B. Scott Whipple (OSB # 983750)
Email: swhipple@whippleduyck.com
Whipple & Duyck, PC
1500 SW First Avenue, Suite 1170
Portland, OR 97201
Telephone: 503-222-6004
Facsimile: 503-222-6029

William Douglas Sprague (admitted *pro hac vice*)
Email: dsprague@cov.com
Tammy Albarran (admitted *pro hac vice*)
Email: talbarran@cov.com
Ashley M. Simonsen (admitted *pro hac vice*)
Email: asimonsen@cov.com
Covington & Burling LLP
One Front Street
San Francisco, CA 94111-5356
Telephone: 415-591-6000
Facsimile: 415-591-6091

Attorneys for Defendant N. Scott Gillis

UNITED STATES DISTRICT COURT

DISTRICT OF OREGON

PORTLAND DIVISION

SECURITIES AND EXCHANGE COMMISSION, Plaintiff,	Case No. 3:16-cv-00438-PK
v.	**DEFENDANT N. SCOTT GILLIS'S MOTION TO DISMISS**
AEQUITAS MANAGEMENT, LLC; AEQUITAS HOLDINGS, LLC; AEQUITAS COMMERCIAL FINANCE, INC.; AEQUITAS CAPITAL MANAGEMENT, INC.; AEQUITAS INVESTMENT MANAGEMENT, LCC; ROBERT J. JESENIK; BRIAN A. OLIVER; and **N. SCOTT GILLIS**, Defendants.	**REQUEST FOR ORAL ARGUMENT**

1600438160510000000000001

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

CERTIFICATE OF COMPLIANCE WITH LOCAL RULE 7-1

In compliance with Local Rule 7-1, counsel for defendant N. Scott Gillis certify that they conferred in good faith by telephone conference on May 2, 2016, with counsel for the Securities and Exchange Commission ("SEC"), but that the parties were unable to resolve this dispute without the assistance of the Court.

DEFENDANT N. SCOTT GILLIS'S MOTION TO DISMISS

Pursuant to Federal Rules of Civil Procedure 9(b) and 12(b)(6), Mr. Gillis moves this Court for an order dismissing with prejudice Claims One through Four, Six, Eight, Ten, and Twelve (all claims alleged against Mr. Gillis) of the SEC's Complaint ("Compl.") on the grounds that they fail to state a claim upon which relief can be granted against Mr. Gillis or, in the alternative, for an order requiring a more definite statement under Federal Rule of Civil Procedure 12(e). This motion to dismiss is supported by the following memorandum of law and the accompanying Declaration of Ashley Simonsen ("Simonsen Decl.") and attached exhibits, as well as the documents on file with the Court and such further evidence and argument as the Court may permit. Mr. Gillis requests oral argument on this motion.

MEMORANDUM OF LAW

I. INTRODUCTION

One of the eight defendants named in the SEC's shotgun pleading in this case is N. Scott Gillis—a man who did not join Aequitas Capital Finance, LLC ("ACF") until months after most of the alleged misstatements set forth in the Complaint were made and months after the alleged "scheme to defraud" had been operating; did not assume the title of Chief Financial Officer until several months after he joined ACF; and stayed at ACF for one year. Even after he joined, the SEC does not allege that Mr. Gillis prepared or distributed any of the documents alleged to contain material misstatements and omissions. Nor does the Complaint identify any deceptive conduct *by Mr. Gillis* that could have furthered any alleged scheme to defraud during his brief tenure at ACF. Instead, the SEC tries to satisfy the strict pleading requirements of Rule 9(b) with repeated assertions that certain actions were taken or statements were made (or not made) by other defendants "with Gillis's knowledge in 2015." *See* Compl. ¶¶ 44, 53, 56, 59, 63. These vague and conclusory allegations cannot sustain any of the SEC's claims against Mr. Gillis.

The Complaint should be dismissed in its entirety as to Mr. Gillis. *First*, the SEC's shotgun pleading—incorporating 79 paragraphs of lengthy factual allegations into each of twelve different causes of action asserted against eight defendants—is improper. It provides no notice to Mr. Gillis as to what he is alleged to have done that could support any of the eight claims asserted against him. Because the SEC has failed to connect the facts alleged with the claims asserted in a manner sufficient to satisfy Rule 9(b), the Court should dismiss the Complaint.

Second, the SEC fails to state a claim against Mr. Gillis for aiding and abetting any alleged material misstatement or omission (Claims Six, Eight, Ten, and Twelve) for several reasons. Although the SEC alleges that (other) defendants made misstatements or failed to disclose material information to investors, the SEC makes almost no effort to identify—as it must—the specific statements in specific documents that it contends were misleading, whether on their face or as a result of an alleged omission. Indeed, in several instances, the alleged misstatement was accurate or the allegedly omitted facts were disclosed. The SEC also improperly seeks to hold Mr. Gillis liable for alleged misstatements and omissions in documents that were prepared (1) before Mr. Gillis even joined ACF or (2) with no alleged knowledge or assistance from him. There is no basis for secondary liability against Mr. Gillis.

Third, the SEC fails to state a claim for primary or secondary scheme liability against Mr. Gillis (Claims One through Four, Ten, and Twelve[1]) because it fails to allege with the requisite particularity, as it must to hold any defendant primarily liable, any "scheme to defraud" that is distinct from the alleged misstatements and omissions. Claims One and Three for primary scheme liability against Mr. Gillis fail for the additional reason that the SEC fails to allege with the requisite particularity any deceptive or manipulative act *by Mr. Gillis* in furtherance of the purported scheme.

II. BACKGROUND[2]

A. The Aequitas Group of Companies and Entity Defendants

Defendant Robert J. Jesenik founded the "Aequitas group of companies" over twenty years ago, in 1993. Compl. ¶ 21. Among these companies are defendant ACF and a series of

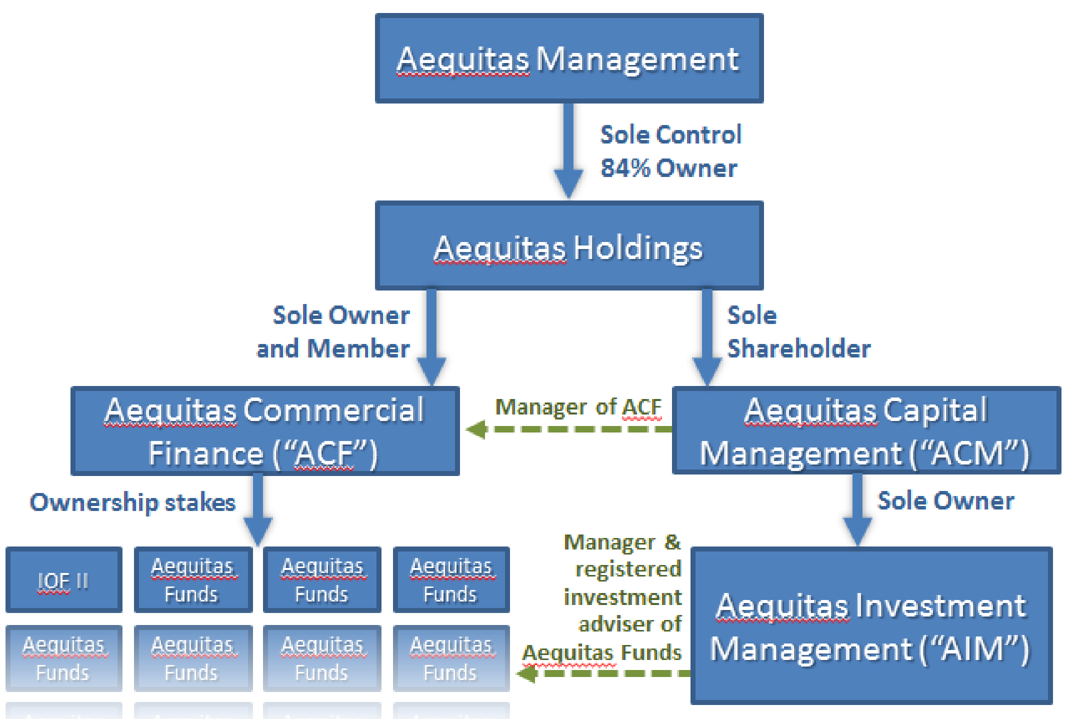
[1] Claims Ten and Twelve are analyzed both as scheme claims and also as misstatements and omissions claims for the reasons explained *infra* n.7.

