UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA

CASE NO.: 8:20-cv-00394-MSS-SPF

SECURITIES AND EXCHANGE COMMISSION,	)
	)
Plaintiff,	)
	)
v.	)
	)
KINETIC INVESTMENT GROUP, LLC and	)
MICHAEL SCOTT WILLIAMS,	)
	)
Defendant, and	)
	)
KINETIC FUNDS I, LLC,	)
KCL SERVICES, LLC d/b/a Lendacy,	)
SCIPIO, LLC,	)
LF42, LLC,	)
EL MORRO FINANCIAL GROUP, LLC, and	)
KIH, INC. f/k/a KINETIC INTERNATIONAL, LLC,	)
	)
Relief Defendants.	)
____	)

PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S ("SEC") OPPOSITION TO DEFENDANT MICHAEL SCOTT WILLIAMS' ("WILLIAMS") MOTION FOR JUDGMENT ON THE PLEADINGS [DE 201]

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INTRODUCTION

Williams takes a scattershot approach to attacking the Complaint in his motion for judgment on the pleadings (the "Motion") filed more than one year after the SEC initiated this action and after he answered the Complaint without moving to dismiss it. In a slew of disjointed arguments, Williams argues that the SEC failed to adequately plead its claims. The Court, however, already rejected his arguments when it granted the SEC's motion to freeze Williams' assets, which tracks verbatim the factual allegations of the Complaint.[1] Furthermore, Williams' unsupported arguments conveniently ignore controlling law and gloss over the plain allegations in the Complaint. The Court should deny the Motion.

MEMORANDUM OF LAW

I. Legal Standard

A motion for judgment on the pleadings is governed by the same standard as a motion to dismiss for failure to state a claim under Rule 12(b)(6). *Carbone v. Cable News Network, Inc.*, 910 F.3d 1345, 1350 (11th Cir. 2018). The threshold is low for surviving a Rule 12(b)(6) motion. *Quality Foods de Centro Am.,S.A. v. Latin Am. Agribusiness Dev. Corp., S.A., et al.*, 711 F.2d 989, 995 (11th Cir. 1983). A plaintiff must plead only enough facts to state a claim to relief that is plausible on its face.

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[1] The Asset Freeze Order (ECF No. 33) was entered by the Honorable William Jung, who presided over this case at the time.

Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570 (2007). The Court must accept as true all facts alleged in the complaint in the light most favorable to the plaintiff. *Perez v. Wells Fargo N.A.*, 774 F.3d 1329, 1335 (11th Cir. 2014).

II. The Complaint Sufficiently Pleads Fraud Against Williams

Williams overstates the requirements for pleading fraud with particularity under Fed.R.Civ.P. 9(b). Rule 9(b) does not abrogate the concept of notice pleading set forth in Rule 8(a). *Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1202 (11th Cir. 2001). The purpose of Rule 9(b) is to ensure allegations of fraud are specific enough to provide sufficient notice of the acts complained of and eliminate those complaints filed as a pretext for discovery of unknown wrongs. *SEC v. Ginsburg*, 2000 WL 1299020, at *6 (S.D. Fla. Jan. 10, 2000). Pleading fraud with particularity does not require pleading "detailed evidentiary matter." *Coquina Invs. v. Rothstein*, 2012 WL 4479057, at *12 (S.D. Fla. Sept. 28, 2012). The complaint need only provide a reasonable delineation of the underlying acts and transactions constituting the fraud. *Anderson v. Transglobe Energy Corp.*, 35 F. Supp. 2d 1363, 1369-70 (M.D. Fla. 1999). A complaint pleads fraud with particularity if it alleges the substance of the fraudulent acts, who engaged in the fraud, and when the fraud occurred. *Hekker v. Ideon Grp., Inc.*, 1996 WL 578335,

at*4 (M.D. Fla. Aug. 19, 1996).[2]

The SEC has sufficiently pled fraud against Williams by setting forth his control over Kinetic Investment Group, LLC ("Kinetic Group" together with Williams, "Defendants") and Relief Defendants, his ultimate authority over the false and misleading statements and omissions made verbally and in writing to investors and prospective investors, his misappropriation of investor funds by funneling investor capital to his entity, Lendacy, and his failure to disclose conflicts of interest to investors. For example, the Complaint alleges:

- Since at least 2013, Defendants have raised at least $39 million from at least 30 investors in an unregistered fraudulent securities offering. *See* DE 1 at ¶1.

- At all relevant times, Williams had an ownership interest in, controlled, and exercised ultimate authority over Kinetic Group and Relief Defendants. *Id*. at ¶8.

- Since 2015, Williams provided potential investors with Bloomberg reports about the KFYield strategy, its performance information, assets under management and holdings, *id*. at ¶24, and marketed Kinetic Funds with Lendacy, *id*. at ¶25. *See also* Williams' Answer, DE 56 at ¶¶24-25.

- Defendants made, both orally and in writing,[3] material misrepresentations to investors and prospective investors regarding Kinetic Funds and the use of investor funds, *see* DE 1 at ¶28:

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[2] Discovery provided the means for seeking additional information on the facts alleged in the Complaint. Indeed, Williams has sought and obtained discovery of additional details surrounding the SEC's allegations. *See United States ex rel. Morsell v. Symantec Corp.*, 471 F. Supp. 3d 257, 316 n.19 (D.D.C. 2020) ("Given that [Defendant] filed this 12(c) motion after the close of discovery, it cannot credibly argue that it was deprived of the opportunity to prepare a response and to warrant further process.").

[3] William provides no authority for his proposition that notice pleading requires the Complaint to specify for each misrepresentation and omission whether it was oral or in writing; if it was in writing, what document; where it was made; and to which investor or prospective investor it was

  - Defendants told investors that their money would be invested in income-producing U.S. listed financial products. *Id*. at ¶28(a).

  - Defendants advised investors that their principal would be secure because the KFYield portfolio would be hedged with listed options. *Id*. at ¶28(b).

  - Defendants led prospective investors to believe Lendacy had a separate funding source that would finance the loan from Lendacy to the investor, and that their entire capital would be invested in KFYield. *Id*. at ¶28(c).

  - Defendants touted the liquidity of KFYield assets. Written brochures claim: "Your money is always available . . . The fund's positions are hedged out to 90 days, so with a 30 day written notice prior to the quarter end, the fund can redeem 100% principal without penalties." *Id*. at ¶28(d).

- Defendants knew the representations were false, *id*. at ¶29:

  - Defendants did not invest all investor funds in U.S. listed financial products. Since at least 2013, Defendants invested a substantial portion of investor capital in Lendacy, Williams' entity. Lendacy is not a U.S. listed financial product. *Id*. at ¶29(a).

  - Defendants did not hedge at least 90% of KFYield's portfolio using listed options. KFYield assets diverted to Lendacy accounted for more than 23% of KFYield's holdings between January 2015 and September 2019. And, Lendacy could not be hedged using listed options. *Id*. at ¶29(b).

  - Defendants used KFYield assets, not a separate funding source, to fund Lendacy and its undisclosed loans. Most investors were not told KFYield assets were used to fund their or others' Lendacy loans. *Id*. at ¶29(c).

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made. Nonetheless, the Complaint alleges oral and written misrepresentation, *see* DE 1 at ¶¶19, 24, 28(a)-(d), 30, and alleges that Defendants raised funds from at least 30 investors located mostly in Florida and Puerto Rico, *id*. at ¶27.

