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' REPLY BRIEF

KARA M. ROLLINS
JOHN J. VECCHIONE
NEW CIVIL LIBERTIES ALLIANCE
1225 19th St. NW, Suite 450
Washington, DC 20036
Phone: (202) 869-5210
Kara.Rollins@ncla.legal
John.Vecchione@ncla.legal
Counsel for Defendants-Appellants

AMENDED CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT

Defendants-Appellants amend the CIP contained in their first brief as required by Fed. R. App. P. 26.1, 11th Cir. R. 26.1, and 11th Cir. R. 26.1-2(b):

1. Barbero, Megan, attorney for the Commission

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

TABLE OF CONTENTS

AMENDED CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT C-1

TABLE OF CONTENTS i

TABLE OF CITATIONS ii

ARGUMENT 1

I. THE DISTRICT COURT ERRED WHEN IT DENIED DEFENDANTS' POST-TRIAL MOTION FOR JUDGMENT AS A MATTER OF LAW 6

A. Eldred Did Not Make Any Actionable Misrepresentations 9

B. Dilley Did Not Make Any Actionable Misrepresentations 12

C. Spartan Did Not Make Any Actionable Misrepresentations 15

D. Island Did Not Make Any Actionable Misrepresentations 15

II. THE DISTRICT COURT ABUSED ITS DISCRETION WHEN IT PERMITTED THE SEC EXPERT'S UNQUALIFIED TESTIMONY 16

III. THE DISTRICT COURT ERRED IN ORDERING DISGORGEMENT AND OTHER PENALTIES IN THIS CASE 18

A. The Disgorgement Order Exceeds the Bounds of Equity and Is a Penalty 18

B. The District Court Erred When It Denied a Jury Determination on the Facts Necessary to Establish the Civil Penalties and Issued Penalties that Were Inconsistent with the Jury's Liability Determination 23

C. The District Court Abused Its Discretion When It Ordered Remedies Based on Conduct for Which Appellants Were Not Found Liable 24

D. The Penalties Ordered Against Dilley, Spartan, and Island Violate the Eighth Amendment's Excessive Fines Clause 25

CONCLUSION 26

CERTIFICATE OF COMPLIANCE 28

CERTIFICATE OF SERVICE 29

TABLE OF CITATIONS

Cases

Badger v. S. Farm Bureau Life Ins. Co.,
612 F.3d 1334 (11th Cir. 2010) 7
Basic v. Levinson,
485 U.S. 224 (1988) 11
Chiarella v. U.S.,
445 U.S. 222 (1980) 7
Cordoves v. Miami-Dade Cty.,
104 F. Supp. 3d 1350 (S.D. Fla. 2015) 16
Daubert v. Merrell Dow Pharmaceuticals, Inc.,
509 U.S. 579 (1993) 16
In re Wild,
994 F.3d 1244 (11th Cir. 2021) 22
Kokesh v. SEC,
581 U.S. 455 (2017) 20, 21, 22
Levie v. Sears Roebuck & Co.,
676 F. Supp. 2d 680 (N.D. Ill. 2011) 11
Liu v. SEC,
140 S. Ct. 1936 (2020) 20, 21, 22
Marshall v. Vicksburg,
15 Wall. 146 (1873) 20
Porter v. Warner Holding Co.,
328 U.S. 395 (1946) 22
Pottinger v. City of Miami,
805 F.3d 1293 (11th Cir. 2015) 5
Rink v. Cheminova,
400 F.3d 1286 (11th Cir. 2005) 16
SEC v. Calvo,
378 F.3d 1211 (11th Cir. 2004) 19
SEC v. First City Fin. Corp.,
890 F.2d 1215 (D.C. Cir. 1989) 19, 20
SEC v. Goble,
682 F.3d 934 (11th Cir. 2012) 13
SEC v. Lemelson,
596 F. Supp. 3d 227 (D. Mass. 2022) 19
SEC v. Merch. Capital, LLC,
483 F.3d 747 (11th Cir. 2007) 5, 7

SEC v. Zandford,
535 U.S. 813 (2002) 7, 8
Stransky v. Cummins Engine Co., Inc.,
51 F.3d 1329 (7th Cir. 1995) 11
Timbs v. Indiana,
139 S. Ct. 682 (2019).....26
Wright v. Ernst & Young LLP,
152 F.3d 169 (2d Cir. 1998) 7
Yates v. Pinellas Hematology & Oncology, P.A.,
21 F.4th 1288 (11th Cir. 2021).....26

Rules

17 C.F.R. § 229.401(f)(2) 12
17 C.F.R. § 240.15c2-11 12
Federal Rule of Evidence 702.....16

Other Authorities

Lie, Black's Law Dictionary (11th ed. 2019) 5

ARGUMENT

After years of investigations, a 12-day jury trial, and securing a finding of no liability on 13 of 14 counts, Appellants are still in the unenviable position of correcting the Securities and Exchange Commission's ("SEC") myriad errors of fact and law. They also must contend with SEC's subjective recitation of the facts, which makes assertions based on theories and factual premises the jury explicitly rejected. At trial, the SEC attempted to prove that Appellants knew that Mr. Mirman, Mr. Rose, Ms. Harrison, and Mr. Daniels were lying to the SEC and the Financial Industry Regulatory Authority ("FINRA"). The jury found otherwise. SEC's brief makes assertions of alleged misbehavior throughout that the jury did not believe and outright rejected.

