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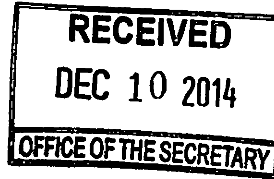

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16213

In the Matter of **DAVID G. DERRICK, Sr.,** **Respondent.**	**OPPOSITION TO RESPONDENT DAVID G. DERRICK, SR.'S MOTION FOR MORE DEFINITE STATEMENT**

The Division of Enforcement (the "Division"), through counsel of record, respectfully submits this Opposition to Respondent David G. Derrick, Sr.'s Motion for More Definite Statement ("Motion"). By any objective measure, the Division's Order Instituting Cease-and-Desist Proceedings ("OIP") sets forth specific detail both as to the Respondent's alleged violations and the factual allegations underlying the violations. In doing so, the OIP fully satisfies the requirements set forth in Rule 200(b)(3) of the Commission's Rules of Practice, 17 C.F.R. §201.200(b)(3), and provides the Respondent with ample notice of the Commission's claims against him.

As the OIP is legally sufficient for purposes of initiating this action, the Respondent's Motion should be seen for what it really is: a backdoor attempt to advance a discredited

argument that the Division's requested relief, including equitable relief, is somehow barred by the five-year statute of limitations set forth in 28 U.S.C. § 2462. If the Respondent wishes to assert such an unproductive defense, he should do so in a straightforward manner, not under the auspices that he is somehow unable to discern the factual basis of the Division's claims, notwithstanding a years-long investigation by the Division into the Respondent's unlawful activities, including extensive discussions, testimony, and negotiations between the Division and the Respondent regarding the underlying facts that culminated in the Respondent's 13 page Wells submission addressing the very same facts and claims set forth in the OIP. While the Respondent may disagree with the Division's allegations, and he may believe they are time barred, he cannot claim that he is unaware either of the alleged violations or the factual basis underlying those allegations. As a result, the Respondent's Motion should be denied.

ARGUMENT

I. The OIP Sets Forth the Factual and Legal Basis for the Division's Claims and is Adequate Under Rule 200(b)(3).

The OIP sets forth in specific detail the factual allegations underlying the Respondent's violations of the federal securities laws. Specifically, by way of example and without limitation, as to the related party transactions between the Respondent and a SecureAlert distributor that should have been disclosed to SecureAlert's board and in the company's public filings, the OIP states that:

- "Derrick and Dalton did not disclose the [September 2007] Guarantee to other Board members or employees of SecureAlert, nor did they disclose it to SecureAlert's independent auditor or outside securities counsel." OIP, ¶ 8.
- As to the December 2007 shipment, "Derrick and Dalton again agreed to provide a personal guarantee that they would pay for any unused units. Derrick and Dalton did not disclose this agreement to other Board members or employees of SecureAlert, nor did they disclose it to SecureAlert's independent auditor or outside securities counsel." OIP, ¶ 9.

- "Derrick and Dalton knew or should have known that the personal guarantees were material related-party transactions that should have been disclosed and should have been considered in SecureAlert's financial statements." OIP, ¶ 10.

- "Derrick signed certifications for the 200 Form 10-KSB as CEO. The 2007 Form 10-KSB did not disclose the personal guarantee and did not consider the personal guarantee in its accounting treatment of the $1 million purported sale in September 2007." OIP, ¶ 11.

- "Derrick signed certifications for the December 31, 2007 Form 10-QSB. The December 31, 2007 Form 10-QSB did not disclose the personal guarantee that Distributor would not be liable for unsold product and did not consider this personal guarantee in its accounting treatment of the $1 million purported sale in December 2007." OIP, ¶ 13.

- "Derrick and Dalton did not disclose their personal financing of the Third Party transactions to other Board members or employees of SecureAlert, nor did they disclose it to SecureAlert's independent auditor or outside securities counsel." OIP, ¶ 22.

- "On December 26, 2008, SecureAlert filed its Form 10-K for the fiscal year ended September 30, 2008 ('2008 Form 10-K). The entire $2 million for the September and December 2007 purported sales was reported as revenue in the year-end financial statements. . . . . Derrick signed certifications as CEO for the 2008 Form 10-K." OIP, ¶ 33.

- "The materially misstated financial statements continued to be reported in SecureAlert's filings through the end of fiscal year 2009. The filings included Forms 10-Q for the periods ended December 31, 2008, March 31, 2009, and June 30, 2009. The Form 10-K for the fiscal year ended September 30, 2009 ("2009 Form 10-K") was the last report to contain the misstated financial statements and was filed on January 13, 2010. Derrick signed certifications as CEO for each of the quarterly reports field during fiscal year 2009 and the 2009 Form 10-K." OIP, ¶ 34.

