

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING

File No. 3-20331

In the Matter of
ROY Y. GAGAZA,
Respondent.

**DIVISION OF ENFORCEMENT'S REPLY IN SUPPORT OF ITS MOTION
FOR SUMMARY DISPOSITION AGAINST ROY Y. GAGAZA**

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I. INTRODUCTION

As argued extensively in the Motion for Summary Disposition (“Motion”), the undisputed material facts show Roy Gagaza ignored a series of red flags that should have alerted him that 1 Global Capital was lying to him and investors about its business operations and use of investor funds. Contrary to Gagaza’s assertions, the Division of Enforcement has set forth detailed undisputed facts in its Motion showing why the *Steadman* factors weigh heavily in favor of the Commission barring Gagaza from the securities industry, and why a hearing is unnecessary.

Gagaza’s arguments and admissions in his Response only further serve to demonstrate his recklessness and egregious conduct. Rather than identifying genuine issues of material fact, Gagaza’s Response raises a number of arguments that are legally incorrect or irrelevant, attempts to inject facts that are fabricated out of whole cloth, argues alleged mitigating factors that ignore the harm he caused by offering and selling 1 Global notes, and blames others involved in 1 Global’s scheme in a feeble effort to distract from his own egregious conduct. For example, Gagaza baselessly argues the Division’s facts are limited to the Complaint in the District Court case giving rise to these proceedings, claims without a shred of evidentiary support that he learned 1 Global Capital had lied about having audited financial statements months after the record shows he did, and has the hubris to assert that his clients’ good fortune to not lose *all* their money in 1 Global should be a mitigating factor. For these reasons, the Division is entitled to summary disposition, and to the relief of securities industry and penny stock bars.

II. THE DIVISION IS NOT LIMITED TO FACTS IN THE COMPLAINT

Gagaza falsely claims in his Response that the Division may not present facts outside those in the District Court Complaint that gave rise to this action. Response at 11-15 and 28. This is flat out wrong, and Gagaza cites no legal or factual support for this statement – because there is

none. Gagaza did agree in his consent to the Final Judgment entered in the District Court not to contest the facts in the Complaint in this matter. See Exhibit 2 to Division's Motion. However, nowhere did the consent (Exhibit 2) purport to limit the facts in this proceeding to those in the District Court Complaint. *Id.* Furthermore, there is no Administrative Proceeding Rule of Practice that so limits the Division or the facts it presents. Thus, Gagaza's argument is wholly meritless, and the facts he claims the Commission should not consider – that Gagaza owed his investment adviser clients who bought 1 Global notes a fiduciary duty, that Gagaza was severely reckless in his lack of due diligence into 1 Global, and that he failed to investigate 1 Global's assertions that its merchant cash advances were secured through Uniform Commercial Code filings - are properly before the Commission.

III. GAGAZA INVENTS FACTS

One of the most damaging pieces of evidence against Gagaza as set forth in the Division's Motion is that he learned in April 2017, early on in his tenure selling 1 Global notes that 1 Global had lied about having audited financial statements. Motion at 9-11. Yet Gagaza did not confront 1 Global about this lie, investigate any other 1 Global claims, or tell the clients to whom he continued to offer and sell 1 Global notes for the next 14 months about this major inconsistency. *Id.* Most of this evidence comes from Gagaza's own sworn testimony during the investigation of this matter. *Id.*; see also Exhibit 5 to Division's Motion (page and line citations in the Motion at 9-11).

In his Response, Gagaza alleges for the first time without a scintilla of evidence that he actually only found out 1 Global didn't have audited financial statements in October 2017, six months later. Response at 15-17 and Exhibit U. This is directly contrary to his sworn testimony. Gagaza was specifically questioned about a "Pitch Deck," which he received in April 2017 and

which contained the statement that 1 Global had audited financial statements. When asked whether, after receiving the Pitch Deck, he asked for 1 Global's audited financial statements, Gagaza said "yes," he asked 1 Global officer Scott Merkelson. Ex. 5 at 134 L.9 - 135 L.2. Gagaza further testified that Merkelson's response was that 1 Global was not a publicly-traded company and "they were still expanding and growing and that they had not, as a firm, decided to do that." Id. at 135 L.12-23. In answering the questions related to the April 2017 time frame, Gagaza never stated that he only communicated with Merkelson six months later, and never mentioned the October 9, 2017 text message to Merkelson on which he now relies. Response at Ex. U.