Appellants start by highlighting for this Court exactly on what the SEC failed to carry its burden to prove at trial:[1]

- SEC did *not* prove that Appellants furthered any scheme by "submit[ting] false Form 211 applications to FINRA;" "contribut[ing] to false [Depository Trust Company ("DTC")] applications;" "effectuat[ing] the bulk transfer" of a "deceptive public float[;]" or "support[ing] ... the manufacture

[1] SEC suggests that Appellants are arguing that the jury's verdict is "inconsisten[t]," SEC Br. 27, but given that Jury Instruction 19 provides a list of possible misrepresentations or omissions, the question here is what did the SEC prove or fail to prove, and what SEC failed to prove at trial is both significant and substantial.

of undisclosed blank check companies." Doc 249 - Pg 23-24 (Instruction 16 describing SEC's theories of liability relating to rejected Count 3).

- SEC did *not* prove that Appellants schemed "to defraud the public that the [issuers] were operating businesses with independent management and shareholders, rather than undisclosed 'blank check' or 'shell' companies for sale" by "sign[ing] and submit[ting] false Form 211 applications to FINRA;" "contribut[ing] to false DTC applications;" "effectuat[ing] the bulk transfer of" a deceptive public float; "support[ing]" the manufacture of undisclosed blank check companies[;]" providing services that "were critical" to Form 211 filings; or possessing "information that undermined any reasonable basis that the information required by Rule 15c2-11 was materially accurate and from a reliable source." Doc 249 - Pg 28-29 (Instruction 17 describing SEC's theories of liability relating to rejected Count 4); Doc 249 - Pg 36-37 (Instruction 19 describing SEC's theories of liability relating to rejected Count 5); Doc 249 - Pg 39-40 (Instruction 19 describing SEC's theories of liability relating to rejected Count 7).[2]

[2] Critically, as to Count 6, for which liability was found and Appellants now contest, Jury Instruction 19 contains none of these theories. It contains only a list of 19 alleged misrepresentations or omissions. *See* Doc 249 - Pg 37-39.

- SEC did *not* prove that Appellants schemed to "fraudulently obtain effective registration of shell companies" and to "issue unrestricted stock for" companies "secretly controlled by [Mirman and Rose]" or taking part in a scheme to create a "deceptive public float of purportedly unrestricted shares." Doc 249 - Pg 32 (Instruction 18 describing SEC's theories of liability relating to rejected Counts 8, 9, and 10); Doc 249 - Pg 41-42 (Instruction 20 describing SEC's theories of liability relating to rejected Counts 11, 12, 13).

- SEC did *not* prove that Appellants transferred stock from the shareholders of certain issuers without "an effective registration statement." Doc 249 - Pg 43 (Instruction 21 describing SEC's theories of liability relating to rejected Count 14).

And yet, reading SEC's brief in isolation suggests that Appellants engaged in, and are liable for, all this conduct. *See*, *e.g.*, SEC Br. 21 (alleging that Appellants "opened" the gates by making shares free trading that SEC alleges should have been restricted). For example, as their own expert agreed, there is *nothing* unlawful about forming shell, blank check, and startup companies. Doc 234 - Pg 109-112. Nor is it illegal for such legitimate companies to participate in "reverse mergers." *Id.*

SEC also misconstrues the standards that market-makers, transfer agents, and their principals, like Appellants, are held to. SEC alleges that Appellants were "gatekeepers" who abused their responsibilities, SEC Br. 21, but it ignores the fact

that the jury rejected the SEC's gatekeeping theory when it determined that Appellants did not submit false information to FINRA or possess information that materially undermined those applications. *See*, *e.g.*, Doc 249 - Pg 23-24; Doc 249 - Pg 28-29; Doc 250. Moreover, Appellants only filed Form 211s for SEC-registered or foreign exchange-registered issuers because they were entitled to rely on the information provided to the SEC by those issuers. *See*, *e.g.*, Doc 224 - Pg 32-34 ("virtually all" the "required" Form 211 information was from the SEC's website); Doc 206 - Pg 108-109. Because all of this information was taken by Appellants from the SEC's own website that the SEC placed there itself, the SEC let all of these actors past "the gate" before Appellants even knew about them. SEC was the "gatekeeper" and let them through before Appellants ever saw them. They were also permitted to rely on documents, like signed, notarized, and/or sworn documents, that were from a reliable source like the issuer itself. Doc 224 - Pg 32-34.

SEC's brief also misleads this Court by using the legally imprecise term "lie" and its variations. *See*, *e.g.*, SEC Br. 21 ("Dilley, Eldred, and Spartan lied in Forms 211."). This may seem like another "hypertechnical" point, *cf.* SEC Br. 22, but it is not.[3] "In the hierarchy of law, language is king. Words matter in constitutions, treaties, statutes, rules, cases, and contracts." *Pottinger v. City of Miami*, 805 F.3d

[3] Despite SEC's protestation, so-called hypertechnical arguments do not mean that an argument is incorrect or legally insufficient.