- "In addition, Derrick and Dalton executed and signed a second undisclosed side agreement, dated July 13, 2009, to personally guarantee the re-purchase of any unused product in Distributor's possession by December 31, 2010. . . . Derrick and Dalton did not disclose this personal guarantee to other Board members or employees of SecureAlert, nor did they disclose it to SecureAlert's independent auditor or outside securities counsel." OIP, ¶ 39.

Furthermore, as to the disclosures that the Respondent should have made to auditors regarding these related-party transactions, but failed to, the OIP alleges that, in addition to the paragraphs cited above:

> 35. Derrick made misrepresentations to SecureAlert's independent auditor during the yearly audit and quarterly review periods for each of the relevant periods. For each period, he signed a management representation letter to the auditor, representing, among other things, that: financial statements were fairly presented in conformity with GAAP along with all related party disclosures, that he had no knowledge of any fraud or suspected fraud, and that all related party transactions had been properly recorded or disclosed. These representations were false in light of the undisclosed personal guarantees and personal related-party financing of transactions.

OIP, ¶ 35. The OIP is similarly specific as to the internal control deficiencies caused by the Respondent. Specifically pertaining to the period between September 2007, when the Respondent guaranteed the first purchase, through January 2010, when the Respondent executed the final Form 10-K containing the materially false and misleading information, the OIP provides:

> 41. During the relevant period, Derrick and Dalton knowingly failed to implement a system of internal accounting controls for SecureAlert and directly or indirectly caused to be falsified SecureAlert's books, records, and accounts.
>
> 42. Through their conduct, Derrick and Dalton caused SecureAlert's books and records to be inaccurate and caused SecureAlert to fail to devise or maintain a system of internal accounting controls.

OIP, ¶¶ 41-42.

In light of the foregoing detail underlying the Division's allegations, it strains credibility to suggest that the Division has failed to "set forth the factual and legal basis alleged therefor in such detail as will permit a specific response thereto." Rule 200(b)(3). The OIP is clear in its description of the facts as to the Respondent's alleged fraudulent activities, including his failure to disclose related-party transactions either to the Board, to auditors, or in the public filings (with the associated dates as to each of the offending transactions); his certification of quarterly and annual statements that contained false or misleading information (including the dates and periods of each report in question, spanning the timeframe of December 2007 through January 2010);

and his failure, as SecureAlert's Chairman and CEO, to implement sufficient internal accounting controls during the same relevant time period so as to detect or prevent the falsification of SecureAlert's books, records, and accounts.

Moreover, as referenced above, none of these factual issues or legal claims are new to the Respondent. He has had the opportunity to engage the Division and provide testimony numerous times throughout this investigation. He provided the Division with an extensive Wells submission that addresses all of these topics at length – including whether any statute of limitations period could somehow preclude the Division's claims here and whether he acted with scienter in engaging in the subject transactions. *See* Confidential Wells Submission on Behalf of David G. Derrick, attached hereto as Exhibit A. In light of all of these interactions, the Respondent is perfectly aware of the alleged violations, and the facts that the Division asserts underlie the violations and the theories upon which they are based, as evidenced by the fact that he was sufficiently informed so as to be able to provide an adequate Answer to the OIP.

There OIP sets forth in sufficient detail the factual and legal basis underlying the Division's claims. It is sufficient on its face to enable the Respondent to craft a response and mount a defense thereto. Because it is adequate under Rule 200(b)(3), the Respondent's Motion should be denied.

II. The Respondent's Reference to a Possible Statute of Limitations Defense Provides No Support for His Request for a More Definite Statement.

The Respondent's reference to a possible argument that the Division's claims are precluded by a statute of limitations defense is incorrect as a matter of law and cannot support his instant Motion. The Division's claims are tied to specific dates and thus no additional information would be necessary for him to assert such a defense.

First and foremost, although the Respondent has obliquely raised the limitations issue in his Motion, the reality is that it appears to be the primary issue underlying the Motion. Nevertheless, he has not actually asserted the defense, nor asked for any relief based thereon, and as such it should be unnecessary to engage in a lengthy discussion as to the scope of Section 2462 and its application to actions brought by the Division. As a practical matter, since the Respondent certified SecureAlert's annual filings containing the false and misleading information that were filed as late as January 2010, well within the five year limitations period, such a defense would seem to have little if any benefit. The Respondent knew the filings contained misleading information concerning the financial health and revenues of the company, and he chose to certify them anyway. Nevertheless, notwithstanding that such actions are within the five-year limitations period, if the Respondent still believes he would be well served in raising such a defense and that it is an appropriate use of this Court's limited time, he is free to assert the defense affirmatively. The OIP clearly sets forth the relevant dates during which the Respondent's unlawful conduct occurred, and no additional clarity is necessary for him to assert such a defense.