[2] This summary is based on the factual allegations of the Complaint, which must be taken as true for purposes of this motion but which are not admitted by Mr. Gillis, and documents cited therein. Those documents are attached as exhibits to the Declaration of Ashley Simonsen ("Simonsen Decl."), filed concurrently herewith. This Court may consider these documents because they are incorporated by reference into the Complaint. *See Marder v. Lopez,* 450 F.3d 445, 448 (9th Cir. 2006); *Lee v. City of L.A.*, 250 F.3d 668, 688 (9th Cir. 2001). The Court may disregard the SEC's allegations about the content of these documents if contradicted by the documents themselves. *See Sprewell v. Golden State Warriors*, 266 F.3d 979, 988 (9th Cir. 2001) *amended on other grounds*, 275 F.3d 1187 (9th Cir. 2001).

affiliated investment funds, referred to in the Complaint as the "Aequitas Funds." *Id.* ¶ 2. The largest of these funds is the Aequitas Income Opportunity Fund II, LLC ("IOF II"). *Id.* ¶ 30.

Defendant ACF and the Aequitas Funds invested, directly or indirectly, in portfolios of loans, leases, and trade receivables in the healthcare, education, transportation, and consumer credit sectors. *Id.* ¶¶ 1, 17, 20, 33; *see* Simonsen Decl. Ex. A at 2; *id.* Ex. E at 2. They raised funds for these investments by issuing promissory notes to investors. Compl. ¶ 2. Defendant Aequitas Investment Management, LLC ("AIM") was the manager and registered investment advisor for the Aequitas Funds. *Id.* ¶¶ 19, 21. Defendant Aequitas Capital Management, Inc. ("ACM") was the manager of ACF, and the sole owner and member of AIM. *Id.* ¶¶ 18, 21.

The entities at the top of the Aequitas structure (depicted in the chart below) are defendants Aequitas Management, LLC ("Aequitas Management") and Aequitas Holdings, LLC ("Aequitas Holdings"). *Id.* ¶ 21. Aequitas Management owns 84% of Aequitas Holdings; Aequitas Holdings, in turn, owns ACF and ACM. *Id.* ¶¶ 15-16, 21.



B. The Individual Defendants

Defendant Robert Jesenik was the Chief Executive Officer and President of Aequitas Management, Aequitas Holdings, ACF, ACM, and AIM (collectively, the "Entity Defendants"), and Chief Investment Officer of ACM and AIM. *Id.* ¶ 12. Mr. Jesenik was a 35% owner of Aequitas Management. *Id.*

Defendant Brian Oliver was an Executive Vice President of the Entity Defendants and a 25% owner of Aequitas Management. *Id.* ¶ 13. Mr. Oliver was allegedly the primary fundraiser for ACF and the Aequitas Funds and a member of the management committees responsible for selecting or approving their investments. *Id.* Mr. Oliver allegedly met regularly with prospective investors and Registered Investment Advisors ("RIAs") about investing in ACF and the Aequitas Funds; those RIAs, in turn, recommended the notes to their clients. *Id.* ¶ 29.

Defendant N. Scott Gillis did not join ACF until 2015. *Id.* ¶ 14. For a brief period from approximately late April 2015 to January 2016, Mr. Gillis was the CFO of ACF, ACM, and AIM, *id.*; another individual, not mentioned by name in the Complaint, was the CFO when the alleged "scheme to defraud" began and during most of its alleged operation. Mr. Gillis also held the titles of Chief Operating Officer of ACF, ACM, and AIM and Executive Vice President of the Entity Defendants from approximately January 2015 to January 2016, at which point he left ACF. *Id.* Importantly, the Complaint alleges incorrectly that Mr. Gillis was a 10% owner of Aequitas Management, *id.*; he had no ownership interest in that company.

C. The Public Placement Memoranda

At the time of their initial investment, investors in ACF or the Aequitas Funds received a Public Placement Memorandum ("PPM"). *Id.* ¶¶ 25, 28, 32. The Complaint alleges that Mr. Jesenik had ultimate approval authority over the disclosures contained in the PPMs and the distribution of the PPMs to investors. *Id.* ¶¶ 25, 31. Mr. Oliver allegedly oversaw distribution of the PPMs to prospective investors and sometimes personally sent PPMs and other offering materials to prospective investors. *Id.* ¶¶ 29, 32. The Complaint does not allege that Mr. Gillis had any knowledge of the content of the PPMs or any role in their preparation or distribution.

The Complaint focuses on a PPM for ACF dated November 2013 (the "ACF PPM") and a PPM for IOF II apparently dated October 2014 (the "IOF II PPM"), both of which were prepared long before Mr. Gillis joined the Aequitas Funds. *See id.* ¶¶ 25, 31. Each PPM was replete with warnings that investment in the notes involved a "significant" and "high degree" of risk, including risk of loss of a noteholder's entire investment and investment concentration and illiquidity risks. *See* Simonsen Decl. Ex. A at cover, i, 4, 9, 24, App. A; *id.* Ex. E at cover, i, 8, 14, 31, App. A.

The IOF II PPM explained how proceeds raised from new investors were to be used:

> **The Manager of the Fund will have broad discretion over the use of the proceeds of the Offering**
>
> The Manager will have broad discretion in determining how the proceeds of the Offering will be used. The Fund expects to use the proceeds from the sale of Senior Notes to acquire Portfolio Assets, *to pay obligations with respect to Senior Notes and for Organizational Expenses and Operating Costs*.

Id. Ex. E at App. A at 19 (emphasis added); *see also id.* Ex. E at 6 (disclosing "the issuance of additional Senior Notes" as one of three "Sources of Repayment" for the notes). Similarly, the ACF PPM provides that ACF

> uses proceeds from the issuance of Secured Notes to engage in various specialty financing transactions, to provide senior and junior debt and equity funding for the benefit of its affiliates and its related investment programs *and to repay previously issued Secured Notes*. These activities include but are not limited to: . . .
>
> *Providing working capital and operating liquidity lines of credit to [ACF] and its affiliates*, including . . . investments in funds managed by [AIM].

> [ACF] generally pays the principal and interest of Secured Notes from the proceeds from repayments of loans, leases, subordinated debt investments and similar assets of the Company and sales of Company assets. *From time to time, the Company may use proceeds of the sale of Secured Notes to repay the principal and interest of previously issued Secured Notes* . . . .

Id. Ex. A at 3 (emphasis added), 6-7 (same); *see* Compl. ¶ 27.

D. The Quarterly Updates and the Holdings Note

In addition to the PPMs, ACF and the Aequitas Funds also sent one-page quarterly updates to investors. Compl. ¶ 28; *see, e.g.*, Simonsen Decl. Exs. B-D, F-G. The Complaint focuses on quarterly updates that were issued from the second quarter of 2014 through the second quarter of 2015. *See* Compl. ¶¶ 57, 61.[3] The SEC alleges that Jesenik and Oliver approved the content and distribution of the quarterly updates; Mr. Gillis's only alleged involvement was approval of the "financial information" in the first and second quarter 2015 updates. *Id.* ¶¶ 28, 33.

The ACF quarterly updates contain, *inter alia*, a one-paragraph description of ACF and the allocation of ACF's assets by book value, including its trade receivable assets. *See* Compl. ¶ 33; *see* Simonsen Decl. Exs. B-D. Among the assets listed in the ACF quarterly updates was "Corporate Equity," which reflected an intercompany loan from ACF to Aequitas Holdings (the "Holdings Note"). *See, e.g.*, Simonsen Decl. Ex. D; Compl. ¶¶ 46, 51. The SEC alleges that the Holdings Note was used primarily as a means of moving cash from ACF to Aequitas Management, ACM, and another Aequitas affiliate to cover operating expenses. Compl. ¶ 48. Mr. Gillis is not alleged to have had any involvement in the making of the intercompany loan,

[3] The SEC does not specify which of the 2014 quarterly updates it contends were misleading. *See* Compl. ¶ 28. However, the circumstances allegedly concealed from investors arose (according to the Complaint) in July 2014—*after* the quarterly update for the first quarter of 2014 would have been prepared. *See id.* ¶ 55. The SEC does not appear to contend that the quarterly updates for the third quarter of 2015 or thereafter were misleading. *See id.* ¶¶ 57, 61.

which occurred long before he joined the company. *See id.* ¶¶ 14, 47. The Complaint does not allege anything deceptive or unlawful about the intercompany loan itself.

The stated value of the assets disclosed in the ACF quarterly updates, including the Holdings Note and ACF's trade receivable assets, was expressly identified as their "book value." *See, e.g.*, Simonsen Decl. Ex. C; *see also id.* Ex. C at n.1 ("Book value of assets is not an indication of liquidation value. In the event of a sale of assets, the cost basis or book value of the underlying investments may or may not be realized."). The book value of the Holdings Note was also reflected on ACF's books, which were audited by an independent third party audit firm at year-end. *See id.* Ex. C at n. 5; Compl. ¶¶ 28, 46.