1293, 1295 (11th Cir. 2015). So too here, where Section 10(b) and Rule 10b-5(b) of the Exchange Act specifically preclude only certain material misrepresentations and materially misleading omissions. *SEC v. Merch. Capital, LLC*, 483 F.3d 747, 766 (11th Cir. 2007). As the district court instructed, "[a] 'misrepresentation' is a statement that is not true." Doc 249 - 25, 37. And, "[a]n 'omission' is the failure to state facts that would be necessary to make the statements made by the Defendants not misleading to the Plaintiff." Doc 249 - 25, 37. In contrast, "[a] 'fraud or deceit' means a *lie* or a trick." Doc 249 – 28 (Jury Instruction 17 relating to rejected Count 4), 39 (Jury Instruction 19 relating to rejected Count 7) (emphasis added). The ordinary meaning of "lie" infers that a false statement is made with a knowing intent to deceive. *Lie*, Black's Law Dictionary (11th ed. 2019). But the jury rejected SEC's theory that Appellants engaged in any fraud or deceit—that they lied—knowingly or otherwise. Doc 250 - Pg 2, 3.

Moreover, the evidence at trial was clear that the only liars in this case were Mr. Mirman, Mr. Rose, and the CEOs and shareholders who submitted signed, sworn, or notarized documents in furtherance of their schemes. *See*, *e.g.*, Doc 264-35 (notarized affidavit from First Xeris' CEO); Doc 264-44 (signed questionnaire from Global Group's president); Doc 264-47 (signed questionnaire from First Xeris' president); Doc 264-60 - Pg 16-17 (signed and initialed checklist by On the Move indicating it is "not a shell" and that there are no other persons controlling it); Doc

257-23; *cf.* S.A. 612 (FINRA examiner admitting that a broker-dealer presented with "documents that are notarized and/or certified by the issuer" may be unable to determine it was being misled). As Mr. Rose testified, he and Mr. Mirman specifically sought out CEOs that had the skills and knowledge of the business described in the S-1 registration to look legitimate. Doc 190 - Pg 24-26. Mr. Rose crafted elaborate business plans described in the S-1, again to provide an air of legitimacy. Doc 190 - Pg 36. They opened bank accounts in the issuer's name to collect money from shareholders, from which they then made payments to others. Doc 190 - Pg 28-29. And this whole elaborate scheme only worked if Mirman and Rose weren't found out, which they achieved by lying and concealing it from Appellants. Doc 199 - Pg 92 (Appellants were "never told" that Mirman and Rose controlled the issuers); Doc 186 - Pg 44, 46 (same). SEC's imprecise choice of words regarding Appellants and their alleged conduct only serves (i) to conceal that the jury rejected any theory that the Appellants "lied," (ii) to confuse Appellants' actions with others' misdeeds and schemes, and (iii) to color this Court's understanding of the facts and the law on appeal.

Turning to the merits, SEC's arguments fare no better.

I. THE DISTRICT COURT ERRED WHEN IT DENIED DEFENDANTS' POST-TRIAL MOTION FOR JUDGMENT AS A MATTER OF LAW

The inquiry here turns on what is left when the SEC's theories that the jury rejected are cross-referenced with Instruction 19's list of potential

misrepresentations and omissions. Which of *those* misrepresentations and omissions remain *and* are consistent with the jury's verdict in this case? From there, the inquiry is whether, as a matter of law, Appellants made any of those misrepresentations and omissions and they were "(1) material misrepresentations or materially misleading omissions, (2) in connection with the purchase or sale of securities, (3) made with scienter." *Merch. Capital, LLC*, 483 F.3d at 766. Each of these discrete misrepresentations or omissions must have been made within the applicable statute of limitations. *See* Br. 11-16 (discussing statute of limitations considerations).

As discussed in Appellants' opening brief, the materiality of any misrepresentation or omission turns on whether it is the type of information a "reasonable investor" would rely on *and* is available to them. Br. 19-20. 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). Omissions only violate Rule 10b-5 if the 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). But "mere possession of nonpublic market information" does not create a duty to disclose. *Chiarella v. U.S.*, 445 U.S. 222, 235 (1980). To violate the rule, the misrepresentation or omission must also, at a minimum, "coincide" with the purchase or sale of securities. *SEC v. Zandford*, 535 U.S. 813, 820 (2002).

SEC has conceded that Appellants did not make *any* materially misleading omissions. *See* SEC Br. 21 ("Each defendant made material misrepresentations"); *id.* at 28 ("The defendants' misrepresentations were 'in connection with' the purchase or sale of securities").[4] Moreover, they have waived their argument that by "cho[o]s[ing] to speak" there arose a "duty" to "speak fully and truthfully" because they did not argue that such a duty existed below. *See id.* at 24-25. SEC has also abandoned any reliance on the "continuing violations doctrine[,]" *see id.* at 54, which at least suggests tacit agreement with Appellants that misrepresentations and omissions that violate Section 10(b) and Rule 10b-5(b) of the Exchange Act are discrete acts and must be reviewed as such. *See* Br. 17.

