No. 22-13129

IN THE

United States Court of Appeals for the Eleventh Circuit

U.S. SECURITIES AND EXCHANGE COMMISSION,
Plaintiff-Appellee,

v.

SPARTAN SECURITIES GROUP, LTD., ET AL.
Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF FLORIDA, TAMPA DIVISION
DISTRICT JUDGE VIRGINIA M. HERNANDEZ COVINGTON
(NO. 8 :19-cv-00448-VMC-CPT)

DEFENDANTS-APPELLANTS' OPENING BRIEF

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CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT[1]

Defendants-Appellants certify that the following is a complete list of interested persons as required by Fed. R. App. P. 26.1 and 11th Cir. R. 26.1:

1. Aristocrat (ASCC), *microcap issuer involved in charged conduct**
2. Berkowitz, Dan, *Attorney for the Commission*
3. Bustillo, Eric I., *Regional Director for Plaintiff-Appellant*
4. Changing Technologies (CHGT), *microcap issuer involved in charged conduct**
5. Conley, Michael A., *Attorney for the Commission*
6. Connect X Capital Markets LLC, *Non-party owner of Defendants-Appellants Island Capital Management, LLC and Spartan Securities Group, LTD*
7. Cook, Jeffrey, *Senior Counsel for Plaintiff-Appellee*
8. Court Document Services, Inc. n/k/a ChinAmerica Andy Movie Entertainment Co. (CAME), *microcap issuer involved in charged conduct**

[1] On September 30, 2022, Appellants filed a CIP in accordance with 11th Cir. R. 26.1-1(a)(2). On October 17, 2022, Appellee filed a CIP which included certain microcap issuers. Appellants take the position that these issuers are not "interested persons" within the meaning of 11th Cir. R. 26.1-2 but includes the issuers in this CIP and has marked them with a "*".

9. Dhillon Law Group, Inc., *District Court Law Firm for Defendants-Appellants* (added)
10. Dilley, Carl E., *Defendant-Appellant*
11. Dinello Restaurant Ventures, Inc., n/k/a AF Ocean Investment, *microcap issuer involved in charged conduct**
12. Eldred, Micah J., *Defendant-Appellant*
13. Eldred, Toni, *Indirect owner of Defendants-Appellants Island Capital Management, LLC and Spartan Securities Group, LTD through her interest in Connect X*
14. Envoy Group, Corp. (BLGI), *microcap issuer involved in charged conduct**
15. E-Waste Corp. n/k/a EZ Raider Co. (EZRG), *microcap issuer involved in charged conduct**
16. Fernandez, Wilfredo, *District Court Counsel for Plaintiff-Appellee*
17. First Independence Corp. n/k/a Codesmart Holdings, Inc. (ITEN), *microcap issuer involved in charged conduct**
18. First Social Networx, Corp. n/k/a Rebel Group, Inc. (MOXG), *microcap issuer involved in charged conduct**
19. First Titan n/k/a GlobeStar Therapeutics Corp. (RSTC), *microcap issuer involved in charged conduct**
20. First Xeris, *microcap issuer involved in charged conduct**

21. Global Group n/k/a Tyme Technologies, Inc. (TYME), *microcap issuer involved in charged conduct**
22. Gordon, Glenn S., *Associate Regional Director for Plaintiff-Appellant*
23. Grilli, Peter J., *District Court Mediator*
24. Hernandez Covington, Virginia, U.S.D.J., *United States District Court Judge*
25. Island Capital Management, LLC, d/b/a Island Stock Transfer, *Defendant-Appellant*
26. Johnson, Alise M., *District Court Counsel for Plaintiff-Appellee*
27. Kelly, Michael J., *Counsel for Plaintiff-Appellee*
28. Kids Germ n/k/a Topaz Resources, Inc. (TOPZ), *microcap issuer involved in charged conduct**
29. Kruckenberg, Caleb, *District Court Counsel for Defendants-Appellants*
30. Lopez, David D., *Former Defendant (terminated July 30, 2021)*
31. Morales-Christiansen, Anna Patricia, *District Court Counsel for Defendants-Appellants*
32. Nestor, Christine, *District Court Counsel for Plaintiff-Appellee*
33. Matthew Seth Sarelson P.A., *District Court Law Firm for Defendants-Appellants*
34. Mooney, Brian, *District Court Mediator*

35. Neutra Corp. (NTPR), *microcap issuer involved in charged conduct**
36. New Civil Liberties Alliance, *Legal Organization for Defendants-Appellants*
37. Obscene Jeans n/k/a MyGo Games Holding Co. (OBJE), *microcap issuer involved in charged conduct**
38. On the Move n/k/a Artificial Intelligence Technology Solutions (AITX), *microcap issuer involved in charged conduct**
39. Peter J. Grilli, PA, *Law Firm for District Court Mediator*
40. PurpleReal.com, Corp., *microcap issuer involved in charged conduct**
41. Rainbow Coral Corp. (RBCC). *microcap issuer involved in charged conduct**
42. Reynolds, Scott Richard, *Indirect owner of Defendants-Appellants Island Capital Management, LLC and Spartan Securities Group, LTD through his interest in Connect X*
43. Rollins, Kara McKenna, *Counsel for Defendants-Appellants*
44. Sarelson, Matthew S., *District Court Counsel for Defendants-Appellants*
45. Spartan Securities Group, LTD., *Defendant-Appellant*
46. Staroselsky, Daniel, *Counsel for Plaintiff-Appellee*
47. Sum, Alice K., *District Court Counsel for Plaintiff-Appellee*
48. Top to Bottom Pressure Washing, Inc. n/k/a Ibex Advanced Mortgage Technology, Inc. (IBXM), *microcap issuer involved in charged conduct**

49. The Mooney Firm, PLLC, *Law Firm for District Court Mediator*
50. Tuite, Christopher P., U.S.M.J., *United States District Court Magistrate Judge*
51. Ulmer & Berne LLP, *District Court Law Firm for Defendants-Appellants*
52. U.S. Securities and Exchange Commission, *Plaintiff-Appellee*
53. Vecchione, John J., *Counsel for Defendants-Appellants*
54. VonderHeide, Heidi E., *District Court Counsel for Defendants-Appellants*
55. Quality Wallbeds, Inc. n/k/a Horrison Resources Inc. (SLPC), *microcap issuer involved in charged conduct**
56. Wolper, Alan Mitchell, *District Court Counsel for Defendants-Appellants*
57. Zitman, Christine, *Indirect owner of Defendants-Appellants Island Capital Management, LLC and Spartan Securities Group, LTD through her interest in Connect X*

No publicly traded company or corporation has an interest in the outcome of this case or appeal.

STATEMENT REGARDING ORAL ARGUMENT

Oral argument is requested as it may aid this Court in deciding the complex and important issues in this case. Among other issues, this case involves one of first impression regarding the availability of disgorgement for violations of the securities laws when the disgorged monies are returned to the Treasury of the United States.

TABLE OF CONTENTS

TABLE OF CITATIONS

Cases

Constitutional Provisions

Statutes

Regulations

Rules

Other Authorities

STATEMENT OF SUBJECT-MATTER AND APPELLATE JURISDICTION

On August 10, 2022, the District Court for the Middle District of Florida issued final judgments as to Defendants-Appellants Spartan Securities Group, Ltd. ("Spartan"), Island Capital Management ("Island"), Carl E. Dilley ("Dilley"), and Micah J. Eldred ("Eldred"). *See* Doc 298 (Dilley), Doc 299 (Spartan), Doc 300 (Eldred), Doc 301 (Island). Appellants filed a timely notice of appeal on September 16, 2022. Doc 305. This Court has appellate jurisdiction under 28 U.S.C. § 1291.

STATEMENT OF THE ISSUES

1. Did the court err in permitting time-barred claims and remedies to be put before the jury?
2. Did the court err in finding sufficient evidence to support a jury verdict that Appellants violated Rule 10b-5(b)?
3. Did the court abuse its discretion in permitting unqualified and unreliable expert testimony to go before the jury?
4. Did the court err in depriving Appellants of their right to a jury determination on the facts necessary to calculate civil penalties?
5. Did the court abuse its discretion in ordering remedies based on conduct as to which the jury found no liability?
6. Did the court err in ordering Island to pay disgorgement to the U.S. Treasury rather than for the benefit of investors?

7. Did the court abuse its discretion in failing to consider Dilley's, Spartan's, and Island's ability to pay the penalties ordered?

STATEMENT OF THE CASE

I. STATEMENT OF THE FACTS

Plaintiff-Appellee Securities and Exchange Commission ("SEC") filed a 14-count complaint against Appellants in February 2019. The complaint charged Appellants with participating in a broad pair of schemes to aid and abet the creation of fake publicly traded companies and subsequent issuances of stock between December 2009 and August 2014. Doc 1; Doc 263 - Pg 1.

Appellants moved to dismiss arguing, among other things, that SEC's claims and remedies were untimely under the five-year statute of limitations imposed by 28 U.S.C. § 2462. Doc 22; Doc 23. The district court denied those motions finding that SEC had sufficiently pled a "continuing violation" that straddled the five-year limitations cutoff. Doc 44 - Pg 21-22. Defendants also filed other pretrial motions, including a *Daubert* motion to exclude the report and testimony of SEC's expert witness, James M. Cangiano, Doc 101; a motion to require a jury determination on the facts necessary to determine any civil penalties, Doc 122; and a motion for summary judgment, Doc 102. The court denied each motion. Doc 134; Doc 135; Doc 159.

Trial evidence described the process by which companies go public. First, a company typically registers with SEC by filing a registration statement on SEC Form S-1. Doc 263 - Pg 2 (citing Doc 228 - Pg 23). After SEC approves registration, the company's stock offering is declared "effective" and its shares are eligible to be sold. *Id.* (citing Doc - Pg 23-24). Next the company, otherwise known as an "issuer," requests a broker-dealer—such as Spartan—to file a Rule 15c-211 application ("Form 211") with the Financial Industry Regulatory Authority ("FINRA"). *Id.* (citing Doc - Pg 23-25).