  - o KFYield's investment in Lendacy, the assets of which were unsecured loans primarily to Williams, significantly limits its ability to honor redemption requests to all investors equitably. *Id*. at ¶29(d).

- Defendants provided false account statements to investors regarding their holdings in Kinetic Funds. Kinetic Funds' known assets are less than the aggregate amount reflected on investor account statements. *Id*. at ¶30.

- Williams had ultimate authority for the false and misleading statements and omissions made orally and in documents provided to clients and prospective clients. *Id*. at ¶31.

The Complaint also describes Williams' misappropriation of investor funds:

- In April 2015, Williams used $37,000 of KFYield funds, routed to Lendacy, to pay off the mortgage on his relative's house. *Id*. at ¶33.

- In March 2017, Williams purchased for $1,512,575.50 three luxury apartments and two parking spaces for himself in San Juan, Puerto Rico. Williams used KFYield funds, diverted to Lendacy, to pay for the properties. *Id*. at ¶34.

- In May 2018, Williams used at least $2,755,000 of KFYield funds, routed to Lendacy in the form of a Lendacy loan, to purchase a historic bank building in Old San Juan, Puerto Rico. *Id*. at ¶36.

- In April 2019, Williams used $2,050,000 of additional KFYield funds in the form of two Lendacy loans to provide financial support to his outside business ventures. *Id*. at ¶37.

Furthermore, the Complaint pleads that Williams failed to disclose conflicts of interests to investors and prospective investors:

- Defendants transferred investor capital amounting to at least $9.1 million net to Lendacy, an entity owned by Williams. *Id*. at ¶39(a).

- Williams and two of his entities took unsecured, purported loans amounting to at least $6.8 million funded with KFYield assets. *Id*. at ¶39(b).

- Defendants used $30,872.44 of investor funds to pay Silexx Financial Systems, LLC ("Silexx"), another company that Williams partially owned and/or had a financial interest in. *Id*. at ¶30(c).

The SEC has more than met its low burden by identifying in its 88-paragraph Complaint the circumstances of Williams' fraud, thus satisfying Rule 9(b)'s pleading requirements. *See SEC v. Homa*, 2000 WL 1100783, at *3-4 (N.D. Ill. Aug. 4, 2000) (SEC "pleaded the who, what, when, where, and how of the fraud in sufficient detail" by setting forth the role of the defendants in the offerings, how the securities were marketed to investors nationwide, the time frames of the offerings, and the substance of the misrepresentations); *see also SEC v. Davison*, 8:20-cv-00325-MSS-AEP (M.D. Fla. March 8, 2021) (denying motion to dismiss where complaint alleged that PPMs, whose contents defendants controlled, contained misrepresentations and omissions about how investor funds would be used), attached hereto as **Exhibit "1"**; *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082 (2d Cir. 1972) ("We hold that the misappropriation of the proceeds [of a securities offering] is a garden variety type of fraud.").[4]

[4] Additionally, the law-of-the- case doctrine holds that "when a court decides upon a rule of law, that decision should continue to govern the same issues in subsequent stages in the same case." *Klay v. All Defendants*, 389 F. 3d 1191, 1197 (11th Cir. 2004), *quoting Christianson v. Colt Indus. Operating Corp.*, 486 U.S. 800, 816 (1988). Here, there has not been a change in the law since March 6, 2020, when the Court granted the SEC's Emergency Motion for Asset Freeze (DE 33) which, importantly, mirrors the factual allegations in the Complaint. *Compare* DE 1 *with* DE 2. The Court did not make any error of law in entering the freeze order, and there is no new evidence supporting Williams' challenges to the Complaint. *See Klay*, 389 F. 3d at 1197-98 (setting forth the elements for revisiting previously decided issues under the law-of-the-case doctrine).

III. The Complaint Sufficiently Pleads That Williams Violated the Antifraud Provisions of the Federal Securities Laws

Sections 17(a)(1)-(3) of the Securities Act of 1933 ("Securities Act"), § 10b of the Securities Exchange Act of 1934 ("Exchange Act") and Exchange Act Rule 10b-5(a)-(c) prohibit essentially the same type of conduct. *United States v. Naftalin,* 441 U.S. 768, 773 n. 4 (1979); *SEC v. Unique Financial Concepts,* 119 F. Supp. 2d 1332, 1339 (S.D. Fla. 1998), *aff'd,* 196 F.3d 1195 (11th Cir. 1999). The language of these provisions is "expansive" and "capture a wide range of conduct." *Lorenzo v. SEC*, 139 S. Ct. 1094, 1101-02 (2019). In *Lorenzo*, a case Williams curiously fails to cite in his motion, the Supreme Court recognized that there is "considerable overlap among the subsections of" Rule 10b-5 and § 17(a), and thus the same underlying conduct may establish a violation of more than one subsection. *Id.* at 1101-02 (knowing dissemination of misrepresentations with an intent to deceive violates Rule 10b-5(a) and (c) and § 17(a)(1)).

A violation of § 17(a)(1) requires: (1) a material misrepresentation or materially misleading omission; (2) in the offer or sale of securities; (3) made with scienter. *SEC v. Merchant Capital, LLC*, 483 F.3d 747, 766 (11th Cir. 2007). The elements for § 17(a)(2)-(3) are similar, except proof of mere negligence is sufficient to establish a violation. *SEC v. Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014).

A violation under § 10(b) requires: (1) a device, scheme, or artifice to defraud or materially false misrepresentations or misleading omissions; (2) in

connection with the purchase or sale of securities; (3) made with scienter. *Id*. at 1333-34. The SEC must also show the use of interstate commerce, the mails, or a national securities exchange. *SEC v. Corporate Relations Group*, 2003 WL 25570113, at *7 (M.D. Fla. March 28, 2003).[5]

Notably, facts showing a violation of § 17(a) and § 10(b) by an investment adviser will also support a violation of § 206 of the Investment Advisers Act of 1940 ("Advisers Act"). *SEC v. Berger,* 244 F. Supp. 2d 180, 188-89 (S.D.N.Y. 2001).

A. Williams' Fraud Occurred "In the Offer or Sale" and "In Connection With the Purchase or Sale" of a Security

The Supreme Court has counseled that § 17(a)'s "in the offer or sale" requirement is to be read broadly because the Securities Act was intended not just to protect investors, but also "to achieve a high standard of business ethics . . . in every facet of the securities industry." *Naftalin*, 441 U.S. at 773–75. It likewise has rejected a narrow interpretation of § 10(b)'s "in connection with the purchase or sale" requirement. *See SEC v. Zandford*, 535 U.S. 813, 819 (2002) ("[W]e have explained that [§ 10(b)] should be construed not technically and restrictively, but flexibly to effectuate its remedial purposes."); *Superintendent of Ins. of State of N.Y.*

[5] Williams argues the Complaint fails to allege which means or instrumentality of interstate commerce Defendants used or when. *See* DE 201 at p. 10, ¶11. But Williams provides no authority that notice pleading requires this information. The Complaint nonetheless alleges that Defendants used their websites to solicit investors. *See* DE 1 at ¶19; *see United States v. Hornaday*, 392 F.3d 1306, 1311 (11th Cir. 2004) ("[t]he internet is an instrumentality of interstate commerce.").

v. Bankers Life & Cas. Co., 404 U.S. 6, 12-13 (1971) (explaining that the "in connection with" requirement is satisfied where the deception "touch[es]" the transaction, even if the deception does not occur alongside the purchase or sale of securities).