Second, and just as importantly, the Division rejects the Respondent's suggestion that a statute of limitations defense could preclude the Division's claims in this action. The Respondent's argument has been raised and rejected by numerous courts, and rehashing already-plowed ground would be an unnecessary sideshow and distraction in this matter.

Section 2462 provides, in relevant part, "[e]xcept as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any *civil fine, penalty, or forfeiture*, pecuniary or otherwise, shall not be entertained unless commenced within five years for the date when the claim first accrued...." 28 U.S.C. § 2462 (emphasis added). Courts have

held that § 2462 does not apply to the Commission's claims for injunctive relief, stating that "[n]o statute of limitations applies to the SEC's claims for equitable remedies, and thus [any defense based on this argument] fails as a matter of law and fact." *SEC v. McCaskey*, 56 F.Supp.2d 323, 326 (S.D.N.Y. 1999). The *Gabelli* decision is no different. The Court ruled in *Gabelli* that the five year statute of limitation applies to "any penalty or sanction sought by the SEC related to the Security Act of 1933 and the Exchange Act of 1934." *Gabelli v. SEC* 133 S.Ct. 1216, 1219-20 (2013). By its own description, the *Gabelli* decision did not extend to disgorgement or injunctive relief because the District Court found those claims to be timely and the petitioner did not raise them as issues before the Supreme Court. *Gabelli* at 1220, fn. 1.

Subsequent courts to *Gabelli* that have addressed this statute of limitations issue have likewise distinguished between civil penalties, which are subject to the five year statute of limitations, and equitable relief, which is not. For instance, in *SEC v. Geswein*, 2014 WL 861317 (N.D. Ohio March 5, 2014), the defendants moved to dismiss the Commission's entire case on the argument that it was untimely under *Gabelli*. The court rejected the argument, concluding that "[a]fter a careful reading of *Gabelli*, and upon consideration of Defendants' thoughtful arguments, the Court refuses to read more into the Supreme Court's decision than it says on its face. . . . The Court finds that *Gabelli* announces *only* the narrow holding that the discovery rule is inapplicable to actions for civil penalties brought by the SEC." *Id.* at *8. Likewise, the court in *SEC v. Wyly*, 950 F.Supp.2d 547, 558 (S.D.N.Y. 2013), also concluded that because equitable relief sought by the Commission is remedial in nature, "*i.e.* seeks to undo prior damage or protect the public from future harm," it would not be subject to the five year statute of limitations.

The rationale for not applying the statute of limitations to the Division's equitable claims for relief is straightforward. Civil penalties are different in nature from equitable relief in that civil penalties are punitive in nature, whereas disgorgement and injunctive relief are remedial in nature. *SEC v. Wyly*, 950 F.Supp.2d at 558-59 (holding that the defendant who allegedly profited from insider trading could not assert a statute of limitations defense because equitable remedies act as reparations and deterrence, and not punishment). Congress has charged the Commission with upholding public rights and protecting public interest, and as part of that charge the Commission must be able to prevent violators from profiting from past and future wrongs. As stated by another court, "[t]he Commission seeks disgorgement in order to deprive the wrongdoer of his or her unlawful profits and thereby eliminate the incentive for violating the securities laws. The theory behind the remedy is deterrence, and not compensation." *SEC v. Rind*, 991 F.2d 1486, 1490 (9th Cir. 1993).

In this case, the Respondent falsely certified the company's financial statements and caused them to filed as late as January 2010. That places his actions within the five-year limitations period. Nevertheless, even if all activity before that point were somehow found to be outside the limitations period (which the Division believes would be a legally improper finding), the Respondent still would be subject to injunctive relief and possible disgorgement. The statute of limitations applies only to penalties, but would not apply to the Division's claim for disgorgement and injunctive relief. The Respondent engaged in multiple related-party transactions that he concealed from the Board, from SecureAlert's accountants and legal counsel, and that were not disclosed in the company's public filings. He failed to implement internal accounting controls and falsely certified SecureAlert's financial statements. The Respondent's referenced-but-not-raised statute of limitations defense is legally incorrect and, in any event,

would have no impact on the Division's ability to obtain equitable relief for the Respondent's fraudulent and unlawful conduct. As such, it should not be found to be a sufficient basis to support the Respondent's Motion.