During the Form 211 application process relevant to this case, Spartan, Dilley, and Eldred typically gathered the required information from the issuers. Doc 257-22 - Pg 3-4; Doc 224 - Pg 34-35. Generally, this information included publicly filed documents with the SEC. Doc 224 - Pg 34-35. Spartan also collected additional information that was not required, like notarized and sworn affidavits and questionnaires. Doc - Pg 35; Doc 257-23. Spartan then provided the issuers' information along with the Form 211 application to FINRA. Doc 257-10 - Pg 2-5. FINRA was free to question any information provided, and often did so. Doc 226 - Pg 33; Doc 249 - Pg 12-13.

Whenever FINRA raised questions, Spartan responded and provided information it received from the issuer or retrieved from SEC's publicly available database. Doc 228 - Pg 19-20; Doc 224 - Pg 34-35. FINRA would then "clear" the Form 211

application for stock price quotation if it was satisfied that Appellants-Defendants had provided the requisite information. *See, e.g.,* Doc 255-12 - Pg 18. After a Form 211 application is approved by FINRA, the issuers may seek clearance from the Depository Trust Company ("DTC"), which permits the issuer's shares to trade freely and electronically. Doc 228 - Pg 3 (citing Doc 228 - Pg 37-38). Crucially, information exchanged in the Form 211 application process is not publicly available. Doc 226 - Pg 84.

During the relevant time, Spartan filed Form 211 applications to initiate quotations for well over 1,200 issuers. Doc 208 - Pg 25; Doc 224 - Pg 41.

SEC's Complaint alleged violations regarding 19 issuers: Kids Germ, Obscene Jeans, On the Move, Rainbow Coral, First Titan, Neutra, Aristocrat, First Social, Global, E-Waste, First Independence, Changing Tech., First Xeris, Envoy Group, Dinello, Court Document, Quality Wallbeds, Top to Bottom, and PurpleReal. Doc 249 - Pg 12. Al Mirman or Sheldon Rose was involved with 14 of these 19 companies. Doc 249 - Pg 10 ("Mirman/Rose issuers"). Mirman and Rose later pled guilty to conspiracy to commit securities fraud for their actions related to these issuers and were convicted felons by the time of the trial below. *Id*. The other issuers—Dinello, Court Document, Quality Wallbeds, Top to Bottom, and PurpleReal.com—involved Michael Daniels, Diane Harrison, and/or Andy Fan, who

entered consent decrees with SEC. *See* Doc 249 - Pg 10-11 ("Harrison/Daniels issuers").

At all relevant times, Spartan was registered with the SEC as a broker-dealer and Island was registered with SEC as a transfer agent. Doc 249 - Pg 10. Dilley and Eldred were both registered principals of Spartan. *Id*. Dilley was also the President of Island and Eldred was its CEO. *Id*. Transfer agents serve a recordkeeping function for publicly traded companies. Doc 263 – Pg 3 (citing Doc 228 – Pg 40). They issue and cancel stock certificates, add or remove "restrictive legends" on stock certificates, and record transactions after they occur. *Id.* (citing Doc 228 - Pg 40); 234 - Pg 62.

After a 12-day trial in July 2021, the jury returned a verdict in Appellants' favor on 13 of SEC's 14 counts, and a verdict for SEC on a single count.[2] Doc 263 - Pg 9. That count alleged that Appellants made materially misleading statements or omissions in connection with purchases of certain issuers' securities in violation of Section 10(b) of the Exchange Act, 15 U.S.C. § 78(j)(b), and SEC Rule 10b-5(b), 17 C.F.R. § 240.10b-5(b), thereunder. Doc 263 - Pg 2. As to this count, the jury instructions outlined 19 types of misrepresentations or omissions that Appellants allegedly made. Doc 249 - Pg 38-39. Appellants had sought to determine the

[2] The jury's verdict fully exonerated a fifth defendant, David D. Lopez. *See* Doc 250 - Pg 1; 256 - Pg 1.

substance of their alleged misstatements throughout discovery, but SEC articulated them in writing only at the jury instruction stage. Doc 219 - Pg 8. SEC objected to a requirement that the jurors specify which of the statements they found false. *Id.* After trial, Appellants filed a renewed motion for judgment as matter of law under Federal Rule of Civil Procedure 50(b), which the district court denied. Doc 263 - Pg 30.

SEC subsequently requested various monetary and equitable sanctions, including civil penalties, permanent injunctions, lifetime penny stock bars, and disgorgement, which the court granted in part. *See generally* Doc 297. The court significantly reduced SEC's requested civil penalties and disgorgement as well as the duration of its requested injunctions and penny stock bars. Doc 297 - Pg 8 (no injunction as to Spartan); Doc 297 - Pg 10 (revising injunctive language as to Island); Doc 297 - Pg 12, 15-16 (ordering five-year injunctions as to Dilley and Eldred and revising injunctive language); Doc 297 - Pg 17-18 (ordering lifetime penny stock ban for Spartan and ten-year bans for Dilley and Eldred); Doc 297 - Pg 31 (reducing the amount of disgorgement Island was ordered to pay); Doc 297 - Pg 34-35, 37-38 (ordering Tier Two penalties); Doc 298; Doc 299; Doc 300; Doc 301.

Appellants timely appealed. Doc 305.

II. STANDARDS OF REVIEW

This Court reviews questions of statutory interpretation *de novo*. *U.S. v. Jones*, 962 F.3d 1290, 1296 (11th Cir. 2020), *cert. granted, judgment vacated on other*

grounds by 143 S. Ct. 72 (2022) (mem.). This Court also "review[s] a district court's application of a statute of limitations … *de novo*." *McCaleb v. A.O. Smith Corp.*, 200 F.3d 747, 750 (11th Cir. 2000). Likewise, "[a] district court's denial of a defendant's motion for judgment as a matter of law is reviewed *de novo*, applying the same legal standard as the district court." *Bianchi v. Roadway Exp., Inc.*, 441 F.3d 1278, 1282 (11th Cir. 2006). "The question before the district court regarding a motion for judgment as a matter of law remains whether the evidence is 'legally sufficient to find for the party on that issue,' … regardless of whether the district court's analysis is undertaken before or after submitting the case to the jury." *Chaney v. City of Orlando,* 483 F.3d 1221, 1227 (11th Cir. 2007) (quoting Fed. R. Civ. P. 50(a)(1)). Under Rule 50(b), "a court's sole consideration of the jury verdict is to assess whether that verdict is supported by sufficient evidence." *Id.*

The district court's decisions regarding the exclusion or admission of expert testimony are reviewed under "an abuse-of-discretion framework." *Hughes v. Kia Motors Corp.*, 766 F.3d 1317, 1328 (11th Cir. 2014). Under this framework, a district court's determination is provided "considerable leeway[,]" *Kumho Tire Co. v. Carmichael*, 526 U.S. 137, 152 (1999), and "requires that [appellate courts] defer to the district court's ruling unless it is 'manifestly erroneous.'" *Rink v. Cheminova, Inc.*, 400 F.3d 1286, 1291 (11th Cir. 2005) (internal quotation marks omitted). Similarly, under the securities laws, "the amount of a monetary remedy … is

reviewed for abuse of discretion." *SEC v. Warren*, 534 F.3d 1368, 1369 (11th Cir. 2008) (per curiam).

> [A]n abuse of discretion "can occur in three principal ways: [1] when a relevant factor that should have been given significant weight is not considered; [2] when an irrelevant or improper factor is considered and given significant weight; and [3] when all proper factors, and no improper ones, are considered, but the court, in weighing those factors, commits a clear error of judgment."

Ameritas Variable Life Ins. Co. v. Roach, 411 F.3d 1328, 1330 (11th Cir. 2005) (quoting *Kern v. TXO Prod. Corp.*, 738 F.2d 968, 970 (8th Cir. 1984)).

SUMMARY OF ARGUMENT

The district court erred throughout the pendency of this litigation.

First, all the relief SEC sought constituted "penalties" subject to 28 U.S.C. § 2462's five-year statute of limitations. *See Kokesh v. SEC*, 581 U.S. 455, 457 (2017). Likewise, the requested injunctions and penny stock bars were "penalties" because those sanctions serve "retributive or deterrent purposes." *Id.* at 467 (citation omitted). The district court committed legal error by permitting time-barred claims to be presented to the jury, which directly harmed Appellants' statutory and procedural rights. The court then abused its discretion when it considered the same time-barred evidence in determining sanctions and remedies.

Second, Appellants did not make material misrepresentations or materially misleading omissions in connection with the sale of securities because the relevant statements were made to a *regulator* in a nonpublic process, they were not material,

and they did not "coincide with" any securities transaction. In addition, the only arguably false statements the jury could have found were either not material, conclusively rejected by the jury, or omissions that Appellants had no duty to disclose. For instance, Appellants were under no duty to disclose nonpublic information about hypothetical future events. The court committed legal error when it denied Appellants' Rule 50(b) motion.

Third, the district court failed in its gatekeeping role under Federal Rule of Evidence 702 and abused its discretion when it permitted SEC's expert witness to provide unqualified, unreliable, and unfettered testimony outside the scope of his knowledge and expertise. The court abused its discretion by considering this unreliable evidence in denying Appellants Rule 50(b) motion and in determining sanctions.

Fourth, the Seventh Amendment guarantee of a jury trial extends to factual determinations necessary to calculate penalty amounts under the Exchange Act's three-tier penalty scheme. The court erroneously denied Appellants' constitutional right to a jury determination on the facts necessary to calculate the penalty.

Fifth, disgorgement was impermissible because the disgorged funds were ordered to be paid to the Treasury rather than for the benefit of investors; because there was no causal connection between the disgorged funds and the conduct at issue, SEC did not provide a reasonable approximation of the allegedly ill-gotten gains, and Island's

conduct was not the cause of any uncertainty in the disgorgement calculation. The district court erred when it ordered Defendant-Appellant Island to pay disgorgement to the Treasury when there were no identified harmed investors and the monies sought to be disgorged were from a third-party's unclean hands.

Sixth, due process and justice forbid courts from ordering remedies based on conduct for which the jury found no liability. The district court erred when it ordered relief based on alleged conduct—aiding and abetting securities violations or participation in a scheme to defraud—that was rejected by the jury multiple times. Doc 250; Doc 256 (jury found no liability under Counts 1-3, 5, 7, and 11 for aiding and abetting violations or participating in schemes to defraud).

Finally, a defendant's ability to pay is a factor that should be given significant weight at the penalty phase, as not doing so violates the Excessive Fines Clause of the Eighth Amendment. The district court erred when it failed to consider Dilley's, Spartan's, or Island's ability to pay the civil penalties it ordered.