According to the Complaint, ACF used the outstanding balance of the Holdings Note as its book value. Compl. ¶ 73. The SEC does not contend that the outstanding balance of the Holdings Note or the book value of ACF's trade receivable assets (as reflected on ACF's books and/or in its quarterly updates) was inaccurate. Nor does the SEC allege anything improper with respect to the 2014 year-end audit of ACF's books. Rather, the SEC contends that the amount of unpledged collateral securing the Holdings Note and ACF's trade receivable assets—referred to in the Complaint as their "fair value"—should have been disclosed to investors. *Id.* ¶¶ 46, 59-60, 73. The SEC suggests that failure to disclose the fair value of the Holdings Note operated to "conceal the insolvency of the companies" in 2014 and 2015. *See id.* ¶ 46.

E. Default of Corinthian Colleges and ACF's Collapse

The Complaint focuses on an 18-month period following the default of Corinthian Colleges on payment obligations it owed to ACF in June of 2014—seven months *before* Mr. Gillis joined ACF. *See id.* ¶¶ 14, 34-36. At that time, ACF's receivables investments were allegedly heavily concentrated in student loan debt that had been purchased from Corinthian and that Corinthian had agreed to guarantee. *Id.* ¶ 35.

Corinthian's default in June 2014 allegedly left ACF with a cash shortfall for the payment of (1) operating expenses and (2) redemptions and interest to prior investors. *Id.* ¶¶ 4-5, 37, 40. Around this time and continuing through 2015, the SEC alleges, "Jesenik and Oliver began to issue" short-term ACF notes and IOF II notes. *Id.* ¶¶ 41, 53.[4] The Complaint does not allege any involvement by Mr. Gillis in the issuance of or decision to issue any of these notes, either before or after he joined the company.

ACF also issued notes to IOF II around this time. *Id.* ¶¶ 63-64. According to the Complaint, Jesenik and Oliver used the money that was loaned from IOF II to ACF for these notes to pay operating expenses and to cover redemptions and interest payments to prior investors. *Id.* The SEC alleges that by July 2014, or six months before Mr. Gillis joined the company, Jesenik and Oliver were using "the vast majority of investor money" for these purposes. *Id.* ¶ 55. The SEC contends that this should have been disclosed to investors in ACF and the Aequitas Funds, and that defendants' alleged failure to do so rendered statements in the quarterly updates and PPMs materially misleading, while simultaneously constituting a "scheme to defraud." *See id.* ¶¶ 1, 53, 56-57.

The SEC alleges that beginning in early 2015, the notes issued by ACF to IOF II were not fully collateralized by unpledged trade receivables owned by ACF, *id.* ¶¶ 65, 67; the "vast majority" of ACF's trade receivable assets had been pledged as security for other debt, *id.* ¶ 60; and Aequitas Holdings had just $67.0 million in assets available as collateral for the $127.6

---

[4] The Complaint alleges that Jesenik and Oliver raised $350 million through ACF and the Aequitas Funds between January 2014 and January 2016, *id.* ¶ 45, but does not specify how much of this was raised *after* mid-2014, when the purported "scheme to defraud" is alleged to have begun—let alone after Mr. Gillis joined the company or became CFO in about April 2015. *See id.* ¶¶ 39, 44, 55. The Complaint alleges only that Jesenik and Oliver raised $23.7 million through the issuance of ACF notes from July to November 2014, *id.* ¶ 41, and $70 million through the issuance of IOF II notes in 2015, *id.* ¶ 62.

million then outstanding on the Holdings Note, *id.* ¶ 51. The SEC does not contend that there was anything independently deceptive or unlawful about the alleged under-collateralization of these assets; rather, the SEC contends that it should have been disclosed. *See id.* ¶¶ 46, 68.

In July 2015, in connection with securing a line of credit, ACF obtained a legal opinion that it was not required to register with the SEC as an investment company under the Investment Company Act of 1940. *Id.* ¶ 69. The legal opinion relied on an exemption from registration that requires 55% of a company's overall business to consist of a type that qualifies under the exemption. *Id.* ¶ 71. At that time, the ratio of ACF's qualifying to non-qualifying assets was 56%. *Id.* ¶ 73. This ratio was calculated using the "fair value" of the Holdings Note, *as required under the Investment Company Act*. *Id.*; *see* 15 U.S.C. § 80a-2(a)(41)(A) (requiring assets for which market quotations are not readily available to be valued at their "fair value"). Mr. Gillis therefore signed a certification stating that, using the "fair value" of the assets (in accordance with the Investment Company Act), ACF held at least 55% in qualifying asset, and the legal opinion was obtained. *See* Compl. ¶¶ 73-76. The SEC does not allege that there was anything improper about avoiding registration as an investment company or valuing the Holdings Note at its fair value; indeed, the statute required that it be valued that way. Nor does the SEC allege that the certification or legal opinion were ever discussed with or distributed to investors.

According to the Complaint, the alleged misstatements and omissions on which the SEC's claims are based were corrected or disclosed in December 2015. *See id.* ¶¶ 57, 61.

III. LEGAL STANDARDS

A complaint must be dismissed under Rule 12(b)(6) if it lacks sufficient facts to "state a claim to relief that is plausible on its face." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). This "facial plausibility" standard requires factual allegations that add up to "more than a sheer possibility that a defendant has acted unlawfully." *Id.*; *see Bell Atl. Corp. v. Twombly*, 550 U.S.

544, 555 (2007) (factual allegations must "raise a right to relief above the speculative level"). While allegations of fact in the Complaint must be assumed to be true, the Court need not accept as true "allegations that are merely conclusory, unwarranted deductions of fact, or unreasonable inferences." *In re Gilead Scis. Sec. Litig.*, 536 F.3d 1049, 1055 (9th Cir. 2008). Nor is the Court required to "assume the truth of legal conclusions merely because they are cast in the form of factual allegations." *Fayer v. Vaughn*, 649 F.3d 1061, 1064 (9th Cir. 2011).

Rule 9(b) applies to all of the SEC's claims because the entire complaint sounds in fraud. *See Kearns v. Ford Motor Co.*, 567 F.3d 1120, 1125 (9th Cir. 2009). Rule 9(b) requires that the Complaint state "the who, what, when, where, and how of the misconduct charged." *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1106 (9th Cir. 2003). The complaint also "must set forth, as part of the circumstances constituting fraud, an explanation as to why [any] disputed statement was untrue or misleading *when made*." *Fecht v. Price Co.*, 70 F.3d 1078, 1082 (9th Cir. 1995) (emphasis in original); *Rieckborn v. Jefferies LLC*, 81 F. Supp. 3d 902, 913 (N.D. Cal. 2015) (same). The SEC's fraud claims also require allegations of scienter, which the Supreme Court has defined as "a mental state embracing intent to deceive, manipulate, or defraud." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 319 (2007).[5]

IV. ARGUMENT

A. The Complaint Constitutes an Impermissible "Shotgun" Pleading.

The SEC's Complaint should be dismissed as an impermissible shotgun pleading. "Shotgun pleadings are those that incorporate every antecedent allegation by reference into each subsequent claim for relief or affirmative defense." *Wagner v. First Horizon Pharm. Corp.*, 464

[5] The SEC may argue that negligence is sufficient under Sections 17(a)(2) and 17(a)(3) of the Securities Act of 1933 ("Securities Act") and Section 206(2) of the Investment Advisers Act of 1940 ("Advisers Act") and Rule 206(4)-8 thereunder, but its claims are based entirely on fraud; indeed, the term "negligence" appears nowhere in the Complaint.

F.3d 1273, 1279 (11th Cir. 2006). Shotgun pleadings "do[] not meet Rule 9(b)'s particularity requirement." *SEC v. Fraser*, 2009 WL 2450508, at *14 (D. Ariz. Aug. 11, 2009). That is because, to give proper notice, the factual allegations of a complaint "must be tied directly to each individual count." *SEC v. Solow*, 2007 WL 917269, at *3 (S.D. Fla. Mar. 23, 2007). "[C]ourts cannot perform their gatekeeping function with regard to . . . averments of fraud" when plaintiffs fail to "connect[] their facts to their claims." *Wagner*, 464 F.3d at 1279-80.

Courts regularly dismiss such shotgun pleadings by the SEC.[6] For example, in *Fraser*, the complaint "sets forth a lengthy narrative facts section, next incorporates the facts section into each claim by reference, and then simply states that 'defendants' violated various provisions of the securities laws 'by engaging in the conduct alleged above.'" 2009 WL 2450508, at *13. The court dismissed the complaint because it

> ma[de] no attempt to lay out which conduct constitutes the violations alleged. Rather, the claims sections simply paraphrase or quote the language of the statutes and rules, leaving Defendants (and the Court) with the task of combing the Complaint and inferring, rightly or wrongly, what specific conduct the SEC intended to assert as a violation.

