* at 683:20684:6; Defs.' Hrg. Ex. 99 at 2433. Similarly, for calendar years 2011, 2012 and 2013, WDNC earned zero dollars in gross receipts and sustained an overall operating loss of $446,786, $135,851 and $38,479 in each year respectively. *See id.* at 684:20–686:16; Defs.' Hrg. Ex. 99 at 3106, 3144, 3179. With respect to Emancipation Corporation, Nadel stated that for tax year 2013, Emancipation Corporation incurred a loss of $162,919. Moreover, he expected that income would not exceed losses during calendar year 2014. *See id.* at 687:9–20; Defs.' Hrg. Ex. 99 at 2338.

With respect to his real estate holdings, Nadel testified that he currently has "approximately $4.1 million" in outstanding mortgage loans. *Id.* at 698:18–21. Nadel personally owns two residential properties in New York and New Jersey while his corporate entity, Emancipation Corporation, owns two properties in New York (one residential and one commercial) and one vacation property on the island of Turks and Caicos. *Id.* at 692:24693:694:7. With respect to the two residential properties personally owned by Nadel in New York and New Jersey, the evidence established that significant mortgage liabilities exist on each property that are past due. Specifically, Nadel owes at least $748,941.83 on his New York residence. On his New Jersey residence, he owes $968,485.99 on his second mortgage and $354,824.32 on his first mortgage, along with $48,467.41 in unpaid escrow funds. *Id.* at 699:5704:12; Defs.' Hrg. Ex. 99 at 216–217, 220. Although Nadel's two personally held residential properties have significant mortgage balances, the properties held by Emancipation Corporation are "all current" with respect to any mortgage liability.[17] *Id.* at 707:15–19. Nadel presented no documentary evidence of the outstanding mortgage on the Turks and Caicos property, *see id.* at 710:6–16, but he did present cancelled checks made out to "Tamarro TC LTD" in the amount of $10,193.00 which Nadel claimed were "monthly mortgage payments for the property in Turks and Caicos." *Id.* at 712:25–713:3; 714:19–24; Defs.' Hrg. Ex. 99 at 17.

***25** In addition to the above debt, Nadel claims to owe $142,977 in credit card debt. See Defs.' Hrg. Ex. 99 at 10. However, at the time of the hearing, Nadel produced only a statement with respect to his corporate American Express account for which he owes $7,977.39. *See id.* at 3. Further, although he claims to owe over $200,000 in "professional services," Nadel did not provide receipts substantiating the vast majority of these expenses.

With respect to tax liabilities, Nadel provided evidence that he owes approximately $249,826.84 to the Internal Revenue Service and $80,787.20 to the New York State Division of Taxation and Finance. *Id.* at 718:719:15; Defs.' Hrg. Ex. 99 at 201, 222. Nadel also provided evidence that he owes $222,034.63 to Navient for unpaid student loans. *Id.* at 721:6–722:16; Defs.' Hrg. Ex. 112.

Despite his seemingly bleak financial picture, there was evidence presented that Nadel may not be quite so destitute. First, the evidence shows that Nadel withdrew over $2 million from individual retirement accounts between 2010–2012, *see* Defs.' Hrg. Ex. 99 at 1126–1139 ($1.9 million withdrawal in 2010); 1212–1218 ($146,000 withdrawal in 2011); 1226–1232 ($82,000 withdrawal in 2012). As of 2012, both Nadel and his wife held over $500,000 in assets in multiple brokerage and / or retirement accounts. *Id.* at 1246 ($141,546.83 held at TD Ameritrade in Acct. ending 807191), 1420 ($55,715.62 held at TD Ameritrade in Acct. ending 698796), 1600

($223,829.10 held at TD Ameritrade in Acct. ending 913748), 1776 ($59,240.82 held at TD Ameritrade in Acct. ending in 730456), 1975 ($68,860.28 held at TD Ameritrade in Acct. ending 698545). During the hearing, Nadel did not address these particular funds or otherwise produce records establishing the whereabouts of this money at the present time. However, when pressed regarding IRA withdrawals in general, Nadel stated "I don't consider taking money out of an IRA [and] putting it into a firm [and] paying myself necessarily a stream of income...." Hrg. Tr. at 841:22–25.

Moreover, when questioned regarding certain bank account transfer activity, Nadel was vague and somewhat evasive in his responses. For example, when questioned concerning a $214,937.47 deposit into his joint checking account and an immediate withdrawal on the same date of $200,000 into two unidentified savings accounts, Nadel responded:

> Q: What does [the $214,937.47] correspond to? Or why did you receive that amount?
>
> A: I don't specifically recall
>
> Q: Do you see the entry below dated the same date? Do you see that?
>
> A: Yes, I see the $200,000 withdrawal.
>
> Q: You see two withdrawals of 100[,000]?
>
> A: Actually, transfer to savings account.
>
> Q: The first one is to savings 5580. Is that the one that you believe may be your daughter's savings account, sir?
>
> A: I honestly don't remember.
>
> Q: What about the savings 7357? Does that refresh your memory as to whose savings account that is?
>
> A: No.

Id. at 805:14–806:6. Despite the above testimony and Nadel's seeming inability to recollect whether the first $100,000 transfer to a savings account ending in 5580 was an account held by his daughter, Nadel had nevertheless previously testified that he believed the account ending in 5580 was, in fact, his daughter's account. *See id.* at 801:12–17.

Another area which Nadel neglected to fully explain during his testimony involved the receipt of a significant amount of rental income on the properties held by Emancipation Corporation between 2011 and 2013.[18] For example, although Nadel highlighted the fact that in 2013 Emancipation Corporation had no gross receipts or sales and operated at a loss of—$162,919, *see id.* at 687:9–16, he neglected to identify or explain the $531,095 in rental income that Emancipation Corporation received in tax year 2013. *See* Defs.' Hrg. Ex. 99 at 2338, 2345. Similarly, Nadel did not address or explain the $543,291 in rental income received in 2012 nor the $569,162 received in 2011. *See id.* at 2275, 2283, 2218. When confronted with this information, Nadel disavowed the receipt of rental income, claiming instead that rental income "goes right into Emancipation Corporation and [ ] is paid out to mortgage payments. It was not income that I would sit there and wait with my bushel basket to pick up." Hrg. Tr. at 818:6–9. However, since Nadel is the owner of Emancipation Corporation, *see id.* at 818:10–11, these payments would have effectively been made to him in any event. Nevertheless, Nadel could not account for the receipt of these funds other than to suggest that the funds were used to pay mortgage payments. *See id.* at 818:4–15.

***26** Nadel was also unable to produce rental statements or any other documentation for any of the three properties currently held by Emancipation Corporation. *Id.* at 818:10–11819:4–11. Moreover, certain deposits credited to Emancipation Corporation's corporate bank accounts, along with wire transfers from the Caribbean (where his property in Turks and Caicos is located), belie the notion that he is unable to properly account for these as well as other sums. *See, e.g.*, Defs.' Hrg. Ex. 99 at 3520 (wire transfer in the amount of $23,916.59 made on January 1, 2014 from the Grace Bay Club[19] into Acct. ending 9876); 3624 (deposit in the amount of $50,000 made on March 23, 2015 from Acct. ending 6075).

Although Nadel's present and future financial condition, as presented through hearing testimony and documentary evidence, does not appear to be robust, there are some gaps and otherwise fairly sizable amounts of income which have thus far been unexplained. As such, the Court finds that this factor weighs narrowly in favor of the imposition of third-tier civil penalties.

3. Imposition and Amount of Penalty

After considering all of the above factors in conjunction with the unique factual circumstances which exist in this case, the Court finds that the imposition of a third-tier penalty is appropriate. *See Opulentica,* 479 F.Supp.2d at 331 (quoting *Moran,* 944 F.Supp. at 296–97); *Tavella,* 77 F.Supp.3d at 363; *see also Neurotech,* 2011 WL 1113705, at *4 (imposition of third-tier penalty appropriate where defendants made misleading statements and engaged in reckless conduct); *East Delta Resources,* 2012 WL 3903478, at *9. As such, having determined that imposition of a third-tier penalty is appropriate, the remaining issue is the proper amount to be imposed.

Nadel's conduct was egregious, deliberate, and resulted in the risk of significant losses and continued for a span of several years. As such "the seriousness of [Defendants'] wrongdoing justifies a serious punitive response." *Spongetech Del. Sys., Inc.,* 2015 WL 5793303, at *11. In addition, Nadel's failure to acknowledge his wrongdoing must also be taken into consideration in calculating the total amount of the penalty to be levied. *See McCaskey,* 2002 WL 850001, at *14; *S.E.C. v. Coates,* 137 F.Supp.2d 413, 430 (S.D.N.Y.2001); *Moran,* 944 F.Supp. at 297. However, the Court is also mindful that "despite the severity of [Defendants'] violations and the extent to which those violations should be punished ... the Court also considers the extent to which other aspects of the relief and/or judgment issued in this matter will have the desired punitive effect." *Univ. Express, Inc.,* 646 F.Supp.2d at 568. In addition, although gaps admittedly exist in Defendants' overall financial picture, the Court cannot ignore the documentary evidence presented—including tax returns for the individual and corporate Defendants, tax liability notices, mortgage lien notices, student loan accounting and at least some bank account statements – evidencing Defendants' distressed financial condition which lends some credence to the assertions of their inability to pay a maximum monetary penalty on top of an award of disgorgement and prejudgment interest.