For all of these reasons, the Division's OIP provides the Respondent with a factual and legal basis for the claims pending against him. He has answered the OIP, and the Parties are now prepared to move ahead with the litigation. The Court should not indulge the Respondent's cynical attempts to delay or distract these proceedings through frivolous and unfounded motions, such as his Motion for a More Definite Statement.

CONCLUSION

For the foregoing reasons, the Division respectfully requests that the Court deny the Motion for A More Definite Statement.

Respectfully submitted this 9th day of December, 2014,

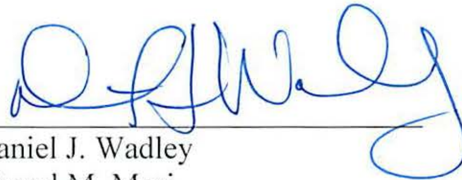

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EXHIBIT “A”

BEFORE THE
UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of SecureAlert, Inc.	File No. SL-2595

CONFIDENTIAL WELLS SUBMISSION ON BEHALF OF DAVID G. DERRICK

Dated: May 2, 2014

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FOIA CONFIDENTIAL TREATMENT REQUESTED

INTRODUCTION[1]

David G. Derrick, Sr. respectfully makes this submission in the hopes of persuading the Commission to not bring unfounded, unnecessary, and legally barred and otherwise insufficient charges against him relating to accounting classifications and related transactions and disclosures that took place more than six years ago, caused no harm, and indeed had no impact whatsoever. As explained further below, the Staff has proposed charging Mr. Derrick with securities fraud, along with other less serious violations, based on the accounting treatment accorded to a mere $2 million of actual or potential revenue with respect to transactions that were fully disclosed to his company's board, auditors, and counsel. Any such charges would be barred from the outset by the five-year federal statute of limitations applicable to civil fines and other penalties. Moreover, even absent that, there are no facts supporting any claim that accounting errors or related actions were made with the scienter necessary to sustain a fraud charge, even assuming such transactions were material, which in all events they were not. Nor do the circumstances of this matter (including the lack of any pecuniary or other personal benefit to Mr. Derrick, the fact that he self-reported to the Staff, and the pristine record he has earned over the course of three decades in business) justify the level of charges or support the sanctions being sought by the Staff. Accordingly, Mr. Derrick respectfully requests that the Commission exercise its judgment and discretion to preserve valuable agency resources in lieu of authorizing an action that would be inappropriate and ultimately unsuccessful.

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[1] This submission is made solely in response to the Staff's request for a confidential Wells Submission to assist it in its investigations. Nothing set forth herein is intended to be an admission that the conduct under investigation violated any laws, rules or regulations. David Derrick requests that, pursuant to 17 C.F.R. § 200.83 (2008), this Wells Submission is not to be disclosed in response to any request made under the Freedom of Information Act, 5 U.S.C. § 552 (2009).

BACKGROUND

Mr. Derrick is a respected businessman and community leader with a long, distinguished, and unblemished career as an entrepreneur and philanthropist. He graduated from the University of Utah Magna Cum Laude with a Bachelor of Arts degree in Economics in 1975 and with a Master in Business Administration degree in 1976. After graduating, he taught at the University of Utah Business School for four years. He then began his business career. It started in real estate development, where he incorporated innovative technologies. Since then, he has created several high tech Utah-based public companies that have received numerous international patents. Mr. Derrick has donated millions of dollars to various charities, particularly in the areas of science and science education. He sits on Brigham Young University's President's Leadership Council, has been awarded BYU's Honorary Alumni Award, and has been honored by the Smithsonian Institution and the International Astronomical Union. Finally, Mr. Derrick, who has been married for nearly 40 years and has five children and six grandchildren, is deeply involved in his church, where he has held various leadership positions.

One of Mr. Derrick's prior business ventures was serving as Chief Executive Officer of SecureAlert, Inc. That company began in 2001 developing various patents and technologies centered around the commercialization of GPS products combined with cellular transmissions, including developing (with Matsushita (Panasonic), which was an early investor and partner) the first hand-held cell phone incorporating GPS, and, later, a car-based product similar to On-Star. In the mid-2000s, the company created a sophisticated tracking device that is worn on the ankles of offenders to track where they are in real time, and then spent millions of dollars creating algorithms and software to enable authorities to monitor those individuals and intervene

when they violate their parole mandates. Today, SecureAlert has monitoring revenues from governments around the world of approximately $20 million annually, holds 15 patents, and has a market value of approximately $200 million.