1. Williams' Misappropriation of Investor Assets

Williams argues that his misappropriation of at least $6.3 million of investor assets fail to satisfy the "in connection with" requirement for Counts I, III-IV, VI-X, and XIII-XIV because it occurred after investors invested in KFYield. *See* DE 201 at p. 7, ¶3. This argument has no legs. *Zandford* involved a broker with discretionary authority to manage his clients' investment account. 535 U.S. at 815. The broker misappropriated his clients' funds by writing checks to himself from the clients' investment account, all the while knowing that redeeming the check would require the sale of securities from that account. *Id*. at 821. The defendant argued that the subsequent misappropriation did not have the requisite connection with the securities sales to state a 10(b) violation, but was more akin to simple theft of cash. *Id*. at 820. The Supreme Court rejected this argument, holding that the sales constituted a scheme to defraud. *Id*. at 821. It explained that the broker's breaches of fiduciary duty "coincide[d]" with the transactions and, thus, were "in connection with" securities sales. *Id*. at 825.

Similar to *Zandford*, Williams was able to siphon investor assets because he offered Kinetic Funds as an investment opportunity to investors and deployed

some of their capital to purchase securities in Kinetic Funds. But instead of deploying their entire capital for investment, Williams diverted a substantial portion to Lendacy in order to fund purported loans to himself. Thus, Williams' misappropriation of investor assets coincided with his securities offering and transactions and, thus, was made "in the offer or sale" and "in connection with the purchase or sale" of a security. *See Bankers Life*, 404 U.S. at *8, 12 (Section 10(b)'s "in connection with" requirement met where new owners of a corporation used the proceeds of a legitimate bond sale to cover a kited check they used to acquire the corporation's stock; "[s]ince there was a 'sale' of a security and since fraud was used 'in connection with' it, there is redress under [Section] 10(b)[.]").

2. Williams' Misrepresentations and Omissions

Williams claims that Counts II, V, XI-XII, as well as Counts I, III-IV, VI-X and XIII-XIV to the extent they are based on a misrepresentation or omission, fail to state a claim because the Complaint does not allege when *each* misrepresentation and omission occurred and, thus, that they were made "in connection" with an offer, purchase, or sale of a security. *See* DE 201 at p. 6-7, ¶2. Williams provides no authority that notice pleading requires this level of detail.

In any event, the Complaint sufficiently pleads the timeframe for Williams' misrepresentations and omissions. It alleges that he engaged in an unregistered fraudulent securities offering since 2013 (*see* DE 1 at ¶1); that since 2015, he

marketed Kinetic Funds with Lendacy and provided potential investors with Bloomberg reports about the KFYield strategy and its performance (*Id*. at ¶¶24-25); and that contrary to his representation that 90% of KFYield's portfolio is hedged using listed options, more than 23% of KFYield's holdings between January 2015 and September 2019 consisted of KFYield assets diverted to Lendacy, which could not be hedged using listed options (*Id*. at ¶¶28(b), 29(b)). *See Seville Indus. Mach. Corp. v. Southmost Mach. Corp.*, 742 F.2d 786, 791 (3d Cir. 1984), abrogated in part on other grounds by *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 557 (2007) ("Rule 9(b) requires plaintiffs to plead with particularity the "circumstances" of the alleged fraud in order to place the defendants on notice of the precise misconduct with which they are charged[.] It is certainly true that allegations of "date, place or time" fulfill these functions, but nothing in the rule requires them."); *SEC v. Kingdom Legacy General Partner, LLC*, 2017 WL 417093, at *4 (M.D. Fla. Jan. 31, 2017) ("To be sure, the Complaint does not list with exact temporal specificity the moment that each misrepresentation or omission was made. Even so, when the allegations are taken as true, it is clear the misrepresentations and omissions *were* made to potential and actual investors through a number of different channels, and that they were made on an ongoing basis from December 2010 to September 2015."). Furthermore, it is well established that reliance, damages, and loss causation are not required elements

of SEC civil enforcement actions, *see SEC v. Morgan Keegan & Co.*, 678 F.3d 1233, 1244 (11th Cir. 2012); therefore, precise temporal allegations are not critical.

Williams also suggests that, in order to meet the "in connection with" requirement, the misrepresentations and omissions must have occurred before the investors completed their purchases. *See* DE 201 at n. 8. But as discussed above, what matters is that the fraud "coincides", *Zandford*, 535 U.S. at 825, or "touches" the securities transaction, *Bankers Life*, 404 U.S. at 12-13. Plus, the Complaint alleges Williams made misrepresentations and omissions to investors *and* prospective investors as to the use of investor funds. *See* DE 1 at ¶¶28-29.

B. Williams Was the "Maker" of the False Statements and Omissions

Williams argues that the Complaint does not identify which defendant – him or Kinetic Group – made the alleged misrepresentations and omissions – as if it must be one or the other. *See* DE 201 at p. 4, n. 4. Williams has somehow missed the Supreme Court's holding in *Janus Capital Grp., Inc. v. First Derivative Traders*, that a person may be held primarily liable under § 10(b) and Rule 10b-5(b) for "making" a misleading statement if he or she had "ultimate authority over the statement, including its content and whether and how to communicate it." 564 U.S. 135, 142 (2011). As alleged in the Complaint, Williams *controlled* Kinetic Group (*see* DE 1 at ¶¶7-8) and, thus, was ultimately responsible for the misstatements and omissions made by it. *See Davison*, 8:20-cv-00325, at p. 8

(finding the SEC sufficiently pled that individual defendant was the "maker" of several misstatements in PPMs where he controlled their contents). Moreover, the Complaint specifically alleges that "Williams had ultimate authority for the false and misleading statements and omissions made orally and in documents provided to clients and prospective clients" (*Id*. at ¶31), including in Bloomberg reports, written marketing materials, brochures, and account statements (*Id*. at ¶¶24, 28(b), 28(d), 30). Therefore, it is clear that Williams is the maker of the misrepresentations and omissions made to investors and prospective investors, and the SEC adequately alleged this in its Complaint.

C. The Alleged Representations and Omissions Were False

Williams lodges a series of tortured arguments in an attempt to pass off his representations and omissions as non-fraudulent. None catch hold:

- Williams "told investors that their money would be invested in income-producing U.S. listed financial products"; this was false because Williams "did not invest all investor funds in U.S. listed financial products" and instead "invested a substantial portion of investor capital in Lendacy [which] is not a U.S. listed financial product." *See* DE 1 at ¶¶ 28(a), 29(a).

  Ignoring the plain allegations, Williams argues that what the Complaint really alleges is that Williams told investors that "KFYield assets" would be invested in U.S. listed financial products and this was false because "investor capital" was diverted to Lendacy. *See* DE 201 at p. 4. According to Williams, there can be no falsehood because "KFYield assets" and "investor capital" are two different things. *Id*. But it is Williams who is conflating concepts. The Complaint clearly premises Williams' misrepresentations on the difference between what he said he would do with investor funds and what he actually did with them.

- Williams argues that his diversion of investor funds to Lendacy does not render false his representation to investors that "their money would be invested in income-producing U.S. listed financial products" because the Complaint fails to allege that "all" investor funds would be so invested. *See* DE 201 at p. 5.