The Court should vacate the judgment against Appellants and remand for entry of judgment in favor of Appellants on the sole remaining count.

ARGUMENT

I. SEC'S CLAIMS AND THE REMEDIES ORDERED WERE TIME-BARRED

A. There Were No Actionable Statements Within the Statute of Limitations Period

The district court erred when it denied Appellants' motion for summary judgment and permitted time-barred claims to go before the jury, and again when it denied their Rule 50(b) motion and ordered sanctions based on that same time-barred conduct.

"Statutes of limitation are vital to the welfare of society and are favored in the law." *Wood v. Carpenter*, 101 U.S. 135, 139 (1879). That is particularly true where SEC sat on its rights and, by its own admission, willfully delayed in commencing this action. When the Complaint was filed, and when the district court ruled on the Appellants' motions to dismiss, *see* Doc 44, as well as their motion for summary judgment, *see* Doc 135, all forms of relief SEC sought in its complaint were subject to the five-year statute of limitations codified at 28 U.S.C. § 2462. *See Kokesh*, 581 U.S. at 457.[3] SEC injunctions and penny stock bars are "penalties" because they serve "retributive or deterrent purposes." *Id.* at 467 (citation omitted); *but see SEC*

[3] During the pendency of this litigation, the statute of limitations for disgorgement and certain claims for equitable relief were amended and retroactively extended to ten years under specified circumstances. *See* The William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021 ("2021 NDAA"), Pub. L. No. 116-283, § 6501, 134 Stat. 3388, 4625-26 (2021) (amending 15 U.S.C. § 78u).

v. Graham, 823 F.3d 1357, 1360 (11th Cir. 2016) (pre-*Kokesh* case finding injunction an equitable remedy not subject to § 2462). "[T]he most natural reading of [28 U.S.C. § 2462]" is that a claim, even one based on fraudulent conduct, accrues when the alleged conduct occurs. *Gabelli v. SEC*, 568 U.S. 442, 448 (2013). Section 2462 "sets a fixed date when exposure to the specified Government enforcement efforts ends[.]" *Id.* All the remedies SEC sought were subject to § 2462's five-year statute of limitations at the time the Complaint was filed and when the district court denied Appellants' summary judgment motion. SEC was without lawful power to bring this case in the first instance, let alone carry it through to trial.

Section 2462 promotes "repose, elimination of stale claims, and certainty about a plaintiff's opportunity for recovery and a defendant's potential liabilities." *Rotella v. Wood*, 528 U.S. 549, 555 (2000). It also "promote[s] justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared." *Gabelli*, 568 U.S. at 448 (quoting *Order of R.R. Telegraphers v. Railway Express Agency, Inc.*, 321 U.S. 342, 348-349 (1944)).

The court erred when it denied Appellants' statute of limitations arguments. *See* Doc 44 - Pg 20-22; Doc 135 - Pg 15-16. And that error was not harmless; just days after the district court denied Appellants' summary judgment motion, Congress extended SEC's statute of limitations and purported to apply the newly extended

limitations period not only to future cases but also pending cases. *See supra* footnote 3.

There is no legally sufficient evidence that any misrepresentations or omissions occurred within the time prescribed by § 2462. *See Chaney*, 483 F.3d at 1227. Spartan, a registered broker-dealer, was involved in the FINRA Form 211 application process and played no role in recording or transferring shares of any issuer. Doc 249 - Pg 10; Doc 263 - Pg 2-3, (describing FINRA Form 211 process and how transfer agents operate). Only Dilley, Eldred, and Spartan could have possibly made misrepresentations or omissions in relation to the Form 211 application process. *See* Doc 263 - Pg 18.[4] As a transfer agent, Island played no role in the FINRA Form 211 application process, nor did SEC allege such involvement, nor did the district court find it. Doc 263 - Pg 2-3, 8, 28-30 (no mention of Island in connection with FINRA Form 211 application process).

Jury Instruction 19 listed nineteen alleged misrepresentations and omissions. Doc 249 - Pg 35-40. It provides a framework for establishing the timeline for when any misrepresentations or omissions could have been made. *Id.* Considering the tolling agreement between the parties, the conduct at issue must have occurred *after*

[4] The court committed legal error in determining that statements were "made" by Appellants at all. *See infra*, Sec. II.

October 24, 2013, to fall within Section 2462's five-year limitations period. Doc 303 - Pg 83, 94.

First, the latest date that any misrepresentation or omission could have been made to FINRA is the date FINRA cleared the issuer's Form 211 application. Doc 263 - Pg 2-3. Of the Mirman/Rose issuers, only three—Envoy, Changing Technologies, and First Xeris—were still pending within the statute of limitations period. *See* Doc 257-11 - Pg 5 (Envoy application cleared December 31, 2013); Doc 257-22 - Pg 15 (Changing Technologies application cleared January 28, 2014); Doc 255-12 - Pg 18 (First Xeris application cleared March 18, 2014). Of the Harrison/Daniels issuers, only two—Top to Bottom Pressure Washing and PurpleReal.com–were still pending. *See* Doc 255-63 - Pg 4 (Top to Bottom's application cleared October 29, 2013); Doc 257-82 - Pg 20 (PurpleReal.com application certified on July 31, 2014, but never cleared by FINRA). Liability could be found, if at all, only for misrepresentations or omissions related to the Form 211 applications for these five issuers. But the court, in denying Appellants' Rule 50(b) motion, relied on misrepresentations or omissions relating to issuers other than these five. *See, e.g.,* Doc 263 - Pg 27 (discussing Kids Germ Defense).

Second, the Jury Instruction list included alleged misrepresentations or omissions made to DTC. Doc 249 - Pg 38-39. Such misrepresentations or omissions occurred, if at all, when the statements were made. At trial, SEC established that statements

were made only by Spartan, Island, or Dilley in relation to three issuers: Kids Germ, On the Move, and Obscene Jeans. *See, e.g.,* Doc 257-139 (email dated Jan. 20, 2010); Doc 240 - Pg 111-13, 115-16. The court relied only on statements made regarding Kids Germ to deny Appellants' Rule 50(b) motion. *See* Doc 263 (relying on Doc 257-139 - Pg 2-3 (email dated Jan. 20, 2010)); Doc 240 - Pg 110, 111 (trial testimony discussing Doc 257-139 (email dated Jan. 13, 2010) and Kids Germ's February 2010 reverse merger); Doc 257-87 (email dated Jan. 4, 2010); Doc 254 - Pg 69-70 (expert testimony discussing Doc 257-139).[5] But all those statements were made *before* October 24, 2013, and were outside the statute of limitations period. There is no legally sufficient evidence establishing misrepresentations or omissions made to DTC, so there can be no finding of liability on that basis.

Finally, the Jury Instruction 19 list also included alleged misrepresentations and omissions regarding the designation of shares of the Mirman/Rose issuers as free trading and the bulk issuance and sales of those securities. Doc 249 - Pg 39.[6] But SEC never established any specific misrepresentations or omissions made about those issuers within Section 2462's five-year limitations period. Such a showing is foreclosed by the jury's determination that Dilley, Spartan, and Island did not sell

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[5] Doc 254 is the redacted version of Doc 230.

[6] Of the three Mirman/Rose issuers who had Form 211 applications pending within the statute of limitations period, SEC only established the bulk transfer date of one issuer, Changing Technologies on June 13 and 20 of 2014. *See* Doc 292-1.

unregistered securities. *See* Doc 250 - Pg 6 (Count 14); Doc 256 - Pg 4. Even if it were not, there is a total failure of proof that any specific misrepresentations or omissions were made *after* October 24, 2013. At best, SEC established only that some discrete statements were made by Dilley regarding the designation of shares of Global Group and E-Waste Corp., but those were *prior to* October 24, 2013. *See* Doc 255-34 (email dated Jan. 1, 2013); Doc 257-145 (email dated Jan. 2, 2013). The court erroneously relied on those time-barred statements in denying Appellants' Rule 50(b) motion. *See* Doc 263 - Pg 29-30. There was no legally sufficient evidence establishing any misrepresentations or omissions within the statute of limitations period.

This Court should vacate the district court's order denying Appellants' Rule 50 motion and remand for entry of judgment in favor of Appellants.

B. The "Continuing Violations Doctrine" Is Inapplicable to Discrete Acts Like the Misrepresentations and Omissions SEC's Theory of Liability Under Rule 10b-5 Relied Upon

In rejecting Appellants' statute of limitations arguments, the district court relied on the "continuing violations doctrine," which can toll a statute of limitations "where the violation giving rise to the claim continues to occur within the limitations period." Doc 135 - Pg 15-16 (quoting *Nat'l Parks & Conservation Ass'n, Inc. v. Tenn. Valley Auth.*, 502 F.3d 1316, 1322 (11th Cir. 2007). Quoting its earlier denial of Appellants' motion to dismiss, the district court applied this doctrine because SEC

had alleged "scheme liability extending into a period within the statute of limitations." Doc 135 - Pg 16. But the court's reasoning was erroneous.

This Court has never applied the continuing violations doctrine in the context of a securities enforcement case. Courts have been "extremely reluctant" to extend the continuing violations doctrine beyond employment discrimination matters. *Nat'l Parks Conservation Ass'n, Inc. v. Tenn. Valley Auth.*, 480 F.3d 410, 416 (6th Cir. 2007). Other courts have questioned the applicability of the doctrine in SEC enforcement actions. *See SEC v. Jones*, No. 05-cv-7044, 2006 WL 1084276, at *4 (S.D.N.Y. Apr. 25, 2006). Even if this Court were to extend the doctrine to securities enforcement matters the doctrine would be inapplicable here because misrepresentations and omissions that violate Section 10(b) and Rule 10b-5(b) of the Exchange Act are discrete acts, not part of a scheme or continuing related action. And the jury found no such scheme. The Supreme Court has "held that discrete acts that fall within the statutory time period do not make timely acts that fall outside the time period." *Nat'l R.R. Passenger Corp. v. Morgan*, 536 U.S. 101, 112, 114-115 (2002). Any claim "based on particular misrepresentations and omissions" is barred by the usual statute of limitations. *SEC v. Kovzan*, No. 11-cv-2017, 2013 WL 5651401, at *3 (D. Kan. Oct. 15, 2013).