Id. at *14; *see also Solow*, 2007 WL 917269, at *2-4 (dismissing SEC's securities fraud complaint because there was "no linkage between the facts summary and the substantive counts"); *SEC v. Patel*, 2009 WL 2015794, at *2 (D.N.H. July 7, 2009) (directing the SEC to present its allegations "defendant by defendant, and distinct legal theory by distinct legal theory, pointing out, element by element, the specific factual allegations pled in the amended complaint (by paragraph number) that support each claim"); *SEC v. Levin*, 2013 WL 594736, at *8 (S.D.

[6] Courts have also required plaintiffs to provide a more definite statement pursuant to Rule 12(e). *See, e.g.*, *Wagner*, 464 F.3d at 1280. In the alternative to dismissal, Mr. Gillis moves for a more definite statement under Rule 12(e).

Fla. Feb. 14, 2013) (holding that SEC's shotgun pleading "fail[ed] to give adequate notice to each Defendant of the respective bases underlying each of the SEC's claims against them").

The Complaint here suffers from the same infirmities as the SEC's shotgun pleadings in *Fraser*, *Solow*, *Patel*, and *Levin*. After setting forth 79 paragraphs of lengthy factual allegations, the Complaint then incorporates every single one of them by reference into every one of twelve causes of action against various combinations of eight different defendants. Compl. at 18-27. It connects none of those allegations to any specific cause of action or element thereof, let alone a particular defendant. *See Wagner*, 464 F.3d at 1279 ("The central problem is that the factual particularity of the first 175 paragraphs is not connected to the otherwise generally pled claim in any meaningful way."). Nor does it specify which allegations support the SEC's primary liability claims as opposed to its aiding and abetting claims. This is textbook shotgun pleading.

Indeed, the majority of allegations against Mr. Gillis consist entirely of the conclusory allegation that certain actions were taken or statements made (or not made) by other defendants "with Gillis's knowledge in 2015," *see* Compl. ¶¶ 44, 53, 56, 59, 63—an assertion that, even if supported by the factual allegations of the Complaint, could not sustain *any* of the SEC's theories of liability against him. A defendant's mere awareness that others may be deceiving investors (which Mr. Gillis did not have), without contributing in any way to that deception, is not actionable under the securities laws. *See infra* Parts IV.B-C. As a result, Mr. Gillis and this Court are left to guess as to what Mr. Gillis is alleged to have done during his one year at ACF—during only some of which he held the title of CFO—that could support the eight claims asserted against him.

The SEC's burden of matching its factual allegations to its legal theories is especially pronounced in this case where it has been investigating this matter behind closed doors for some time. *See SEC v. Tambone*, 417 F. Supp. 2d 127, 131 (D. Mass. 2006) (applying "the particularity requirements in [a] rigorous manner" where the SEC conducted extensive discovery); *SEC v. Parnes*, 2001 WL 1658275, at *5 (S.D.N.Y. Dec. 26, 2001) (after three years of discovery and investigation, SEC had no excuse for failing to meet pleading requirements). The SEC has failed to connect the facts alleged in the Complaint with the claims asserted in a manner sufficient to satisfy Rule 9(b); the Complaint should be dismissed.

B. The Complaint Fails to State a Claim that Mr. Gillis Aided and Abetted Any of the Alleged Misstatements or Omissions (Claims Six, Eight, Ten and Twelve).

Claims Six, Eight, Ten, and Twelve of the Complaint assert that Mr. Gillis aided and abetted alleged misstatements and omissions by ACF, ACM, and AIM in the PPMs and quarterly updates.[7] To state a claim for a primary violation based on alleged misstatements and omissions, the SEC must allege with particularity (1) a material misstatement or omission (2) made with scienter (3) in connection with the offer or sale of a security (4) by means of interstate commerce. *See SEC v. Dain Rauscher, Inc.*, 254 F.3d 852, 855-56 (9th Cir. 2001); *see also SEC v. Phan*, 500 F.3d 895, 907-908 (9th Cir. 2007); *SEC v. Quan*, 2013 WL 5566252, at *16 (D. Minn. Oct. 8, 2013).

A misstatement is a statement that was "untrue or misleading *when made*." *Fecht*, 70 F.3d at 1082 (emphasis in original). However, an omission of fact, even one that is material, does not subject a defendant to liability unless there is a duty to disclose. *See, e.g.*, *Basic Inc. v.*

[7] These claims are asserted under Section 17(a)(2) of the Securities Act (Claim Six); Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5(b) thereunder (Claim Eight); Sections 206(1) and (2) of the Advisers Act (Claim Ten); and Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder (Claim Twelve). While Claims Six and Eight are premised entirely on alleged misstatements and omissions, Claims Ten and Twelve may be premised on both misstatements and omissions and also an alleged scheme to defraud. *See* Compl. ¶¶ 114, 126-127. Mr. Gillis therefore analyzes these claims here and also in Part IV.C below (addressing scheme liability).

Levinson, 485 U.S. 224, 230-31 (1988); *SEC v. Fehn*, 97 F.3d 1276, 1289 (9th Cir. 1996); *Greenberg v. Cooper Cos.*, 2013 WL 100206, at *10 (N.D. Cal. Jan. 7, 2013). To trigger the duty to disclose, the SEC "must show that the omission actually renders *other statements* misleading." *City of Roseville Emps.' Ret. Sys. v. Sterling Fin. Corp.*, 963 F. Supp. 2d 1092, 1109 (E.D. Wash. 2013) (emphasis added); *Fehn*, 97 F.3d at 1290 n.12.

To state a claim for aiding and abetting liability, the SEC must allege (1) an independent primary violation; (2) actual knowledge by Mr. Gillis of the primary violation and of his own role in furthering it;[8] and (3) "substantial assistance" by Mr. Gillis in the commission of the primary violation. *Fehn*, 97 F.3d at 1288; *SEC v. Daifotis*, 2011 WL 2183314, at *8 (N.D. Cal. June 6, 2011), *modified on other grounds*, 2011 WL 3295139 (N.D. Cal. Aug. 1, 2011). The SEC's conclusory allegation throughout the Complaint that alleged misstatements and omissions were made "with Gillis's knowledge in 2015," *see* Compl. ¶¶ 44, 53, 56, 59, must be "grounded in some facts." *See In re Worlds of Wonder Sec. Litig.*, 694 F. Supp. 1427, 1433 (N.D. Cal. 1988).[9] "[A]llegations that a securities-fraud defendant, because of his position within the company, must have known a statement was false or misleading are precisely the types of inferences which courts, on numerous occasions, have determined to be inadequate to withstand

[8] Recklessness is sufficient under the Dodd-Frank Act. *See* 15 U.S.C. §§ 78t(e), 77o(b), 80b-9(f).

[9] *See also SEC v. Hopper*, 2006 WL 778640, at *8 (S.D. Tex. Mar. 24, 2006) ("Rule 9(b) requires more than a simple allegation that a defendant had fraudulent intent. To plead scienter adequately, the SEC must set forth specific facts that support an inference of fraud."); *Scognamillo v. Credit Suisse First Boston LLC*, 2005 WL 2045807, at *5 (N.D. Cal. Aug. 25, 2005) ("The Court need not accept as true such conclusory allegations where, as here, Plaintiffs have pointed to no specific factual allegations regarding [the defendants'] knowledge.") *aff'd*, 254 F. App'x 669 (9th Cir. 2007); *Cammer v. Bloom*, 711 F. Supp. 1264, 1299-1300 (D.N.J. 1989) (finding insufficient the SEC's "broad conclusory allegation" that the defendant knowingly participated in the issuance of false and misleading statements to the investing public).

Rule 9(b) scrutiny." *In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 539 (3d Cir. 1999), *abrogated on other grounds by Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 325 (2007) (internal marks omitted).

To plead substantial assistance, the SEC must allege facts sufficient to show that Mr. Gillis "associated himself with the venture, participated in it as something that he wished to bring about, and sought by his action to make it succeed." *SEC v. Apuzzo*, 689 F.3d 204, 214 (2d Cir. 2012). In other words, Mr. Gillis must be alleged to have "consciously assisted the commission of the specific [violation] in some active way." *Id.* at 212 n.8 (quoting *United States v. Ogando*, 547 F.3d 102, 107 (2d Cir. 2008)); *see, e.g.*, *Ponce v. SEC*, 345 F.3d 722, 738 (9th Cir. 2003) (allegations that accountant prepared misleading financial statements that were eventually filed with quarterly and annual reports adequately pled substantial assistance); *Fehn*, 97 F.3d at 1293-94 (where attorney allegedly had a "hand in the editing" and "personally altered" an allegedly false and misleading report filed with the SEC, substantial assistance was adequately pled). "[M]ere awareness and approval" of the primary violation is insufficient to make out a claim for substantial assistance. *SEC v. Baxter*, 2007 WL 2013958, at *9 (N.D. Cal. July 11, 2007).