Moreover, the text message lacks any context or evidentiary connection to the conversation about which Gagaza testified. Gagaza asks the Commission to assume, without one shred of evidence, that because he texted Merkelson in October 2017 about audited financial statements, that must have been when the conversation he testified about under oath occurred. At best this is highly disingenuous. There simply is no evidence that supports Gagaza's claim that the text was related to the Pitch Deck he received in April 2017. The Commission should see this for what it is – a desperate attempt to avoid the obvious conclusion that Gagaza recklessly ignored significant evidence that 1 Global was a fraud.

Furthermore, even if the Commission accepts Gagaza's timeline as true, this version of events does not help him. It means that Gagaza knew in October 2017 at the latest that 1 Global lied about having audited financial statements. Yet he still continued to offer and sell 1 Global notes for another eight months until June 2018, without disclosing to investors (before and after October 2017) that 1 Global had lied to him about an important fact. His decision to continue offering and selling 1 Global notes for eight months after October 2017 was highly reckless, if not outright fraudulent. Even by his own admissions, Gagaza's conduct was egregious.

IV. GAGAZA'S IRRELEVANT FACTS

Gagaza begins his Response by outlining his purported efforts to atone for his conduct and to reduce the harm to his clients. He also piggybacks on the efforts of the 1 Global bankruptcy trustee to recover assets and compensate defrauded 1 Global investors for the harm he caused by acting as an unregistered broker-dealer and selling almost \$11 million of 1 Global's unregistered securities. Response at 4-9. That Gagaza entered into a settlement to disgorge all his commissions to the bankruptcy trustee is admirable, but this does not negate his extensive misconduct outlined in the Division's Motion, and the Commission should not consider it in determining sanctions. Moreover, Gagaza is no different or better, as his Response implies, than other 1 Global sales agents because he disgorged his profits. At least six other 1 Global sales agents are paying disgorgement amounts and civil penalties to the Commission and/or the bankruptcy trustee.

Gagaza's use of the bankruptcy trustee's extraordinary efforts to recover funds for the benefit of 1 Global's innocent investors – who were defrauded out of \$320 million through the efforts of Gagaza and other sales agents - is especially repugnant. Gagaza had nothing to do with the trustee's efforts, and it is ridiculous for him to claim he should benefit because he was fortunate enough to participate in a fraud where investors recovered funds. Had the outcome been different, and investors recovered nothing for reasons having nothing to do with Gagaza, the Division is quite sure Gagaza would strenuously object if the Division tried to use that fact to argue for harsher sanctions. Conversely, it is absurd for Gagaza to argue he should benefit by the result here.

Finally, Gagaza's recommendation to his clients to opt out and not renew at the expiration of the nine-month note term does not negate his original conduct of selling unregistered securities as an unregistered broker-dealer and his reckless disregard of red flags set forth in the Division's Motion. The Commission should reject out of hand Gagaza's attempt to mitigate his conduct by

arguing that his clients lost less money than other sales agents' clients or less because of the trustee's efforts. If Gagaza had not sold unregistered securities as an unregistered broker-dealer or done the least bit of investigation of the red flags, his clients never would have been placed in the position to suffer *any* harm. Put simply, Gagaza's efforts to evade responsibility and apparent "no harm, no foul" attitude demonstrate his fundamental lack of responsibility for the consequences of his misconduct and the precipitous harm he caused his clients. This attitude only demonstrates the need for significant sanctions against Gagaza.

V. THE PUBLIC INTEREST FACTORS SUPPORT A BAR

The Division's Motion outlined an extensive record of undisputed facts that clearly demonstrate Gagaza ignored obvious red flags about 1 Global that should have alerted him that 1 Global officers were not telling the truth. Gagaza has not identified any disputed issues of material fact to alter this conclusion.

A. Gagaza's Lack Of Due Diligence Efforts Rises To The Level Of Egregiousness

Gagaza incorrectly argues that his due diligence efforts do not rise to the necessary level of egregiousness. His reliance on *In the Matter of OTC Global Partners, LLC and Raimundo Dias*, Initial Dec. Rel. No. 1163, 2017 WL 3588042 (Aug. 21, 2017) for the proposition that "egregiousness does not typically exist where there is no scienter and the defendant has conducted due diligence" is misplaced. Response at 10-11. Gagaza's testimony and the undisputed evidence reflect that he did not conduct the necessary due diligence to sell 1 Global notes, and he continued to sell them for 14 months despite numerous red flags.