In light of the above, and mindful of the fact that "to withhold the remedy of [a civil] penalty simply because a swindler claims that she has already spent all the loot and cannot pay would not serve the purposes of the securities laws," *S.E.C. v. Inorganic Recycling Corp.,* No. 99 Civ. 10159, 2002 WL 1968341, at *4 (S.D.N.Y. Aug. 23, 2002), the Court finds that the imposition of a third-tier civil penalty in the amount of $1,000,000 is appropriate. *See Univ. Express, Inc.,* 646 F.Supp.2d at 568 (levying a monetary penalty of $1,000,000 and noting that this amount was appropriate since defendant would already be required to pay $13 million in disgorgement and prejudgment interest and had been permanently enjoined from participating in trading stock); *Svoboda,* 409 F.Supp.2d at 348 (viewing defendant's financial submissions "with skepticism" but determining that imposition of over $3 million in civil penalties on top of $2.2 million "already imposed ... and the $300,000 fine assessed ... goes too far" and instead imposing a lesser penalty amount); *Neurotech,* 2011 WL 1113705, at *6 (finding that defendant's "current situation and the other remedies awarded against him ... [warrant] a reduced penalty [which] would serve the purpose of deterring future conduct"); *but see Spongetech Del. Sys., Inc.,* 2015 WL 5793303, at *11 (imposing maximum third-tier civil penalties but noting that despite defendant's submission of a financial affidavit in support of his inability to pay a penalty, "he failed to make any showing regarding his actual financial condition ... [and] has not supported his claims with any documentation....").

*27 Based upon the foregoing assessment, the Court respectfully recommends to Judge Kuntz that a third-tier civil penalty be imposed upon Defendants in the amount of $1,000,000.

F. Liability of Relief Defendant

1. Applicable Law

"Federal courts may order equitable relief against a person who is not accused of wrongdoing in a securities enforcement action where that person: (1) has received ill-gotten funds; and (2) does not have a legitimate claim to those funds. *Cavanagh I,* 155 F.3d at 136; *see Contorinis,* 743 F.3d at 307–08 (noting that since "disgorgement is designed to equitably deprive those who have obtained ill-gotten gains of enrichment, it may be imposed upon innocent third parties who have received such ill-gotten funds and have no legitimate claim to them."); *Commodity Futures Trading Comm'n v. Walsh,* 618 F.3d 218, 226 (2d Cir.2010) ("District courts may only require disgorgement of the assets of a relief defendant upon a finding that

she lacks a 'legitimate claim.' "). Thus, "[w]hen there has been no consideration given for the receipt of the ill-gotten gains, there is no legitimate claim to the funds and a relief defendant must return the proceeds." *S.E.C. v. Aimsi Techs., Inc.*, 650 F.Supp.2d 296, 304 (S.D.N.Y.2009).

2. Application to the Facts

The Commission seeks to disgorge from Relief Defendant, Katherine Nadel, the sum of $807,346.51 in ill-gotten gains in addition to $156,033.03 in prejudgment interest calculated on that amount. *See* Plaintiff Securities and Exchange Commission's Post–Hearing Brief on Remedies ("Pl.'s Post Hearing Br.") at 19. As such, the total amount sought to be disgorged from the Relief Defendant is $963,379.85. *See* Pl.'s Hrg. Ex. 208. The Commission provided underlying support for the principal amount of disgorgement in the form of a Declaration from Warren D. Nadel as well as Schedule K–1 forms showing distributions made to Katherine Nadel from RIA. Based upon these submissions, the Court finds that the principal amount is adequately substantiated. *See* Pl.'s Hrg. Ex. 138 at ¶ 20 (showing chart prepared by Warren D. Nadel outlining direct compensation amounts paid by WDNC to third-parties for calendar years 2007–2009); Pl.'s Hrg. Exs. 20 at 2, 4; 173 at 18 (Schedule K–1 forms for Katherine Nadel showing distributions made from RIA).[20] In addition, the Commission's examiner Fioribello stated during the damages hearing that the amount of prejudgment interest was calculated using the Commission's prejudgment interest calculator, which itself uses the Internal Revenue Service underpayment rate. *See* Hrg. Tr. at 205:16–206:2; Pl.'s Hrg. Ex. 208. The Court therefore finds an adequate factual basis substantiating the amount of prejudgment interest sought.

***28** In light of the fact that the Relief Defendant received a total of $807,346.51 from RIA and WDNC between calendar years 2007 and 2009 – which encompassed the violations period in this case – the Court finds that these funds constituted ill-gotten gains to the Relief Defendant.[21] Therefore, the sole issue for the Court to determine is whether the Relief Defendant had a legitimate claim to these funds. *See Cavanagh I*, 155 F.3d at 136; *Contorinis*, 743 F.3d at 307–08.

At the damages hearing, the Relief Defendant testified concerning the duration and scope of her employment with WDNC and RIA. In addition, Plaintiff introduced the Relief Defendant's earlier deposition testimony taken on August 3, 2011. *See* Pl.'s Hrg. Ex. 176.[22]

During her deposition, the Relief Defendant testified that she was trained as a registered nurse and that apart from a few credits taken at Mercy College in the field of psychology, she had no other post-high school education and did not hold any other professional licenses. Pl.'s Hrg. Ex. 176, 10:6–11:6. After working in the field of nursing for approximately 13 years, and following a period of unemployment, the Relief Defendant went to work for her husband, Warren Nadel, in 2000. *Id.* at 11:13–25. With respect to her duties at WDNC, the Relief Defendant stated she performed primarily "secretarial kind of work" which included decorating the office, ordering supplies and keeping the office and facility clean. *Id.* at 12:4–14. Relief Defendant stated that her official title was Chief Operating Officer because she oversaw operation of the facility, but she stated that she had no training and held no licenses in the securities industry. *Id.* at 16:10–24. In addition, Katherine Nadel testified that she did not work full time, that her hours varied on a daily basis and she estimated her hours worked per week as "[s]ometimes 15, sometimes 50." *Id.* at 17:15–25. Further, when asked whether she "ha[d] any responsibilities at any time at [WDNC] for the operation of the business itself," she responded "No." *Id.* at 20:9–12. Katherine Nadel also stated that although she acted as WDNC's corporate secretary, *see id.* at 16:25–17:9, she had no responsibilities for maintaining the books and records. *Id.* at 21:7–9.

With respect to RIA, the Relief Defendant stated in her deposition that she was a partner, but nevertheless could not clarify whether she actually owned any part of the business or whether she received distributions, stating only that "I may have been paid a salary from there, but I don't know." *Id.* at 21:10–22:4. Her primary knowledge concerning her partnership role at RIA seemed to be the fact that she signed RIA's tax returns. *Id.* at 24:3–9. In addition, Relief Defendant stated that she could not identify a distinction between the businesses of WDNC and RIA, that she had no role in running or operating RIA and contributed no capital to the RIA partnership. *Id.* at 30:5–14.

***29** Notwithstanding this earlier deposition, the testimony provided by the Relief Defendant at the damages hearing differed considerably with respect to

the duration of her employment and the range of her responsibilities at WDNC and RIA. For instance, during the hearing, Relief Defendant testified that she had worked at WDNC since 1987 as Chief Operating Officer and Corporate Secretary and had varied roles, including: responsibility for written supervisory procedures for both WDNC and RIA, for human resources and for keeping current with publications. Hrg. Tr. at 601:9–602:3. Specifically, Relief Defendant stated that she was "in charge of personnel," *id.* at 603:18, was responsible for the "physical plants,"[23] *id.* at 605:24606:17, kept track of the books and corporate meeting minutes, represented the company in the community and otherwise held a supervisory role which included mediating territorial disputes among the brokers. *Id.* at 606:19–609:4. In addition, Relief Defendant stated that she worked a total of approximately 35 hours per week between 2007 and 2009 and considered her work to be full-time. *Id.* at 609:5–10.

In addition to the discrepancies between the Relief Defendant's deposition and hearing testimony, the facts demonstrate that payments from WDNC and RIA to her were altogether inconsistent. For example, of the total $807,346.52 that the Commission seeks to disgorge, Relief Defendant received $435,800 in 2007 alone. *See* Pl.'s Hrg. Ex. 20 at 2 (Distribution of $210,800 from RIA); Pl.'s Hrg. Ex. 138 ¶ 20 (receipt of $225,000 from WDNC). However, in calendar years 2008 and 2009, the Relief Defendant's combined payments from RIA and WDNC totaled $235,559.92 and $135,986.60 respectively. *See* Pl.'s Hrg. Exs. 20 at 2, 4; 173 at 18; 138 ¶ 20. Further, when Relief Defendant's compensation is broken out separately, the difference in amounts between 2007 and 2009 are even more apparent. For instance, with regard to payments from WDNC, Relief Defendant purportedly received $225,000 in 2007, $49,999.92 in 2008 and $41,666.60 in 2009. *See* Pl.'s Hrg. Ex. 138 ¶ 20. As to payments from RIA, in which Relief Defendant had no role and otherwise made no capital contribution, *see* Pl.'s Hrg. Ex. 176 at 30:9–14, she nevertheless received $210,800 in 2007, $185,560 in 2008 and $94,320 in 2009. *See* Pl.'s Hrg. Exs. 20 at 2, 4; 173 at 18.