During the latter part of 2007, SecureAlert reached agreements with Puerto Rican businessman Hector Gonzalez for SecureAlert to sell a total of 4,000 tracking devices to one of his companies for distribution in much of Latin America. Mr. Derrick assisted in securing third-party financing, from a company named Fladbog Capital, Inc. ("Fladbog"), for the distributor's purchases. The payments to SecureAlert for the distributor's two $1 million purchases of the tracking devices pursuant to the September 20, 2007 distribution agreement and the December 13, 2007 distribution agreement were financed by $1 million promissory notes to Fladbog dated March 26, 2008 and September 26, 2008, respectively. In financial statements filed with the Commission during 2008, the $2 million proceeds of the sales to the distributor were variously classified as revenue and deferred revenue, and, in 2012, SecureAlert filed restated financials in which it reclassified the $2 million as additional paid-in capital rather than as part of the company's accumulated deficit. Neither the reclassifications nor the restatement prompted any shareholder lawsuits.

On February 28, 2012, Mr. Derrick and SecureAlert jointly reported the transactions and their accounting to Bill McKean at the SEC. Mr. Derrick, who left the company effective June 30, 2011, thereafter cooperated with SecureAlert's internal investigation conducted by outside counsel and with the SEC Staff's investigation, making himself available to company counsel and providing testimony and documents to the Staff. On April 14, 2014, the Staff issued

its Wells notice to Mr. Derrick, and thereafter extended its deadline for making a Wells submission until today.

Though not the focus of this Wells submission, the Commission should understand that the Staff's case, at least as presented in the draft Offer of Settlement it prepared ("Offer"),[2] depends on numerous factual errors that would be hotly contested in any litigated proceeding. For example, the vast majority of the Staff's case appears to be based on the testimony of Mr. Gonzalez, whom, we predict, the Commission (or any fact finder) would not find to be a credible witness (based on, among other things, his own background and his longstanding personal bias against Mr. Derrick). Contrary to the Staff's belief that Mr. Gonzalez told Mr. Derrick and SecureAlert founder James Dalton that he had no customers or need for additional SecureAlert products (see Offer ¶¶ 8, 10), Mr. Gonzalez represented to SecureAlert prior to execution of the September 2007 distribution agreement that he already had a deal to sell 2,000 units to the Puerto Rican Corrections Department. In fact, he required SecureAlert to put up a $500,000 performance bond for that sale. Likewise, at the time of the December 2007 distribution agreement, Mr. Gonzalez represented that he had a deal to sell 2,000 units in Pernabuco, Brazil, in connection with which he required SecureAlert to send a team of specialists to Brazil for four months to set up a monitoring center.

Even putting those and other factual disputes aside, however, and accepting, for purposes of argument only, the Staff's view of the facts, the proposed case against Mr. Derrick suffers from insurmountable legal flaws and otherwise should not be brought, as explained below.

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[2] A copy of the Offer is attached hereto as Exhibit A.

DISCUSSION

I. Any Action Would Be Barred By Statute of Limitation.

The claims set forth in the Offer are untimely and cannot be tolled. A federal action for "any civil fine, penalty, or forfeiture, pecuniary or otherwise," must be brought "within five years from the date when the claim first accrued." 28 U.S.C. § 2462; *see also S.E.C. v. Bartek*, 484 Fed. Appx. 949, 957 (5th Cir. 2012) (holding that all remedies sought by SEC, including civil penalties, permanent injunctions, and officer and director bars, were barred by statute of limitations). That five-year statute of limitation cannot be extended by using the discovery rule. *See Gabelli v. SEC*, 133 S. Ct. 1216, 1224 (2013).

Here, the Staff claims that Mr. Derrick engaged in violative conduct in 2007 and 2008. Indeed, virtually the entire Offer -- *see* Offer ¶¶ 6-35 -- asserts allegations concerning those years. But the SEC has not yet filed a complaint against Mr. Derrick, and it is now more than six years since the transactions at issue and more than six years since SecureAlert first reported them on its Forms 10-K and 10-Q. The SEC thus did not commence any claim against Mr. Derrick "within five years from the date when the claim first accrued," as required under the statute. 28 U.S.C. § 2462. Regardless of when the Staff may have first discovered facts relating to the transaction in question, the plain language of the statute and *Gabelli* bar the proposed claims.

Moreover, the continuing violation doctrine is likewise unavailable to revive any claim against Mr. Derrick. Most courts did not apply that doctrine in securities cases even before *Gabelli*, *see, e.g.*, *SEC v. Fisher*, No. 07 C 4483, 2008 WL 2062699, at *7 (N.D. Ill. May 13, 2008), and, outside the securities context, courts have cautioned that "continuous violations" must not be confused "with a single violation followed by continuing consequences; only

continuous unlawful acts can form the basis of a continuous violation." *McGregor v. Louisiana State Univ. Bd. Of Sup'rs*, 3 F.3d 850, 867 (5th Cir. 1993) (citing *United Air Lines, Inc. v. Evans*, 431 U.S. 553, 558 (1977)). That is, "'the emphasis should not be placed on mere continuity . . . [but on] whether any present violation existed.'" *Id.* (alteration in original).

