UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-20828

In the Matter of

GREGORY LEMELSON,

Respondent.

DIVISION OF ENFORCEMENT'S REPLY MEMORANDUM IN SUPPORT OF ITS MOTION FOR SUMMARY DISPOSITION

The district court, analyzing substantially the same factors set forth in *Steadman*, issued a five-year injunction and a $160,000 Tier III penalty. Specifically, the district court found, largely based on the jury's verdict, that:

1. Respondent violated Section 10(b) of the Exchange Act and Rule 10b-5(b) three times;
2. Respondent's conduct was egregious;
3. Respondent acted with scienter;
4. Respondent refuses to recognize the wrongful nature of his conduct or give assurances against future violations; and
5. Respondent is in a position to violate the securities laws again.

These findings are binding on Respondent and should not be disturbed here.

As set forth below, Respondent's opposition (1) invites the Commission to re-litigate matters repeatedly decided against him by the jury and the district court and (2) puts forward numerous irrelevant facts and arguments. None of Respondent's arguments have merit. Summary disposition is appropriate and the Division's motion should be granted.

OS Received 08/12/2022

I. RESPONDENT'S CONSTITUTIONAL ARGUMENT IS MISPLACED AND SHOULD BE REJECTED.

Respondent incorrectly argues that the removability provisions for the Commission's ALJs are unconstitutional. [Oppn. at 9.] But any constitutional questions regarding the removability of the Commission's ALJs are irrelevant to this proceeding, over which the Commission, not an ALJ, is presiding. [*See* Order Instituting Administrative Proceedings Pursuant to Section 203(f) of the Investment Advisers Act of 1940 and Notice of Hearing (April 20, 2022).]

Even if the removability of the Commission's ALJs was relevant here, Respondent's reliance on the Fifth Circuit's recent decision in *Jarkesy v. SEC*, 34 F.4th 446 (5th Cir. 2022) (*pending petition for en banc reh'g, filed July 1, 2022*), to support his removal argument is misplaced. In *Jarkesy*, the majority applied a flawed reading of the Supreme Court's decision in *Free Enter. Fund v. Pub. Co. Acct. Oversight Bd.*, 561 U.S. 477 (2010) to hold, over a dissent, that "the statutory removal restrictions for SEC ALJs are unconstitutional." *See Jarkesy*, 34 F.4th at 463.[1] The *Jarkesy* majority, however, ignored the *Free Enterprise* Court's explanation that "[n]othing in our opinion . . . should be read to cast doubt on the use of what is colloquially known as the civil service system within independent agencies," including the restrictions on ALJs. *Free Enterprise*, 561 U.S. at 507 & n.10. Indeed, as then-Judge Kavanaugh recognized in the court of appeals decision preceding the Supreme Court's ruling, the separation-of-powers issues presented by ALJs are different than those in *Free Enterprise* because federal agencies have a "choice whether to use ALJs," ALJ decisions "are subject to review by agency officials,"

[1] *Jarkesy*'s removal holding stands in tension with recent decisions of at least two other circuits. *See, e.g.*, *Calcutt v. FDIC*, 37 F.4th 293, 319 (6th Cir. 2022) ("doubt[ing]" that petitioner "could establish a constitutional violation from the ALJ removal restrictions"); *Decker Coal Co. v. Pehringer*, 8 F.4th 1123, 1133 (9th Cir. 2021) (upholding the same statutory removal restrictions for ALJs in the Department of Labor).

OS Received 08/12/2022

and ALJs perform only limited "adjudicatory functions." *Free Enter. Fund v. Pub. Co. Acct. Oversight Bd.*, 537 F.3d 667, 699 n.8 (D.C. Cir. 2008) (Kavanaugh, J., dissenting). That contrast is especially apparent here, where the Commission has chosen ***not*** to utilize an ALJ to preside over Respondent's follow-on proceeding.

II. THE COMMISSION SHOULD NOT RE-LITIGATE MATTERS RESOLVED AGAINST REPONDENT IN THE DISTRICT COURT PROCEEDING.

Respondent's brief rehashes numerous arguments that the jury and the district court rejected. Indeed, each of Respondent's arguments was presented to the district court in opposition to the Division's remedies motion and rejected. [*Compare* Ex. A (opposition to remedies motion) with Div. Mem.[2] Ex. E (remedies order).] No different result should obtain here.

Respondent says he doesn't seek to re-litigate the merits here, instead claiming that his rejected defenses are "relevant" in this proceeding. [Oppn. at 11.[3]] Not so. Respondent is plainly seeking to have the Commission supplant its judgment for that of the jury and the district court by rehashing evidentiary and legal arguments.