The continuing violations doctrine is also "limited" to situations in which "a reasonably prudent plaintiff would have been unable to determine that a violation

had occurred." *Ctr. for Biological Diversity v. Hamilton*, 453 F.3d 1331, 1335 (11th Cir. 2006). But the exception does not apply to SEC, whose "very purpose is to root [fraud] out," and which "has many legal tools at hand to aid in that pursuit." *Gabelli*, 568 U.S. at 451. Just as "grafting" the so-called "discovery rule" onto Section 2462 would be "utterly repugnant to the genius of our laws' [because penalties could] 'be brought at any distance of time[,]'" so too would permitting the continuing violations doctrine to expand the statute of limitations period here. *Id.* at 452 (quoting *Adams v. Woods*, 6 U.S. (2 Cranch) 336, 342 (1805)). SEC knew full well of the alleged misconduct by 2016, when both Mirman and Rose pled guilty to securities fraud for making misstatements related to the issuers involved—years before this case was filed. *See* Doc 249 - Pg 10 (Jury Instruction 10 listing stipulations); *see also* Doc 249 - Pg 10-11 (regarding actions against Daniels, Harrison, and Fan). SEC could have known about the alleged conduct as early as 2012, when its own examiners conducted a months-long, on-site examination of Spartan and Island, where it requested and reviewed records related to at least three of the issuers: Aristocrat, First Titan, and Neutra. Doc 249 - Pg 14; Doc 224 - Pg 48 (SEC's examiners "sat in [Spartan's] conference room, and they requested reams and reams and reams of documentation … And [the] next day [they] requested more and more documents"); Doc 208 - Pg 42. Permitting SEC—one of the most powerful litigating parties in the country—to sleep on its rights by relying on the continuing violations doctrine

contravenes the purpose of Section 2462 and denies defendants their legal protections. *Gabelli*, 568 U.S. at 448. This Court should hold that Section 2462's five-year statute of limitations applies.

The remedies ordered by the district court were time-barred both when SEC filed its Complaint and when the district court denied summary judgment.

II. APPELLANTS DID NOT VIOLATE RULE 10b-5(b) AS A MATTER OF LAW AND THE COURT ERRED WHEN IT DETERMINED USING THE WRONG LEGAL STANDARD THAT THERE WAS SUFFICIENT EVIDENCE THAT THEY DID

To establish a violation of Rule 10b-5(b), SEC must prove Appellants made "(1) material misrepresentations or materially misleading omissions, (2) in connection with the purchase or sale of securities, (3) made with scienter." *SEC v. Merch. Capital, LLC*, 483 F.3d 747, 766 (11th Cir. 2007).

Under Rule 10b-5, the test for materiality is "whether a reasonable man would attach importance to the fact misrepresented or omitted in determining his course of action." *Id.* at 766 (citations omitted). By emphasizing whether an investor would find a particular piece of information important, "the materiality inquiry … filter[s] out essentially *useless information that a reasonable investor would not consider significant*, even as part of a larger 'mix' of factors to consider in making his investment decision." *SEC v. Goble*, 682 F.3d 934, 943 n.5 (11th Cir. 2012) (emphasis in original, cleaned up). "Thus, the relevant 'mix' of information is those facts an *investor* would consider when making an investment decision." *Id.*

(emphasis added). And, to be considered, the information in that mix first would have to be "available to the hypothetical reasonable investor[.]" *SEC v. Morgan Keegan & Co.*, 678 F.3d 1233, 1248 (11th Cir. 2012). It is not enough to suggest that an "investor might have considered the misrepresentation or omission important." *Ganino v. Citizens Utilities Co.*, 228 F.3d 154, 162 (2d Cir. 2000) (citations omitted). Omissions, as opposed to misrepresentations, are "actionable only to the extent that the absence of those facts would, under the circumstances, render another reported statement misleading to the reasonable investor, in the exercise of due care." *In re Galectin Therapeutics, Inc. Sec. Litig.*, 843 F.3d 1257, 1275 (11th Cir. 2016) (internal quotation marks omitted).

Misrepresentations and omissions are different in kind. Material misrepresentations require defendants to "actually make a false or misleading statement in order to be held liable under Section 10(b)." *Wright v. Ernst & Young LLP*, 152 F.3d 169, 175 (2d Cir. 1998).

> For purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker.

Janus Capital Grp., Inc. v. First Derivative Traders, 564 U.S. 135, 142 (2011).

Omissions do not violate Rule 10b-5 unless defendant has "a duty to disclose" the omitted information. *Badger v. S. Farm Bureau Life Ins. Co.*, 612 F.3d 1334,

1340-41 (11th Cir. 2010). The "mere possession of nonpublic market information" does not create a duty to disclose. *Chiarella v. U.S.*, 445 U.S. 222, 235 (1980).

SEC must also prove that any misrepresentation or omission occurred "in connection with" the purchase or sale of securities. This element is constructed flexibly to "effectuate [the statute's] remedial purpose." *SEC v. Zandford*, 535 U.S. 813, 819 (2002) (quotation omitted). But the violation and the sale of securities must, at a minimum, "coincide." *Id.* at 822. The misrepresentation or omission and a securities transaction must occur at the same time. Conduct that is not "the type of behavior meant to be forbidden by § 10(b)," does not usually meet the "in connection with" requirement. *Goble*, 682 F.3d at 946. When conduct "had no effect on the broader securities market and would not impact an investor's decision to purchase a security," it cannot be said to be made "in connection with" the purchase or sale of securities. *Id.*

The district court erred in denying Appellants' Rule 50(b) motion. First, the court failed to differentiate misrepresentations and omissions and, critically, applied the wrong legal standard to the alleged omissions. The court also failed to identify *any* duty that the Appellants had to disclose the facts that they allegedly omitted. Regarding misrepresentations, the court erred in determining that Appellants "made" misrepresentations. There was also no evidence supporting a finding that any of the

alleged statements or omissions listed in Jury Instruction 19 was material, nor that any of them occurred "in connection with" the purchase or sale of securities.

A. Eldred Did Not Make Any Actionable Misrepresentations or Omissions

Eldred was the signing principal for four Form 211 Applications—Court Document, Quality Wallbeds, Top to Bottom, and PurpleReal.com—and could be the "maker" of the statements contained only in those applications and their supporting materials like cover letters. Doc 224 - Pg 62; 249- Pg 12; Doc 257-70 (Court); Doc 257-76 (Quality); Doc 255-62 (Top to Bottom); Doc 255-63 (same), Doc 257-82 (PurpleReal.com). But he cannot be personally responsible for the statements made by the *issuers* in the application materials because, despite the court's determination to the contrary, it was the *issuers* who made the representations in those applications. *See* Doc 214 - Pg 77, 94; Doc 228 - Pg 19-20. Eldred was responsible only for asserting, truthfully, that the *issuers* had made the representations, not that they had made them truthfully. *See Janus*, 564 U.S. at 142. The material in the cover letters regarding initiation of the application was true. Doc 224 - Pg 65; Doc 257-70 - Pg 8; Doc 257-76 - Pg 8; Doc 255-62 - Pg 8; Doc 257-82 - Pg 21.

The district court appears to have premised Eldred's liability on the basis that he omitted some nonpublic information regarding Daniels, Harrison, and Fan regarding their future intentions for the issuers they were involved with. *See* Doc 249 - Pg 38-

39. The court seemed to assume as much in denying the Rule 50(b) motion. *See* Doc 263 - Pg 7, 15–16. But basing Eldred's liability finding on such omissions was erroneous because Eldred was under no duty to disclose information about nonpublic, hypothetical future events, nor did the court identify any duty to disclose such. Absent such a duty, there can be no liability for Eldred. *Badger*, 612 F.3d at 1341 ("[T]his Court has also recognized that 'a defendant's *omission* to state a material fact is proscribed only when the defendant has a duty to disclose.'" (citation omitted and emphasis added)).

Even if Eldred had a duty to disclose, these omissions were not material. Daniels, Harrison, and Fan's involvement with these issuers, and their involvement in other business deals, was disclosed to FINRA before these four applications were cleared. Doc 228 - Pg 41-42; Doc 255-62 - Pg 14-15; Doc 257-70 - Pg 23-26; Doc 257-76 - Pg 13-17; Doc 257-82 - Pg 27-30.

Nor can it be said that anything about these individuals or their involvement with the issuers was material to the investing public. This information might have changed a *regulator*'s mind about the application, but that is not enough to establish liability. *See* Doc 263 - Pg 22-23 (court discussing FINRA investigator's testimony). Such information would have had no impact on an *investor's* decision to purchase shares at some point in the future and was immaterial. *See Goble*, 682 F.3d at 944.

Finally, it cannot be said that the statements made to FINRA in nonpublic applications have been made "in connection" with the purchase or sale of securities. It is undisputed that the investing public had no access to the Form 211 applications, or any communications related thereto. *See, e.g.*, Doc 224 - Pg 37. The statements or omissions Eldred allegedly made did not "coincide" with any securities transaction because the alleged statements and omissions were related to the Form 211 application process, which occurred well before any securities transactions. The undisputed evidence is that FINRA clearance is but one step, entirely in the control of a third-party regulator, that must occur before any issuer's stock could be publicly traded. Doc 263 - Pg 2-3 (generally describing the process to go public).

There being no legally sufficient evidence to support the jury's verdict as to Eldred, this Court should vacate the district court's judgment and enter a judgment in favor of Eldred.

B. Island Did Not Make Any Actionable Misrepresentations or Omissions

Of the nineteen types of alleged misrepresentations and omissions identified in the jury instructions, only the last three, regarding statements made to DTC and those relating to the stock's registration status, could have been made by Island or Dilley. Doc 249 - Pg 38-39. But none is actionable.

First, the statements to DTC concerning shell status were true because the issuers had "nominal" assets and operations as shown by publicly available filings on SEC's

EDGAR system. Doc 238 - Pg 54; Doc 194 - Pg 20-21, 24, 26-28; Doc 257-93 (sending copy of On the Move's 8-K); Doc 257-12 (Kids Germ 10-K). The statements were made contemporaneously with the underlying information supporting the conclusion in nonpublic communications. *Ibid.* And they were not made to the investing public and were not made "in connection" with the purchase or sale of securities because they were made in relation to DTC clearance, which is but one step in the process and controlled by a third party. Doc 263 - Pg 3; *see also* Doc 257-92; Doc 257-100; Doc 257-139. The court's determination is not supported by the facts. *See* Doc 263 - Pg 28-29. True statements cannot mislead a reasonable investor. *See Morgan Keegan*, 678 F.3d at 1250. Nor could they have influenced the broader securities market. *See Goble*, 682 F.3d at 946.