The Staff has suggested that, because the transactions at issue were reflected in the company's 2008 financial statements, and those financial statements were repeated in subsequent years' filings, the potential claims against Mr. Derrick are not barred by the five-year statute of limitations. The Staff's assertion fails. The 2007 and 2008 transactions, and disclosure of the same, were discrete occurrences. They happened in 2007 (purchase) and 2008 (loans and disclosures). The fact that the transactions were disclosed in financial statements that were also repeated in later years' financial statements does not make the alleged violation an ongoing or continuous one. Rather, any republication of previously disclosed financials could not be considered "anything other than a continued ill effect of [the] alleged lack of disclosure" or mistaken disclosure in 2008. *SEC v. Jones*, No. 05 Civ. 7044 (RCC), 2006 WL 1084276, at *5 (S.D.N.Y. Apr. 25, 2006) (rejecting SEC's assertion of continuing violation doctrine). Indeed, given that the focus under the continuing violation doctrine is on "whether any present violation existed," the transactions at issue were clearly a present violation (if any) in 2008 when first disclosed.

Moreover, any rule under which the subsequent attachment or repeating of the initial disclosure were to constitute a continuing violation would effectively serve to eliminate the statute of limitation altogether because, based on the nature of SEC reporting, it would eviscerate the purpose of the statute by causing the statute repeatedly to be tolled, contrary to the intention

of Section 2462 as interpreted by the unanimous Supreme Court in *Gabelli*. This is not the state of the law. Accordingly, the proposed claims against Mr. Derrick are barred by the five-year statute of limitation.

Nor can the Staff's allegations concerning the 2009 assignment of the promissory notes (see Offer ¶¶ 38-41) resuscitate the claims. Simply put, those allegations have nothing to do with any disclosure or accounting errors by SecureAlert, and had no impact one way or another on any of SecureAlert's filings. Accordingly, they do not form a basis for any claim and cannot revive the barred claims that instead are the subject of the investigation.[3]

II. Mr. Derrick Did Not Act With Scienter.

Even putting aside the statute of limitation issue, any charges under, at a minimum, Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder -- or any other scienter-based charges -- should not be brought, and cannot succeed, for the additional reason that the Staff has adduced no evidence of any scienter by Mr. Derrick with respect to the alleged misconduct, and there is none. Indeed, Mr. Derrick's actions belie any suggestion of scienter. For example, when the Fladbog loans were transferred from Fladbog to another entity (JBD

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[3] This is, of course, also true of any claims based on SecureAlert's comments and interactions with the Commission's Division of Corporation Finance staff during the period from March 13, 2008 through June 2008. Furthermore, the company and Mr. Derrick were at all times accurate in referring to and relying upon the written and integrated terms of the distribution agreement, as well upon the advice of legal and accounting professionals involved in the responses at the time, including Kent Bowman and Kevin Pinegar. During the comment process, SecureAlert reviewed the distribution agreement, and decided that the limited right to return defective product did not allow for revenue to be recognized. Therefore, SecureAlert decided to restate the $1 million initially recorded as revenue in September 2007 to "deferred revenue." Subsequently, based on the advice of securities counsel and audit professionals, SecureAlert amended the distribution agreement in April 2008 (the "Amended Distribution Agreement") to remove the ability to return product. As a result, securities counsel and audit professionals advised SecureAlert that it did not need to restate revenue from the December 2007 sale. The Amended Distribution Agreement, which was negotiated by John Hastings, included an integration clause and provided for no right to return the product. The Amended Distribution Agreement was the only lawfully binding and effective agreement as of April 2008 with the distributor. Accordingly, all statements to Division Corporation Finance staff during the above period were accurate at all times.

Management) in 2009, Mr. Derrick sought the assistance of SecureAlert's counsel (Durham Jones & Pinegar) in drafting the appropriate paperwork, which necessarily included express references to the very 2008 promissory notes that the Staff discusses in the Offer. (See Offer ¶¶ 18, 21.) In connection with securities counsel's drafting of these documents, Mr. Derrick discussed the Fladbog transactions, including the ADP financing, with Kevin Pinegar. Further, a booklet entitled "Chronological History of Transactions With Mr. Gonzalez" [Exh. B] was later provided to Durham Jones & Pinegar, and contains the handwriting and notes of Mr. Pinegar. The booklet sets forth the history of the Fladbog loans and transactions, including the relevant documents.