SEC's interpretation of the law is wrong on several accounts. As discussed above misrepresentations and omissions like the ones at issue here are *discrete* actions at specific points in time. As *Zandford* suggests, those discrete actions must coincide with the purchase or sale of securities to establish liability. 535 U.S. at 820. The jury instructions are not in conflict with this point as SEC suggests. *See* SEC Br. 29. SEC points to no misrepresentation or omission that occurred *at the same time as* any purchase or sale of any security. Similarly, SEC is incorrect in its view that the

---

[4] Considering SEC's waiver on omissions, Appellants reply only to SEC's arguments that they made misrepresentations that support the jury's verdict. Appellants stand on their arguments from their opening brief that there were no materially misleading omissions. *See* Br. 19-29.

portions of the Form 211 applications that they alleged included misrepresentations were public. *Id.* at 30. The overwhelming testimony, including by a FINRA examiner, was that the accompanying correspondence (where the alleged misrepresentations were) is confidential and not publicly available. *See* Doc 226 - Pg 84; Doc 224 - Pg 37; S.A.795-96; Doc 210 - Pg 119. Indeed, if Appellants are mistaken on this point, so was the district court. *See* Doc 263 - Pg 24. SEC's view that it was Appellants and not the issuers who "made" the statements relies on the false assumption that the Appellants "knew that those issuer representations were false" and the jury could deduce the same. SEC Br. 22. Similarly, SEC's argument that Appellants' misrepresentations were material also hinges on the false assumption that Appellants knew who controlled the issuers. *Id.* at 25-26. But both of those fail because Appellants did not know the issuer representations were false or who controlled the issuers, and the jury rejected the SEC's contentions that Appellants had knowledge of these facts. Doc 199 - Pg 92; Doc 186 - Pg 44, 46 (same); Doc 249 - Pg 23-24, 28-29, 32, 41-42.

A. Eldred Did Not Make Any Actionable Misrepresentations

SEC argues that Eldred "falsely represented" his relationship with Mr. Daniels. SEC Br. 21. Specifically, it alleges that Eldred made this misrepresentation "in the Court Form 211." SEC Br. 12. But SEC's theory is factually and legally incorrect. As a general matter, the jury rejected that Eldred had "filed false Forms 211 with

FINRA[,]" that there was some impropriety regarding Spartan and Island's potential acquisition by one of the Harrison and Daniels issuers, and that that he possessed information undermining his reasonable basis for the information in those applications. Doc 249 - Pg 23-24 (Instruction 16 describing SEC's theories of liability relating to rejected Count 3); Doc 249 - Pg 28-29 (Instruction 17 describing SEC's theories of liability relating to rejected Count 4); Doc 249 - Pg 36-37 (Instruction 19 describing SEC's theories of liability relating to rejected Count 5); Doc 249 - Pg 39-40 (Instruction 19 describing SEC's theories of liability relating to rejected Count 7).

SEC's argument ignores that misrepresentations are discrete actions that must be reviewed at the time they are made. At the time the Court Form 211 was filed in July 2012, it had been over a year since Dilley had filed the Dinello Form 211. *See generally* S.A.37-38. Court was also only the second Form 211 Spartan filed for the Harrison and Daniels issuers, so Eldred was incapable of having actual knowledge of future Form 211 applications Spartan may or may not be approached to do at the time the application was filed. The emails SEC relies on, S.A.928-929, do not show otherwise. At best they show that Mr. Fan may be dealing with issuers who may need Form 211s filed in the future. Likewise, Eldred also did not "misleadingly state[]" that Court "had represented not having entered into discussions or

negotiations for mergers or acquisitions."[5] SEC Br. 13. That representation was made on July 24, 2012 and *all* of the emails SEC relies on are dated *after* the representation was made. S.A.928-929 (emails dated July 30, 2012); The statement was true when it was made, and true statements are not misrepresentations that violate Rule 10b-5(b). Doc 264-56 (Court's July 13, 2012 certified 211 due diligence questionnaire completed by Daniels); Doc 249 - 25, 37. But such hypothetical filings or potential future actions, including a potential reverse merger between Spartan, Island, and Dinello (that never came in fruition), were not disclosable events under Rule 10b-5(b). *See Basic v. Levinson*, 485 U.S. 224, 239 n.17 (1988); *see also Levie v. Sears Roebuck & Co.*, 676 F. Supp. 2d 680, 687 (N.D. Ill. 2011) (finding that there is no "duty to disclose something that had yet to occur"); *Stransky v. Cummins Engine Co., Inc.*, 51 F.3d 1329, 1332 (7th Cir. 1995) (no basis for "liability on circumstances that arise after the speaker makes the statement"). In any event, it was no secret that Court would consider a merger, the issuer said as much in its July 5, 2012 S-1 filing to the SEC. Doc 255-40 - Pg 6; *see also* Doc 255-43 - Pg 2 (Top to Bottom's July 23, 2013 S-1 filed stating "we have included information in our prospectus that we will consider a merger, acquisition or business combination").

[5] Appellants thoroughly briefed their arguments that they did not "make" any of the statements at issue in their opening brief. Br. 20, 22, 26-27.