The statements regarding the stock's registration status are also not actionable, and the jury's determination to the contrary, Doc 263 - Pg 29-30, was foreclosed by the jury's verdict rejecting the theory that the stock needed to be registered and stamped with restrictive legends. Doc 250 - Pg 6 (Count 14); Doc 256 - Pg 4. The court's reliance on the SEC's expert witness's testimony is improper and cannot support its finding. *See infra*, Sec. III. And to the extent Island's liability hinges on omissions, neither the SEC nor the court identified what (if any) duty Island had to disclose the allegedly omitted information. *See Badger*, 612 F.3d at 1341. SEC's

expert was not qualified to opine on such a duty, and he never did. The order must be vacated.

C. Spartan Did Not Make Any Actionable Misrepresentations or Omissions

Of the nineteen alleged misrepresentations and omissions identified in the jury instructions, sixteen relate to statements or omissions in Form 211 applications that Spartan filed with FINRA. Doc 249 - Pg 38-39.

Neither Spartan, nor Eldred, nor Dilley were "makers" of any statement to FINRA. As the evidence showed, all the statements provided to FINRA were from the issuers themselves. Doc 257-22 - Pg 8 ("The Issuer described … ."); *id.* ("The issuer has represented … ."). The evidence established that *the issuers* had made these statements, and that they were backed up by written certifications from the issuers' officers attesting to the accuracy of each of these statements, and attesting that the issuers had not omitted any relevant or material information. Doc 214 - Pg 77, 94; Doc 224 - Pg 34-35; Doc 257-23. Spartan cannot be held liable under Rule 10b-5(b) because it had no "control" over the *issuers*' statements, whether false or not, and "[o]ne who prepares or publishes a statement on behalf of another is not its maker." *See Janus*, 564 U.S. at 142. Accurately repeating or forwarding an issuer's statements to FINRA is not sufficient to show that Spartan "made" statements in violation of Rule 10b-5(b).

Even if Spartan could be deemed to have "made" actionable statements or omissions, none of the statements or omissions listed in Jury Instruction 19 was material. It is undisputed that the listed statements and omissions were made in the context of the Form 211 application process, particularly the cover letters, and that those materials were not visible to investors or anyone else other than FINRA. Doc 226 - Pg 64; Doc 224 - Pg 37. The materiality test asks whether a reasonable *investor* would consider the misrepresentation or omission significant. Here, at best, SEC and the district court found that *regulators* may have considered the cover letter information to be important in determining whether to clear an issuer, but that is not enough to support a Rule 10b-5(b) violation. Doc 226 - Pg 52-53, 71. The court makes a logical leap to assume that nonpublic information that is important to regulators is also significant to investors, Doc 263 - Pg 22-23, but that is not so. *Goble*, 682 F.3d at 944 (finding a "scheme to defraud FINRA" would not affect an investor's underlying investment decision). The undisputed evidence shows that when FINRA examiners questioned an issuer about Mirman's role, disclosures about Mirman had no material impact on FINRA's decision to clear the issuer. Doc 226 - Pg 52, 66. And if disclosure of Mirman's role had no material impact on FINRA, how could it be material to an *investor*'s decision? Likewise, the omissions relating to Daniels, Harrison, and Fan, who were never convicted of any wrongdoing, are

even less material as discussed above. Spartan, like Eldred, was not determined to have any duty to disclose information about nonpublic, hypothetical future events.

Finally, the Form 211 applications and related communications cannot support liability under Rule 10b-5(b) because they would not have an impact on an investor's decisions to purchase any security. Section 10(b) was not targeted at misleading statements *to regulators* like FINRA, so it does not encompass alleged misstatements or omissions directed at FINRA. *See Goble*, 682 F.3d at 946. And, as discussed above, these alleged statements and omissions, made before FINRA cleared the relevant issuers' applications did not "coincide" with any securities transactions. The district court's apparent view that the "in connection with" requirement encompasses *any* step in the process of going public cannot be squared with the fact that the violative action must "coincide with" a securities transaction. *See Zandford*, 535 U.S. at 822.

The court erred when it found that there was legally sufficient evidence to support the jury's verdict as to Spartan. This Court should vacate the district court's judgment and enter a judgment in favor of Spartan.

D. Dilley Did Not Make Any Actionable Misrepresentations or Omissions

The verdict against Dilley cannot be supported for the same reasons discussed above. Dilley was responsible only for the Form 211 applications that he signed but none of them was actionable as a matter of law. *See supra,* Sec. II.C. And with

respect to his role at Island, the statements concerning shell status were not false or misleading, much less materially so, and the statements concerning past transfers were also true, and could not have retroactively influenced investment decisions. *See supra,* Sec. II.B.

The court erred when it found that there was legally sufficient evidence to support the jury's verdict as to Dilley. This Court should vacate the district court's judgment and enter a judgment in favor of Dilley.

III. THE COURT ABUSED ITS DISCRETION WHEN IT ADMITTED UNRELIABLE EXPERT EVIDENCE OUTSIDE THE WITNESS'S AREA OF EXPERTISE

The district court also failed in its gatekeeping duty, causing unqualified and unreliable evidence to go before the jury. Under Federal Rule of Evidence 702, courts may consider expert testimony if

> (a) the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue; (b) the testimony is based on sufficient facts or data; (c) the testimony is the product of reliable principles and methods; and (d) the expert has reliably applied the principles and methods to the facts of the case.

Fed. R. Evid. 702. The court serves a "gatekeeping duty to determine whether the expert testimony 'is not only relevant, but reliable.'" *Bostick v. State Farm Mut. Auto. Ins. Co.*, 321 F.R.D. 414, 416 (M.D. Fla. 2017) (quoting *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 589 (1993)); *see Daubert*, 509 U.S. at 597 (expert's testimony must be "relevant to the task at hand"). The gatekeeping

function "ensure[s] that speculative, unreliable expert testimony does not reach the jury' under the mantle of reliability that accompanies the appellation of 'expert testimony." *Rink*, 400 F.3d at 1291 (quoting *McCorvey v. Baxter Healthcare Corp.*, 298 F.3d 1253, 1256 (11th Cir. 2002)).

An expert's "qualifications, reliability, and helpfulness" must not be conflated by the district court. *U.S. v. Frazier*, 387 F.3d 1244, 1260 (11th Cir. 2004). These considerations must be satisfied by a preponderance of the evidence, and the party offering the expert bears the burden of persuasion. *Rink*, 400 F.3d at 1292; *Frazier*, 387 F.3d at 1259-60.

Being an expert in general does not make one an expert for *everything*. This is because an expert's qualifications to offer opinions may be based on a combination of his "knowledge, skill, experience, training, or education[,]" but he "must be *at least minimally qualified* in his field." *Hendrix v. Evenflo Co.*, 255 F.R.D. 568, 578 (N.D. Fla. 2009) (quoting Fed. R. Evid. 702) (emphasis added), *aff'd sub nom. Hendrix ex rel. G.P. v. Evenflo Co.*, 609 F.3d 1183 (11th Cir. 2010). "Assuming an expert is qualified to testify, the expert may testify only about matters within the scope of his or her expertise." *Cordoves v. Miami-Dade Cty.*, 104 F. Supp. 3d 1350, 1358 (S.D. Fla. 2015) (citing *City of Tuscaloosa v. Harcors Chemicals, Inc.*, 158 F.3d 548, 562 (11th Cir. 1998)). Time in an industry *may* give a witness a generalized understanding, but that understanding does "not endow[] him with a sufficient body

of specialized knowledge to assist the trier of fact in understanding the evidence or issues of this case relating to the precise contours of [a regulated-entity's] duties … or its performance of those duties." *Pleasant Valley Biofuels, LLC v. Sanchez-Medina*, No. 13-23046-CIV, 2014 WL 2855062, at *4 (S.D. Fla. June 23, 2014). The opinions and testimony of experts with no experience, or experience that is limited or dated in the field they are purporting to testify about, should be excluded. *See Payne v. C.R. Bard, Inc.*, 606 F. App'x 940, 943 (11th Cir. 2015) (unpublished) (upholding exclusion of "limited and dated" experience because there was no sufficiently established "nexus" between the experience and the opinions offered). "[E]xpert testimony regarding matters outside of the witness's expertise is inadmissible, even if the expert is qualified to testify about other matters." *Cordoves*, 104 F. Supp. 3d at 1358.

An expert's lack of experience creates a reliability problem because experts "must explain *how* [their] experience leads to the conclusion reached, why that experience is a sufficient basis for the opinion, and how that experience is reliably applied to the facts." *Frazier*, 387 F.3d at 1261. Where, as here, there is a "clear 'overlap' between [the] expert's qualifications and the reliability of his [testimony,]" the reliability analysis cannot be conducted absent consideration of the expert's qualifications. *Hendrix*, 255 F.R.D. at 578.

The Appellants objected to the admission of testimony by SEC's proffered expert witness, James Cangiano, regarding transfer agents and DTC eligibility because he had *no experience* in the transfer agent industry. None. The court nonetheless permitted Cangiano to testify "on the role of transfer agents in the microcap market and how entities generally use transfer agents concerning stocks … [and the] standards, customs and practices [of transfer agents] in the microcap over-the-counter market." Doc 254 - Pg 19; Doc 228 - Pg 117-120. Cangiano had no basis for his testimony, as evidenced during his *voir dire* examination. During that examination, Cangiano admitted he never worked for a transfer agent. Doc 228 - Pg 108-109. He also testified that neither he nor either of the self-regulatory organizations he worked for, FINRA and its predecessor National Association of Securities Dealers, ever regulated transfer agents. Doc 228 - Pg 109. Nothing in the record establishes even minimal qualifications—via education or experience—that would permit Cangiano to opine on matters related to transfer agents and DTC eligibility, so the court's determination to the contrary was manifestly erroneous. Cangiano not only had no experience with transfer agents, but he also had never written about them and certainly not in any peer-reviewed forum. He was a classic "expert on everything," and his wide-ranging and unfettered testimony was prejudicial and unreliable and should not have gone to the jury. *See Schaffer v. Merrill Lynch Pierce Fenner & Smith LLC*, 779 F.Supp.2d 1085, 1091 (N.D. Cal.