Moreover, the separate $1 million payments to Fladbog that the Staff describes as Messrs.' Derrick's and Dalton's personal financing, far from being concealed from SecureAlert or its auditors, were made from the checking account of an entity -- ADP Management -- that the auditors knew belonged to those individuals and of which Mr. Derrick provided the check register to SecureAlert's auditors each quarter. Mr. Derrick provided the auditors with ADP's check register showing the March 2008 payment to Fladbog occurring at the same time as Fladbog's payment to SecureAlert of the amount due on the September 2007 Distribution Agreement as reflected in SecureAlert's bank statement.

Similarly, numerous other officers and professionals at SecureAlert were likewise aware of the Fladbog loans and the funding of the loans, as evidenced by, among other things, the December 4, 2009 Board of Directors Meeting Minutes, which expressly reference Mr. Derrick's "personal guarantee of various loans" [Exh. C]; the August 16, 2010 memorandum from Mr.

Derrick to Mr. Hastings and Mr. Olsen [Exh. D]; the August 27, 2010 Memorandum to John Hastings from David Derrick, which provides that "Hector agreed to assign his debenture to Fladbog/JBD as partial payments on amounts owed to it" [Exh. E]; the November 22, 2010 Exhibit "A" Term Sheet Amendment to Distribution Agreement, which includes the statements that "The guarantors will provide financial statements – both personal and with respect to Fladbog and ADP Management – sufficient to allow BQN to assess the adequacy of the guaranties and determine whether additional collateral is required" [Exh. F]; the Agreement between JBD Management, International Surveillance Services Corporation and Borinquen Container Corp dated July 14, 2009 [Exh. G]; and the December 3, 2009 e-mail to Bob Childers, David Hanlon, John Hastings, Larry Schafran, Mike Acton and Chad Olsen from David Derrick [Exh. H].

In short, the Fladbog transactions were widely known and discussed within the company, as Mr. Derrick did nothing to hide the existence of those transactions, which he did not understand to be improper or inadequately disclosed. Those facts belie any suggestion that Mr. Derrick acted with the scienter necessary to sustain a Section 10(b) and Rule 10b-5 claim (or any other scienter-based claim). Accordingly, any action should, at an absolute minimum, not include any such claims or the officer/director bar that the Staff suggested in its Offer.

III. The Materiality Threshold Is Not Met.

The Staff's proposed claims would also fail for the additional reason that the transactions and disclosures at issue are not material under the law. To state "an actionable claim for securities fraud, the alleged misstatements must be material." *In re AMDOCS Ltd. Sec. Litig.*,

390 F.3d 542, 547 (8th Cir. 2004) (citation omitted); *see also, e.g.*, 17 C.F.R. § 240.13b2-2. Generally, materiality is a question of fact, but "misrepresentations are immaterial as a matter of law where a court determines that no reasonable investor could have been swayed by the alleged misrepresentation." *Id.* Additionally, alleged misrepresentations are "immaterial as a matter of law if they . . . present or conceal such insignificant data that, in the total mix of information, it simply would not matter." *Id.* at 548 (citation omitted). In contrast, to be material a misrepresentation must have "'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.'" *Id.* at 548 (quoting *Basic, Inc. v. Levinson*, 485 U.S. 224, 232 (1988)).

Here, the transaction at the heart of the SEC's allegations was not a material transaction. Contrary to the Staff's suggestion (see Offer ¶¶ 13, 35), the transaction's impact on the company's net income was less than 1.4%. Classifying the $2 million as revenue, the net loss for 2008 was $49,932,406; had the transaction (which had a 35% profit margin) not been recorded as revenue, the company's net loss for the year would have been $50,632,000. That small difference can hardly be said to have altered the total mix of information about the company (the financials of which included a going concern warning). Further, any suggestion that the total mix of information was somehow different in 2008 would be irrelevant because, as noted above, claims from that time period are barred by statute. *See, e.g.*, *Fisher*, 2008 WL 2062699, at *7 ("the Commission may not rely on any pre-July 19, 2002 events in attempting to prove its claims for civil penalties"). Thus, even if claims as to filings made in 2009 that merely repeated previously disclosed financial statements from 2008 were not time barred, the

materiality issue would need to assess the total mix of information that existed in 2009, not as it existed in 2008.

Moreover, in 2012 the company hired separate legal counsel and independent auditors to review the company's prior disclosures of the transaction at issue. Both the legal counsel and the auditors determined that a simple reclassification would help clarify the transaction. The auditors specifically opined that the reclassification was merely a technical change and not a material change to the company's financial statements because the transaction itself was not material. Accordingly, the transaction at issue was not material and cannot be the basis for claims by the SEC against Mr. Derrick.