Eldred was also under no obligation to disclose Daniels's regulatory history. *See* 17 C.F.R. § 240.15c2-11 (as effective from June 19, 2015 to December 27, 2020) (describing information required for Form 211 application but no mention of providing regulatory violations history). Indeed, it's not clear what Eldred could even report because when a Spartan employee ran a background check on Daniels, nothing came up. S.A.810. Moreover, even Daniels was not required to disclose his history to the SEC. *See* 17 C.F.R. § 229.401(f)(2) (Item 401) (as effective from Feb. 28, 2010 to May 1, 2019) (individuals like Daniels were required to report certain legal proceedings if they occurred within 10-year period before an SEC filing). As has been a theme throughout this case, what the requirements of the law are and what SEC wishes they were are two different things. But the SEC's whims and wishes do not have the force of law. *Cf*. Doc 249 - Pg 47 (Instruction 22 indicating that agency guidance lacks the force of law).

B. Dilley Did Not Make Any Actionable Misrepresentations

SEC argues that Dilley "made false statements in Form 211 filings to initiate the public question of issuer stock." SEC Br. 21. In support of this it makes two separate connections: (1) that Dilley "falsely stated that the nominal CEOs of the Mirman-Rose issuers had initiated Form 211 process (in fact, those persons never even spoke with Spartan);" and, (2) that Dilley "falsely represented that Mirman had 'no relationship' with an issuer that Mirman controlled." *Id.* Neither of these arguments

is sufficient as a matter of law. As a general matter, the jury rejected that Dilley had signed and submitted "false" Form 211 applications to FINRA and that he possessed information undermining his reasonable basis for the information in those applications. Doc 249 - Pg 23-24 (Instruction 16 describing SEC's theories of liability relating to rejected Count 3); Doc 249 - Pg 28-29 (Instruction 17 describing SEC's theories of liability relating to rejected Count 4); Doc 249 - Pg 36-37 (Instruction 19 describing SEC's theories of liability relating to rejected Count 5); Doc 249 - Pg 39-40 (Instruction 19 describing SEC's theories of liability relating to rejected Count 7).

As to the first example SEC provides, it was, at best, established that "who" introduced the issuer to Spartan and whether they had a conversation with Dilley was of interest to FINRA. Br. 20. This argument is baseless. Even if Dilley had spoken to every issuer, those issuers were directed by Mirman and Rose to lie to Appellants and direct them back to Mirman and Rose. Doc 190 - Pg 86-87 (Mirman and Rose told CEOs that if Appellants contacted them that they "would handle the situation"). And even if those types of statements made to FINRA were not true, that information would have no impact on an *investor's* decision to purchase shares at some point in the future, and it thus immaterial. *See SEC v. Goble*, 682 F.3d 934, 944 (11th Cir. 2012). Indeed, whether FINRA found the information material has no

effect on whether it is material for the purposes of establishing a Rule 10b-5(b) violation. *See* Br. 23.

The second example SEC provides is based on the false assumption that Dilley knew Mirman controlled any of the issuers, which he did not. Doc 199 - Pg 92 (Appellants were "never told" that Mirman and Rose controlled the issuers); Doc 186 - Pg 44, 46 (same). That, and other similar false or disproven assumptions appear throughout SEC's briefing and should be rejected. *Compare* SEC Br. 10-11 (alleging that Dilley knew Mirman and Rose's plan to sell shells) *with* Doc 190 - Pg 71-73 (Rose did not "recall discussing how we're selling the company. Okay? With Carl Dilley or anybody at [Spartan].").

SEC also argues that Dilley made misrepresentations through "false statements in DTC applications that the issuers were not shells" SEC Br. 26; 13-14. But those statements were true when they were made. The issuers had at least "nominal" assets and operations as shown in publicly available documents filed on the SEC's EDGAR System. Doc 238 - Pg 54; Doc 194 - Pg 20-21, 25, 24, 26-28; Doc 257-93 (sending copy of On the Move's 8-K showing over "$100,000 in revenues"); Doc 257-12 - Pg 4 (Kids Germ 10-K showing "cash of $25,254"). Once again, the SEC provided the information to Appellants that it now claims they could not rely upon. These statements were made contemporaneously with the underlying information supporting the conclusion in nonpublic communications so cannot constitute a

violation. Finally, SEC argues Dilley made a misrepresentation by confirming to a "buyer that Island had not any restriction on the shell's free-trading shares." SEC Br. 14. But any falsity in this statement is again necessarily reliant on the rejected theory that Dilley knew the issuer was controlled by Mirman and Rose and that the shares should have been restricted. *But see* Doc 249 - Pg 32; Doc 249 - Pg 41-42.

C. Spartan Did Not Make Any Actionable Misrepresentations

Because neither Eldred nor Dilley made actionable misrepresentations for the reasons argued above, it is also true that Spartan did not make any actionable misrepresentations because their liability was predicated on the actions Eldred and Dilley took. *See also* Br. 24-28.