2011) (a degree does not make one an "expert on everything" in the field). Cangiano simply parroted SEC's views and provided no genuine expertise on these issues that any court could deem reliable under the *Daubert* standard. All his testimony in connection with *Island* should be excluded. Outside of his testimony that the issuer's stock was restricted, nothing else in the record supports a judgment that Spartan, Island, or Dilley made material misrepresentations or omissions regarding the registration status of the shares. *See* Doc 263 - Pg 26, 27, 28-29 (relying on Cangiano's testimony at Doc 254 - Pg 44-45, 45-46, 69-70 and Doc 234 - Pg 28-29, 42). And the jury found no liability on the Count that required a finding the stock was restricted. Doc 250 - Pg 6 (Count 14); Doc 256 - Pg 4.

The district court not only abused its discretion by allowing this unqualified and unreliable testimony to go before the jury, but it also pointed to the same unreliable testimony in denying Appellants' Rule 50(b) motion. *See, e.g.*, Doc 263 - Pg 26, 27, 28-29.

IV. APPELLANTS WERE DENIED THEIR CONSTITUTIONAL RIGHT TO A JURY DETERMINATION OF THE FACTS NECESSARY TO ESTABLISH THE CIVIL PENALTY

The right to a trial by jury is, and remains, a "fundamental" component of our justice system. *Reid v. Covert*, 354 U.S. 1, 9-10 (1957). "[A]ny seeming curtailment of the right to a jury trial should be scrutinized with the utmost care." *Dimick v. Schiedt*, 293 U.S. 474, 486 (1935). The Framers "considered the right to trial by jury

'the heart and lungs, the mainspring and the center wheel' of our liberties, without which 'the body must die; the watch must run down; the government must become arbitrary.'" *U.S. v. Haymond*, 139 S. Ct. 2369, 2375 (2019) (quoting Letter from Clarendon to W. Pym (Jan. 27, 1766), in 1 Papers of John Adams 169 (R. Taylor ed. 1977)). This right provides "an important bulwark against tyranny and corruption, a safeguard too precious to be left to the whim of the sovereign, or, it might be added, to that of the judiciary." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 343 (1979) (Rehnquist, J., dissenting). As Blackstone said, "the most transcendent privilege which any subject can enjoy, or wish for [is] that he cannot be affected either in his property, his liberty, or his person, but by the unanimous consent of twelve of his neighbors and equals." *Reid*, 354 U.S. 9-10 (quoting 3 William Blackstone, *Commentaries* 379).

A. The Seventh Amendment Right to a Jury Trial Attaches to Any Factual Determinations that Impact Appellants' Liability

The Seventh Amendment guarantees the right to trial by jury in "Suits at common law." U.S. Const. amend. VII. Where, as here, a plaintiff's claim is created by statute that is silent with respect to jury trial rights, courts determine whether the statutory action "is more similar to cases that were tried in courts of law than to suits tried in courts of equity or admiralty" by "exam[ining] both the nature of the action and of the remedy sought." *Tull v. U.S.*, 481 U.S. 412, 417 (1987) (finding a constitutional

right to a jury trial to determine liability on legal claims in an action to enforce civil penalties under the Clean Water Act).

Under *Tull*'s two-part analysis, courts first "compare the statutory action to 18th-century actions brought in the courts of England prior to the merger of the courts of law and equity," and then, "examine the remedy sought and determine whether it is legal or equitable in nature." *Id.* at 417-18. The second inquiry into the nature of the remedy sought "is more important than the first." *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 42 (1989). The Seventh Amendment right applies even when a proceeding "involve[s] a mix of legal and equitable claims[.]" *Jarkesy v. SEC*, 34 F.4th 446, 454 (5th Cir. 2022). "[T]he facts relevant to the legal claims should be adjudicated by a jury, even if those facts relate to equitable claims too." *Id.* (citing *Ross v. Bernhard*, 396 U.S. 531, 537-38 (1970)).

The Supreme Court has held that a government enforcement action is "clearly analogous to the 18th-century action in debt," which would have been tried in a court of law. *Tull*, 481 U.S. at 420. Actions for securities fraud also fall within the Seventh Amendment's ambit. As the Fifth Circuit recently explained, "[s]ecurities fraud actions are not new actions unknown to the common law." *Jarkesy*, 34 F.4th at 455. "Common-law courts have heard fraud actions for centuries, even actions brought by the government for fines." *Id.* And "the Supreme Court has often looked to common-law principles to interpret fraud and misrepresentation under securities

statutes." *Id.* (citations omitted). "[F]raud actions under the securities statutes echo actions that historically have been available under the common law[,]" *id.*, such that the Seventh Amendment applies.

SEC enforcement actions that seek civil penalties and/or allege fraud fall within the Seventh Amendment's protection. *See id.* at 457 (right to jury trial to adjudicate "the facts underlying any potential fraud liabilities that justifies penalties"); *SEC v. Jensen*, 835 F.3d 1100, 1106 (9th Cir. 2016) (constitutional right to a jury trial in SEC enforcement action); *SEC v. Smyth*, 420 F.3d 1225, 1233 n.14 (11th Cir. 2005) (noting Seventh Amendment right to a trial by jury in SEC actions); *SEC v. Lipson*, 278 F.3d 656, 662 (7th Cir. 2002) (jury trial permitted in case seeking legal and equitable relief).

B. The Exchange Act's Three-Tier Penalty Scheme Requires Factual Determinations to Establish Liability for Each Penalty Tier

When the Seventh Amendment applies to the imposition of penalties, a jury is not necessarily required to determine the measure of such damages. *Tull*, 481 U.S. at 426. Congress may "fix the [amount] of civil penalties" and may "delegate that determination to trial judges" consistent with the Seventh Amendment. *Id.* at 427. This is because the jury determination of facts is not a "necessary" component of a fixed damage assessment. *Id.* at 426. But under the Exchange Act's three-tier penalty scheme, courts may impose civil penalties only "upon a proper showing" by SEC. 15 U.S.C. § 78u(d)(3)(A)(i). The penalty amount "is determined by the court in light

of the facts and circumstances." 15 U.S.C. § 78u(d)(3)(B)(i). The factfinder must make at least two inquiries. The first is how many violations occurred. *Id.* (penalties may be assessed "[f]or each violation"). The second is whether "the gross amount of pecuniary gain to [a] defendant as a result of the violation" exceeded the base penalty set by Exchange Act Section 21(d). Then, any upward departure from the base penalty to a tier two or tier three penalty requires additional findings. Tier two penalties require an additional determination that the violation "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement." 15 U.S.C. § 78u(d)(3)(B)(ii). Tier three penalties require the same factual determinations necessary to establish tier two penalties *plus* a determination that the defendant's conduct "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons." 15 U.S.C. § 78u(d)(3)(B)(iii); Matthew T. Martens & Troy A. Paredes, *The Scope of the Jury Trial Right in SEC Enforcement Actions*, 71 N.Y.U. ANN. SURV. AM. L. 147, 176-77 (2015) (text of penalty statute "sound[s] in both reliance and causation" and requires proof of a "causal connection," which are additional factual determinations that must be made by the factfinder).

When the statutory assessment of penalties requires factual determinations that can increase the penalty tier (and the penalty amount), those determinations *must* be made by a jury. *See Apprendi v. New Jersey*, 530 U.S. 466, 490 (2000) (in the context

of the Sixth Amendment "any fact that increases the penalty for a crime beyond the prescribed statutory maximum must be submitted to a jury"); *see also Feltner v. Columbia Pictures Television, Inc.*, 523 U.S. 340, 353 (1998) ("The right to a jury trial includes the right to have a jury determine the *amount* of statutory damages, if any, awarded to the copyright owner."). The Seventh Amendment's "aim is not to preserve mere matters of form and procedure, but substance of right. This requires that questions of fact in common-law actions shall be settled by a jury, and that the court shall not assume, directly or indirectly, to take from the jury or to itself such prerogative." *Walker v. New Mexico & S. P. R. Co.*, 165 U.S. 593, 596 (1897).

Appellants were entitled to a jury determination of the facts necessary to establish liability for any increase in the civil penalty tier beyond the base tier-one penalty of $7,500 (Eldred and Dilley) and $80,000 (Spartan and Island) (as adjusted for inflation as of the time of the alleged violations). The court erred and deprived them of that constitutionally protected right when it denied Appellants' motion, Doc 159, and ordered tier two civil penalties of $150,000 each for Eldred and Dilley, and $250,000 each for Spartan and Island, Doc 297 - Pg 37-38. The number of separate violations SEC claimed and the district court found during the remedies phase makes this error clear. The court erroneously stated that Appellants did not "dispute" that SEC sought assessment of penalties "for three 'violations' against Dilley, two violations against Eldred, and one violation against the corporate Defendants." Doc

297 - Pg 37. Appellants consistently asserted that *no* violations occurred and were under no obligation to squabble with SEC about how thinly the court should slice up and count violations. *Cf.* Doc 303 - Pg 95-96 (SEC arguing that it could have requested more violations based on the alleged "19 separate misreps" but *chose* to count only one violation for each issuer). The law does not allow SEC to argue like scholastics about how many violations can dance on the head of an alleged pin. Such arbitrary determinations about the number of violations that may have occurred is untethered from the jury's verdict and highlights why the jury must make these factual determinations.

The judgment also runs headlong into the rule of lenity, which "requires courts to construe ambiguous criminal statutes narrowly in favor of the accused." *U.S. v. Wright*, 607 F.3d 708, 716 (11th Cir. 2010) (Pryor, J., concurring); *see id.* at 716-17 (discussing how the rule of lenity serves the constitutional principles of due process and separation of powers). Because the fraud provisions at issue here can be prosecuted criminally, the rule of lenity attaches to this action. *See Kasten v. Saint-Gobain Performance Plastics Corp.*, 563 U.S. 1, 16 (2011) ("[W]e have said that the rule of lenity can apply when a statute with criminal sanctions is applied in a noncriminal context."). The number of violations, if ambiguous, should be subject to lenity, not the whims of SEC or the court.