  But using the word "all" in that sentence is superfluous, particularly when the Complaint alleges his statement was false as he "did not invest *all* investor funds in U.S. listed financial products." *See* DE 1 at ¶29(a)(emphasis added).

- Williams told investors that 90% of KFYield's portfolio was hedged using listed options; this was false because KFYield assets diverted to Lendacy accounted for more than 23% of KFYield's holdings. *Id*. at ¶¶28(b), 29(b).

  Williams, however, argues that "[i]f 23% [of the portfolio] were unhedged, that would not render the alleged representation untrue." *See* DE 201 at p. 5. Math dictates otherwise. If 90% of the portfolio is supposed to be hedged with listed options, then that means only up to 10% – not 23% – could be unhedged.

- Williams led potential investors into believing Lendacy independently funded its loans and their entire capital would be invested in KFYield; this was false as Lendacy funded its loans with KFYield assets. *See* DE 1 at ¶¶28(c), 29(c).

  Williams counters, though, that because KFYield and Lendacy are distinct entities, then "by definition, Lendacy *did* have a separate funding source when *KFYield's* assets were used to fund *Lendacy's* loans." *See* DE 201 at p. 5 (emphasis in original). Williams' admission proves our case: the fact that Lendacy is a distinct, non-U.S. listed entity controlled by Williams means that it never should have received funding from KFYield.

- Williams "touted the liquidity of KFYield assets"; this was false because KFYield's investment in Lendacy limited its ability to honor redemption requests equitably and redemptions made would further concentrate KFYield's assets in its illiquid investment in Lendacy. *See* DE 1 at ¶¶ 28(d), 29(d).

  In response, Williams curiously argues that honoring some redemption requests by "wire" and others by "check" – as if that is the inequity at issue – would have no bearing on the liquidity of KFYield's assets. *See* DE 201 at p. 6. The point is that KFYield was not liquid and its ability to honor redemption

requests fairly was limited because a significant portion of its assets were tied up in unsecured Lendacy loans to Williams.

- Williams also misses the mark when challenging the falsity of the account statements he provided to investors. The Complaint does not allege, as Williams suggests, that reported investor "holdings" in Kinetic Funds were false because reported "assets" of Kinetic Funds were false. *See* DE 201 at p. 6.

  Rather, it alleges that "Defendants provided false account statements to investors regarding their holdings in Kinetic Funds" (*e.g.*, the actual holdings and value of such holdings) *and* the assets of Kinetic Funds. *See* DE 1 at ¶30.

D. Williams' Misrepresentations and Omissions Were Material

The test for materiality is "whether a reasonable man would attach importance to the fact misrepresented or omitted in determining his course of action." *SEC v. Monterosso*, 786 F. Supp. 2d 1255, 1263 (S.D. Fla. 2011), *aff'd* 756 F.3d 1326 (11th Cir. 2014). Williams' misrepresentations were clearly important to a reasonable person. Instead of investing investor funds as promised, he misappropriated them to the tune of at least $6.3 million. *See SEC v. Smart*, 678 F.3d 850, 857 (10th Cir. 2012) (the fact money was not being used as represented would be material to a reasonable investor); *SEC v. Reynolds*, 2010 WL 3943729, at *3 (N.D. Ga. Oct. 5, 2010) (misrepresentations that investor funds would remain in defendant's bank account until the transaction was approved were material).

E. Williams Acted With Scienter

Williams argues that "Counts I, IV-VIII, X, XII, and XIV fail to state a claim because Plaintiff has failed to allege Defendants acted with scienter." *See* DE 201

at p. 9, ¶9. According to Williams, the absence of the word "scienter" is fatal. *Id.* at n. 13. Yet, it is well-settled that scienter may be established by a showing of knowing misconduct or severe recklessness. *ZPR Inv. Mgmt. Inc. v. SEC*, 861 F.3d 1239, 1252 (11th Cir. 2017); *SEC v. Carriba Air Inc.*, 681 F.2d 1318, 1324 (11th Cir. 1982). To that end, the Complaint specifically alleges that Williams acted "knowingly or recklessly" in each of the challenged claims. *See* DE 1 at ¶¶43, 52, 55, 58, 62, 66, 72 and 85. It further sets forth the facts showing Williams scienter; *i.e.*, his misrepresentations regarding the use of investor funds, misappropriation of investor funds, and failure to disclose conflicts of interest. *See Kingdom Legacy*, 2017 WL 417093, at *6-7 (finding scienter adequately pled for 17(a)(1), 10(b) and Rule 10(b)-5 claims where complaint alleged misrepresentations and omissions regarding the funds' administrative charges and performance).

Continuing down the same spiral, Williams argues first that "Count II-III, IX, XI, and XIII — and X, XII, and XIV (with regard to the primary violation) – fail to state a claim because Plaintiff has failed to allege Defendants acted negligently", but next follows that up with: "Plaintiff conclusorily alleges 'Defendants' [] acted 'negligently' []." *See* DE 201 at p. 9, ¶10 and n. 14. Not only does Williams contradict himself, but each of those counts specifically allege that Defendants acted "negligently"[6] and each is sufficiently pled. *See Kingdom Legacy*, 2017 WL

[6] *See* DE 1 at ¶¶46, 49, 68, 75, 81, and as to the primary violations, 68, 75, and 81.

417093, at *7 (finding negligence sufficiently pled "because the Complaint explicitly alleges that Defendants negligently violated § 17(a)(2) and 17(a)(3).").

IV. The Complaint Sufficiently Pleads Williams' Aiding and Abetting of Kinetic Group's Primary Violations of the Advisers Act

In yet another misapprehension of the law, Williams argues that he cannot be held liable for Counts VIII, X and XIV for aiding and abetting Kinetic Group's primary violations of § 206(1), (2) and (4) of the Advisers Act and Advisers Act Rule 206(4)-8(a)(2).[7] *See* DE 201 at p. 10, ¶12. Williams claims that these provisions cover scheme liability and can only be violated when conduct, other than misrepresentations or omissions, are involved. From this faulty premise, Williams concludes that Kinetic Group's scheme liability must be predicated on his misappropriation of investor funds, but because he cannot aid and abet his own misappropriation, Counts VIII, X and XIV necessarily fail.

The Supreme Court already rejected this narrow view of the federal securities laws' antifraud provisions. *Lorenzo*, 139 S. Ct. at 1101 ("[b]y sending emails he understood to contain material untruths" the defendant employed a device, scheme, and artifice to defraud within the meaning Rule 10b-5(a), § 10(b), and § 17(a)(1) and engaged] in an act, practice, or course of business that operated

[7] Aiding and abetting requires: (1) a primary or independent securities law violation committed by another party; (2) awareness or knowledge by the aider and abettor that his or her role was part of an overall activity that was improper; and (3) that the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation. *See SEC v. Goble*, 682 F.3d 934, 947 (11th Cir. 2012); *Graham* v. *SEC,* 222 F.3d 994, 1000 (D.C. Cir. 2000).

as a fraud or deceit under Rule 10b-5(c)); *See Malouf v. SEC*, 933 F.3d 1248, 1263 (10th Cir. 2019) (Because misstatements could create scheme liability under § 17(a)(1) and Rule 10b-5(a) and (c) per *Lorenzo*, the defendant's failure to correct his investment advisory firm's misstatements could establish scheme liability under the nearly identical provisions of § 206(1) and (2) of the Advisers Act).