IV. The Staff's Proposed Claims and Sanctions Are Excessive.

At bottom, this case is about technical accounting errors that took place several years ago, were corrected, had no material impact, and were entirely innocent. Mr. Derrick did not act with fraudulent intent, and there is no evidence to the contrary. Indeed, just the opposite is true, as explained in Section II, above. Moreover, Mr. Derrick did not profit from any of the activity, did not sell any stock during the period at issue, and, indeed, took very little compensation from the company at all. In July 2008, Mr. Derrick received one million shares of common stock in lieu of future cash compensation, but, in July 2010, returned these shares to the company (as reported in its applicable Form 10-K). He also received an additional stock award of 1,500,000 shares valued at $2,325,000, but, as reported in the 2008 Form 10-K, returned those shares as well. In 2009, Mr. Derrick received a bonus paid in 300 shares of Series D Preferred stock, but he did not sell those shares until 2012 (for $90,000). In terms of trading activity, the

only open market transaction he had in 2008 was the purchase of $400,000 worth of shares, and he had no open market sales until several months after he left SecureAlert.

In light of that, and the other circumstances described above, it is difficult to see how the Staff (or the Commission) could justify any charges in excess of those for which it settled with Christopher Hohol and Brian Poshak earlier this year. In *SEC v. Hohol* (LR-22906), Veolia Special Services' senior vice president for operations (Hohol) and its controller (Poshak) were found to have made false accounting entries, including entries for fictitious revenue accrual, that caused the corporation to overstate its earnings before taxes by $64 million. Hohol received $136,000 in incentive bonuses as a result of the fraud. Neither defendant was charged with Section 10(b) or Rule 10b-5 violations. The respondents consented to a judgment enjoining them from violating the securities laws and requiring Hohol and Poshak to disgorge $106,000 and $28,000, respectively.

Furthermore, here, even an injunction (or bar) would not be appropriate. As the Commission knows, "[t]o obtain an injunction . . . the SEC must demonstrate that there is a reasonable likelihood that [the respondent] will engage in future violations," and that, to make that determination, "courts should consider whether defendant's violation was part of a pattern, whether the violation was flagrant and deliberate or merely technical in nature, and whether the defendant's business will present opportunities to violate the law in the future." *SEC v. Brown*, 878 F. Supp.2d 109, 119 (D.D.C. 2012) (internal quotation marks omitted). That standard plainly is not met here. As noted above, Mr. Derrick's more than 30-year business career includes no history of accounting or disclosure errors or any other disciplinary matters; he proactively brought this matter to the attention of the Staff; the applicable accounting entries

were revised and disclosed more than two years ago; the matters at issue took place more than six years ago; and Mr. Derrick has not even been an officer or director of the company for nearly three years. Thus, regardless of how the Staff, Mr. Derrick, or the Commission may view the question of liability, one point on which there can be no reasonable disagreement is that there is no continuing or likely future conduct that needs to be enjoined or barred prospectively. Accordingly, there are no legal grounds for an injunction or bar.

CONCLUSION

Based on the above, the Staff should not pursue its current contemplated action against Mr. Derrick. The claims are time barred. Mr. Derrick also did not act with scienter. And, as already conclusively determined by SecureAlert's auditors following the company's outside independent investigation, the transactions at issue were not material to SecureAlert's financials. Accordingly, to protect Mr. Derrick's well-earned reputation, he respectfully requests that the Commission decline to pursue the charges outlined in the Staff's April 14, 2014 Wells Notice and not assert claims against him under Section 17(a) of the Securities Act, Sections 10(b), 13(a), or 13(b) of the Exchange Act, Rules 10b-5, 12b-20, 13a-1, 13a-11, 13a-13, 13a-14, 13a-15, 13b2-1, or 13b2-2 thereunder, or any other provision.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
SALT LAKE REGIONAL OFFICE
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SUITE 1800
SALT LAKE CITY, UTAH 84101

December 8, 2014

VIA UPS OVERNIGHT

Office of the Secretary
Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549

Re: *In the Matter of David G. Derrick, Sr.*
Administrative Proceeding File No. 3-16213

To Whom It May Concern:

Pursuant to Rules 151 and 152 of the Rules of Practice, enclosed for filing are the original and three copies each of the Opposition to Respondent David G. Derrick, Sr.'s Motion for More Definite Statement in the above-captioned matter. I have also sent a courtesy copy to Administrative Law Judge Jason S. Patil via email to alj@sec.gov.

Regards,

Misty Reiter
Paralegal Specialist
(801) 524-3321

Enclosures