V. THE DISTRICT COURT ABUSED ITS DISCRETION WHEN IT ORDERED REMEDIES BASED ON CONDUCT THAT THE JURY FOUND DID NOT VIOLATE THE LAW

Courts have found that due process considerations preclude the court from ordering remedies based upon conduct that the jury found non-culpable. *Cf. People v. Beck*, 504 Mich. 605, 629 (2019) ("due process bars sentencing courts from" relying on acquitted conduct in sentencing); *State v. Marley*, 321 N.C. 415, 425 (1988) ("due process and fundamental fairness precluded the trial court" from increasing sentence based on acquitted conduct). In the criminal context, federal courts may consider acquitted conduct "so long as that conduct has been proved by a preponderance of the evidence." *U.S. v. Watts*, 519 U.S. 148, 157 (1997); *U.S. v. Scott*, 798 F. App'x 391, 394 (11th Cir. 2019).

But the same is not true in the civil context, where the jury's determinations are already made under a preponderance of the evidence standard. *See* Doc 249 at 16 (Jury Instruction 12). When the jury found that Appellants did not aid or abet violations of the securities laws and did not participate in schemes to defraud, the district court was not free to consider that unproven conduct when imposing penalties. *See* Doc 250; Doc 256. To hold otherwise would permit the district court to penalize Appellants and order remedies based on conduct SEC could not prove and the jury found did not violate the law, all in violation of their due process rights.

But the district court did just that and abused its discretion by doing so. In determining the disgorgement amount as to Island and the civil penalty amounts as to all Appellants, the court impermissibly considered the aiding and abetting and scheme liability counts that the jury rejected. Regarding the civil penalty determinations, the court "considered Defendants' roles in the overall scheme" and "the fact that [Form 211 application] information was originally provided by third parties (at the behest of Mirman and Rose)." Doc 297 - Pg 37. And, in ordering Island to pay disgorgement, the court determined that "Island collected fees from 14 identified issuers as part of scheme[,]" Doc 297 - Pg 19, and that Island was "a key player in a scheme to put dubious equities on the market[,]" Doc 297 - Pg 25. Relying on theories of liability that the jury rejected to fashion remedies is impermissible and violates Appellants' due process rights.

On this ground alone the Court should reverse and remand to the district court with instructions to recalculate the civil penalties and disgorgement based solely on what the jury indisputably found.

VI. THE COURT ERRED WHEN IT ORDERED ISLAND TO PAY DISGORGEMENT

The SEC's request for disgorgement was a thinly veiled attempt to extract penalties for the aiding and abetting and scheme liability counts the jury explicitly rejected. The district court committed multiple legal errors when it ordered Island to pay disgorgement based on its non-existent role in a scheme the jury rejected. Doc

297 - Pg 15, 25. As a matter of law, disgorgement that is paid to the Treasury is not "for the benefit of investors" as required by the Exchange Act. There is no causal connection between the alleged ill-gotten gains and Island's conduct. SEC failed to establish a "reasonable approximation" of the alleged unjust gain, and the court's application of the burden-shifting framework under *SEC v. Calvo*, 378 F.3d 1211, 1217 (11th Cir. 2004), was erroneous.

A. Disgorgement Paid into the Treasury Is Not 'For the Benefit of Investors' as Required by the Exchange Act

1. Principles of Statutory Construction Require 15 U.S.C. § 78u(d)(5) and § 78u(d)(7) to Be Read Together

As the parties and the district court recognized, it remains unsettled whether SEC's practice of depositing disgorged funds into the Treasury is permissible where it is infeasible to distribute the funds to investors. *Liu v. SEC*, 140 S. Ct. 1936, 1948 (2020). This is because Exchange Act Section 21(d) authorizes equitable relief only when "appropriate or necessary for the benefit of investors." 15 U.S.C. § 78u(d)(5). "The Eleventh Circuit has yet to issue any guidance on this topic." Doc 297 - Pg 24. That question is squarely presented here. But the question was further complicated by post-*Liu* congressional amendments to Section 78u, which, among other things, codified disgorgement as a remedy available in SEC enforcement cases. *See* 15

U.S.C. § 78u(d)(7).[7] The district court determined that disgorgement under Section 78u(d)(7) is a remedy that sounds in equity, yet held "that it may order disgorgement and direct that disgorged funds be sent to the Treasury under Section 78u(d)(7)."[8] *See* Doc 297 - Pg 23, 25.

That holding is in substantial tension with a recent Supreme Court holding that SEC disgorgement awards constitute permissible equitable relief under Section 78u(d)(5) only where they "do[] not exceed a wrongdoer's net profits and [are] awarded for victims." *Liu,* 140 S. Ct. at 1940. As the *Liu* Court noted, Section 78u(d)(5) "*restricts* equitable relief to that which 'may be appropriate or necessary for the benefit of investors.'" *Id.* at 1947 (emphasis added). This investor-benefit restriction should also apply to disgorgement ordered under Section 78u(d)(7).

Despite the district court's decision to the contrary, Doc 297 - Pg 21, 23, a statute's subsections should not be read in isolation. *In re Wild*, 994 F.3d 1244, 1272

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[7] The amendments comprised two pages tucked belatedly into a 1,480-page defense authorization bill passed on New Year's day in 2021. *See generally* 2021 NDAA, Pub. L. No. 116-283, 134 Stat. 3388 (2021).

[8] While SEC's remedies motion was pending, the Fifth Circuit determined that "[a]s amended, Section 78u(d) authorizes disgorgement in a legal—not equitable—sense." *SEC v. Hallam*, 42 F.4th 316, 338 (5th Cir. 2022). But that determination leads to distinct issues in SEC enforcement actions. For example, if Section 78u(d) created legal disgorgement, as opposed to equitable disgorgement, then SEC is not entitled to collect prejudgment interest absent congressional authority to do so because SEC is a "creature[] of statute" and "possess[es] only the authority that Congress has provided." *NFIB v. OSHA*, 142 S. Ct. 661, 665 (2022).

(11th Cir. 2021) (Pryor, J., concurring). This Court has long recognized that proper statutory interpretation considers the context of the entire statute as assisted by the canons of statutory construction. *Edison v. Douberly*, 604 F.3d 1307, 1310 (11th Cir. 2010). Statutory terms are not read in "isolation" but rather statutory context. *Id.* Statutes should be read as a whole. *See* Antonin Scalia & Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts* § 24, at 167 (West 2012) (explaining that a "judicial interpreter" is called on "to consider the entire text, in view of its structure and of the physical and logical relation of its many parts"). "Because statutory construction is a 'holistic endeavor,'" courts must interpret statutory provisions, like Section 78u(d)(7), in the context of the entire statute. *Black Warrior Riverkeeper, Inc. v. Black Warrior Mins., Inc.*, 734 F.3d 1297, 1302 (11th Cir. 2013). "The Supreme Court has instructed that the 'fundamental canon of statutory construction [is] that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme' and that a court should 'fit, if possible, all parts into a harmonious whole.'" *Id.* (quoting *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 132-33 (2000)). Relatedly, "a court should also avoid interpreting a provision in a way that would render other provisions of the statute superfluous." *Black Warrior*, 734 F.3d at 1303; *see also* Scalia & Garner, *supra*, § 26, 174 (the "surplusage canon" holds that "[i]f possible, every word and every provision is to be given effect (*verba cum effectu sunt accipienda*). None should be

ignored. None should needlessly be given an interpretation that is to duplicate another provision or to have no consequence.")).

Legislative history reinforces this view. That history shows that the purpose of adding Section 78u(d)(7) was to make explicit that which had previously been only implicit—*i.e.*, that disgorgement is an available equitable remedy in SEC enforcement actions under Section 78u(d)(5). *Cf.* 165 Cong. Rec. H8931 (daily ed. Nov. 18, 2019) (statement of Rep. McAdams).

To reach a harmonious whole reading of Section 78u(d)(7), that section must be read in context with the statute, specifically Section 78u(d)(5). Disgorgement has historically been considered an equitable remedy. *See SEC v. Levin*, 849 F.3d 995, 1006 (11th Cir. 2017). And, under Section 78u(d)(5), equitable remedies must be "appropriate or necessary" and "for the benefit of investors." 15 U.S.C. § 78u(d)(5). Disgorgement sought under Section 78u(d)(7) must also be "appropriate or necessary" and "for the benefit of investors" because it is an equitable remedy within the meaning of Section 78u(d)(5). The court's reading of the statute renders the investor-benefit requirement for equitable relief superfluous by permitting disgorged monies to be paid to the *Treasury* instead of harmed investors notwithstanding the

Supreme Court's contrary holding in *Liu*.[9]

2. Depositing Disgorged Funds into the Treasury Is Incompatible with Traditional Notions of Equity

The district court's disgorgement award contravenes traditional equitable principles because the award does not benefit investors. "Equity never, under any circumstances, lends its aid to enforce a forfeiture or penalty, or anything in the nature of either." *Marshall v. City of Vicksburg*, 82 U.S. 146, 149 (1872). Yet just as the Supreme Court recognized in *Kokesh*, the district court's disgorgement order "bears all the hallmarks of a penalty: It is imposed as a consequence of violating public law and it is intended to deter, not to compensate." 581 U.S. at 465. Stated another way, it "'go[es] beyond compensation, [is] intended to punish, and label[s] [Appellants] wrongdoers' as a consequence of violating public laws." *Id.* at 467 (quoting *Gabelli*, 568 U.S. at 451-452).

Disgorgement was ordered as a consequence of the alleged violation of the Exchange Act. It was also intended to deter future violations of the securities laws. SEC admitted as much at the evidentiary hearing, arguing that it was seeking disgorgement for its "deterrent effect" and that enforcement of the securities laws would be undermined if it was not awarded. Doc 303 - Pg 86. Because the disgorged

[9] The parties stipulated that a distribution to investors was "infeasible" but did not agree why that was so. Doc 287 - Pg 1. Appellants maintain no investors were harmed.

funds are to be paid to the Treasury rather than to harmed investors, the disgorgement order is not compensatory and does not benefit any affected investors. *See Kokesh*, 581 U.S. at 462. Still, the district court determined it would be more "equitable" to divert the disgorged funds to the Treasury than to let the funds remain with Island, who the court improperly described as a "key player in a scheme"—one that the jury rejected. Doc 297 - Pg 25. It is hard to see how the court's determination was not meant to penalize Island.