In accord with *Lorenzo* and *Malouf,* Kinetic Group's misrepresentations and omissions to investors establish its scheme liability under § 206(1), (2) and (4) of the Advisers Act and Advisers Act Rule 206(4)-8(a)(2).[8] Furthermore, the Complaint sufficiently alleges that Williams was aware of his role in the improper activity and knowingly and substantially assisted Kinetic Group's primary violations. Among other things, the Complaint alleges that Williams: (1) controlled Kinetic Group and the misrepresentations it told investors about Kinetic Funds' investment strategy, *see* DE 1 at ¶¶8, 31; (2) directed the transfer of investor assets to Lendacy, and then to his entities and third parties to fund personal expenses and his business ventures, *id*. at ¶¶29(a), 32-37; and (3) failed

[8] *IBEW Local 595 v. ADT Corp*., 660 Fed. App'x 850 (11th Cir. 2016)—the unpublished pre-*Lorenzo* case Williams relies upon for the proposition that deceptive conduct beyond misrepresentations is required to establish a scheme to defraud or a fraudulent course of conduct—is no longer good law in light of *Lorenzo*. *See SEC v. Kameli*, 2020 WL 2542154, *14 (N.D. Ill. May 19, 2020) (requirement that scheme liability requires conduct beyond misrepresentations "is no longer tenable . . . in light of . . . *Lorenzo*"); *SEC v. See ThruEquity, LLC*, 2019 WL 1998027, *5 (S.D.N.Y. Apr. 26, 2019) (rejecting defendants' argument that scheme liability allegations were defective for "fail[ing] to allege a deceptive act that is distinct from misstatements").

to disclose his ownership of Lendacy, *id*. at ¶¶39(a), 40, and use of investor assets to fund purported loans to himself, his entities, and others, *id*. at ¶¶39(b), 40.[9]

V. The Court Should Reject Williams' Frivolous One-Off Arguments

Williams advances several scattered arguments that are patently frivolous:

- Williams argues that Count II fails to allege that any of the purported misrepresentations and omissions were made 'to obtain money or property.'" *See* DE 201 at p. 8, ¶4. But ¶46 of Count II alleges exactly that: "Defendants . . . negligently *obtained money or property by means of untrue statements of material facts and omissions* . . . ".

- Williams argues that Counts VIII-XIV fail to plead Defendants were investment advisers." *See* DE 201 at p. 9, ¶7. Again, the Complaint (in ¶61) alleges precisely what Williams claims is missing: "Since at least 2013, Defendants, for compensation, engaged in the business of directly advising Kinetic Funds, and thus the potential and actual investors in Kinetic Funds, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities. *Defendants were therefore "investment advisers"* within the meaning of § 202(a)(11) of the Advisers Act, 15 U.S.C. § 80b-2(a)(11)." (emphasis added).

- Williams argues that Counts XI-XIV fail because the Complaint alleges Kinetic Funds was a "private pooled investment fund", as opposed to a "pooled investment vehicle". *See* DE 201 at p. 9, ¶8. Williams is off target again. Paragraph 74 of the Complaint alleges: "Kinetic Funds investments were 'pooled investment vehicles' within the meaning of Rule 206(4)-8(b) of the Advisers Act." Moreover, a "pooled investment vehicle" includes a "private pooled investment fund" such as Kinetic Funds.[10]

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[9] In another misfire, Williams mischaracterizes the aiding and abetting counts as a shotgun pleading. But in *Kingdom Legacy*, 2017 WL 417093, at *4, upon which he relies, the Court held that the complaint was not a shotgun pleading and explained that "[t]o the extent that the Complaint incorporates factual allegations into its claims, each of the allegations within the specified paragraph range relate to each securities fraud count." The same is true here: the aiding and abetting counts incorporate allegations related to the primary violation.

[10] *See Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles* (SEC Rel. No. IA-2628, 2007 WL 2239114, *3 Aug. 9, 2007) ("[Rule 206(4)-8(b)] defines a pooled investment vehicle as any investment company defined in section 3(a) of the Investment Company Act and any privately

- Williams argues that Counts I, III-IV, VI-X, and XIII-XIV fail because the Complaint does not identify the "specific" device, scheme, or artifice to defraud, or act, transaction, practice, or course of business that operates as a fraud. *See* DE 201 at p. 8, n. 10. Williams cites no authority that notice pleading requires this information. In any event, the Complaint does, in fact, describe Williams' scheme to defraud, *i.e.*, his misrepresentations and omissions, *see* DE 1 at ¶¶28-29, the false account statements, *id*. at ¶30, and the credit agreements he used to paper his purported loans, *id*. at ¶¶33, 35, 36-37.

- Williams similarly argues that Counts VII, VIII, IX, and X fail to allege that Defendants employed a scheme to defraud a client, *i.e.*, Kinetic Funds. *See* DE 201 at p. 8, ¶6. The Complaint, however, alleges that Williams acted against the interest of Kinetic Funds by misappropriating and misusing investor funds, and failing to disclose conflicts of interest to investors, and getting their consent before engaging in the conflicted transactions. *See* DE 1 at ¶¶32-38, 39-40; *SEC v. DiBella*, 587 F.3d 553, 568 (2d Cir. 2009).

- Williams plays a game of "gotcha" in arguing that the Complaint should be dismissed with prejudice because the time to amend has passed pursuant to the deadline in the scheduling order. Williams conveniently fails to mention that he never moved to dismiss the Complaint – but rather answered it (*see* DE 56) without asserting as affirmative defenses either failure to state a claim or to plead fraud with particularity – despite all of the Complaint's purported inadequacies that he now raises more than a year after its filing. Williams' disingenuous argument should be seen for what it is – gamesmanship – which the Court should reject. *See* DE 201 at p. 23-25.

CONCLUSION

The Court should deny Williams' motion for judgment on the pleadings.

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offered pooled investment vehicle that is excluded from the definition of investment company by reason of either section 3(c)(1) or 3(c)(7) of the Investment Company Act. As a result, the rule applies to advisers to hedge funds, private equity funds, venture capital funds, and other types of privately offered pools that invest in securities . . .").

March 26, 2021 Respectfully submitted,

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<u>CERTIFICATE OF SERVICE</u>

I HEREBY CERTIFY that on March 26, 2021, I electronically filed the foregoing document with the Clerk of the Court using CM/ECF. I also certify that the foregoing document is being served this day on all counsel of record via transmission of Notices of Electronic Filing generated by CM/ECF.

<u>/s/ Stephanie N. Moot</u>
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UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v. **Case No: 8:20-cv-325-MSS-AEP**

BRIAN DAVISON, BARRY M. RYBICKI, EQUIALT LLC, EQUIALT FUND, LLC, EQUIALT FUND II, LLC, EQUIALT FUND III, LLC, and EA SIP, LLC,

Defendants,

128 E. DAVIS BLVD, LLC, 310 78TH AVE, LLC, 551 3D AVE S, LLC, 604 WEST AZEELE, LLC, BLUE WATERS TI, LLC, 2101 W. CYPRESS, LLC, 2112 W. KENNEDY BLVD, LLC, BNAZ, LLC, BR SUPPORT SERVICES, LLC, CAPRI HAVEN, LLC, EANY,LLC, BUNGALOWS TI, LLC, EQUIALT 519 3RD AVE S., LLC, MCDONALD REVOCABLE LIVING TRUST, 5123 E. BROADWAY AVE, LLC, SILVER SANDS TI, LLC, and TB OLDEST HOUSE EST. 1842, LLC,

Relief Defendants.