When confronted at her deposition about the lopsided payments from WDNC between 2007 and 2009, Relief Defendant's only answer was that she "must have been doing less work." Pl.'s Hrg. Ex. 176 at 36:2:37:2. Further, comparing Relief Defendant's payments from WDNC to those of Warren Nadel's executive assistant, Ethel Waldron, for the same period lends credence to the assertion that Relief Defendant's payments had little if any relationship with the scope and duration of her duties. *See* Pl.'s Hrg. Ex. 138 ¶ 20 (noting both Relief Defendant's and Ethel Waldron's payments from WDNC for 2007–2009 and confirming the linear nature of Ethel Waldron's payments when compared to Relief Defendant's payments).

After considering the Relief Defendant's deposition transcript and hearing testimony as well as the evidence presented concerning the overall amount of payments received by her from both WDNC and RIA for what she asserts were services rendered, the Court finds that Relief Defendant does not possess a legitimate claim to the funds. Most troubling to the Court, in addition to the Relief Defendant's contradictory testimony, is the overall disjointed amounts of compensation she received, for which she provided no plausible explanation. In addition, whatever her ultimate role may have been, the Court is hard pressed to find plausible the fact that in 2007 alone, Relief Defendant's contributions, in the form of services performed, warranted a total gross payment from WDNC and RIA of $435,800—especially when compared to payments made in 2008 and 2009. In addition, the fact that Ethel Waldron's payments remained altogether consistent during this same time period further belies the notion that the payments made to Relief Defendant were in consideration of the services she performed.

***30** In light of the above information, the Court finds that the Relief Defendant remained in possession of ill-gotten gains to which she had no rightful claim. Thus, disgorgement is appropriate here. Indeed, in a case such as this, "the broad equitable powers of the federal courts can be employed to recover ill[-]gotten gains for the benefit of the victims of wrongdoing, whether held by the original wrongdoer or by one who has received the proceeds after the wrong." *S.E.C. v. Colello,* 139 F.3d 674, 676 (9th Cir.1998) (alteration added). *See U.S. Commodity Futures Trading Comm'n v. EJS Capital Mgmt., LLC,* No. 14 CV 3107, 2015 WL 5679688, at *4 (S.D.N.Y. Sept. 24, 2015) (noting that disgorgement from a relief or nominal defendant is appropriate where relief defendant is "in possession of funds to which they have no rightful claim, such as money that has been fraudulently transferred by the defendant in the underlying securities or commodity futures enforcement action"); *S.E.C. v. China Energy*

Sav. Tech., Inc., 636 F.Supp.2d 199, 204 (E.D.N.Y.2009) ("District courts are authorized to order disgorgement from parties who, though not directly involved, profit from a fraud and have no just claim to their profits."); see also S.E.C. v. Egan, 856 F.Supp. 401, 402 (N.D.Ill.1993) ("To be sure, Relief Defendants may not have been directly culpable in the securities violations, but what the SEC seeks to have them disgorge are the benefits that they derived from the violations by the culpable defendants."); S.E.C. v. Ross, 504 F.3d 1130, 1142–44 (9th Cir.2007) (suggesting that a "mere puppet" or "empty vessel into which the true wrongdoers funneled their proceeds" would be a nominal defendant).

The Court respectfully recommends to Judge Kuntz that disgorgement in the amount of $807,346.52, coupled with prejudgment interest in the amount of $156,033.03, for a total overall amount of $963,379.85, be awarded to the Commission.

IV. *CONCLUSION*

For the foregoing reasons, the Court respectfully recommends to Judge Kuntz that:

(1) the Commission's request for permanent injunctive relief against Defendants be granted;

(2) the Commission be awarded disgorgement in the amount of $10,776,687.62;

(3) the Commission be required to submit a revised prejudgment interest calculation based upon the deduction of $183,026.68 from total disgorgement, this amount representing clearing charges paid by Defendants to RBC to execute the cross-trades during the period January 1, 2007 through December 31, 2009;

(4) Defendants be found jointly-and-severally liable for the total amount of disgorgement and prejudgment interest to be awarded;

(5) a third-tier civil penalty be imposed upon Defendants in the amount of $1,000,000; and

(6) Relief Defendant be ordered to disgorge $807,346.52, coupled with prejudgment interest in the amount of $156,033.03, for a total overall amount of $963,379.85.

V. *OBJECTIONS*

Pursuant to 28 U.S.C. § 636(b)(1)(c) and Rule 72 of the Federal Rules of Civil Procedure, the parties shall have fourteen (14) days from service of this Report and Recommendation to file written objections. *See also* FED. R. CIV. P. 6(a), (e). Such objections by an attorney of record shall be filed with the Clerk of the Court via ECF. ***A courtesy copy of any objections filed is to be sent to the Chambers of the Honorable William F. Kuntz, and to the Chambers of the undersigned. Any requests for an extension of time for filing objections must be directed to Judge Kuntz prior to the expiration of the fourteen (14) day period for filing objections.*** Failure to file objections will result in a waiver of those objections for purposes of appeal. *Thomas v. Arn*, 474 U.S. 140, 155 (1985); *Beverly v. Walker*, 118 F.3d 900, 901 (2d Cir.1997), *cert. denied*, 522 U.S. 883 (1997); *Savoie v. MerchantsBank*, 84 F.3d 52, 60 (2d Cir.1996).

SO ORDERED.

All Citations

Slip Copy, 2016 WL 639063, Fed. Sec. L. Rep. P 99,024

Footnotes

1 For purposes of this Report and Recommendation, the Court presumes the reader's familiarity with Judge Kuntz's Summary Judgment Decision and Order, which includes a detailed statement of the underlying facts of this case. *See* DE 100. As such, this Court will dispense with a detailed account of the underlying facts. The Court further points out that citations to Judge Kuntz's Decision and Order are made pursuant to the version published in the Federal Supplement.

2 Section 206(3) of the Advisers Act, codified at 15 U.S.C. § 80b–6, provides, in pertinent part, that "[i]t shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly– (3) acting as principal for his own account, knowingly to sell any security to or purchase any security from a client, or acting as broker for a person other than such client, knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transaction. The prohibitions of this paragraph shall

not apply to any transaction with a customer of a broker or dealer if such broker or dealer is not acting as an investment adviser in relation to such transaction[.]"

3 Rule 10b–10 "requires broker-dealers to disclose specified information in writing to customers at or before completion of a transaction. The requirements under this section that particular information be disclosed is not determinative of a broker-dealer's obligation under the general antifraud provisions of the federal securities laws to disclose additional information to a customer at the time of the customer's investment decision." 17 C.F.R. § 240.10b–10.

4 Judge Kuntz found that Defendants' failure to provide trading confirmations which correctly denoted whether the broker or dealer was acting in a principal or agency capacity violated Rule 10b–10 of the Exchange Act. *See Nadel,* 97 F.Supp.3d at 130.

5 All subsequent references to the record of the July 2015 Damages Hearing are designated "Hrg. Tr. at ____."

6 Judge Kuntz found that Defendants' misrepresentation to both clients and prospective clients concerning the amount of assets they had under management violated Section 10(b) of the Exchange Act and Rule 10b–5 thereunder. *See Nadel,* 97 F.Supp.3d at 122.

7 Judge Kuntz stated in his summary judgment decision that "Part I filings with the SEC revealed that Defendants overstated the actual amount of assets under management. Specifically, RIA's assets under management were only $147.28 million in January 2007; $147.37 million in January 2008; $127.63 million in January 2009; and $54.84 million in January 2010 —not the over $400 million that RIA claimed in its marketing materials, a fact undisputed by Defendants." *Nadel,* 97 F.Supp.3d at 120.

8 All page references are made pursuant to PDF page numbers.

9 Nadel's response to the Commission's inquiry was that "[a]s a result of my review of our firm's web site in connection with the commencement of this audit, the claim as to assets under management was noted and deleted." Pl.'s Hrg. Ex. 35. Although the AUM claim may have been deleted from Defendants' website, the record demonstrates that this statement was, at best, disingenuous in as much as Defendants continued to disseminate emails misrepresenting the amount of AUM and sending these emails to prospective clients. *See* Pl.'s Hrg. Exs. 19; 135.

10 Judge Kuntz found that Defendants' failure to obtain transaction-by-transaction notice and consent before engaging in principal transactions and by conducting cross-trading violated Section 206(3) of the Advisers Act. In addition, Judge Kuntz determined that "[a]lthough Defendants claim that certain trade confirmations sent to clients advised them that 90% of transactions were cross-trades, this is simply not the case ... Nothing in the documents suggests that 90% of the transactions were cross-trades." *See Nadel,* 97 F.Supp.3d at 129.