Here, as best Mr. Gillis is able to discern from the shotgun Complaint, the SEC alleges that ACF, ACM, and AIM (via Jesenik and/or Oliver, not Mr. Gillis) made material misstatements and omissions regarding (1) the alleged primary use of investor funds to pay operating expenses and to repay prior investors and (2) the alleged under-collateralization of the Holdings Note and notes issued by ACF and the Aequitas Funds. *See, e.g.*, Compl. ¶ 5. Depending on the particular document(s) in which the alleged misstatement or omission is alleged to have appeared (if any such document is specified), each alleged misstatement or omission suffers from one or more of the following fatal defects:

- The alleged misstatement or omission is not pled with the requisite particularity under Rule 9(b) (*e.g.*, every alleged misstatement and omission in the "Aequitas Funds" PPMs and quarterly updates);
- The alleged misstatement or omission was not false or misleading at the time it was made and did not become misleading in 2014 or 2015 (*e.g.*, every alleged misstatement and omission in the ACF PPM and IOF II PPM and the financial information in the ACF quarterly updates); and/or
- The alleged misstatement or omission was not made with Mr. Gillis's knowledge or substantial assistance (*e.g.*, every alleged misstatement and omission in the PPMs and the first paragraph of the quarterly updates).

1. The Alleged Misstatements or Omissions Regarding the Use of Investor Proceeds Provide No Basis for Liability Against Mr. Gillis.

The Complaint fails to state a claim that Mr. Gillis aided and abetted any alleged misstatements or omissions in the ACF PPM, Aequitas Funds PPMs, or quarterly updates regarding the alleged use of investor funds to pay operating expenses and to repay prior notes.

a. ACF PPM

The SEC contends that the alleged use of new investor proceeds to repay prior notes during an 18-month period in 2014-2015 rendered misleading the ACF PPM's statement that such payments would be made "from time to time." Compl. ¶ 56. This theory of liability is insufficiently pled for three reasons.

First, the SEC does not allege that the statement was misleading *when made*. *Fecht*, 70 F.3d at 1082. Rather, the SEC contends that the ACF PPM became misleading in mid-2014 when Jesenik and Oliver allegedly began using new investor proceeds to repay prior notes. *See* Compl. ¶ 55. However, the statements in the ACF PPM were not made in 2014 (or 2015); they were made in November 2013. *See id.* ¶ 25; Simonsen Decl. Ex. A at cover. Indeed, the PPM expressly provided that "all statements made herein are made as of the date of" the PPM, and that none of its forward-looking statements would be updated or revised to reflect future conditions, which "may require actions that differ from those contemplated at this time." *Id.* Ex. A at ii-iv. The PPM further explained that the "affairs of [ACF]" may have changed since the date on which the statements in the PPM were made, and that delivery of the PPM after that date should not be construed to mean otherwise. *Id.* at iii.

Another district court recently rejected any duty to update a PPM containing similar cautionary language. In *Seaman v. California Business Bank*, 2013 WL 5890726 (N.D. Cal. Oct. 30, 2013), the plaintiff alleged that the defendant bank maintained a duty to update statements characterizing the state of its loan portfolio and loss reserves in a PPM dated September 28, 2010. *Id.* at *5. The *Seaman* court held that there could be no duty to update because the PPM specifically stated, "NOTHING CONTAINED HEREIN IS, OR SHOULD BE RELIED UPON AS, A PROMISE OR REPRESENTATION AS TO THE FUTURE PERFORMANCE OF THE BANK." *Id.* As a result, "the PPM only characterize[d] the bank's financial condition as of September 28"; and the plaintiff therefore failed to show that the statement was false or misleading when made. *Id.*; *see also Mercury Air Grp., Inc. v. Mansour*, 237 F.3d 542, 547, 547 n.4 (5th Cir. 2001) (defendant had no duty to update because, *inter alia*, document disclosed that company "did not intend to update or otherwise revise the projections").

Like the PPM at issue in *Seaman*, the ACF PPM expressly disclaimed any duty to update any statements therein should circumstances change. Any new use – or, in this case, purportedly more frequent use – to which investor proceeds allegedly were put beginning in mid-2014 cannot have rendered any statement in the PPM retroactively misleading; such "fraud by hindsight" allegations are not actionable. *Jackson v. Fischer*, 2015 WL 1143582, at *9 (N.D. Cal. Mar. 13, 2015); *see also Ronconi v. Larkin*, 253 F.3d 423, 430 (9th Cir. 2001) (statements not misleading, because the statements must have been "known to be false or misleading at that time by the people who made them," and "[t]he complaint does not plead facts that show that company insiders knew what the complaint says 'would' occur in what was then the future").[10]

Second, the alleged misstatement did not become materially misleading in 2014-2015. The ACF PPM expressly discloses that ACF uses proceeds from the issuance of notes "to repay previously issued Secured Notes" and to provide "operating liquidity lines of credit" to ACF and its affiliates. Simonsen Decl. Ex. A at 3. This is unsurprising, since the liquidity and concentration risks inherent in ACF's investment strategy, and expressly disclosed in the PPM, *see id.* Ex. A at App. A at 3, 9, naturally could have led to cash shortfalls. The PPM also states:

> From time to time, the Company may use proceeds of the sale of Secured Notes to repay the principal and interest of previously issued Secured Notes . . . .

Id. Ex. A at 3. According to the SEC, the language "[f]rom time to time" was misleading because, by July 2014, ACF was "generally" using investor proceeds to repay prior notes. Compl. ¶ 56. No explanation is offered for how the "general[]" use of investor proceeds for this expressly disclosed purpose is inconsistent with such use "from time to time." *See Fecht*, 70 F.3d at 1082 (a fraud complaint must set forth "an explanation as to why [any] disputed statement was untrue or misleading").

Furthermore, no investor could reasonably have relied on the PPM's vague "from time to time" language to connote some specific limitation on this use of investor proceeds—particularly where the previous paragraph disclosed unequivocally that investor proceeds would be used for this purpose. *See San Diego Cty. Emps. Ret. Ass'n v. Maounis*, 749 F. Supp. 2d 104, 122 (S.D.N.Y. 2010) (statements that fund allegedly operating as a single-strategy natural gas fund

---

[10] Even if the ACF PPM did not contain express disclaimers, "[n]either the Supreme Court nor the Ninth Circuit have endorsed an affirmative duty to update or correct past statements." *Seaman*, 2014 WL 1339649, at *5; *see In re Foxhollow Techs., Inc. Sec. Litig.*, 359 F. App'x 802, 804 (9th Cir. 2009).

was "diversifi[ed]" were not misleading where, among other disclosures, the PPM qualified that "[t]he Manager is not subject to any formal diversification requirements, and the Fund's portfolio may *from time to time* be concentrated in a limited number of positions or strategies." (emphasis added)). "[F]ederal courts everywhere have demonstrated a willingness to find immaterial as a matter of law . . . statements that are so vague, [and] so lacking in specificity, . . . that no reasonable investor could find them important to the total mix of information available." *City of Monroe Emps. Ret. Sys. v. Bridgestone Corp.*, 399 F.3d 651, 669 (6th Cir. 2005).

Even if "from time to time" could reasonably be interpreted to place some specific limit on the frequency with which investor proceeds could be used to repay prior notes, the 18-month period over which this allegedly occurred in the span of ACF's 13-year existence (and ACM's 23-year existence) fell within it. The Complaint does not allege anything irregular about ACF's operations during the first 10 years of its existence (beginning in 2003), and recognizes that the company was profitable from 2011 to 2013. *See* Compl. ¶¶ 17, 34. Nor does the Complaint allege anything improper, prior to 2014, with respect to ACM (formed in 1993). *See id.* ¶¶ 18, 19. On these alleged facts, even if the alleged misstatement in the ACF PPM was "made" in 2014 or 2015 (it was not), the SEC has still failed to allege that it was materially false or misleading in any way.

Third, even if the alleged misstatement was materially misleading (it was not), the Complaint fails to allege a single fact to support the inference that Mr. Gillis had actual knowledge of (or was reckless with respect to) the statement's falsity or substantially assisted it. *Fehn*, 97 F.3d at 1288. Indeed, the SEC's own allegations establish that Mr. Gillis played no role in the preparation or distribution of any of the PPMs. *See* Compl. ¶¶ 25, 29, 31-32. He was not even employed by ACF until after the contents of the ACF and IOF II PPM were finalized.