ORDER

THIS CAUSE comes before the Court for consideration of Defendant Brian Davison's Motion to Dismiss the Amended Complaint, (Dkt. 177), and Plaintiff's

response in opposition thereto. (Dkt. 195) Upon consideration of all relevant filings, case law, and being otherwise fully advised, the Court **DENIES** the Motion to Dismiss the Amended Complaint.

I. BACKGROUND

A. Factual Background

The Securities and Exchange Commission ("SEC") brought this civil enforcement action, alleging that EquiAlt LLC—a real estate investment company controlled by Brian Davison and Barry Rybicki—defrauded investors who participated in EquiAlt's unregistered securities offerings. (Dkt. 1; Dkt. 138 at ¶ 1) The SEC alleges that Davison and Rybicki promised investors that (i) approximately 90% of investor money would be used to purchase real estate in distressed markets and (ii) the investments would generate fixed annual returns of 8% to 10%. (Dkt. 138 at ¶¶ 1, 46, 57) Instead, Davison and Rybicki allegedly "misappropriated millions in investor funds for their personal benefit." (Id. at ¶ 1)

EquiAlt began raising money from investors in 2011 through the sale of unregistered debentures issued by EquiAlt-managed funds. (Id. at ¶ 45) Beginning in 2016, EquiAlt allegedly operated as a Ponzi scheme, paying existing investors' monthly interest payments with funds raised from new investors. (Id. at ¶ 48) Meanwhile, Davison and Rybicki are alleged to have received millions of dollars in undisclosed cash distributions, funds they used "to purchase high-end luxury items." (Id. at ¶¶ 51-52)

The SEC alleges that Davison and Rybicki made several material misrepresentations and omissions to raise money from investors. (Id. at ¶¶ 57-82) Some of the alleged misrepresentations appeared in private placement memoranda ("PPMs") used to solicit investments. (E.g., id. at ¶ 57) Both Davison and Rybicki are alleged to have "controlled the content included in the PPMs," "review[ing], revis[ing], and ma[king] changes" to the offering documents. (Id. at ¶¶ 40, 57) According to the SEC, the PPMs for several of the funds stated that approximately 90% of investor funds would be used to "invest in property," when in fact "less than 50% of investor funds were actually used for that purpose." (Id. at ¶ 57) The SEC also alleges that the PPMs failed to adequately disclose, among other things, that (i) money raised for one fund would be used to pay investors in another fund, (ii) investor funds would be used to pay "substantial undisclosed commissions to unregistered sales agents," and (iii) Davison and Rybicki would receive "substantial improper" cash distributions. (Id. at ¶¶ 54-56, 63)

Some of the alleged misrepresentations were made orally and in EquiAlt marketing materials. For example, the SEC alleges that, "[w]hile pitching investments in the [f]unds," Davison and Rybicki represented that the investments were "low risk," "safe," and "conservative," when in fact the funds "ha[d] suffered substantial financial losses since their inception." (Id. at ¶ 72) Likewise, Davison and Rybicki allegedly "exercised control over the drafting of marketing materials and 'fact sheets' that falsely stated," among other things, that "assets are quickly brought to cash flowing (28 day

average)" and investors' "principal is not brokered or lent on someone else's asset." (Id. at ¶ 74)

B. Procedural History

The SEC commenced this civil enforcement action in February 2020, alleging that the conduct described above violated (i) Sections 5(a) and (c) of the Securities Act of 1933; (ii) Sections 17(a)(1), (2) and (3) of the Securities Act; (iii) Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder; (iv) Section 20(a) of the Exchange Act; and (v) Section 15(a) of the Exchange Act. (Dkts. 1, 138) The SEC sought and obtained a temporary restraining order, which was subsequently converted into a preliminary injunction that, among other things, forbade Defendants from violating the securities laws mentioned above during the pendency of this litigation. (Dkts. 10, 184) The Court also appointed a receiver to exercise authority over EquiAlt and the funds it managed. (Dkt. 11)

Now before the Court is Davison's Motion to Dismiss the Amended Complaint. (Dkt. 177)[1] Davison advances several arguments in support of dismissal, but his principal contention is that the fraud claims against him fail because he "did not communicate directly with investors and was not responsible for any misrepresentations that might have been made to them." (Id. at 3)

[1] The other Defendants have not moved to dismiss the Amended Complaint.

II. LEGAL STANDARD

The threshold for surviving a motion to dismiss for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6) is a low one. Quality Foods de Centro Am., S.A. v. Latin Am. Agribusiness Dev. Corp., S.A., et al., 711 F.2d 989, 995 (11th Cir. 1983). A plaintiff must plead only enough facts to state a claim to relief that is plausible on its face. Bell Atlantic Corp. v. Twombly, 127 S. Ct. 1955, 1968-69 (2007) (abrogating the "no set of facts" standard for evaluating a motion to dismiss established in Conley v. Gibson, 355 U.S. 41, 45-46 (1957)). Although a complaint challenged by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff is still obligated to provide the "grounds" for his entitlement to relief, and "a formulaic recitation of the elements of a cause of action will not do." Berry v. Budget Rent A Car Sys., Inc., 497 F. Supp. 2d 1361, 1364 (S.D. Fla. 2007) (quoting Twombly, 127 S. Ct. at 1964-65). In evaluating the sufficiency of a complaint in light of a motion to dismiss, the well pleaded facts must be accepted as true and construed in the light most favorable to the plaintiff. Quality Foods, 711 F.2d at 994-95. However, the court should not assume that the plaintiff can prove facts that were not alleged. Id. Thus, dismissal is warranted if, assuming the truth of the factual allegations of the plaintiff's complaint, there is a dispositive legal issue that precludes relief. Neitzke v. Williams, 490 U.S. 319, 326 (1989).

III. DISCUSSION

A. Rule 9(b)

Davison contends that the SEC has failed to plead fraud with the particularity required by Federal Rule of Civil Procedure 9(b). (Dkt. 177 at 9) Specifically, Davison argues that although "the Amended Complaint asserts that investors were misled, it does not contain the kind of detailed statements required to demonstrate that it was Davison who misled them, let alone specify the time or place of each such misstatement or identify the investors to which they were made." (Id.) This argument fails.

Rule 9(b) requires a party "alleging fraud or mistake" to "state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9(b). "The particularity rule serves an important purpose in fraud actions by alerting defendants to the precise misconduct with which they are charged and protecting defendants against spurious charges of immoral and fraudulent behavior." Ziemba v. Cascade Int'l, Inc., 256 F.3d 1194, 1202 (11th Cir. 2001). "The application of Rule 9(b), however, must not abrogate the concept of notice pleading." Id. "Rule 9(b) is satisfied if the complaint sets forth (1) precisely what statements were made in what documents or oral representations or what omissions were made, and (2) the time and place of each such statement and the person responsible for making (or, in the case of omissions, not making) same, and (3) the content of such statements and the manner in which they misled the plaintiff, and (4) what the defendants obtained as a

consequence of the fraud." Mizzaro v. Home Depot, Inc., 544 F.3d 1230, 1237 (11th Cir. 2008).