As an initial matter, Respondent's statement of "undisputed" facts is anything but undisputed. The vast majority of the "facts" (in reality, almost all of Section II of Respondent's brief is argument) were hotly contested at trial. The jury and the district court were unpersuaded by Respondent's arguments and the Commission should not second-guess the jury's verdict.

Respondent's brief is rife with arguments about why the jury and the district court got it wrong, which is improper and irrelevant to the question before the Commission. For example, with respect to Respondent's false statement about the demise of Ligand's flagship drug,

[2] "Div. Mem." refers to the Division's memorandum in support of its motion for summary disposition.

[3] "Oppn." refers to Respondent's opposition brief.

Promacta, Respondent argues, among other things, that the statement was allegedly made in passing,[4] that Ligand's counsel didn't include the statement in a presentation to the Division, that Ligand's stock price closed higher the day the statement was made, and so forth. [Oppn. at 11-13.] As Respondent concedes, these arguments were all presented to the jury and rejected. [Oppn. at 11 (arguments presented here were "asserted at trial" and in "pending motions" for a stay pending appeal and for a new trial[5]).] And the district court rejected the same arguments numerous times: at summary judgment and on motions for judgment as a matter of law, judgment notwithstanding the verdict, stay pending appeal, and for a new trial.

Respondent retreads arguments that his false statements about Viking were "objectively true" and, in any event, constituted opinions protected by the First Amendment. He also argues that investors could have hunted around in public documents to discover the truth and that no Viking employees or investors raised concerns about the false statements.[6] [Oppn. at 13-16.] Again, every single one of these arguments was presented to the jury and the district court and rejected—repeatedly in the case of the district court.

Respondent's assorted legal arguments were also rejected at every stage of the district court proceeding. Respondent continues to argue, for example, (1) that his false statements were protected opinions as a matter of law and (2) the Division was required to show stock price movement with an event study to prove materiality. [Oppn. at 14-15 (opinion) and 16-18 (stock

[4] Respondent seeks to minimize the import of his statement about Promacta by focusing on one line from the June 19 interview that contained his false and fraudulent statement that Ligand's investor relations representative agreed that Promacta was "going away." [Oppn. at 12.] This ignores the broader context of a significant section of the interview devoted to Ligand and Promacta. [Div. Mem. Ex. I at 15-19.]

[5] The district court subsequently denied both motions, once again rejecting many of the arguments Respondent puts forward here. [*See* Exs. B & C, attached.]

[6] As to the last point, Respondent's argument is disingenuous. Viking was a private company at the time and did not have public investors. Further, the false statements about Viking were contained in reports ***about Ligand***, not Viking. It is therefore unsurprising that the jury and the district court were unpersuaded by Respondent's argument on this point.

price movement).] The jury was instructed on how to determine whether a statement is one of fact or opinion and materiality, including the significance of stock price movement (which the district court held was probative but not required to prove materiality). [*See* Ex. C (Memorandum and Order denying motion for stay).] The jury was again unpersuaded and the district court rejected the same arguments repeatedly.

The ***only*** way Respondent's various arguments could be "relevant" to whether an industry bar should issue is if the Commission were to reach a different conclusion than the jury and the district court. Respondent offers no authority that it is permissible or appropriate for the Commission to supplant its judgment for that of the jury and the district court. Indeed, Commission precedent is exactly the opposite: A respondent is collaterally estopped from challenging the basis for a district court injunction after trial "as well as factual and procedural issues that were actually litigated and necessary to the court's decision to issue the injunction." *James E. Franklin*, Exchange Act Release No. 56649, 2007 WL 2974200, at *4 (Oct. 12, 2007). Respondent had a full and fair opportunity to make these arguments and did not prevail as to the three statements for which Respondent was found liable. The jury's finding and district court's rulings should not be disturbed.

III. EACH OF THE *STEADMAN* FACTORS COUNSELS FOR IMPOSING AN INDUSTRY BAR.

A. Respondent's Conduct Was Egregious.[7]

The district court, in imposing the injunction and a Tier III penalty, found that "one of the three statements"—Lemelson's misrepresentation that Ligand's investor relations representative

[7] In the interest of not repeating its prior arguments, the Division incorporates by reference Section II.C.1 of its opening brief concerning the egregiousness of Respondent's conduct.

said Ligand's main product was going away—"was particularly egregious."[8] [Div. Mem. Ex. E at 9.] This finding is binding on Respondent and, as a result, should end the inquiry into whether his conduct was egregious. *James E. Franklin*, 2007 WL 2974200 at *4.