11 Plaintiff's Exhibits 9 and 10 illustrate summary data for Defendants' 11 Corporate Advisory Clients. Exhibit 9 encompasses the date range January 1, 2007 through February 29, 2008, while Exhibit 10 encompasses the dates of March 1, 2008 through December 31, 2009. When Column 5, "Commission on Crosses" in Exhibit 9 is added together with Column 5 in Exhibit 10, the total Commissions on Crosses is $5,404,849.40. However during his hearing testimony, Michael Fioribello, the Commission's examiner, stated that due to a miscalculation "the commissions on crosses [in Exhibit 10] was approximately, after the change, $20,000 less than the number that is stated [in Exhibit 10]." Hrg. Tr. at 183:15–184:16. This accounts for the difference in the total "Commissions on Crosses" contained when summing up Column 5 in Exhibits 9 and 10 and the amount the Commission is seeking as part of Defendants' profits in conjunction with the illicit cross-trading.

12 A principal trade is "an example of [Defendants'] proprietary account, both buying and selling the same security on the same date but at a different price." *See* Hrg. Tr. at 185:4–6 (Fioribello testimony).

13 For the reasons stated in this section, the payments totaling $218,783.33 that were made to Nat Allen and Joe Saxton, Hrg. Tr. at 751:14–763:14, likewise do not constitute direct transaction costs and should therefore not be applied to reduce the Defendants' total amount of disgorgement.

14 The parties stipulated on the record that "the clearance charges are as stated on the front of [Defendants'] Exhibit 103.... " Hrg. Tr. at 771:20–772:3. *See* Defendant's Hearing Exhibit ("Defs.' Hrg. Ex.") 103 at 1 (noting the total amount of clearing charges incurred from 20072009 as $301,201.90).

15 The maximum statutory amounts are periodically adjusted for inflation. *See Tavella,* 77 F.Supp.3d at 362; *China Energy Sav. Tech., Inc.,* 2008 WL 6572372, at *15. The inflationary adjustments are set forth in 17 C.F.R. §§ 201.1001–201.1005.

16 The citation format used to refer to certain portions of Walter Boilieu's testimony differs from the overall citation format due to an alteration in the pagination of the hearing transcript.

17 Nadel also testified that the property owned by Emancipation Corporation which was located in Brentwood, New York, has since been sold and therefore "that would reduce the item *asset real estate Emancipation New York* from $520,900 to $260,900." Hrg. Tr. at 722:17–21 (emphasis in original).

18 Nadel confirmed that he was the owner of Emancipation Corporation. Hrg. Tr. at 818:10–11.

19 The Grace Bay Club is the name of the residential complex located on Turks and Caicos where Nadel owns a villa. Hrg. Tr. at 694:4–12.

20 In a footnote in their post-hearing brief, Defendants allege that "the Schedule K–1 Instructions make clear that one should 'not include the amount of property distributions included in the partner's income.' " Def.'s Post–Hearing Br. at 14 n. 8 (citing I.R.S.2014 Instructions for Schedule K–1 at 2). However, Defendants have not provided any case law supporting this proposition, nor has this issue been properly put before the Court in Defendants' post-hearing brief. As such, the Court declines to consider the issue and notes that in any event, even if the distributions are not treated as "income" from a taxation perspective, the Schedule K1 clearly shows that a distribution was made in cash to the Relief Defendant and thus there is at least a strong inference that the Relief Defendant took custody of these funds.

21 The Court notes that in their post-hearing brief, Defendants did not argue against the assertion by the Commission that the Relief Defendant received ill-gotten funds, other than with respect to the perfunctory argument made by Defendants in note 8 of their brief which the Court has previously addressed. *See* n. 20 *supra.*

22 During the Commission's case-in-chief, it sought leave to admit the August 3, 2011 deposition testimony of Katherine Nadel in lieu of calling her as a witness at the hearing. *See* Hrg. Tr. at 593:3–6. There being no objection from Defendants' counsel, the Court admitted the deposition testimony. See Hrg. Tr. at 593:16–22; Pl.'s Hrg. Ex. 190.

23 Despite testifying that the physical structure housing RIA and WDNC was owned by Emancipation Corporation, Relief Defendant testified that she did not work for Emancipation Corporation and did not perform the facilities work on its behalf. Hrg. Tr. at 636:25–637:17.

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EXHIBIT 4

206 F.Supp.3d 782
United States District Court,
E.D. New York.

SECURITIES & EXCHANGE COMMISSION, Plaintiff,
v.
Warren D. NADEL; Warren D. Nadel & Co.; and Registered Investment Advisers, LLC, Defendants,
and
Katherine Nadel, Relief Defendant.

11-CV-215 (WFK) (AKT)
|
Signed September 8, 2016
|
Filed September 9, 2016

Synopsis

Background: Securities and Exchange Commission (SEC) filed civil enforcement action alleging that broker-dealer, investment adviser, and their principal fraudulently induced broker-dealer's clients to invest in investment strategy by misrepresenting to clients and to prospective clients amount of assets they had under management and by failing to provide written notice and to obtain consent for cross-trade transactions amongst clients, in violation of Securities Exchange Act, Securities Act, and Investment Advisers Act. Summary judgment was entered in SEC's favor, 97 F.Supp.3d 117.

Holdings: The District Court, William F. Kuntz, II, J., adopted report and recommendation of A. Kathleen Tomlinson, United States Magistrate Judge, 2016 WL 639063, and held that:

[1] defendants were not entitled to offset their principal trading losses in calculating disgorgement amount;

[2] SEC properly incorporated into its disgorgement calculation brokerage commissions obtained from all of defendants' unlawful transactions, including those that resulted in loss;

[3] defendants were not entitled offset payments to financial consultants in calculating disgorgement amount;

[4] payments to client that stemmed from their non-compliance with client's investment policy could not be offset from disgorgement;

[5] payments made to execute "hedging" trades could not be used as offset from disgorgement; and

[6] payments to principal's wife were subject to disgorgement.

Ordered accordingly.

West Headnotes (8)

[1] **Securities Regulation**
↩ Relief granted in general

Civil penalties may not be imposed on joint and several basis in Securities and Exchange Commission (SEC) enforcement actions.

Cases that cite this headnote

[2] **Securities Regulation**
↩ Insiders' Profits, Recovery of

Broker-dealer, investment adviser, and their principal were not entitled to offset their principal trading losses in calculating disgorgement amount in Securities and Exchange Commission (SEC) civil enforcement action alleging that they fraudulently induced broker-dealer's clients to invest in investment strategy, where SEC expressly considered all principal trades during relevant period and incorporated only those groups of principal trades resulting in overall net profit, and any principal trades that included some internal profit but resulted in overall net loss were not incorporated into SEC's disgorgement figure.

Cases that cite this headnote

[3] **Securities Regulation**
↩ Insiders' Profits, Recovery of

Profit made on independently unlawful trade is subject to disgorgement in Securities and Exchange Commission (SEC) enforcement action regardless of whether losses were sustained on any other transaction.

Cases that cite this headnote

[4] **Securities Regulation**
Insiders' Profits, Recovery of

In calculating disgorgement amount in Securities and Exchange Commission (SEC) civil enforcement action, SEC properly incorporated into its disgorgement calculation brokerage commissions obtained from all of defendants' unlawful transactions, including those that resulted in loss.

3 Cases that cite this headnote

[5] **Securities Regulation**
Insiders' Profits, Recovery of

Payments by broker-dealer, investment adviser, and their principal to financial consultants were not brokerage commissions, and thus they were not entitled offset payments to them in calculating disgorgement amount in Securities and Exchange Commission (SEC) civil enforcement action, where it was principal himself who executed trades, received commission income from trades, and parsed out their share based upon fee arrangement.

Cases that cite this headnote

[6] **Securities Regulation**
Insiders' Profits, Recovery of

Payments made by broker-dealer, investment adviser, and their principal to client that stemmed from their non-compliance with client's investment policy were not repayment of ill-gotten gain that could be offset from disgorgement in Securities and Exchange Commission (SEC) civil enforcement action.

Cases that cite this headnote

[7] **Securities Regulation**
Insiders' Profits, Recovery of

Payments made by broker-dealer, investment adviser, and their principal in order to execute "hedging" trades were not unlawful, and thus could not be used as offset from disgorgement in Securities and Exchange Commission (SEC) civil enforcement action, even though defendants intended trades to hedge against losses incurred in other, unlawful trades, where trades themselves did not violate any securities laws.

Cases that cite this headnote

[8] **Securities Regulation**
Insiders' Profits, Recovery of

Wife of broker-dealer's and investment adviser's principal lacked any plausible legitimate claim to funds paid to her for period during which broker-dealer and investment adviser executed fraudulent investment scheme, and thus wife was required to disgorge funds in Securities and Exchange Commission (SEC) civil enforcement action, despite her contention that she had plausible legitimate claim to funds based on her work for defendant companies, where wife had very limited role at companies consisting mostly of secretarial work, but received $807,346.52 over three year period, while principal's full-time assistant received consistent income of $74,363.66 over same time frame.

Cases that cite this headnote

Attorneys and Law Firms

*783 George S. Canellos, Jorge G. Tenreiro, Richard G. Primoff, Andrew M. Calamari, Maureen Peyton King, United States Securities and Exchange Commission, New York, NY, for Plaintiff.

Michelle N. Tanney, Paulina A. Stamatelos, Samuel Jay Lieberman, Sadis & Goldberg, LLP, New York, NY, for Defendants.