See id. ¶¶ 14, 25; Simonsen Decl. Exs. A, E (covers). Any alleged misstatements therein accordingly can provide no basis for liability against Mr. Gillis.

b. Aequitas Funds PPMs

According to the Complaint, the alleged use of investor proceeds to pay operating expenses and prior notes was "contrary to the disclosures provided to investors in the Aequitas Funds." Compl. ¶ 56. Nowhere in the Complaint does the SEC identify the "time, place, and specific content" of these disclosures, as required under Rule 9(b). *Edwards v. Marin Park, Inc.*, 356 F.3d 1058, 1066 (9th Cir. 2004). The SEC's general allegation that the Aequitas Funds PPMs "state that investment proceeds will be used for the direct or indirect purchase of trade receivables," Compl. ¶ 31—even if it were misleading—is not enough; the SEC must allege "the misleading language relied upon *in each individual PPM*, as well as the facts relied upon to demonstrate that each statement was fraudulent." *Baskin v. Lagone*, 1993 WL 59781, at *4 (S.D.N.Y. Mar. 3, 1993) (emphasis added) (finding general allegations of misrepresentations and omissions contained in seven different PPMs insufficient); *Town N. Bank, N.A. v. Shay Fin. Servs., Inc.*, 2014 WL 4851558, at *19 (N.D. Tex. Sept. 30, 2014) (where pleading "refers generally to information in the offering documents regarding risk, but fails to identify the specific statements in the offering documents alleged to be misleading due to the omissions," omissions were not adequately alleged under Rule 9(b)). Having failed to do so, any alleged misstatements in or omissions from the "Aequitas Funds PPMs" fail under Rule 9(b).

The SEC identifies a specific alleged misstatement in the IOF II PPM that "proceeds will be used to invest, directly or indirectly, in a portfolio of receivables in various sectors." *See* Compl. ¶ 31. However, it overlooks the PPM's concurrent disclosure that the Fund "expects" to use investor proceeds "to pay obligations with respect to Senior Notes and for Organizational Expenses and Operating Costs"; and that one of three "Sources of Repayment" for the notes would be "the issuance of additional Senior Notes." Simonsen Decl. Ex. E at 6, App. A at 19. Thus, in the one Aequitas Fund PPM in which the SEC identifies a specific statement, the PPM disclosed exactly what the SEC contends was omitted.

The Complaint also alleges that the IOF II PPM states that investor proceeds may be used to make loans to ACF "for the purpose of investing in receivables," Compl. ¶ 31, but that "[d]uring . . . 2015" defendants used such loan funds to pay operating expenses and to repay prior notes, *id.* ¶¶ 62-63. However, the statements in the IOF II PPM were not made in 2015; they were made in October 2014. *See* Simonsen Decl. Ex. E at iii ("all statements made herein are made as of the date of [this PPM]"). Just like the ACF PPM, the IOF II PPM expressly disclaimed any obligation to update the PPM in the future should circumstances change. *See id.* Ex. E at iii-iv, App. A at 5. Accordingly, and because the SEC does not contend that this alleged misstatement was misleading as of October 2014, it cannot support a primary violation for which Mr. Gillis could be secondarily liable. *Fecht*, 70 F.3d at 1082; *see Seaman*, 2013 WL 5890726, at *5.

Furthermore, the SEC fails to allege with the requisite particularity how the statement *became* materially misleading in 2015, where the IOF II PPM expressly disclosed that investor funds could be used not only to invest in trade receivables, but also to pay prior notes and operating expenses. *See* Simonsen Decl. Ex. E at 6, App. A at 19. Whether this happened through IOF II or through ACF (via a loan from IOF II) is immaterial; that investor proceeds may be used to repay prior notes or to pay operating expenses was disclosed. Thus, the Complaint fails to plead a primary violation.

Even if a primary violation had been adequately pled, the SEC fails to allege that Mr. Gillis substantially assisted the making of any statements in any PPM with the requisite scienter. *See supra* Part IV.B.1.a. Accordingly, any alleged misstatement therein cannot support an aiding and abetting claim against Mr. Gillis.

c. Quarterly Updates

The Complaint alleges that the quarterly updates "failed to disclose that the primary use of investor funds was to repay investors or to cover the operating expenses of the Aequitas enterprise" in 2014 and 2015. Compl. ¶ 57. However, the Complaint does not identify a single statement in any of the Aequitas Funds quarterly updates that was rendered misleading as a result of defendants' alleged failure to disclose the alleged "primary use" of investor funds, failing under Rule 9(b). *Baskin*, 1993 WL 59781, at *4. Indeed, the IOF II quarterly updates say nothing about the "primary" use of investor funds. *See* Simonsen Decl. Exs. F-G. Accordingly, the SEC has failed sufficiently to plead that the alleged omission rendered any statement therein misleading. *See Fehn*, 97 F.3d at 1290 n.12. Without a predicate violation, there is no basis for secondary liability against Mr. Gillis based on alleged misstatements or omissions in the Aequitas Funds quarterly updates.

The Complaint also alleges that the ACF quarterly updates "falsely stat[ed] in 2015 that ACF was using investor money primarily to purchase receivables." Compl. ¶ 5.[11] Nowhere in the Complaint does the SEC even attempt to allege that Mr. Gillis "consciously assisted the commission of the [violation] in some active way." *Apuzzo*, 689 F.3d at 212 n.8. The only information in the quarterly updates that Mr. Gillis is even alleged to have *seen* was the financial information, which he merely "approved." Compl. ¶¶ 28, 33. There is no allegation that he was even aware of anything else that was stated in the quarterly updates—including the introductory paragraph explaining how investor proceeds were used. *Id.*; *see, e.g.*, Simonsen Decl. Ex. D.

[11] The ACF quarterly update for the third quarter of 2015 disclosed that ACF "uses proceeds from Private Note[s] primarily to repay prior investors." *Id.* ¶ 57; *see* Simonsen Decl. Ex. D.

For these reasons, Mr. Gillis cannot have aided and abetted any alleged misstatement about the "primary" use of investor proceeds in the quarterly updates.

2. The SEC Fails to Allege With the Requisite Particularity Any Duty to Disclose the Alleged Under-Collateralization of Certain Assets.

The Complaint fails to state a claim that Mr. Gillis aided and abetted any alleged misstatements or omissions regarding the alleged under-collateralization of the Holdings Note or investor notes in the ACF quarterly updates, the IOF II PPM, or any other document.

a. ACF Quarterly Updates

The Complaint alleges that defendants failed to disclose (1) that only a "fraction" of ACF's trade receivable assets were secured by unpledged receivables in the quarterly updates, Compl. ¶ 60; or (2) that the outstanding balance of the Holdings Note far exceeded the assets of Aequitas Holdings available to satisfy it, *id.* ¶ 46. According to the SEC, defendants "acted to conceal the insolvency of the companies" by listing the Holdings Note on ACF's "books" according to its outstanding balance (rather than its "fair value"). *Id.*; *see id.* ¶¶ 73, 76.

However, the quarterly updates made no representations about the amount of unpledged receivables securing ACF's trade receivable assets or the Holdings Note, the fair value of the Holdings Note, or the solvency or financial stability of ACF, such that these alleged omissions could render any statements therein misleading; nor does the SEC identify any specific statement in ACF's "books" (or any other document) that it contends was rendered misleading as a result of carrying the Holdings Note according to its outstanding balance. Companies are "not required to disclose a fact merely because a reasonable investor would very much like to know that fact." *Dalberth v. Xerox Corp.*, 766 F.3d 172, 183 (2d Cir. 2014).

The *only* information disclosed in the quarterly updates about the Holdings Note and ACF's trade receivable assets was their "book value" (or "cost basis")—clearly identified as such. *See* Simonsen Decl. Exs. B-C. The SEC does not contend that the disclosed book value was inaccurate. Nor does the SEC explain how failing to disclose the amount of unpledged assets backing these assets could possibly have rendered this information misleading—particularly because quarterly updates for 2015 expressly clarified that

> Book value of assets is not an indication of liquidation value. In the event of a sale of assets, the cost basis or book value of the underlying investments may or may not be realized.
> . . .
> The assets held in Corporate Equity [including the Holdings Note] include equity investments which are internally fair valued by Aequitas. Year-end valuations are audited by an independent third party audit firm.