But that is not all. Respondent's fraudulent falsehoods are egregious when considered in context. *First*, as the jury heard at trial, Lemelson falsely stated that Ligand's investor relations representative agreed that Ligand's most profitable drug was "going away." The evidence at trial showed that Respondent used this misrepresentation as the tent-pole[9] for his repeated assertion that Promacta was doomed. *Second*, Lemelson fraudulently misrepresented that Ligand's partner, Viking, had not consulted its auditor on any material issues and its financial statements were unaudited. Lemelson used this falsehood to assert that the Ligand-Viking transaction was a "sham" intended to fraudulently pad Ligand's balance sheet. *Third*, Lemelson falsely stated that Viking did not intend to develop drugs ***at all***. Lemelson used this misrepresentation to advance the fiction that Viking was an empty shell that Ligand was using to engage in an illegal transaction.

Further, in imposing a Tier III penalty, the district court concluded that Respondent's conduct created a significant risk of substantial losses because the false statements were material ***and*** moved the market. [Div. Mem. Ex. E at 16-17.] Indeed, Respondent's contention that his falsehoods didn't move the market mischaracterizes the record. The district court specifically credited the Division's expert, Dr. Erin Smith of the Division of Economic and Risk Analysis, who found that there were statistically significant intraday declines in Ligand's stock price on the

[8] The district court characterized the Promacta falsehood as "***particularly*** egregious" (emphasis added); it did not hold that the Viking statements were ***not*** egregious.

[9] Respondent says his June 19, 2014 falsehood could not undergird his assertions about Promacta's alleged demise in his June 16 report. The Division argued at trial that the June 19 falsehood bolstered the June 16 report, the thesis of which focused on a severe competitive threat to Promacta and the negative impact it would have on Ligand's value, ***and*** that Respondent continued to peddle his story about Promacta in at least his July 3 and August 4 reports.

OS Received 08/12/2022

dates of Respondent's fraudulent statements. [*Id.* at 14-15.] It is manifestly egregious to disseminate false and fraudulent statements that ran a significant risk of substantial investor losses.[10]

Respondent points to a single matter in which an ALJ declined to impose an industry bar under the particular facts and circumstances of that case, which were entirely unlike the facts of this case. *In re Piper Capital Management Inc.*, 2000 WL 1759455 (Nov. 30, 2000). Critically, that case was ***not*** a follow on administrative proceeding based on an injunction already imposed by the district court. There was no underlying jury finding or finding by a district court that the factors warranting an injunction had been met. *Piper* would only be relevant by analogy here if this was an original proceeding to determine liability and remedies. It is not. Liability and the factual predicate for the district court's injunction are established and binding on Respondent.

B. Respondent's Conduct Was Repetitive.

In his answer to the OIP, Respondent admitted that the jury found that he made three separate false and fraudulent statements to the investing public: *First*, Respondent's false statement about Promacta "going away." *Second*, the jury found that Respondent made two separate false statements of fact about Viking in a July 3, 2014 report—that the company was unaudited and didn't plan to conduct clinical studies. Defendant thus made three separate false and fraudulent statements—*i.e.*, repeated fraudulent conduct. [Div. Mem. Ex. H (Answer to OIP) at 2.][11]

[10] As detailed in the Division's opening brief, there are yet more facts supporting the district court's finding of egregiousness, such as Respondent bragging about bringing Ligand's stock price down. [Div. Mem. at 8-10.]

[11] Respondent argues that the three fraudulent statements for which he was found liable were few among many that were not charged. [Oppn. at 18-19.] This same argument was rejected by the district court and, in any event, it is no defense to fraud to say that the defendant made truthful statements on other occasions.

C. Lemelson Acted with a High Degree of Scienter.

The jury found that Lemelson acted with scienter—a "conscious intent to defraud" or an "extreme departure from the standards of ordinary care [that] presents a danger of misleading buyers or sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it." [Div. Mem. Ex. Q (jury instructions) at 105-06.] The District Court also found that Lemelson's "fraud is not in question." [Div. Mem. Ex. E at 14.]

Respondent's only argument in this regard is that his conduct was more "consistent" with recklessness than intentional misconduct. As an initial matter, this is a distinction without a difference. "Recklessness" is not a "lesser" form of scienter—it is one of two ways to establish that a defendant acted with fraudulent intent. Indeed, the case Respondent cites holds that recklessness consists of "highly unreasonable omissions or misrepresentations that . . . present a danger of misleading buyers or sellers which is ***either known to the defendant, or is so obvious that the defendant must have been aware of it***." *SEC v. Shanahan*, 2010 WL 173819, at *9 (D. Minn. Jan. 13, 2010) (emphasis added). It is therefore a species of fraudulent conduct that stands on equal footing with intentional misconduct in establishing scienter.