D. Island Did Not Make Any Actionable Misrepresentations

SEC argues that, in addition to Dilley's actions, Island also "improperly gave to Mirman and Rose … unrestricted shares[.]" SEC Br. 14. But that action is neither a misrepresentation nor an omission, so it cannot support a finding of liability under Rule 10b-5(b). It is also not a transfer agent's responsibility to impose restrictions on shares. Doc 234 - Pg 79-80 ("[T]he *shareholder* needs to provide evidence that there's an available exemption from registration." (emphasis added)). Because neither Eldred nor Dilley made actionable misrepresentations for the reasons argued above, it is also true that Spartan did not make any actionable misrepresentations

because its liability was predicated on the actions Eldred and Dilley took. *See also* Br. 24-28.

II. THE DISTRICT COURT ABUSED ITS DISCRETION WHEN IT PERMITTED THE SEC EXPERT'S UNQUALIFIED TESTIMONY

The SEC's proffered expert witness, James Cangiano, was unqualified to provide testimony regarding transfer agents and DTC eligibility because he had *no* experience in the transfer-agent industry. None. SEC conflates his general "experience as a regulator and consultant in the over-the-counter securities industry" as being sufficient to permit him to testify about the specific intricacies of "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. The district court failed in its gatekeeping obligation under Federal Rule of Evidence 702 and *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 589 (1993). "[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 v. Miami-Dade Cty.*, 104 F. Supp. 3d 1350, 1358 (S.D. Fla. 2015). Mr. Cangiano is a classic example of "expert on everything" which is discouraged under Rule 702, and indeed defeats the filtering purpose the rule is meant to serve. *Rink v. Cheminova*, 400 F.3d 1286, 1291 (11th Cir. 2005). While he may have been a

regulator at FINRA's predecessor, neither it nor FINRA had any regulatory oversight over transfer agents. Doc 234 - Pg 106.

Contrary to SEC's protestation, Mr. Cangiano's testimony was not harmless. For example, he opined about how transfer agents were "gatekeepers" without any basis for that opinion. Doc 234 - Pg 123-24. As we have seen, the SEC was the gatekeeper, and it let all these bad actors in and put their filings on its own website that Appellants relied upon in filing the issuer's 211 forms. But his assertion left the overall impression that Island and Dilley were obligated to take certain actions that they were not. When asked if there is rule requiring transfer agents "to inquire of the underlying validity of the stock" he answered pithily "there's a rule called the federal securities laws." Doc 234 - Pg 125. Which again leaves an overall impression of some legal obligation on Dilley and Island that either does not exist or he could not articulate. He also testified that Island "should not have done the deals" but he has no basis for forming that opinion because he has no experience in how transfer agents operate or the actions they are obligated to take. Doc 234 - Pg 41. And SEC's assertion that Island "had no basis for giving unrestricted shares to issuer control-persons" includes a fatal assumption that the jury rejected: it assumes that Island *knew* it was giving unrestricted shares to a control person. *See* SEC Br. 33. But the jury rejected that theory in rendering its verdict. *See* Doc 249 - Pg 32, 41-43; Doc 250 - Pg 3-5. Mr. Cangiano's unfettered testimony and opinions went to core

questions in this case, whether Island and Dilley were liable for misrepresentations or omissions relating to the designation of the issuer's securities as "free trading" or effectuating issuances and transfers without "restrictive legends." Doc 249 - Pg 39 (Jury Instruction 19). As such, his testimony was not harmless.

III. THE DISTRICT COURT ERRED IN ORDERING DISGORGEMENT AND OTHER PENALTIES IN THIS CASE

A. The Disgorgement Order Exceeds the Bounds of Equity and Is a Penalty

The district court committed reversible error when it ordered disgorgement. While the SEC pushes policy arguments in favor of disgorgement, *see, e.g.,* SEC Br. 45-46, the issue before this Court is not a policy decision about where disgorged money should go but rather a legal question about whether the district court had the power to order disgorgement. And, if so, whether it exceeded the bounds of that equitable power by ordering payment to the Treasury. On the facts and circumstances of this case, the answers to these inquiries resolve in favor of the Appellants.

First, there was no "nexus" between the conduct the jury found liability for, violations of Rule 10b-5(b), and the fees Island received for its transfer agent services, which it was ordered to disgorge. *See SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989); Doc 302 - Pg 36 (SEC accountant who tabulated disgorgement calculation couldn't tell which line items related to any allegations or

who paid the fees); Doc 190 - Pg 28-29 (issuers had own bank accounts from which they paid vendors). The transfer agent fees the issuers paid were not for illicit participation in a scheme to issue unrestricted stock as the SEC argued below. The jury rejected that basis when it rejected the SEC's theory that the issuers were "secretly controlled by [Mirman and Rose]" and it rejected the scheme liability counts. *See* Br. 48; *see also* Doc 249 - Pg 30-34, 41-42; Doc 250. *SEC v. Lemelson*, 596 F. Supp. 3d 227, 238 (D. Mass. 2022), *aff'd sub nom. SEC v. Lemelson*, 57 F.4th 17 (1st Cir. 2023) (denying SEC disgorgement request due to "the jury's lack of a finding of scheme liability" and "lack of adequate discussion of victims"). Those determinations foreclose the disgorgement sought here. That the jury *also* rejected the SEC's theory that Island sold unregistered securities simply reinforces the fact that there is no nexus. Doc 249 - Pg 43-46.