DECISION & ORDER

WILLIAM F. KUNTZ, II, United States District Judge

The Securities and Exchange Commission ("SEC") brought this action against Defendants Warren D. Nadel ("Nadel"), Warren D. Nadel & Co. ("WDNC"), and Registered Investment Advisers, LLC ("RIA") (collectively, "Defendants"), as well as Relief Defendant Katherine Nadel ("Relief Defendant"), seeking damages and injunctive relief for alleged violations of the Securities Act of 1933 ("Securities Act"), the Securities Exchange Act of 1934 ("Exchange *784 Act"), and the Investment Advisers Act of 1940 ("Advisers Act"). ECF No. 11 ("Amended Complaint"). On March 31, 2015, the Court granted the SEC's motion for partial summary judgment and denied Defendants' cross-motion for summary judgment. ECF No. 100 ("Summary Judgment Order"). The Court referred the issue of relief to Magistrate Judge Tomlinson, who conducted a four-day evidentiary hearing and issued a Report and Recommendation on February 11, 2016. ECF No. 128 ("R&R"). Defendants filed their objections to the Report and Recommendation on March 8, 2016, and the SEC filed its reply papers on April 8, 2016. ECF Nos. 130 ("Objections"), 131 ("Reply"). After a *de novo* review of the record, the Court ADOPTS the Report and Recommendation.

BACKGROUND

The Court assumes the parties' familiarity with the underlying facts of this case, which are detailed in the Court's Summary Judgment Order and Magistrate Judge Tomlinson's Report and Recommendation.

On March 31, 2015, the Court granted the SEC's motion for summary judgment against Defendants for violations of: (1) Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rules 10b-5 and 10b-10 promulgated by the SEC thereunder, 17 C.F.R. §§ 240.10b–5, 240.10b–10; (2) Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a); and (3) Sections 206(1), 206(2), and 206(3) of the Advisers Act, 15 U.S.C. § 80b–6. Summary Judgment Order at 1. The Court reserved decision on the issue of relief at that time, referring it to Magistrate Judge Kathleen Tomlinson for further fact-finding. *Id.* at 21-22. Magistrate Judge Tomlinson conducted an evidentiary damages hearing over a period of four days, from July 20, 2015, through July 23, 2015. R&R at 2.

On February 11, 2016, Magistrate Judge Tomlinson issued a Report and Recommendation recommending the Court: (1) grant the SEC's request for permanent injunctive relief against Defendants; (2) award the SEC disgorgement in the amount of $10,776,687.62; (3) require the SEC to submit a revised prejudgment interest calculation based upon a deduction of $183,026.68 in clearing charges from total disgorgement; (4) find Defendants jointly-and-severally liable for the total amount of disgorgement and prejudgment interest to be awarded; (5) impose a third-tier civil penalty on Defendants in the amount of $1,000,000.00; and (6) order the Relief Defendant to disgorge $963,379.85, inclusive of prejudgment interest. *Id.* at 64-65. Defendants filed objections to the Report and Recommendation on March 8, 2016, and the SEC filed reply papers on April 8, 2016. *See* Objections; Reply. After a *de novo* review of the record, the Court ADOPTS the recommendations contained in the Report and Recommendation as follows.

DISCUSSION

I. Legal Standard

In reviewing a Report and Recommendation, the Court "may accept, reject, or modify, in whole or in part, the findings or recommendations made by the magistrate judge." 28 U.S.C. § 636(b)(1). The Court must conduct a *de novo* review of any contested portions of the Report and Recommendation when a party makes specific objections to the magistrate judge's findings. *Norman v. Metropolitan Transp. Authority*, 13–CV–1183, 2014 WL 4628848, at *1 (E.D.N.Y. Sept. 15, 2014) (Matsumoto, J.). The Court is "permitted to adopt those sections of a magistrate judge's report to which no specific objection is made, so long as those sections are not facially erroneous." *Id.* (citing *785 *Batista v. Walker*, 94–CV–2826, 1995 WL 453299, at *1 (S.D.N.Y. July 31, 1995) (Sotomayor, J.)).

II. Analysis

A. Injunctions and Civil Penalties

[1] In her Report and Recommendation, Magistrate Judge Tomlinson recommends (1) Defendants be permanently enjoined from future violations of the anti-fraud provisions of the securities laws and (2) Defendant

Nadel be required to pay $1,000,000.00 in third-tier civil penalties. R&R at 20, 57. Neither party objected to these recommendations. After a careful *de novo* review of the record, the Court ADOPTS those sections of the Report and Recommendation concerning injunctions and civil penalties. [1]

B. Defendants' Disgorgement

Magistrate Judge Tomlinson recommends this Court order Defendants to disgorge $10,959,714.30—the disgorgement figure calculated by the SEC—less $183,026.68 in clearing costs, plus prejudgment interest. *Id.* at 24, 35, 41–42. Defendants do not object to the imposition of disgorgement or prejudgment interest. Rather, Defendants contend they are entitled to further offsets from the disgorgement figure calculated in the Report and Recommendation. Objections at 1. The Court addresses each of Defendants' arguments in turn.

1. Principal Trades

Defendants object to Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset of $2,256,644.54 in principal trading losses, as these losses "were netted out... and thus should not be double-counted by offsetting [them] from the overall disgorgement figure." R&R at 28. First, Defendants argue the SEC improperly incorporated the commissions earned on Defendants' losing principal trades into its disgorgement calculation, while excluding the trading losses suffered on these trades. Objections at 4. Second, Defendants cite to *SEC v. McCaskey*, 98–CV–6153, 2002 WL 850001, at *4 (S.D.N.Y. Mar. 26, 2002) (Peck, M.J.), for the proposition that the SEC erred in excluding Defendants' principal trading losses from disgorgement while including principal trading profits occurring at the same time—and as part of the same scheme—as the losing trades. Objections at 5. Third, Defendants argue it is improper for the SEC to exclude principal trading losses from its disgorgement calculation because it is undisputed that Defendants had larger total principal trading losses than profits. *Id.* at 8.

To Defendants' first objection, the SEC responds that it was proper to include brokerage commissions from Defendants' losing trades into their disgorgement calculation, as such commissions represent a wholly separate stream of unlawful income from any profits obtained through the trades themselves. Reply at 11-12. In response to Defendants' second and third objections, the SEC argues *McCaskey* is inapposite, as that case involved a series of otherwise facially valid trades which became unlawful only when considered together. *Id.* at 10. In this case, however, the SEC argues that each of Defendants' trades was independently unlawful, and therefore disgorgement should be measured without regard for any separate unprofitable ***786** trades, or for the fact that Defendants had larger total losses than profits. *Id.*

[2] [3] This Court finds Magistrate Judge Tomlinson's recommendation regarding principal trades to be supported by the evidence. It is well-established in this Circuit that the profit made on an independently unlawful trade is subject to disgorgement regardless of whether losses we re sustained on any other transaction. *See, e.g., SEC v. Svoboda*, 409 F.Supp.2d 331, 344–45 (S.D.N.Y.2006) (Mukasey, J.) (refusing to deduct losses incurred in separate, unlawful insider trades from insider trading disgorgement calculation); *SEC v. Boock*, 09–CV–8261, 2012 WL 3133638, at *4 (S.D.N.Y. Aug. 2, 2012) (Cote, J.) (refusing to deduct losses incurred on separate trades from disgorgement of profitable sales). Furthermore, this Court is not persuaded *McCaskey* governs. In *McCaskey*, the SEC calculated disgorgement by focusing on sixteen particular transactions, "ignoring all other transactions during the more than six month manipulation scheme." 2002 WL 850001, at *7. Those "other transactions" were critical in *McCaskey*, as the scheme-liability provision of Section 10(b) of the Securities Exchange Act requires a court to analyze an entire set of facially valid trades to determine whether they became unlawful when considered as a whole. In contrast, violations of Section 206(3) of the Advisors Act and Rule 10b-10 of the Exchange Act—such as those found in this case—are transaction specific, and require calculation of disgorgement on a trade-by-trade basis.

The SEC expressly considered all principal trades during the relevant period, from January 1, 2007, through December 31, 2009, and incorporated only those seventy-one groups of principal trades resulting in an overall net profit. *See* R&R at 28. Any principal trades which included some internal profit but resulted in an overall net loss were not incorporated into the SEC's disgorgement figure. Therefore, as Magistrate Judge Tomlinson correctly stated, "such losses were netted out... and thus should not be double-counted by offsetting those

losses from the overall disgorgement figure." *Id.* That Defendants had more total losses than profits is irrelevant; they are liable for each individual transaction resulting in a profit.

[4] The Court also finds that the SEC properly incorporated into its disgorgement calculation brokerage commissions obtained from all of Defendants' unlawful transactions, including those which resulted in a loss. As undisclosed principals, Defendants were not entitled to brokerage commissions under Section 206(3) and Rule 10b-10 regardless of whether the trades resulted in a profit or a loss. Consequently, the Court ADOPTS Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset of $2,256,644.54 in principal trading losses.

2. Payments to Pasetsky, Allen, and Saxton

Defendants also object to Magistrate Judge Tomlinson's recommendations that Defendants are not entitled to an offset of $2,885,269.58 in payments made to Hal Pasetsky, Nate Allen, and Joe Saxton, as these payments were "closer to a general business expense than a direct transaction cost" and therefore could not be deducted from disgorgement as brokerage commissions. R&R at 31. Defendants argue these payments were in fact brokerage commissions, and, as such, should be considered "direct trading costs" and discounted from any disgorgement award under Second Circuit precedent. Objections at 8-10 (citing ***787** *McCaskey*, 2002 WL 850001, at *4; *SEC v. East Delta Res. Corp.*, 10-CV-310, 2012 WL 3903478, at *6 (E.D.N.Y. Aug. 31, 2012) (Feurstein, J.); *Litton Indus. v. Lehman Bros. Kuhn Loeb Inc.*, 734 F.Supp. 1071 (S.D.N.Y.1990) (Cannella, J.)).