Simonsen Decl. Exs. C-D at nn. 1, 5; *see also id.* Ex. A at App. A at 7 (explaining that "[t]he book value of . . . collateral should not be relied upon as a measure of realizable value for such assets"). On these undisputed facts, the SEC fails to plead with the requisite particularity that any statements in the quarterly updates, ACF's "books," or elsewhere were rendered misleading as a result of the alleged under-collateralization omissions.

b. IOF II PPM

According to the Complaint, the IOF II PPM states that any loan from IOF II to ACF would be collateralized by unpledged trade receivables held by ACF; but that "beginning in early 2015," IOF II transferred funds to ACF (in exchange for notes) despite the fact that ACF no longer held sufficient trade receivables with which to collateralize the loan. Compl. ¶ 65. However, the statements in the IOF II PPM (like the ACF PPM) were not made in 2015; they were made in October 2014, as explained *supra* Part IV.B.1.a-b. Accordingly, and because the SEC contends only that this statement *became* misleading in 2015, it cannot support a primary violation for which Mr. Gillis could be secondarily liable.

Even if the statements in the IOF II PPM had been made in early 2015, the PPM expressly provides that if ACF borrows funds from other affiliated entities, IOF II "may have overlapping security interests" with the affiliated entities in the collateral. Simonsen Decl. Ex. E at 17-18; *see also id.* at 22 (same). In fact, the PPM expressly discloses that affiliated entities' security interests "would reduce or eliminate the value of [IOF II's] security interests." *Id.* at 20; *id.* at 23 (same). Because the IOF II PPM disclosed exactly what the SEC contends was omitted, it could not have been misleading—even if the statements therein were deemed to have been made in 2015.

Finally, even if a primary violation had been adequately pled, the SEC fails to allege that Mr. Gillis substantially assisted the making of *any* statements in the IOF II with the requisite scienter. *See supra* Part IV.B.1.a-b. Accordingly, any alleged misstatement therein cannot support an aiding and abetting claim against Mr. Gillis.

C. The Complaint Fails to Allege Deceptive Conduct to Support a Claim Against Mr. Gillis for Scheme Liability or Aiding and Abetting Any Scheme to Defraud (Claims One Through Four, Ten and Twelve).

The SEC asserts in Claims One through Four, Ten, and Twelve of the Complaint that Mr. Gillis participated in and aided and abetted a purported "scheme to defraud."[12] To state a claim for primary scheme liability, the SEC must allege that the defendant (1) "committed a deceptive or manipulative act . . . in furtherance of the alleged scheme to defraud" (2) "with scienter." *SEC v. Lucent Techs., Inc.*, 610 F. Supp. 2d 342, 350 (D.N.J. 2009); *Quan*, 2013 WL 5566252, at *16; *see also In re Galena Biopharma, Inc. Sec. Litig.*, 117 F. Supp. 3d 1145, 1192 (D. Or. 2015). The SEC's aiding and abetting claims against Mr. Gillis are, of course, dependent

[12] The alleged primary violations against Mr. Gillis are asserted under Sections 17(a)(1) and (3) of the Securities Act (Claim One) and Section 10(b) of the Exchange Act and Rules 10b-5(a) and (c) thereunder (Claim Three). The alleged secondary violations are asserted under Sections 17(a)(1) and (3) of the Securities Act (Claim Two); Section 10(b) of the Exchange Act and Rules 10b-5(a) and (c) thereunder (Claim Four); Sections 206(1) and (2) of the Advisers Act (Claim Ten); and Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder (Claim Twelve).

upon sufficient allegations of a primary violation. *See Fehn*, 97 F.3d at 1288. The Complaint fails to state a claim for primary or secondary scheme liability against Mr. Gillis.

1. The Primary and Secondary Scheme Claims Must be Dismissed for Failure to Allege Any Deceptive Conduct Beyond the Alleged Misstatements and Omissions of Others.

Nowhere in the Complaint does the SEC specify the contours of the purported "scheme," let alone "the who, what, when, where, and how of the misconduct charged"—as required under Rule 9(b). *Vess*, 317 F.3d at 1106. Instead, the SEC merely repackages the alleged misstatements and omissions forming the basis for its misrepresentation claims under the banner of a "scheme to defraud"; but "the statute does not permit such legal 'double dipping.'" *SEC v. St. Anselm Expl. Co.*, 936 F. Supp. 2d 1281, 1299 (D. Colo. 2013).

"Scheme liability . . . hinges on the performance of an inherently deceptive act that is distinct from an alleged misstatement." *SEC v. Kelly*, 817 F. Supp. 2d 340, 344 (S.D.N.Y. 2011); *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1057 (9th Cir. 2011); *see also Lucent Techs., Inc.*, 610 F. Supp. 2d at 354 (describing scheme liability as a "theory of liability separate and distinct from liability resulting from making misstatements"). Thus, the alleged scheme "must be more than a reiteration of the misrepresentations that underlie the misstatement claims." *SEC v. Leslie*, 2010 WL 2991038, at *34 (N.D. Cal. July 29, 2010); *see also Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177-78 (2d Cir. 2005); *SEC v. KPMG LLP*, 412 F. Supp. 2d 349, 377-78 (S.D.N.Y. 2006).

The alleged scheme "must involve 'sham' or 'inherently deceptive' transactions." *Lucent Techs., Inc.*, 610 F. Supp. 2d at 360. "[S]cheme liability encompasses only actions which include deceptive conduct *beyond* assistance with a material misstatement or omission." *SEC v. Goldstone*, 952 F. Supp. 2d 1060, 1203 (D.N.M. 2013) (emphasis added); *see also Lucent Techs., Inc.*, 610 F. Supp. 2d at 361 (scheme liability "may only be used to state a claim against a defendant for the underlying deceptive devices or frauds themselves, and not as a short cut to circumvent . . . limitations on liability for a secondary actor's involvement in making misleading statements.").

Conduct is inherently deceptive when it (1) creates a false appearance of fact in furtherance of the scheme and (2) the false appearance of fact was a principal purpose—and not just an accidental effect—of the defendant's conduct. *Simpson v. AOL Time Warner Inc.*, 452 F.3d 1040, 1048 & n.5 (9th Cir. 2006), *vacated on other grounds sub nom. Avis Budget Grp., Inc. v. Cal. State Teachers' Ret. Sys.*, 552 U.S. 1162 (2008); *World Surveillance Grp. Inc. v. La Jolla Cove Inv'rs, Inc.*, 2014 WL 1411249, at *4 (N.D. Cal. Apr. 11, 2014). Conduct creates a false appearance of fact only if it is communicated to the investing public in some way. *Lucent Techs., Inc.*, 610 F. Supp. 2d at 360 ("[D]eception, at a minimum, has to involve an act that gives the victims a false impression."); *see Goldstone*, 952 F. Supp. 2d at 1203. "Conduct that is consistent with the defendants' normal course of business would not typically be considered to have the purpose and effect of creating a misrepresentation." *Simpson*, 452 F.3d at 1050.

For example, in *SEC v. Kelly*, the SEC alleged that two officers of AOL caused the company to report artificially inflated revenues by engaging in "round-trip" transactions, where advertisers paid AOL inflated prices in return for offsetting transactions. 765 F. Supp. 2d 301, 305-06 (S.D.N.Y. 2011). However, the round-trip transactions were alleged to have been deceptive *only* because of "the manner in which those transactions were accounted for by AOL and reported to the public" in SEC filings. *Kelly*, 817 F. Supp. 2d at 344. Since scheme liability refers to conduct "inherently deceptive when performed"—not conduct that "*became* deceptive only through [a company's] misstatements in its public filings"—there was no basis for such liability. *Id.*; *see also Daifotis*, 2011 WL 2183314, at *9 (no scheme liability for marketing of an ultra-short bond because such marketing was not inherently deceptive, absent the alleged misleading statements about them).

Here, as in *Kelly*, none of the conduct set forth in the Complaint was inherently deceptive *when performed*; rather, the SEC's contention is that certain conduct *became* deceptive when defendants failed to disclose it in certain documents. Indeed, while asserting in conclusory fashion that defendants "knowingly or recklessly engaged in a scheme to defraud investors in ACF and the Aequitas Funds," Compl. ¶ 44, the Complaint spends the rest of that section setting forth three "reasons" why "representations made to investors in ACF and the Aequitas Funds were materially false and misleading." *Id.* ¶ 45.[13]

First, the SEC alleges that "Jesenik, Oliver and Gillis, through the Entity Defendants, did not disclose the increasing insolvency of ACF and Aequitas Holdings," but instead "acted to conceal the insolvency of the companies through an intercompany loan from ACF to its parent." Compl. ¶ 46. However, the only allegedly deceptive act taken to "conceal" the alleged insolvency of the companies was to report the outstanding balance of the Holdings Note on ACF's "books", *id.* ¶¶ 6, 77—the same conduct forming the basis for the SEC's misstatements and omissions claims with respect to the Holdings Note. *See* Compl. ¶¶ 47, 51; *supra* Part IV.B.2(a). Such conduct is not independently actionable as a scheme. *See Spot Runner*, 655 F.3d at 1057-58 (affirming dismissal of purported scheme claim that "allegedly involved the [defendants'] planning together to not disclose the Founders' sale of securities in the secondary offering, and then not disclosing those sales; fundamentally, this is an omission claim"). The

[13] In this respect, the SEC's scheme liability claims are dependent on the falsity of the alleged misstatements and omissions. Insofar as those misstatements and omissions were not false or misleading, *see supra* Part IV.B, they cannot support any claim for scheme liability because they cannot have given investors a "false impression." *Lucent Techs., Inc.*, 610 F. Supp. 2d at 360. Insofar as Mr. Gillis did not aid and abet those alleged misstatements and omissions, he cannot have aided and abetted any alleged scheme premised entirely upon them.