Second, by its own admission, the SEC's disgorgement calculation was inaccurate, and therefore unreasonable. SEC Br. 34 (noting all the deductions the district court made to SEC's purportedly reasonable approximation). And SEC failed to meet its burden, *see SEC v. Calvo*, 378 F.3d 1211, 1217 (11th Cir. 2004), because its calculation was riddled with errors and obvious deductions which it failed to account for. Br. 49-51. SEC is not free to throw disgorgement spaghetti against the wall to see if it sticks. *Id.* And it is not the district court's job to correct the SEC's erroneous calculation, as it did here. Doc 297 - Pg 30-31 (and accompanying notes

rejecting portions of SEC's "reasonable" approximation). Nor is Island's challenge merely "academic" as the SEC suggests. SEC Br. 35. The burden-shifting framework requires the illegal conduct to be the cause of the records uncertainty. *See* Br. 50-51. But the liable conduct here, alleged misrepresentations and omissions, is not what caused the records uncertainty; rather, the record is clear that the records were kept, maintained, stored, and destroyed pursuant to a "record retention process and policies," but what remains over a decade later is limited. Doc 302 - Pg 75. And in any event, Island produced all records in its possession to SEC during the investigation and litigation of this case. *Id*. That SEC sat on its rights in prosecuting this case *for years* should not allow it to claim that Appellants' records are the problem now.

Third, disgorgement is an equitable remedy that "never 'lends its aid to enforce a forfeiture or penalty.'" *Liu v. SEC*, 140 S. Ct. 1936, 1941 (2020) (quoting *Marshall v. Vicksburg*, 15 Wall. 146, 149 (1873)). SEC agrees that disgorgement, even under the NDAA amendments, is an equitable remedy or grounded in such a way that it does not depart from equitable practice. SEC Br. 35, 42 n.8. Where the line between penalty and equity lies is often unclear. *First City Fin. Corp.*, 890 F.2d at 1232. But the Supreme Court has provided guideposts for *when* disgorgement becomes a penalty. *Kokesh v. SEC*, 581 U.S. 455, 463-65 (2017) (laying out factors for whether disgorgement is a penalty). Contrary to the SEC's contention that *Liu*

forecloses reliance on *Kokesh*, *Liu* provides additional guidance to the lower courts about equitable disgorgement's limits. *Liu*, 140 S. Ct. at 1947. Thus, just because a disgorgement order is limited to net profits, that does not mean it cannot also be a penalty, as SEC suggests. SEC Br p 45.

The disgorgement order meets all three of the *Kokesh* factors. Br. 46-47. SEC attempts to contest this but fails. SEC Br. 43-44. The Supreme Court has unequivocally said that *in the context of SEC enforcement actions*, deterrent effect means it "is imposed for punitive purposes." *Kokesh*, 581 U.S. at 464. The pre-*Kokesh* cases SEC relies on does not vitiate this fact. *See* SEC Br. 43-44. SEC also attempts to twist the fact that there are no identified harmed investors into a policy rationale for permitting disgorgement, but the reality is—and the evidence at trial supports—that there are no harmed investors. In fact, the only testimony in support of SEC's "broad and diffuse harm" theory is its expert, who despite lacking *any* experience in transfer-agent practice, opined as to how Island's actions "could lead to trouble" but failed to identify any harmed investor. Doc 234 - Pg 24. Not once in the decade since the alleged conduct occurred has the SEC identified a single harmed investor, nor does the record show that SEC even attempted to do so. That fact alone supports Island's view that there was no harm and that the disgorgement order to be paid to the Treasury is (impermissibly) compensatory. *Cf. Liu*, 140 S. Ct. at 1955-

56 (Thomas, J. dissenting) (permitting the SEC to keep equitable relief money "is inconsistent with traditional equitable principles").

Finally, the third *Kokesh* factor supports considering *who* the disgorgement award benefits. 581 U.S. at 465. "When an individual is made to pay a non-compensatory sanction to the Government as a consequence of a legal violation, the payment operates as a penalty." *Id.* at 455 (citing *Porter v. Warner Holding Co.*, 328 U.S. 395, 402 (1946)).[6] Also, because disgorgement is being the paid to the Treasury, the award here benefits the government, not investors or victims. Thus, how the statute is construed may be of little concern as the district court acted outside the bounds of equitable practice, foreclosing the disgorgement ordered here. In any event, Section 78u(d)(5)'s investor-benefit provision places a clear limit on equitable remedies. *Liu*, 140 S. Ct. at 1947. Disgorgement is an equitable remedy, and the SEC has conceded that it is, SEC Br. 35, thus section 78u(d)(7) must be construed in the context of the statute as a whole, not read in isolation as the SEC effectively proposes, SEC Br. 44-46. *See In re Wild*, 994 F.3d 1244, 1272 (11th Cir. 2021) (Pryor, J., concurring).

[6] SEC relies on *Porter*, SEC Br. p 38, 41, 43, 45, but ignores this point.