The SEC replies that Defendants' payments to Pasetsky, Allen, and Saxton were not brokerage commissions, because Defendant Nadel himself acted as the sole broker on all relevant trades. Reply at 14. After collecting brokerage fees and commissions for himself, the SEC contends Defendant "funneled these payments to Pasetsky, Allen, and Saxton" under a profit-sharing arrangement. *Id.* Accordingly, the SEC argues that Magistrate Judge Tomlinson correctly categorized these monetary transfers as "ancillary" payments rather than "direct transaction costs" and that she correctly refused to deduct such payments from disgorgement. *Id.*

[5] After a thorough review of the record, this Court finds that Defendant's payments to Pasetsky, Allen, and Saxton were not brokerage commissions. Magistrate Judge Tomlinson properly identified the ancillary nature of these payments after a four-day damages hearing in which numerous witnesses testified, including Defendant Nadel. It is apparent from Defendant Nadel's testimony that "Nadel himself executed the trades, received the commission income from the trades, and then parsed out Pasetsky's [and Allen's, and Saxton's] share based upon the fee arrangement which was in place." R&R at 31. Defendants' protestations to the contrary are impassioned, but merely "labeling someone a broker and categorizing such payments as direct transaction costs does not make them so." *Id.* at 32.

Given the ancillary nature of Defendants' payments to Pasetsky, Allen, and Saxton, the payments should not be deducted from disgorgement. *See, e.g., SEC v. U.S. Envtl., Inc.*, 94-CV-6608, 2003 WL 21697891, at *28 (S.D.N.Y. July 21, 2003) (Leisure, J.) (refusing to allow deduction from disgorgement for illicit profits defendant shared with his trader under a prior arrangement because the arrangement "was more a method of compensating [defendant's] employees, than it was a brokerage commission[.]"). The Court therefore ADOPTS Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset of $2,885,269.58 in payments made to Hal Pasetsky, Nate Allen, and Joe Saxton.

3. Payments to Polycom

Defendants further object to Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to a deduction of $553,063.37 in payments made to Polycom, as these payments stemmed from "Defendants' non-compliance with Polycom's investment policy," and thus were not a "repayment of an ill-gotten gain" that may be offset from disgorgement. R&R at 37 (internal quotation marks omitted). Defendants argue that because these funds were "repaid" to Polycom—a client harmed by Defendants' fraudulent scheme—the proceeds of Defendants' ill-gotten gains "flowed back to the victim" and should offset Defendants' disgorgement obligation. Objections at 13 (citing, *inter alia*, *Disraeli v. SEC*, 334 Fed.Appx. 334, 335 (D.C.Cir.2009)).

The SEC replies that Defendants' payments to Polycom had nothing to do with the fraud at issue in this case;

rather, these payments were compensation stemming from a prior dispute. Reply at 15. As such, the SEC argues, it would "make no more sense to credit Defendants with these payments than it would to credit them, for example, for repairing property damage they may have caused their clients." *Id.* at 16.

[6] *788 The Court agrees with the reasoned recommendation of Magistrate Judge Tomlinson. Defendants have not satisfied their burden to establish a justification for every offset sought from disgorgement. *See* R&R at 21-22 (citing, *inter alia*, *SEC v. Rosenfeld*, 97–CV–1467, 2001 WL 118612, at *2 (S.D.N.Y. Jan. 9, 2001) (Pauley, J.)). Defendants cite to caselaw holding that restitution payments made to fraud victims may offset disgorgement obligations for that same fraud. *See* Objections at 13-14. Such precedent does not govern this setting, where Defendants repaid Polycom pursuant to a promissory note issued following Defendants' non-compliance with Polycom's investment policy. *See* R&R at 36-37. Accordingly, the Court ADOPTS Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset of $553,063.37 in payments made to Polycom.

4. "Hedging" Trades

Finally, Defendants object to Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset from disgorgement of $118,175.22 in payments made to Man Financial and MF Global in order to execute "hedging" trades, as "any profits garnered on such trades would not have been illegal in the first instance," and the Court may only offset expenses incurred in garnering illegal profits. R&R at 35. Defendants argue that, because hedging was "an integral part of Defendants' Dividend Capture Strategy, from which the advisory fee disgorgement is derived," payments to Man Financial and MF Global are "direct transaction costs of Defendants' advisory fees, which are subject to disgorgement." Objections at 17-18.

The SEC replies that the hedging trades at issue are not in and of themselves unlawful, regardless of whether hedging was a part of Defendants' overall investment strategy. Reply at Because direct trading costs may offset disgorgement only where they were made to effect a fraudulent transaction, Defendants argue any profits made from these hedging trades should not be included in the Court's disgorgement calculation for cross-trading commissions. *Id.* (citing *SEC v. Thomas James Associates*, 738 F.Supp. 88, 94 (W.D.N.Y.1990) (Telesca, C.J.)).

[7] The Court finds that the payments made by Defendants to Man Financial and MF Global were not unlawful. Defendants may have intended the trades to hedge against losses incurred in other, unlawful trades, but the hedging trades themselves did not violate any securities laws. Therefore, the Court ADOPTS Magistrate Judge Tomlinson's recommendation that Defendants are not entitled to an offset from disgorgement of $118,175.22 in payments made to Man Financial and MF Global.

The SEC does not object to Magistrate Judge Tomlinson's recommendation that Defendants are entitled to an offset of $183,026.68 in clearing charges paid to RBC. *See* Reply at 17-18. The Court finds that these charges were direct trading costs made to effect Defendants' unlawful cross-trades, and therefore ADOPTS Magistrate Judge Tomlinson's recommendation that they be offset from disgorgement.

5. Prejudgment Interest

Defendants do not object to Magistrate Judge Tomlinson's recommendation that the Court impose prejudgment interest on the disgorgement figure, and the Court ADOPTS this recommendation as supported by the weight of the evidence. The Court directs the SEC to submit a revised prejudgment interest calculation based upon the deduction of $183,026.68 from total disgorgement, such amount representing *789 clearing charges paid by the Defendants to RBC to execute cross-trades during the period January 1, 2007 through December 31, 2009.

C. Relief Defendant's Disgorgement

Magistrate Judge Tomlinson recommends that this Court order the disgorgement of $807,346.51 from Relief Defendant Katherine Nadel, plus prejudgment interest in the amount of $156,033.03. R&R at 65. Defendants object to this recommendation on two grounds. First, Defendants argue Relief Defendant has a plausible legitimate claim to these assets based on her work for Defendant corporations WDNC and RIA. Objections at 14-16 (citing *C.F.T.C. v. Walsh*, 618 F.3d 218, 226 (2d Cir.2006)) (holding a court "may only require disgorgement of the assets of a relief defendant upon a finding that she lacks a 'legitimate claim' to the

assets"). Second, Defendants argue the Court should exercise its discretion not to impose disgorgement on Relief Defendant in the interest of fairness, as she was "merely collateral damage to her husband's wrongdoing." Objections at 17.

The SEC responds that Relief Defendant has no legitimate claim to the money at issue, which the SEC contends is merely a diverted portion of Defendants' ill-gotten gains. Reply at 18. In support of this claim, the SEC refers to the deposition testimony of Relief Defendant, which "differ[s] considerably with respect to the duration of [Relief Defendant's] employment and the range of her responsibilities" from what is outlined in Defendants' post-trial briefing and objections. *Id.* at 18–19. The SEC also highlights the difference between "the amounts and pattern of payments the Relief Defendant received, and the compensation Nadel paid his actual full time assistant," as further evidence of the illegitimacy of Relief Defendant's claim to these funds. *Id.* at 20.

[8] Upon a *de novo* review of the record, this Court finds that Relief Defendant Nadel lacks any plausible legitimate claim to the funds at issue. Before she was named a Relief Defendant and had a direct financial incentive to adjust her testimony, Ms. Nadel testified that she had a very limited role at WDNC and RIA consisting mostly of "secretarial" work. R&R at 60. Relief Defendant received extraordinarily inconsistent payments from WDNC and RIA; of the $807,346.52 she received as compensation during the 2007-2009 period, she received $435,800 in 2007 alone.[2] *Id.* at 63. Defendant Nadel's full-time assistant, by contrast, received a consistent income of $74,363.66 over the same time frame. *Id.* at 62 (citing to Pl.'s Hrg. Ex. 138 ¶ 20).

In light of the record, the Court declines to exercise its discretion to excuse Relief Defendant from disgorgement. The Court ADOPTS Magistrate Judge Tomlinson's recommendation that Relief Defendant Katherine Nadel disgorge $807,346.51, plus prejudgment interest in the amount of $156,033.03.

CONCLUSION

For the reasons stated above, the Report and Recommendation, ECF No. 128, is ADOPTED in its entirety. The Court directs the SEC to submit a revised prejudgment interest calculation based upon the sole offset of $183,026.68 in clearing charges paid to RBC from disgorgement.