B. Gagaza Was An Investment Adviser When He Sold The 1 Global Product

As a threshold matter, the following facts are undisputed: Gagaza was an experienced securities professional, was the owner and chief compliance officer of a registered investment

adviser firm (Journey Wealth Management Advisors, LLC), owed a fiduciary duty to his investment advisory clients, and sold 1 Global notes to his advisory clients. Gagaza does not dispute any of these facts; rather he claims that because the Commission did not allege investment advisor violations against him in the District Court Complaint the Commission should not consider those facts. We have addressed this argument in Section II above. It is entirely proper for the Commission to include these facts in this proceeding.

Additionally, the Commission's consideration of these facts is not precluded by the Division's allegation in the Complaint that Gagaza offered and sold the 1 Global notes as an outside business activity and as an unregistered broker-dealer on behalf of 1 Global. Gagaza's apparent argument that he can take off his investment adviser hat, put on an independent contractor hat, and thereby shrug off his fiduciary duties to his clients and act recklessly by selling them unregistered securities elevates form over substance. Gagaza essentially asks the Commission to reward him for creating different vehicles to avoid reckless and prohibited conduct. Ultimately, no matter what hat he wore, Gagaza had a fiduciary duty to his investment adviser clients, and his reckless misconduct breached those duties.

C. Gagaza's Due Diligence Was Woefully Deficient

1. Gagaza Knew 1 Global Lied In Its Marketing Materials About Audited Financial Statements

As discussed in Section III above, Gagaza was on alert as early as April 2017 – shortly after he began offering and selling 1 Global notes – that 1 Global had lied in his marketing materials about having audited financial statements. Yet he continued to offer and sell 1 Global notes without disclosing that fact to his clients or conducting further investigation into other 1 Global representations.

Gagaza attempts to justify his actions after he learned that 1 Global lied about the audited

financial statements by explaining that it was reasonable for him to believe that there was nothing suspicious because he could see his clients' monthly account statements showing they were making a profit and stating that the purported auditor, Daszkal Bolton, was verifying 1 Global's rate of return formula. This explanation strains credulity. Gagaza knew 1 Global lied yet he selectively chose to believe two significant pieces of information generated by 1 Global without checking with Daszkal Bolton to confirm what 1 Global said on the monthly account statements. Significantly, this 1 Global statement also turned out to be false. These admissions evidence Gagaza's recklessness and apparent willingness to stick his head in the sand while he continued to offer and sell 1 Global notes and receive commissions. Indeed, Gagaza's state of mind is on full display in the evidence and his own arguments, and no hearing is needed to determine that a bar is necessary to prevent future violations.

2. Gagaza's Failure To Contact The Auditor Was Egregious

Gagaza relies on *South Cherry Street, LLC v. Hennessee Group, LLC*, 573 F.3d 98 (2nd Cir. 2009) for the proposition that failure to contact an issuer's auditor is at best negligence and insufficient to establish scienter. However, the facts of *South Cherry* are not analogous to the instant situation. In that case, South Cherry made investments in a fund based on the recommendation of HG. The fund, however, had been losing millions of dollars each year it traded, and to hide these losses, the fund fired the original auditing firm and replaced it with a second auditing firm. *Id.* at 102-103. The complaint alleged that HG could not have performed any real due diligence because if it had, it would have learned that the second auditing firm was not independent.

Notably, however, unlike the present situation, the *South Cherry* complaint did not allege that HG had received information contrary to an issuer's statements and failed to investigate it.

Here, Gagaza received contrary information – that 1 Global had lied about having audited financial statements (whether in April 2017 or October 2017). Yet he still did not conduct *any* investigation into the situation, including contacting the auditor. That makes this case much different and far more egregious than the situation in *South Cherry*.

As the owner and chief compliance officer of a registered investment adviser firm, Gagaza had an obligation to ensure that he and his firm were not violating the law in offering and selling 1 Global’s notes. But Gagaza utterly disregarded that responsibility, failing to make even the most basic of inquiries into the product he was asking his customers to buy. Ultimately, the fact that Gagaza knew there were inconsistencies (at best) or bald-faced lies (at worst) in important information from 1 Global, and chose not to contact the auditor and continued to offer and sell 1 Global notes, is what elevates his conduct to the egregious level. Again, Gagaza’s state of mind is evident, and a hearing is not needed to determine the sanctions.