The allegations against Davison plead fraud with the particularity required by Rule 9(b). For example, the SEC alleges that the PPMs—whose content was "controlled" by Davison and Rybicki—contained several material misrepresentations and omissions. (E.g., Dkt. 138 at ¶¶ 57-60) Among other things, the PPMs are alleged to have "misrepresented how investor funds would be used" by stating that "approximately 90% of investor funds would be used to 'invest in property,'" when in fact "less than 50% of investor funds were actually used for that purpose." (Id. at ¶ 57) These allegations are sufficient to plead that Davison was responsible for a specific set of misrepresentations in the PPMs, thereby satisfying Rule 9(b)'s requirement to "plead the who, what, when, where, and how of the allegedly false statements." Mizzaro, 544 F.3d at 1237; see also Nichols v. Merrill Lynch, Pierce, Fenner & Smith, 706 F. Supp. 1309, 1344 (M.D. Tenn. 1989) ("Plaintiffs' reference to the PPM satisfies Rule 9(b)'s requirements as to identification of the time, place and content of the alleged misrepresentations.").

B. Section 10(b)

Davison also contends that the Section 10(b) claims should be dismissed because (i) the SEC fails to allege that Davison was the "maker" of any misstatement, (ii) "there are no allegations that Davison directly disseminated misleading materials to investors," (iii) the SEC fails to adequately plead materiality, and (iv) the SEC does not allege "facts that would, if true, demonstrate that Davison's conduct was 'in

connection with' the purchase or sale of securities." (Dkt. 177 at 11-15) None of these arguments is persuasive.

To state a claim under Rule 10b-5(b), the SEC must allege "(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).

Davison first contends that the SEC has failed to allege facts showing that he was the "maker" of any misstatements. (Dkt. 177 at 11) For purposes of Rule 10b-5(b), only the "maker" of a statement—meaning "the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it"—can be held liable for it. Janus Capital Grp., Inc. v. First Derivative Traders, 564 U.S. 135, 142-43 (2011). The SEC sufficiently alleges that Davison was the "maker" of several misstatements. For example, the SEC points to multiple misrepresentations in the PPMs, whose content Davison and Rybicki "controlled" by "review[ing], revis[ing], and ma[king] changes" to the documents. (Dkt. 138 at ¶¶ 40, 57) These allegations adequately plead that Davison exercised "authority over the content of the statement[s] [in the PPMs] and whether and how to communicate [them]." Janus Capital Grp., Inc., 564 U.S. at 144.

Next, Davison maintains that the claims under Rule 10b-5(a) and (c) fail because the SEC does not allege that "Davison directly disseminated misleading materials to investors." (Dkt. 177 at 14) "To state a claim under Rule 10b-5(a) or (c), the SEC must sufficiently allege that a defendant, with scienter, committed a

manipulative or deceptive act in furtherance of an alleged scheme to defraud that affected the market for securities or was otherwise in connection with their purchase or sale." SEC v. Glob. Dev. & Envtl. Res., Inc., No. 8:08-CV-993-T-27MAP, 2008 WL 11338454, at *3 (M.D. Fla. Nov. 26, 2008). A defendant may be found to have violated Rule 10b-5(a) or (c) if he "disseminate[s] false or misleading statements to potential investors with the intent to defraud." Lorenzo v. SEC, 139 S. Ct. 1094, 1099 (2019). Here, the SEC expressly alleges that both Davison and Rybicki "oversaw the distribution of the[ ] [PPMs]" while knowing that the documents "misrepresented how investor funds would be used." (Dkt. 138 at ¶ 57) This is sufficient to plead that Davison knowingly disseminated false statements to EquiAlt investors. See SEC v. Kameli, No. 17 C 4686, 2020 WL 2542154, at *15 (N.D. Ill. May 19, 2020) (holding that complaint adequately pled that defendants "disseminated the false/misleading statements" by alleging that defendants "approved the distribution of the PPMs and their attachments to prospective [ ] investors").

Davison also contends that, because the alleged oral misrepresentations "are contradicted by written disclosures," the SEC has failed to allege any material misstatements for purposes of its Section 10(b) claims. (Dkt. 177 at 14-15) For example, Davison points to the allegation that "EquiAlt falsely told investors in at least one [f]und [that] it was registered with the [SEC]," and claims this alleged oral misstatement is contradicted by the disclosure in the PPMs that the debentures were unregistered. (Id. at 7) "[A] misstatement or omission is material if there is a substantial likelihood that the disclosure of the omitted fact would have been viewed

by the reasonable investor as having significantly altered the total mix of information made available." SEC v. Morgan Keegan & Co., 678 F.3d 1233, 1245 (11th Cir. 2012). "Materiality [ ] is a question of fact that may rarely be resolved at the motion to dismiss stage." SEC v. BIH Corp., No. 2:10-CV-577-FTM-29, 2011 WL 3862530, at *5 (M.D. Fla. Aug. 31, 2011). Indeed, "whether written disclosures should trump oral misrepresentations is highly fact-specific." Morgan Keegan & Co., 678 F.3d at 1252. For example, written disclosures may not trump oral misrepresentations where "[t]he oral misrepresentations were made directly to customer-investors who aver they never received or knew about the written disclosures at the time of their purchases." Id. Here, the SEC alleges that "in many cases investors never received the PPMs" that contained the disclosures on which Davison relies. (Dkt. 138 at ¶ 63) Accordingly, the Court declines to determine at the pleading stage whether any disclosures in the PPMs neutralized the alleged oral misrepresentations. Davison may raise this fact-intensive issue at a later stage of the proceedings.

Davison also argues that the "SEC fails to allege facts that would, if true, demonstrate that [his] conduct was 'in connection with' the purchase or sale of securities." (Dkt. 177 at 15) "In SEC enforcement actions, courts broadly construe the 'in connection with' language to effectuate the securities statutes' remedial purposes and to protect investors." SEC v. Huff, 758 F. Supp. 2d 1288, 1353 (S.D. Fla. 2010), aff'd, 455 F. App'x 882 (11th Cir. 2012).[2] "[W]henever assertions are made . . . in a

[2] The Court notes that "[a]lthough an unpublished opinion is not binding on this court, it is persuasive authority. See 11th Cir. R. 36-2." United States v. Futrell, 209 F.3d 1286, 1289 (11th Cir. 2000).

manner reasonably calculated to influence the investing public, the 'in connection with' requirement is satisfied." Id. For example, the requirement is met if the misstatements "occurred in the context of public dissemination in a document such as a press release, annual report, investment prospectus or other such document on which an investor would presumably rely." Id. The allegations against Davison plainly satisfy the "in connection with" requirement. The SEC pleads that Davison was responsible for misrepresentations and omissions in, among other places, the PPMs—documents designed to solicit investments. (Dkt. 138 at ¶¶ 40, 57) No more is required to plausibly plead that Davison engaged in misconduct in connection with the sale of securities.[3]

C. Control Person Liability

Davison additionally contends that the SEC fails to plead control person liability under Section 20(a) of the Exchange Act because there are no allegations that "Davison controlled Rybicki or the sales agents." (Dkt. 177 at 16) This argument fails.