All Citations

206 F.Supp.3d 782

Footnotes

1 Civil penalties may not be imposed on a joint and several basis in SEC enforcement actions, *See SEC v. Pentagon Capital Mgmt.*, 725 F.3d 279, 287–88 (2d Cir.2013). In adopting this section of the Report and Recommendation, the Court views Magistrate Judge Tomlinson's recommendation to be for a $1,000,000.00 penalty against individual Defendant Warren D. Nadel, and not against the two corporate defendants. *See* R&R at 47-57.

2 Relief Defendant's explanation for the dramatic decrease in her compensation after 2007 was that "[she] must have been doing less work." R&R at 62 (citing Pl.'s Hrg. Ex. 176).

EXHIBIT 5

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	
Plaintiff,	
-against-	
	11 Civ. 0215 (WFK) (AKT)
WARREN D. NADEL, WARREN D. NADEL & CO., and REGISTERED INVESTMENT ADVISERS, LLC	ECF Case
Defendants	
-and-	
KATHERINE NADEL,	
Relief Defendant.	

[~~PROPOSED~~] FINAL JUDGMENT AS TO WARREN D. NADEL

WHEREAS, on March 31, 2015, the Court issued a Decision and Order [DE 100], granting Plaintiff Securities and Exchange Commission ("Plaintiff or "Commission") partial summary judgment against defendant Warren D. Nadel ("Defendant"), holding him liable for violations of Section 10(b) of the Securities and Exchange Act of 1934 and Rules 10b-5 and 10b-10 thereunder, Section 17(a) of the Securities Act of 1933, and Sections 206(1), 206(2) and 206(3) of the Investment Advisors Act of 1940 [DE 71]; and directing U.S. Magistrate Judge A. Kathleen Tomlinson to hold a hearing on relief consistent with its Decision and Order ("2015 Order"); and

WHEREAS, on February 11, 2016, after a hearing (held July 20-23, 2015), Judge Tomlinson issued a Report and Recommendation [DE 128] (the "Report"), recommending that the Court order against Defendant (1) permanent injunctive relief; (2) $10,776,687.62 in

disgorgement, jointly and severally with Defendants Warren D. Nadel & Co. and Registered Investment Advisers, LLC; (3) prejudgment interest, jointly and severally with Defendants Warren D. Nadel & Co. and Registered Investment Advisers, LLC (to be recalculated based upon the deduction of $183,026.68 from the disgorgement amount, for the reasons stated in the Report); and (4) a $1,000,000 third-tier civil penalty; and

WHEREAS on September 9, 2016, the Court issued a Decision and Order [DE 133] (the "2016 Order"), adopting the Report in its entirety and directing Plaintiff to submit a revised prejudgment interest calculation (as set forth in the Report); and

WHEREAS on September 15, 2016, Plaintiff filed with the Court its revised calculation of prejudgment interest (of $2,293,701.57) [DE 134], which the Court endorsed on September 23, 2016 [DE 135] ("Endorsement"); and

WHEREAS the 2015 Order, Report, 2016 Order and Endorsement are incorporated by reference into this judgment as if fully set forth herein,

NOW THEREFORE

I.

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from violating, directly or indirectly, Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 promulgated thereunder [17 C.F.R. § 240.10b-5], by using any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, in connection with the purchase or sale of any security:

(a) to employ any device, scheme, or artifice to defraud;

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

II.

IT IS HEREBY FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from violating Section 17(a) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. § 77q(a)] in the offer or sale of any security by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly:

(a) to employ any device, scheme, or artifice to defraud;

(b) to obtain money or property by means of any untrue statement of a material fact or any omission of a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(c) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

III.

IT IS HEREBY FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from violating, directly or indirectly, Sections 206(1), 206(2) or 206(3) of the Investment Advisors Act of 1940 [15 U.S.C. §§ 80b-6(1), (2) and (3)], by using the mails or any means or instrumentality of interstate commerce, while engaged in the business of advising others for compensation as to the advisability of investing in, purchasing or selling securities:

(a) to employ any device, scheme, or artifice to defraud any client or prospective client; or

(b) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client; or

(c) acting as a principal for his own account, knowingly to sell any security to or purchase any security from a client, or acting as broker for a person other than such client, knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transaction.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who

receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

IV.

IT IS HEREBY FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from aiding and abetting any violation of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-10 [17 C.F.R. § 240.10b-10], thereunder by, by using the mails or any means or instrumentality of interstate commerce, knowingly or recklessly providing substantial assistance to any broker or dealer who effects for or with an account of a customer any transaction in, or induces the purchase or sale by such customer of, any security (other than U.S. Savings Bonds or municipal securities) without providing the information required under Rule 10b-10(a)(1) and (2).

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

V.

IT IS HEREBY FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is liable for disgorgement of $10,776,687.62, jointly and severally with Defendants Warren D. Nadel & Co. and Registered Investment Advisers, LLC, representing profits gained as a result of the conduct alleged in the Amended Complaint, together with prejudgment interest thereon in the amount of $2,293,701.57, for a total of $13,070,389.19. Defendant shall satisfy this obligation

by paying $13,070,389.19 to the Securities and Exchange Commission within 14 days after entry of this Final Judgment.

Defendant may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request. Payment may also be made directly from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm. Defendant may also pay by certified check, bank cashier's check, or United States postal money order payable to the Securities and Exchange Commission, which shall be delivered or mailed to

Enterprise Services Center
Accounts Receivable Branch
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

and shall be accompanied by a letter identifying the case title, civil action number, and name of this Court; Warren D. Nadel as a defendant in this action; and specifying that payment is made pursuant to this Final Judgment.

Defendant shall simultaneously transmit photocopies of evidence of payment and case identifying information to the Commission's counsel in this action. By making this payment, Defendant relinquishes all legal and equitable right, title, and interest in such funds and no part of the funds shall be returned to Defendant.

The Commission shall hold the funds (collectively, the "Fund") and may propose a plan to distribute the Fund subject to the Court's approval. The Court shall retain jurisdiction over the administration of any distribution of the Fund. If the Commission staff determines that the Fund will not be distributed, the Commission shall send the funds paid pursuant to this Final Judgment to the United States Treasury.

The Commission may enforce the Court's judgment for disgorgement and prejudgment

interest by moving for civil contempt (and/or through other collection procedures authorized by law) at any time after 14 days following entry of this Final Judgment. Defendant shall pay post judgment interest on any delinquent amounts pursuant to 28 U.S.C. § 1961.

VI.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant shall pay a civil penalty in the amount of $1,000,000 to the Securities and Exchange Commission pursuant to Section 20(d) of the Securities Act, Section 21(d) of the Exchange Act and Section 209(e) of the Advisors Act. Defendant shall make this payment within 14 days after entry of this Final Judgment.

Defendant may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request. Payment may also be made directly from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm. Defendant may also pay by certified check, bank cashier's check, or United States postal money order payable to the Securities and Exchange Commission, which shall be delivered or mailed to

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6500 South MacArthur Boulevard
Oklahoma City, OK 73169

and shall be accompanied by a letter identifying the case title, civil action number, and name of this Court; Warren Nadel as a Defendant in this action; and specifying that payment is made pursuant to this Final Judgment.

Defendant shall simultaneously transmit photocopies of evidence of payment and case identifying information to the Commission's counsel in this action. By making this payment, Defendant relinquishes all legal and equitable right, title, and interest in such funds and no part

of the funds shall be returned to Defendant. The Commission shall send the funds paid pursuant to this Final Judgment to the United States Treasury. Defendant shall pay post-judgment interest on any delinquent amounts pursuant to 28 USC § 1961.

VII.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. § 523, the allegations in the Complaint are deemed true as to Defendant, and further, any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Defendant under this Final Judgment or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Defendant of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. §523(a)(19).

VIII.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that this Court shall retain jurisdiction of this matter for the purposes of enforcing the terms of this Final Judgment.

Dated: 1/20, 2017

s/WFK

UNITED STATES DISTRICT JUDGE

EXHIBIT 6

Warren D. Nadel
7 Locust Lane
Upper Brookville, NY 11545

(516) 674-3521

April 15, 2017

Mr. Richard G. Primoff, Esq.
SECURITIES AND EXCHANGE COMMISSION
New York Regional Office
Brookfield Place
200 Vesey Street, Suite 400
New York, NY 10281-1022

Mr. Primoff:

I am reaching out to you at this time and for a number of reasons that have necessitated my doing so. First and foremost, I am no longer in a position to afford legal representation in my required dealings with the Securities and Exchange Commission (the "SEC") as I have been out of work for over seven years despite numerous attempts to obtain gainful employment. I feel that in terms of any legal procedural activities that I will be facing, I am hoping that your office might be willing to give me some direction as I am truly out of my element. It is my belief that my qualifications are rather narrowly focused in the securities industry, my ongoing situation with the SEC and my 67 years of age have contributed to my inability to obtain employment thus far. Over the past seven years a number of changes in my family's and my life have necessitated the liquidation of my assets accumulated over my lifetime of work. My wife and I are no longer married and my children have moved away. I am continuing to seek employment as I have little choice to do otherwise. As such, I am financially impaired and quite literally living from hand to mouth.