In any event, the jury was not asked to distinguish between the two paths to scienter, as Respondent concedes. [Oppn. at 20 ("The jury here was not specifically asked to find whether it believed [Respondent] acted intentionally or recklessly.").] There is no basis to assume the jury's verdict was based on a finding of recklessness and there was ample evidence at trial to conclude that Respondent acted intentionally. As the district court observed, the three false statements for which Lemelson was found liable were made "[w]hile Lemelson engaged in a campaign to drive down Ligand's stock [price.]" [Div. Mem. Ex. E at 9.] The jury may well

have—and likely did—conclude that Respondent intentionally disseminated falsehoods for the purpose of moving the market for Ligand stock.

D. Respondent Does Not Recognize the Wrongful Nature of His Conduct and Has Given *No* Assurances against Future Violations.

Respondent has not provided assurances against future violations. To the contrary, the district court found that Respondent is unremorseful:

> Finally, Lemelson continues to unabashedly defend his actions. Lemelson does not recognize the wrongfulness of his conduct or acknowledge when he was clearly wrong (like the statements about Viking). His pugilistic approach to the litigation (*e.g.*, the tweets and the leaked documents) indicates he has not learned his lesson.

[Div. Mem. Ex. E at 10.] This finding is binding on Respondent and should not be second-guessed here.

The district court had ample basis to reach this conclusion. Among other things, Respondent himself, after being found liable for three instances of fraud stated: "***I'll never regret the things I did***." [Div. Mem. Ex. EE (emphasis added).] This alone is sufficient to conclude, as the district court put it earlier in the case, that Respondent "doesn't seem to [show] any real remorse here." [Ex. D at 20 (referring to Respondent's violation of the district court's protective order).] Any assurances against future violations ring hollow.[12]

Respondent also goes on at length about alleged misdeeds of Ligand's counsel and Division staff. [Oppn. at 22-27.] These accusations are irrelevant and, in any event, were

[12] Respondent suggests that he is unlikely to reoffend having endured the underlying district court proceeding, citing *SEC v. Ingoldsby*, 1990 WL 120731, at *3 (D. Mass. May 15, 1990). As an initial matter, *Ingoldsby* is inapposite because it involved the district court weighing the injunction factors under the particular facts and circumstances of that case. Here, the district already weighed the factors and found an injunction appropriate. Respondent's implicit claim that the underlying action makes him unlikely to reoffend is not credible in light of his steadfast refusal to acknowledge the wrongfulness of his conduct or personally provide assurances.

OS Received 08/12/2022

rejected by the district court. The question before the Commission is whether Respondent has given credible assurances that he won't reoffend. He hasn't.

The Division notes that Respondent has hurled baseless allegations at the Division and Ligand throughout the district court proceeding and now this proceeding. Among other things, Respondent clings to his accusation that the Division or Ligand leaked information about the underlying investigation to the press. [Oppn. at 29-30; Div. Mem. Ex. EE.] There was never any evidence, much less a finding, that this happened. In contrast, ***Respondent*** leaked confidential discovery materials to the press in violation of the district court's protective order and, among other things, was sanctioned $100 per page. [Div. Mem. Ex. BB.]

Respondent has also claimed over and over again that this case was brought as a result of the Division doing Ligand's bidding or some alleged "bias" against him. [Oppn. at 29-30.] But Respondent, however, was permitted to examine witnesses at trial regarding this accusation and make arguments in opening and closing. [Ex. B at 2.] The jury didn't buy it. Further, the district court dismissed Respondent's "selective prosecution" defense on summary judgment, finding as a matter of law that there was insufficient evidence supporting Respondent's claims that the case was brought for some improper purpose. [Ex. E at 7-12, 28-31.] In the end, neither the jury nor the district court ever found that the Division or Ligand's counsel engaged in any wrongdoing. Respondent's laundry list of baseless grievances has no relevance here and should be disregarded.

E. Respondent Is In a Position to Reoffend.

There is no dispute that Respondent remains Chief Investment Officer for Lemelson Capital Management. The District Court agreed that Lemelson is therefore in a position "to violate again, as he continues to work as an investment adviser and recently started a new fund . . . ." [Div. Mem. Ex. E at 9.]