D. Others’ Misconduct And Violations Do Not Excuse Gagaza’s Egregious Conduct

Gagaza attempts to use the fact that others at 1 Global, particularly its former outside counsel Dale Ledbetter, committed bad acts to justify or distract from his own egregious conduct. Response at 25-28. The fact that others have violated securities laws does not excuse Gagaza’s actions or otherwise give him a “free pass.” *See, e.g., Imperato v. SEC*, 693 Fed. Appx. 870, 876 (11th Cir. 2017) (affirming that the SEC did not grossly abuse its discretion in imposing a lifetime industry-wide bar against defendant where he “continues to deny wrongdoing and attempts to shift blame to others”); *SEC v. McNulty*, 137 F.3d 732 (2nd Cir.1998) (finding no abuse of discretion in entry of injunction given defendant’s efforts to shift responsibility to others and his persistent denial, notwithstanding the record evidence of scienter, of any culpable conduct); *SEC v. Cavanagh*, 2004 WL 1594818 at *29 (S.D.N.Y. July 16, 2004) (affirming a permanent injunction

and noting defendants' continued efforts to shift blame and responsibility for their illegal actions when defendants were sophisticated businessmen with extensive securities industry experience and they knew or should have known that there was a violation) (citing *SEC v. Frank*, 388 F.2d 486, 489 (2nd Cir. 1968) (a defendant cannot escape liability by "closing his eyes to what he saw and could readily understand"))).

E. Gagaza's Conduct Is Not Isolated And Is Recurrent Because He Sold 1 Global Notes For 14 Months To At Least 178 Customers

Gagaza incorrectly argues that his conduct was not recurrent because he is not a repeat securities law violator. However, this is not the standard to determine whether conduct was isolated or recurrent when seeking a bar from association with any broker or dealer. What determines whether conduct is isolated or recurrent is the conduct *at issue*. In its Motion, the Division notes that Gagaza sold 1 Global notes for 14 months to at least 178 customers and cites to two cases where it was determined that even lesser conduct was repeated and recurrent. *Richard P. Callipari*, Initial Dec. Rel. No. 237, 2003 WL 22250402, at *5 (Sept. 30, 2003) (a scheme lasting several weeks constituted "recurring and egregious" behavior); *Phillip J. Milligan*, Exch. Act Rel. No. 61790, 2010 WL 1143088 at *4-*5 (March 26, 2010) (characterizing scheme that defrauded numerous investors over several months as recurrent). The Commission should be guided by these two cases.

Gagaza relies on two inapposite cases, *iShopNoMarkup.com, Inc.*, 2012 WL 716928 (E.D.N.Y. March 3, 2012) and *SEC v. Shah*, 1993 WL 288285 (S.D.N.Y. July 28, 1993). Both cases are distinguishable because the issue in both was whether the defendant should be subject to a bar from serving as an officer or director of a public company – in which case the defendant's repeat offender status is specifically one of the factors a court must consider. *See, e.g., iShop*, 2012 WL 716928 at *4. Here, in contrast, whether a defendant is a repeat offender is not one of

the *Steadman* factors. Thus, Gagaza's attempt to incorporate the repeat offender discussion into whether the conduct at issue is recurrent is erroneous and misleading. As set forth above and in our Motion, Gagaza's conduct was recurrent because it occurred over a period of more than a year and involved at least 178 transactions.

**F. Gagaza's Reliance On 1 Global's Counsel's Advice That The 1 Global Notes
Were Not Securities Was Not Reasonable**

Gagaza attempts to justify his reliance on advice from Ledbetter that 1 Global's notes were not securities as reasonable where "the respondent has conducted due diligence that convinced him that the transactions at issue were not violative of securities laws." Response at 21-22, *citing OTC Global Partners*, 2017 WL 3588042 at *4. However, the undisputed facts show Gagaza did not conduct sufficient due diligence to be convinced that 1 Global's notes were not securities. As set forth in the Division's Motion, Gagaza's so-called due diligence on 1 Global, as an experienced securities professional and compliance officer for a registered investment firm, consisted of talking to two other 1 Global sales agents, reviewing 1 Global's marketing materials and a sample client account statement, reviewing resumes of 1 Global's officers, and doing internet searches to locate negative information on the Company.