"[A] plaintiff alleging controlling person liability under [S]ection 20(a) must allege that (1) the defendant had the power to control the general affairs of the primary violator, and (2) the defendant had the power to control the specific corporate policy that resulted in the primary violation." Laperriere v. Vesta Ins. Grp., Inc., 526 F.3d 715, 723 (11th Cir. 2008). The allegations against Davison sufficiently plead that he

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[3] Davison also seeks dismissal of the Section 17(a) claims on the grounds that the SEC fails to plead that he committed fraud "in the offer or sale of securities." (Dkt. 177 at 15-16) Courts "have frequently treated" the phrases "in connection with the purchase or sale of a security" and "in the offer or sale of securities" as "interchangeable." SEC v. Mahabub, No. 15-CV-2118-WJM-MLC, 2017 WL 6555039, at *6 n.7 (D. Colo. Dec. 22, 2017). Accordingly, for the reasons explained above, the allegations against Davison sufficiently plead that he committed fraud "in the offer or sale of securities" for purposes of the Section 17(a) claims.

controlled both "the general affairs" of EquiAlt and "the specific corporate polic[ies] that resulted in the primary violation[s]." Id. Davison served as EquiAlt's CEO, "personally controll[ing] the bank accounts, finances, and accounting for each of the [f]unds" and managing "most of [the funds'] real estate activities and administrative activities." (Dkt. 138 at ¶ 10) Davison is also alleged to have (i) "controlled the content included in the PPMs" by "review[ing], revis[ing], and ma[king] changes" to the offering documents, and (ii) "misused millions of investors' dollars in a manner inconsistent with the PPMs and account statements provided to investors." (Id. at ¶¶ 40, 54, 57) These allegations, if true, would show that Davison both controlled EquiAlt and directed the fraudulent scheme that gave rise to this enforcement action, including by participating in the creation and dissemination of EquiAlt offering documents that contained material misrepresentations and omissions.

Davison responds that, because Rybicki "controlled the sales staff," "someone other than Davison [ ] controlled the persons committing the purportedly violative conduct." (Dkt. 177 at 17) Davison is correct that the SEC alleges that "Rybicki primarily controlled the sales force and communications with investors." (Dkt. 138 at ¶ 40) Davison ignores, however, that the "violative conduct" alleged in the Amended Complaint is not limited to oral misstatements made by the sales staff. As explained above, the SEC also alleges that Davison, the CEO of EquiAlt, was directly responsible for the company's distribution of PPMs that contained materially misleading statements and omissions. (Id. at ¶¶ 40, 54, 57) These allegations are

sufficient to plead control person liability against Davison for primary violations committed by EquiAlt and the funds it managed.

D. Section 5

Davison contends that the Section 5 claims fail because the SEC does not allege that he "was a 'necessary participant' and a 'substantial factor' in the sale of the unregistered securities at issue." (Dkt. 177 at 17).[4]

"In order to establish a prima facie case for a violation of [Section] 5 of the Securities Act, the SEC must demonstrate that (1) the defendant directly or indirectly sold or offered to sell securities; (2) through the use of interstate transportation or communication and the mails; (3) when no registration statement was in effect." SEC v. Calvo, 378 F.3d 1211, 1214 (11th Cir. 2004). "To demonstrate that a defendant sold securities, the SEC must prove that the defendant was a 'necessary participant' or 'substantial factor' in the illicit sale." Id. at 1215. "The defendant need not have directly sold the unregistered security" to be held liable for a Section 5 violation. SEC v. Curshen, 888 F. Supp. 2d 1299, 1308 (S.D. Fla. 2012). "Neither negligence nor scienter is an element of a prima facie case under Section 5 of the Securities Act." Id.

The SEC adequately alleges that Davison was both a "necessary participant" and a "substantial factor" in the sale of unregistered securities. Calvo, 378 F.3d at 1214. The SEC expressly alleges that the EquiAlt debentures were "unregistered securities." (Dkt. 138 at ¶ 3) The SEC further pleads that Davison—EquiAlt's CEO—

[4] Davison does not dispute that the SEC adequately alleges the debentures were unregistered.

played a significant role in the sale of these unregistered securities by, among other things, (i) "exercis[ing] control over the drafting of marketing materials and 'fact sheets'" distributed to investors and (ii) "controll[ing] the content included in the PPMs" used to solicit investments. (Id. at ¶¶ 40, 57, 74) Moreover, as the Court explained in granting the SEC's request for a preliminary injunction, Davison was a "controlling individual[ ]" of EquiAlt and allegedly "acted in concert [with Rybicki] to perpetrate the Ponzi scheme." (Dkt. 184 at 4) Taken together, these allegations are sufficient to state a Section 5 claim against Davison.

E. Aiding and Abetting Liability

Finally, Davison maintains that the SEC fails to state an aiding-and-abetting claim against him because "the Amended Complaint is devoid of allegations that [he] 'knowingly and substantially assisted' the purportedly violative conduct of Rybicki and the sales staff Rybicki supervised." (Dkt. 177 at 17) This argument lacks merit.

"[T]o impose aiding and abetting liability under [Section] 20(e) there must be: (1) a primary violation of the securities laws; (2) the aider and abettor must have knowledge of the primary violation; and (3) the aider and abettor must provide substantial assistance in the commission of the primary violation." SEC v. Goble, 682 F.3d 934, 947 (11th Cir. 2012). Here, the primary violation that serves as the basis for the aiding-and-abetting claim is that third-party sales agents solicited investments in EquiAlt funds despite not being registered with the SEC or associated with a registered broker-dealer. (Dkt. 138 at ¶¶ 111-12) This conduct allegedly violated Section 15(a) of

the Exchange Act, which "makes it unlawful . . . for an unregistered dealer to purchase or sell securities." SEC v. Almagarby, 479 F. Supp. 3d 1266, 1271 (S.D. Fla. 2020).

The SEC sufficiently alleges that Davison knowingly provided "substantial assistance in the commission of" the alleged primary violation. Goble, 682 F.3d at 947. For example, the SEC pleads that although Davison and Rybicki learned from multiple sources that "the [f]unds could only be sold by a registered broker-dealer," they nevertheless "chose to ignore these warnings and continued to willfully and intentionally violate the registration laws and to inform third-party sales agents that they did not need to be registered to sell the [f]unds." (Dkt. 138 at ¶ 81; see also id. at ¶ 47 ("Davison and Rybicki misrepresented to outside sales agents that it was permissible for these agents to sell these securities while not registered with state and federal regulatory authorities.")) These allegations are sufficient to state an aiding-and-abetting claim against Davison.[5]

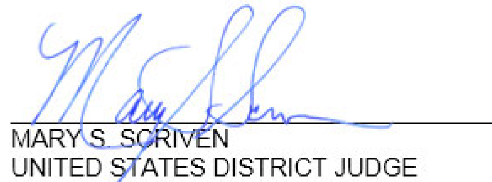
[5] In his Motion, Davison contends that the SEC's request for injunctive relief should be "denied" because "there is no likelihood of the purported wrong continuing." (Dkt. 177 at 20-21) The Court considered and rejected the same argument in granting the SEC's request for a preliminary injunction, and there is no basis to revisit that ruling. (Dkt. 184)

IV. CONCLUSION

Upon consideration of the foregoing, it is hereby **ORDERED** as follows:

1. Defendant Brian Davison's Motion to Dismiss the Amended Complaint, (Dkt. 177), is **DENIED**.
2. Davison shall file an answer to the Amended Complaint within **twenty-one (21) days** of the date of this Order.

DONE and ORDERED in Tampa, Florida this 8th day of March 2021.



MARY S. SCRIVEN
UNITED STATES DISTRICT JUDGE

Copies furnished to:
Counsel of Record
Any Unrepresented Party