Respondent argues that he is not in a position to reoffend because the Division never sought a preliminary injunction. [Oppn. at 1, 7-8.] A preliminary injunction, however, is designed to halt ongoing fraudulent conduct, for example an offering fraud in which investors are still being solicited at the time an enforcement action is filed. This case concerns wrongdoing that began and ended in 2014. There was therefore no basis for the Division to seek preliminary relief. Respondent's argument is a red herring and should be rejected.

F. The Equities Support Imposition of a Bar.

Respondent argues that various factors counsel against a bar. Once again, the majority of his arguments are irrelevant and were unpersuasive to the district court.

Respondent first argues that his current investors would be harmed by a bar. [Oppn. at 28.] Not so. The purpose of a bar is to protect investors (and the securities markets) from fraudsters. Respondent's past conduct, failure to recognize the wrongfulness of his conduct, and refusal to provide assurances against future misconduct all raise the specter that he will reoffend. That could mean defrauding his own investors. And it could also mean engaging in fraud like that underlying this case—market manipulation. A bar protects the investors and markets, generally, and Respondent's current investors should not benefit from fraudulent conduct.

Second, Respondent argues that he did not engage in any misconduct since 2014. [Oppn. at 28.] There is no evidence of this assertion in the record other than Respondent's say-so. And, naturally, he disclaims any further misconduct. However, given that he steadfastly refuses to see his 2014 fraud as wrongful, there is little reason to believe he would recognize any subsequent misdeeds as wrongful. Moreover, Respondent did not dispute in his opposition brief that The Amvona Fund lost all of its investors' money in 2020, which has spawned at least one litigated matter. [Div. Mem. at 14.]

Third, Respondent points to various good works. [Oppn. at 28-29.] This is irrelevant. The fact that he may engage in charitable activities has no bearing on whether his fraud warrants an industry bar. In the same vein, Respondent argues that he did not benefit from his fraud. But he did. There is no dispute that Respondent and his family held a significant stake in The Amvona fund, drew a salary, and received a management fee.

Fourth, Respondent argues there was no investor harm. [Oppn. at 29.] The Division was not required to prove investor harm to prevail at trial. [Div. Mem. Ex. E at 13, 15.] And the district court found that Respondent's conduct created a significant risk of substantial investor losses—one of the bases for imposing a Tier III penalty. [*Id.* at 15 (showing a significant ***risk*** of investor harm sufficient) (emphasis added).]

Fifth, Respondent argues that "Ligand's conduct in pressuring the Division to bring this case was disturbing." [Oppn. at 29-30.] As discussed above, there has never been any evidence whatsoever for this accusation. Moreover, these is nothing inherently suspicious about a victim of fraudulent conduct urging the Division to investigate the matter. In fact, it is encouraged. [sec.gov/tcr ("**We strongly encourage the public (whistleblowers and non-whistleblowers) to submit any tips, complaints, and referrals (TCRs) using the SEC's online TCR system and complaint form at** https://www.sec.gov/tcr." (emphasis in original).]

Lastly, Respondent argues that this case is "unprecedented," distinguishing the underlying facts from certain other "short-and-distort" cases. [Oppn. at 30-31.] This is another red-herring. There is no reason the Division's enforcement powers should not extend to fraudulent conduct in whatever form it takes. And here the jury concluded that Respondent in fact committed fraud. The fact that this case may look different from other cases is of no bearing.

IV. ERROR IN THE DIVISION'S MEMORANDUM.

Respondent has identified that a block quote on page four of the Division's brief was incorrectly sourced to the District Court. [Oppn. at 31.] The Division agrees that this quote is incorrectly sourced, regrets the error, and asks the Commission to disregard this block quote. Respondent makes a number of additional accusations about the Division's supposed making of false statements. The Division disputes Respondent's accusations, which are, in any event, irrelevant to this proceeding.

V. THERE IS NO REASON TO DELAY CONSIDERATION OF THE DIVISION'S MOTION.

Respondent requested that the Commission stay consideration of the instant motion pending the district court's rulings on his motion for stay pending appeal and for a new trial. As noted above, both motions were denied by the district court. Respondent's request is therefore moot.[13]

Dated: August 12, 2022

Respectfully submitted,

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[13] Defendant subsequently filed an "Update to Tribunal Regarding District Court Action." The "update" is not a motion and therefore provides no basis for a stay of this proceeding.

CERTIFICATE OF SERVICE

Undersigned counsel hereby certify that the foregoing document and its attachments were served on Respondent's counsel via electronic mail on August 12, 2022.

/s/ Alfred A. Day
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