I am not looking to make excuses for the inappropriate action that I took but rather trying to give you some feeling for me as an individual and a financial professional now and previously. Frankly, there is no excuse for inflating assets under management and misinforming those considering the use of my investment strategy and services. I cannot apologize more strenuously than I am attempting to do so here. As for the other violations, none of them were the result of an attempt to defraud a client but, rather, the result of my lack of a knowledgeable compliance staff, internally or outsourced. Perhaps requiring small independent firms to have a compliance aspect to their business should be imposed in an attempt to avoid situations like this in the future. It would have been well worth the expense to me.

Since the SEC audit began in September 2009, I lost all my clients, the last leaving in March 2010. I no longer have the ability to attract new clients as a result of the requirement to disclose

that there was an ongoing SEC investigation. Even my clearing firms determined to end our relationship due to the ongoing SEC investigation. Consequently, I was forced to close my broker-dealer and registered investment advisory firms in December 2011 after nearly 25 years of operations as a result of the financial strain on my professional and personal life. Shortly thereafter, I was forced to allow my various personal registrations to laps as no firm would consider housing them under any circumstance.

The bar that the SEC is seeking has truly and literally been in effect for this time period as my ability to practice my profession terminated with the beginning of this investigation back in September 2009. Restoring my ability to work in my profession seems to be what is likely to be the key to getting my personal life restored, not to what it was, as I understand that to be unlikely, but to a degree that makes my life seem somewhat vital. At this point, I hope only that a finality to this litigation would end with a limited bar and that I might then be able to try to see if a firm would engage me, having learned a most painful and powerful lesson as to my ability to work in the securities industry on my own. My desire to operate independently, though generated by a desire to serve my clients, has had an overwhelming effect on every aspect of my family's and my life. Aside from being spurned by some family and by a number of friends of long standing, it has been my family who has suffered the most and totally without cause as I feel that they have done nothing wrong. My level of guilt in this regard has been beyond anything I would have ever thought possible.

[redacted] in New Jersey, [redacted]

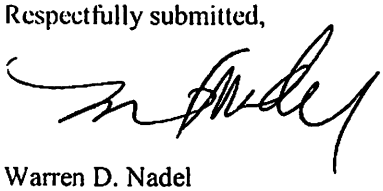
It is my hope that you will determine that the punishment I and my family have experienced is sufficient and has been effective and that there is no need for more than a minimal bar or monetary penalty that I can ill afford. I understand and appreciate that what I did was wrong and I am willing to subject myself to the supervision of compliance professionals at every step in an effort to eliminate any possibility of future violations of any kind if I am given the opportunity to reenter the job market in the securities industry. Without any licenses, my ability to work in the area of investments would be severely restricted. I am desperate to regain my family's life and mine. I am 67 years old and, with my firms being closed, my only hope is to work for another firm, which may not be possible given the damage this action has done to my reputation. Despite the size of the challenge, I would like to try to be employed in my chosen field and am anxious to work toward that end. Before this SEC audit, I never had a serious compliance or regulatory issue, having been audited by FINRA and the NFA every 2 to 3 years since 1987 without any substantive mishaps or warnings.

My mistake was my belief that I could serve my clients best as an independent broker. I was foolish to inflate the amount of funds under management when soliciting clients. I am truly sorry for my errors and would gladly abide by whatever punishment the SEC judicial system deems appropriate. I am asking that your determination not be a lifetime bar from my industry that I loved participating in and that I have been a part of for my entire professional life, giving

me a second chance to employ the strategy that has benefited so many and that could benefit so many more in a suitably supervised environment. Mr. Primoff, it is my fervent hope, and that of my family, that you will consider and grant my request.

Feel free to share this with Administrative Law Judge Cameron Elliot who I believe has been assigned my case if you think it to be appropriate.

Respectfully submitted,



Warren D. Nadel

EXHIBIT 7

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of **WARREN D. NADEL,** **Respondent**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(B) OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940 AND NOTICE OF HEARING**

The Respondent ("NADEL"), due to financial circumstance is acting in the capacity as his own counsel. Every effort is being made to be in compliance with the format and content as prescribed by law and expected by the Court. A copy of the request for this administrative proceeding is included here.

IN ANSWER, the following is in response to a permanent injunction for NADEL not to be employed by a member of the securities industry -

It is understood that the purpose of a lifetime bar is to primarily protect the investing public from a potential negative influence that has the prospect of causing them harm. This can be accomplished in a somewhat different way and still allow NADEL to be penalized in this way and yet have the ability to work in the investment industry while protecting the investing public in much the same way. If a person has no license to practice in this industry they are precluded from effecting any transactions for clients or the firm for which they work. They are also precluded from speaking with any prospective or existing investors in a sales capacity. Expectedly they would be subjected to supervisory oversight and could be designated as someone to be given heightened supervisory oversight by a firm's compliance effort. They would be precluded from corresponding in any form with any existing or prospective client. In fact, they would be precluded from any activity that the SEC and the Court would find to place the investing public at any risk as this person's influence to effect any aspect of investing would be outside their purview of authority.

It is further believed that these restrictions accomplishes and achieves the spirit of that which the SEC and the Court seek without eliminating the individual's ability to attempt to gain employment in the only industry in which they have any knowledge. Clearly, NADEL will no longer be able to pursue employment in the area of securities trading, money management and sales for which NADEL is being fined and punished. Further, as a result of these restrictions being placed upon NADEL and while working with a securities firm having a compliance effort, there would be no realistic likelihood of any

recurrence of any future violations by NADEL. Additionally, NADEL will also promise to never violate any of the rules and regulations of the securities industry.

IN ANSWER, the following is in response to the prospective monetary punishment provided for the SEC in the document of judgment as provided by the Honorable William F. Kuntz, II (Decision & Order Re Nadel) -

In light of the magnitude of this punishment afforded the SEC by the Court, the fact remains that due the current and foreseeable financial circumstances of NADEL, it seems highly unlikely that any monetary reward could be paid. NADEL is willing to complete and provide the SEC with whatever information they require in this regard and is willing to swear to the accuracy and completeness of this document to be provided.

IN ANSWER, the following is in response to the SEC allegations as to their further consideration by the Court -

Various allegations were made previously during the Federal Court damages hearing of July 2015 and have already been adjudicated by the Court and were determined not to have been proven to the Court (Report and Recommendations of A. Kathleen Tomlinson, Magistrate Judge dated February 11, 2016).

Additionally, a Letter to Richard Primoff dated April 15, 2017 has been submitted in the spirit of completeness that, as the name implies, consists of a letter submitted directly to the SEC Prosecuting Attorney Richard Primoff by NADEL that was sent in an attempt to allow for the resolution to the issues in consideration of the Court's time and in the interest of a fair compromise that would lead to a more expeditious conclusion of this matter.

Respectfully submitted by the Respondent,

Warren D. Nadel

Enclosures

Cc: Brenda P. Murray
Chief Administrative Law Judge

Brent J. Fields, Secretary
Office of the Secretary

Richard G. Primoff
Senior Trial Counsel

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding
File No. 3-17883

In the Matter of	
Warren D. Nadel,	
Respondent.	

CERTIFICATE OF SERVICE

I, Richard G. Primoff, certify that on the 16th day of June 2017, I served a true and correct copy of the foregoing: (1) Division of Enforcement's Memorandum of Law in Support of its Motion for Summary Disposition dated June 16, 2017; (2) Division of Enforcement's Motion for Summary Disposition Pursuant to SEC Rule of Practice 250; and (3) June 16, 2017 Declaration of Jorge Tenreiro and exhibits annexed thereto, by UPS Overnight Delivery and email, on the Court and Respondent Warren D. Nadel, as follows:

The Honorable Cameron Elliot
Administrative Law Judge
U.S. Securities and Exchange Commission
100 F Street, N.E., Mail Stop 2557
Washington, DC 20549
ALJ@sec.gov

Mr. Warren D. Nadel
[redacted]e
Glen Head, NY [redacted]
warren@wdnco.com

Dated: New York, New York
June 16, 2017

Richard G. Primoff

HARD COPY

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
NEW YORK REGIONAL OFFICE
200 VESEY STREET, SUITE 400
NEW YORK, NEW YORK 10281-1022

WRITER'S DIRECT DIAL LINE
RICHARD G. PRIMOFF
TELEPHONE: (212) 336-0148
FACSIMILE: (212) 336-1319
PRIMOFFR@SEC.GOV

June 16, 2017

VIA FAX and UPS

Mr. Brent J. Fields, Secretary
Office of the Secretary
Securities and Exchange Commission
100 F. Street, N.E.
Washington, D.C. 20549

Re: In the Matter of Warren D. Nadel
File No. 3-17883

Dear Mr. Fields:

Enclosed please find for filing in the referenced proceeding the original and three copies of (1) the Division of Enforcement's motion for summary disposition against Respondent Warren D. Nadel pursuant to SEC Rule of Practice 250; (2) the supporting Declaration of Jorge Tenreiro dated June 16, 2017; (3) the Division's Memorandum of Law in Support of its Motion for Summary Disposition; and (4) the Certificate of Service.

Copies of this letter and the enclosures are being served today on Respondent and the Court, by email and by UPS overnight delivery.

Respectfully submitted,

Richard G. Primoff

Enclosures

cc: The Hon. Cameron Elliot
Mr. Warren D. Nadel