B. The District Court Erred When It Denied a Jury Determination on the Facts Necessary to Establish the Civil Penalties and Issued Penalties that Were Inconsistent with the Jury's Liability Determination

SEC misunderstands and misrepresents Appellants' jury determination request and the arguments below. As explained in Appellants' opening brief, under the Exchange Act's three-tier penalty structure, there are multiple *factual* determinations that must be made before levying a civil penalty under *any* of the tiers. Br. 36-39. That necessarily includes how many penalties occurred. *Cf.* S.A.85 (arguing that "the Seventh Amendment safeguards the right to have a jury determine the underlying fact(s) giving rise to an assessment of damages"). SEC also describes the district court's jury determination and penalty number decisions as acting within its discretion, but whether Appellants were entitled to a jury determination regarding the civil penalty, and the number of penalties, is a question of law. *Compare* SEC Br. 47-51; S.A.85-86.

Appellants have never wavered in their conviction that they were not liable—that they committed 0 violations—and that they were entitled to have a jury make the factual determinations underlying any civil penalty order. Doc 273 - Pg 6-7; Doc 122. They are not required to reraise their objections in perpetuity to preserve them. This appeal includes all erroneous orders below, and Appellants were not required to constantly raise matters with the district court it had already decided. In any event, SEC's number of violations was never provided to Appellants *until* the remedies

stage, at which point they maintained that they retained their right to defend themselves. S.A.1020; Doc 273 - Pg 6-7. At that point, the SEC seemingly plucked the number of violations from thin air when, at trial, SEC had argued it was incapable of identifying the specific violations because there were so many. *See*, *e.g.*, Doc 303 - Pg 95-96; Doc 219 - Pg 53-55. This sort of gamesmanship shows why a jury should have been permitted to determine the tier level, which necessarily includes a factual determination of how many violations there were.

Despite SEC's arguments to the contrary, the district court's determination conflicts with the jury's determination. SEC Br. 52-53. The jury clearly determined that Appellants did not participate in any scheme to defraud, and no amount of selective citation to the record can undermine that fact. Doc 250 - Pg 1, 3-6. Yet, the district court inappropriately relied on the existence of and Appellants' alleged participation in a scheme to craft its penalty determinations. Br. 40-41. The jury, which was provided a list of 19 possible misrepresentations or omissions, determined that there was *a* single violation of the Exchange Act. Doc. 250 - Pg 3. However, the district court determined that there were three violations against Mr. Dilley, two violations against Mr. Eldred, and single violations against Spartan and Island, a departure from the jury's determination. Doc. 297 - Pg 37.

C. The District Court Abused Its Discretion When It Ordered Remedies Based on Conduct for Which Appellants Were Not Found Liable

The jury rejected the SEC's theory that Appellants participated in a scheme to defraud multiple times. Doc 250 - Pg 1, 3-6. Despite this, the district court impermissibly relied on the existence of these third-party schemes in crafting the penalties and remedies it ordered. Br. 40-41; Doc 297 – Pg 19, 25, 37. This was improper and violates Appellants' due process rights. Br. 40-41. An out-of-context citation to trial counsel, who dared utter the word "scheme," *see* SEC Br. 52 and S.A.1227, does not somehow make proper the district court's improper reliance on conduct for which there was no liability.

D. The Penalties Ordered Against Dilley, Spartan, and Island Violate the Eighth Amendment's Excessive Fines Clause

The excessiveness of the district court's penalty order was not known until it was issued. Appellants raised their challenge under the Eighth Amendment at the first point in time when they were able to so. Their arguments regarding the Eighth Amendment are not waived. That Mr. Dilley's ability to pay was "contested," SEC Br. 51, does not mean that the penalty ordered by the district court was not excessive within the meaning of the Excessive Fines Clause. Indeed, at the Founding the Excessive Fines Clause was understood to include a limiting principle that considered the offender's economic status at the time the fine is levied. Br. 51-52. A rule to the contrary would defeat the Eighth Amendment's guarantee.

Contrary to SEC's assertion that excessiveness is measured by the characteristics of the offense, SEC Br. 52, it is not clear that this Court's excessiveness inquiry

survives after *Timbs v. Indiana*, 139 S. Ct. 682 (2019). Judges Newsom and Jordan have suggested that the inquiry "is incomplete" because it does not consider "the relationship … between the fine and the offender." *Yates v. Pinellas Hematology & Oncology, P.A.*, 21 F.4th 1288, 1323 (11th Cir. 2021) (Newsom, J., joined by Jordan, J., concurring). Likewise, Judge Tjoflat has suggested that district courts should consider "the characteristics of the offender[.]" *Id.* at 1335 (Tjoflat, J., concurring in part and dissenting in part).

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 10th day of April, 2023, by:

/s/ Kara M. Rollins
KARA M. ROLLINS
JOHN J. VECCHIONE
Litigation Counsel
NEW CIVIL LIBERTIES ALLIANCE
1225 19th St. NW, Suite 450
Washington, DC 20036

Phone: (202) 869-5210
Fax: (202) 869-5238
Kara.Rollins@ncla.legal
John.Vecchione@ncla.legal
Counsel for Defendants-Appellants

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 contains 6,398 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: April 10, 2023

/s/ Kara M. Rollins
KARA M. ROLLINS
Counsel for Defendants-Appellants

CERTIFICATE OF SERVICE

I hereby certify that on April 10, 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: April 10, 2023

/s/ Kara M. Rollins
KARA M. ROLLINS
Counsel for Defendants-Appellants