None of these actions constitute an inquiry into whether the transactions violated the securities laws. Furthermore, in his sworn testimony, Gagaza claimed he attempted to look up the definition of a security, but provided no details of these alleged efforts. Division Motion, Ex. 5, at 73-74.¹

¹ In a letter to the Division following Gagaza's sworn testimony, Gagaza's counsel claimed he contacted the Hawaii Division of Securities in March 2017. However, Gagaza provided no evidence of this purported contact, and did not mention it when he was under oath. Furthermore, the only result of this alleged contact was for the State of Hawaii to refer Gagaza to its statutory definition of a security. Response at 21-22 and Ex. S at 2.

While evidence of good-faith reliance on advice of counsel may be a relevant factor in considering the level of a defendant's scienter (*Howard v. SEC*, 376 F.3d 1136, 1147 (D.C. Cir. 2004)), the exact information and its context is also important. Here, Ledbetter told Gagaza 1 Global's notes were not securities because (1) the notes were only nine-month notes, and (2) because 1 Global was using investor money to make merchant cash advances. Ex. 5 at 46 L.8-15 and 47 L. 7-15. On the face of the note, which includes an automatic renewal provision making it last longer than nine months, Gagaza was immediately on notice that Ledbetter's advice was either incorrect or incomplete. The same is true for the note giving 1 Global discretion to use investors' funds for purposes other than making merchant cash advances.

Despite these inconsistencies, Gagaza continued to blindly rely on Ledbetter's advice, even when faced with 1 Global's lie about the audited financial statements.² The Commission cannot ignore Global's lies when evaluating the reasonableness of Gagaza's purported reliance on Ledbetter's advice. When Gagaza's limited due diligence is coupled with his knowledge of 1 Global's lies and Ledbetter's advice being contradicted by the terms of the notes, Gagaza's reliance on Ledbetter is not reasonable.

G. Gagaza Continues To Not Acknowledge His Conduct Is Wrong

The entirety of Gagaza's response demonstrates that Gagaza has not accepted the wrongful nature of his conduct or provided assurances against future violations of the securities laws. He blames others, invents facts to attempt to buttress his position, ignores evidence that directly contradicts his arguments that his conduct was reasonable, and inexplicably argues that his profession as a registered investment adviser will not provide him future opportunities to violate

² *OTC Global Partners* is distinguishable from this case because the facts concerning the due diligence conducted were straightforward and there was no indication that the respondent faced lies or blatantly contradictory information from the issuer as Gagaza did here.

the securities laws. It is hard to imagine someone less contrite and less accepting that his conduct was wrongful. Gagaza's conduct demonstrates that he is a risk to violate the securities laws in the future if he is not barred from the industry.

H. Gagaza's Occupation Will Present Opportunities For Future Violations

It is impossible to not be concerned about the likelihood that Gagaza will have opportunities for future violations when he openly acknowledged in sworn testimony that if the Commission does not bar him from the securities industry, he intends to continue his investment adviser practice. Ex. 5 at 30 L.23 to 31 L.3. Gagaza has admitted he wants to get right back in the saddle assuming he emerges from this proceeding without being barred.

I. A Lesser Remedy Than A Bar Will Not Suffice

Finally, Gagaza accuses the Division of not justifying its request for a bar and failing to explain why a less drastic remedy would not suffice. On the contrary, the entirety of the Division's Motion and the undisputed facts therein and this Reply demonstrate exactly why a bar is the only relief that will achieve the remedial measure necessary to prevent Gagaza from repeating his conduct, especially when he has previewed his intention to restart his investment adviser business.

VI. CONCLUSION

For the reasons discussed above, the Division asks the Commission to sanction Gagaza by issuing a penny stock bar and barring him from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or NRSRO.

Dated: October 5, 2021

Respectfully submitted,

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CERTIFICATE OF SERVICE

Pursuant to Rule 150 of the Commission's Rules of Practice, I hereby certify that on October 5, 2021, the foregoing document was filed using the eFAP system and that a true and correct copy of the document has been served via email on this 5th day of October 2021, on the following persons entitled to notice:

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