Complaint does not allege that there was anything deceptive or unlawful about the intercompany loan itself. To the contrary, it concedes that the Holdings Note was used to cover the operating expenses of the Aequitas enterprise, Compl. ¶ 48, and that the ACF PPM expressly disclosed that investor proceeds would be used for such purposes, *id.* ¶ 26. Such intercompany transfers are a legitimate business practice. *See WM High Yield Fund v. O'Hanlon*, 2013 WL 3230922, at *10-11 (E.D. Pa. June 27, 2013).

Second, the SEC alleges that "Jesenik and Oliver, with Gillis's knowledge in 2015, also raised funds from investors in ACF and the Aequitas Funds without disclosing that funds raised were primarily used to either repay prior investors or to fund growing operating losses of the Aequitas companies." Compl. ¶ 53. The paragraphs that follow are devoted entirely to explaining why this alleged omission allegedly rendered statements in the PPMs and quarterly updates misleading. *Id.* ¶¶ 54-58. The fundraising activity while ACF was allegedly "deteriorating" (*id.* ¶ 44) was not itself deceptive; rather, the SEC's contention is that "representations made to investors in ACF and the Aequitas Funds [about the use of investor proceeds] were materially false and misleading." *Id.* ¶ 45; *see also id.* ¶ 1 (alleging that Jesenik and Oliver "defrauded investors into thinking that they were investing in a portfolio of trade receivables"). But an alleged scheme must be more than a reiteration of the misrepresentations that underlie the misstatement claims. *Leslie*, 2010 WL 2991038, at *34.

Third, the Complaint alleges that "Jesenik and Oliver since 2014, with Gillis's knowledge since 2015, further defrauded investors by misrepresenting the underlying trade receivables available as collateral for the notes issued by ACF and the Aequitas Funds." Compl. ¶ 59. The Complaint then proceeds to identify alleged misstatements in the quarterly updates and IOF II PPM. *See id.* ¶¶ 60-63, 65, 68. The SEC does not (and could not) allege that there is anything inherently deceptive about holding assets or making loans that are insufficiently collateralized; rather, it was the alleged failure to disclose this under-collateralization of which the SEC complains. But that, again, is not actionable as a scheme.

Because the SEC has failed to allege any scheme to defraud against any defendant that is actionable separate and apart from the SEC's misstatement and omissions claims—all of which fail for the reasons explained *supra* Part IV.B—Claims One through Four, Ten, and Twelve against Mr. Gillis for participating in or aiding and abetting any such scheme must be dismissed.

2. The Primary Scheme Claims Must be Dismissed for Failure to Allege With the Requisite Particularity Any Deceptive or Manipulative Act in Furtherance of Any Scheme to Defraud by Mr. Gillis (Claims One and Three).

Even if the SEC had adequately alleged some inherently deceptive conduct to support its scheme claims against other defendants, it fails to allege that Mr. Gillis's "*own conduct* had a deceptive purpose and effect," *Fraser*, 2009 WL 2450508, at *11 (emphasis in original), defeating Claims One and Three for primary scheme liability against Mr. Gillis.

To state a claim for primary scheme liability against Mr. Gillis, the SEC must allege with particularity facts showing that *Mr. Gillis* "engaged in conduct that had the principal purpose and effect of creating a false appearance of fact in furtherance of the scheme." *Simpson*, 452 F.3d at 1048. "It is not enough that a *transaction* in which a defendant was involved had a deceptive purpose and effect; the defendant's *own conduct* contributing to the transaction or the overall scheme must have had a deceptive purpose and effect." *Id.* (emphasis in original). Here, none of the purportedly deceptive conduct alleged in the Complaint was carried out by Mr. Gillis.

First, even if it were inherently deceptive to raise proceeds from new investors in part to pay down prior notes and operating expenses (which, having been disclosed, was not), Mr. Gillis is not alleged to have engaged in any such conduct. *See* Compl. ¶ 44 (alleging that Jesenik and

Oliver, but not Mr. Gillis, raised funds from new investors and convinced prior investors to reinvest); *id.* ¶ 41 (alleging that Jesenik and Oliver, but not Mr. Gillis, issued short-term ACF notes at high interest rates to attract new investors); *id.* ¶ 3 (alleging that Jesenik and Oliver, but not Mr. Gillis, primarily used the new funds to pay down prior ACF notes); *id.* ¶ 4 (alleging that Jesenik and Oliver, but not Mr. Gillis, used new funds to pay operating expenses, including a private jet, pilots, dinners, and golf outings).

Second, Mr. Gillis had no involvement in the issuance of the Holdings Note. Indeed, Mr. Gillis did not even arrive at ACF until long after that note had been issued. *See id.* ¶ 14. Nor can the SEC's scheme claims against Mr. Gillis stand on his mere "approv[al]" of financial information that allegedly failed to include the fair value of the Holdings Note. *Id.* ¶¶ 5, 28, 33; *see Goldstone*, 952 F. Supp. 2d at 1203 (scheme claims require deceptive conduct "beyond assistance with a material misstatement or omission"). Although Mr. Gillis signed a certification stating that ACF held sufficient qualifying assets such that it did not need to register as an investment company—which required valuing the Holdings Note at its "fair value" (Compl. ¶¶ 73-74)—there is nothing deceptive about that. *Trustcash Holdings, Inc. v. Moss*, 668 F. Supp. 2d 650, 662 (D.N.J. 2009) (evading registration requirements under securities laws is not "an inherent deception perpetrated on [investors]," as required to plead scheme liability); *Fraser*, 2009 WL 2450508, at *11 (attending meetings and signing certifications not inherently deceptive). Indeed, the Investment Company Act *required* valuation of the Holdings Note at its "fair value," 15 U.S.C. § 80a-2(a)(41)(A); and the certification stated that the "fair value" of the assets was used, *see* Compl. ¶¶ 73-76. Furthermore, a central premise of the SEC's claims is that the Holdings Note *should* have been valued at its "fair value," just as it was. *See id.* ¶¶ 52, 76.

Even if the use of such a valuation to obtain the legal opinion could somehow be deemed misleading, there is no allegation that it was communicated to *investors*; therefore it cannot qualify as inherently deceptive conduct in furtherance of any purported scheme to defraud those investors. *Lucent Techs., Inc.*, 610 F. Supp. 2d at 360; *see Goldstone*, 952 F. Supp. 2d at 1235 (no scheme liability for defendants' dealings with auditors, because "[d]efendants' representations to auditors are not relayed to the investing public").

Third, Mr. Gillis is not alleged to have engaged in any conduct that itself had a deceptive purpose and effect with respect to the loan from IOF II to ACF or the alleged under-collateralization of that loan and investor notes. Even accepting as true the Complaint's allegation that "Jesenik, Oliver and Gillis, through AIM" transferred IOF II investor proceeds to ACF and then used the money to pay operating expenses and prior notes, Compl. ¶ 63—the only allegation in which Mr. Gillis's name is even mentioned in connection with any actual related *conduct*—neither of those acts is inherently deceptive. Mr. Gillis's mere "approv[al]" of financial information that allegedly failed to disclose the under-collateralization of ACF's trade receivable assets and alleged attendance at meetings likewise cannot qualify as deceptive conduct. *Id.* ¶¶ 5, 28, 33, 64-65; *see Goldstone*, 952 F. Supp. 2d at 1203; *Fraser*, 2009 WL 2450508, at *11.

The SEC's claims for primary scheme liability against Mr. Gillis fail as a matter of law.

V. CONCLUSION

For the reasons stated above, the Court should grant Mr. Gillis's motion and dismiss all claims against him with prejudice.

DATED: May 9, 2016

COVINGTON & BURLING LLP

By: */s/ W. Douglas Sprague*
W. DOUGLAS SPRAGUE

Attorneys for Defendant N. Scott Gillis