Another factual oddity renders payment of the disgorged funds into the Treasury improper here. All funds paid to Island came from the relevant issuers of stock, who were proven at trial to be fraudsters. Doc 194 - Pg 39, 43. But equity requires clean hands, and this is particularly true in cases affecting the public interest. *Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 815-16 (1945) (dismissing patent case because of lack of clean hands). The application of unclean hands in equity is within the sound discretion of the trial court. *Shatel Corp. v. Mao Ta Lumber & Yacht Co.*, 697 F.2d 1352, 1355 (11th Cir. 1983). At trial, SEC put on witness after issuer witness who admitted to lying to Appellants multiple times over a long period. *See*, *e.g.*, Doc 186 - Pg 94. SEC then sought recovery of these fraudsters' funds under the guise of disgorgement and the court granted that request. On any balance of equities, Appellants are less culpable than everyone who paid any money to Island. The jury did not find *any* defendant acted in concert with these

fraudulent issuers—and accordingly it rejected the scheme liability counts—and such a view would not accord with any facts adduced at trial. Hence, it is not equitable to require parties who had no knowledge of a fraud to "disgorge" funds they received from the deceivers. That the district court ordered otherwise was an abuse of discretion.

B. Disgorgement Is Not Appropriate Because There Is No Causal Connection Between the Alleged Ill-Gotten Gains and Island's Conduct

A "court may exercise its equitable power only over property *causally* related to the wrongdoing." *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989) (emphasis added). There must be some nexus between the conduct for which liability is found and the monies ordered to be disgorged. SEC sought disgorgement of fees paid to Island by 14 Mirman/Rose issuers whom SEC alleged were part of a scheme. *See* Doc 297 - Pg 19. SEC introduced various Island statements for these issuers and sought a disgorgement amount equal to all the fees collected in those statements through the issuers' bulk transfer dates. Doc 297 - Pg 27-28. But the jury found no scheme when it rejected those theories at trial. *See* Doc 250; Doc 256. There was no nexus between the violation found by the jury and the fees Island received and was ordered to disgorge. As evidenced by Jury Instruction 19, Island's liability could only have been premised on misstatements or omissions regarding the registration status of the issuer's shares. But the jury also rejected that theory when it determined that Island did not sell unregistered securities. Doc 250 - Pg 6 (Count 14); Doc 256

- Pg 4. The court was therefore without power to order disgorgement of the fees paid to Island because there was no proof that those fees were causally related to the Rule 10b-5(b) violation found by the jury.

C. SEC Failed to Establish a 'Reasonable Approximation' of the Alleged Ill-Gotten Gains and the Court Erroneously Shifted the Burden to Appellants to Disprove That Calculation

When seeking disgorgement, SEC must "produc[e] a reasonable approximation of a defendant's ill-gotten gains." *Calvo*, 378 F.3d at 1217. But that does not mean SEC is free to put together *any* calculation, claim it is reasonable, and then shift the burden to Island. *See FTC v. Vylah Tec LLC*, 378 F. Supp. 3d 1134, 1141 (M.D. Fla. 2019) (finding disgorgement calculation unreasonable when government failed to use the best records available, the calculation was a moving target, and non-party funds were included). The initial inquiry is whether SEC's calculation is reasonable based on the facts and circumstances underlying the disgorgement request and how it is calculated. SEC's disgorgement calculation was rife with errors. These included unsubstantiated fees and payments, fees paid after the bulk transfer date, and a failure to account for legitimate business expenses as the Supreme Court required in *Liu*. *See* Doc 297 - Pg 30-31 (and accompanying notes). Because of these errors, SEC's disgorgement calculation was unreasonable, and the court abused its discretion when it shifted the burden to Appellants to rebut that calculation.

The district court compounded its error by applying a presumption against Island purportedly to account for the risk of uncertainty in calculating the proper disgorgement amount. But any presumption against Island based on uncertainty should apply only if, and only after, the burden of proof has shifted to it, not before. *See FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 69 (2d Cir. 2006) ("This presumption against the wrongdoer should not have been invoked without first establishing a reasonable approximation of unjust gain because this presumption applies only in the second stage of the burden-shifting framework.").

The court committed legal error when it misapplied the burden-shifting framework. *See Calvo*, 378 F.3d at 1217. As a matter of context, the burden-shifting framework was developed in response to the "near-impossible task" of "separating legal from illegal profits" in the insider training context due to the expensive, imperfect, imprecise, and speculative nature of econometric modelling necessary to determine the amount of ill-gotten trading gains. *See First City Fin. Corp.*, 890 F.2d at 1231. Because of that, the D.C. Circuit was reluctant to impose "a strict burden" on the government and instead determined that "the risk of uncertainty should fall on the wrongdoer whose illegal conduct created that uncertainty." *Id.* 1232. In insider trading cases the illegal conduct and the cause of the uncertainty are merged. The risk of uncertainty should fall on the defendant only when the defendant's "illegal conduct [is what] created the uncertainty." *Verity Int'l, Ltd.*, 443 F.3d at 69.

But Island's conduct here created no records uncertainty, nor did SEC allege or the court find that it did. The court erred in shifting the burden to Island and ordering disgorgement, and reversal is warranted.

VII. THE DISTRICT COURT ABUSED ITS DISCRETION BY FAILING TO CONSIDER DILLEY'S, SPARTAN'S, AND ISLAND'S ABILITY TO PAY THE PENALTIES ORDERED

The court did not take into account the financial circumstances of any Appellant in determining the civil penalties ordered.

Courts weigh multiple discretionary factors to determine whether a civil penalty is warranted and, if so, the appropriate penalty amount. *See, e.g.*, *SEC v. Sargent*, 329 F.3d 34, 41-42 (1st Cir. 2003); *SEC v. Huff*, 758 F. Supp. 2d 1288, 1364 (S.D. Fla. 2010). A defendant's ability to pay is "at most … one factor to be considered in imposing a penalty." *Warren*, 534 F.3d at 1370. A court abuses its discretion "when a relevant factor that should have been given significant weight is not considered." *Ameritas Variable Life Ins. Co.*, 411 F.3d at 1330.

While this Court has previously stated that "ability to pay does not merit significant weight in comparison to the other equities[,]" *Warren*, 534 F.3d at 1370, that view cannot be squared with the Eighth Amendment's prohibition of "excessive fines" and the clause's meaning dating back to before the founding. *Timbs v. Indiana*, 139 S. Ct. 682, 695 (2019) (Thomas, J., concurring). Tracing its roots to the Magna Charta, the Excessive Fines Clause incorporates the principle of *salvo*

contenemento suo, which is translated as "'saving his contenement,' or livelihood." Nicholas M. McLean, *Livelihood, Ability to Pay, and the Original Meaning of the Excessive Fines Clause*, 40 HASTINGS CONST. L.Q. 833, 835 (2013). The *salvo contenemento suo* principle provides "an additional limiting principle linking the penalty imposed to the offender's economic status and circumstances." *Id.* at 836. "[A]t common law, the inquiry into excessiveness hinged on an analysis of an individual defendant with individual characteristics and an individual crime." *Yates v. Pinellas Hematology & Oncology, P.A.*, 21 F.4th 1288, 1334 (11th Cir. 2021) (Tjoflat, J., concurring in part and dissenting in part); *see supra*, Sec. IV.A. (discussing common law nature of SEC fraud and penalty actions). As such, ability to pay is a factor that should be given significant weight, as not doing so violates the Excessive Fines Clause of the Eighth Amendment. Failing to consider ability to pay constitutes abuse of discretion. *See Ameritas Variable Life Ins. Co.*, 411 F.3d at 1330.

Neither Spartan nor Island has the assets, resources, nor future business plans that would enable them to pay the court-ordered civil penalties. Doc 273-1 - Pg 1. Spartan and Island are defunct companies maintained only for administrative purposes. Doc 299- Pg 2, 3; Doc 302 - Pg 60-61, 64-65

Dilley is also unable to pay the civil penalty ordered against him. Doc 298 - Pg 3. Around the time SEC filed this action, Dilley suffered "an economic perfect

storm" consisting of personal, medical, and family financial obligations. Doc 303 - Pg 41; Doc 303 - Pg 20, 49. Dilley still has a negative net worth and no significant assets. *Cf.* Doc 273-2 - Pg 2.

While the court stated that ability to pay is a factor, it failed to consider it. *Compare* Doc 297 - Pg 34 (listing factors) *with* Doc 297 - Pg 37 (discussing culpability and mentioning generalized consideration of "pertinent facts and circumstances"). This failure is manifest by the court's imposition of the same penalty amount against Dilley as it imposed against Eldred, who did not claim inability to pay. Doc 297 - Pg 37-38.

The court abused its discretion because ability to pay is a relevant factor that should have been given significant weight but was not. Reversal and remand are warranted, so that Dilley's, Spartan's, and Island's ability to pay may be considered.

CONCLUSION

The Court should reverse the district court's judgment against Eldred, Dilley, Spartan, and Island and remand for entry of judgment in Appellants' favor. In the event the Court finds error only in the district court's failure to allow the jury to determine the predicate facts necessary to justify the civil penalties it imposed, the Court should remand with instructions to enter penalties not to exceed $7,500 for Eldred and Dilley and not to exceed $80,000 for Spartan and Island.

Respectfully submitted, this 17th day of January, 2023, by:

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CERTIFICATE OF COMPLIANCE

I hereby certify that this brief complies with the type-volume limits under Fed. R. App. P. 28(a)(10) and typeface and typestyle requirements under Fed. R. App. P. 32(a)(5)-(6) and 11th Cir. R. 28-1(m) because this brief contain 12,978 words, excluding the parts of the motion exempted by Fed. R. App. P. 32(f), prepared in proportionally spaced typeface using Microsoft Word for Office365 Times New Roman 14-point font.

Dated: January 17, 2023

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CERTIFICATE OF SERVICE

I hereby certify that on January 17, 2023, I electronically filed the foregoing with the Clerk of Court for the United States Court of Appeals for the Eleventh Circuit by using the appellate CM/ECF system which sent notification of such filing to all counsel of record.

Dated: January 17, 2023

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