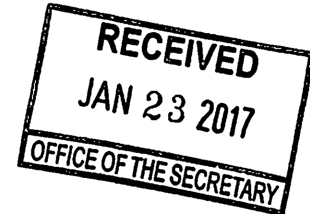
UNITED STATES OF AMERICA
Before the
U.S. SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-17387



In the Matter of

DONALD F. LATHEN, JR.,
EDEN ARC CAPITAL MANAGEMENT, LLC,
EDEN ARC CAPITAL ADVISERS, LLC,

Respondents.

PRE-HEARING BRIEF OF RESPONDENTS DONALD F. LATHEN, JR., EDEN ARC CAPITAL MANAGEMENT, LLC AND EDEN ARC CAPITAL ADVISORS, LLC

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Respondents Donald F. Lathen, Jr., Eden Arc Capital Management, LLC and Eden Arc Capital Advisors, LLC (the "Eden Arc Respondents"), by and through their undersigned counsel, respectfully submit this memorandum of law in advance of the January 30, 2017 hearing in the referenced matter.

PRELIMINARY STATEMENT

The principal question before this Court is whether Mr. Lathen violated any of the antifraud provisions of the federal securities laws set forth in the OIP in connection with the execution of his investment strategy. This Court must answer that question in the negative for at least two reasons. First, the evidence will establish that Mr. Lathen did not make any material false statements or omissions to issuers or survivor's option bonds or CDs. Second, the evidence will demonstrate that Mr. Lathen lacked the requisite scienter to engage in securities fraud.

The "misstatement" that the Division alleges Mr. Lathen made is a peculiar one. The only "misstatements" identified in the OIP are statements in letters that Mr. Lathen sent to his brokerage firms in which he stated in sum and substance that the other joint tenant on a joint tenancy with rights of survivorship (JTWROS) account had passed away and that he, as the surviving joint tenant, wished to exercise the survivor's options on bonds held in the account. The Division does not dispute that Mr. Lathen opened JTWROS accounts with terminally ill individuals (referred to as "Participants"). It is does not dispute that the brokerage firms at which he opened JTWROS brokerage accounts were fully aware of the contractual arrangement between Mr. Lathan and the Participants. It does not dispute that the Participants died, as stated in Mr. Lathen's letter.

The "misstatement" alleged by the Division is not that Mr. Lathen made a false statement of fact *per se*, but rather, that he made an incorrect legal conclusion in his letters.

Even though Mr. Lathen and the Participant opened an account that said they were joint tenants with rights of survivorship, according to the Division, under some unspecified provision of law, that joint tenancy was legally invalid. Thus, although Mr. Lathen's statement to his broker may have been factually accurate, according to the Division, it was legally incorrect and therefore an actionable misstatement. In other words, it was not a misrepresentation of fact; it was a misrepresentation of law.

The "omission" identified by the Division is even more peculiar. In a typical omission case, the allegation is that the defendant made a statement that was not outsight false, but was instead misleading, and that he therefore should have provided additional information to clarify it. Here, the Division does not allege that Mr. Lathen made any misleading statement. The OIP is explicit in asserting that Mr. Lathen's statement about his being a joint tenant was flat out false. Given the Division's position as staked out in the OIP, this is not an omission case, in which a misleading statement needs to be clarified. It is a straight misrepresentation case.

Mr. Lathen disputes the Division's legal conclusion about his misrepresentation. The evidence will establish that when Mr. Lathen told his brokers that he was a joint tenant on accounts, his statement was both factually accurate and legally correct. However, it should be self-evident that, where the very existence of a "misrepresentation" hinges upon the interpretation of an arcane aspect of property law, Mr. Lathen's subjective belief, as informed by his attorneys, is critical to the allegations in the OIP.

For the Division to make out its case, it must establish not only that Mr. Lathen reached an incorrect legal conclusion about the validity of his joint tenancies, but that he knew he was wrong (or was reckless in not knowing) – an impossible hurdle for the Division to overcome. Mr. Lathen's belief that he had formed valid JTWROS with Participants that his was

a lawful, albeit unorthodox, investment strategy, flowed from the advice he received from reputable and competent attorneys over several years. His belief was confirmed by media reports discussing his investment strategy and by his own research. That he held this belief in good faith is demonstrated by his actions.

Among other things, Mr. Lathen, of his own accord, reached out to FINRA to discuss his investment strategy. He filed a complaint with the New York State Department of Financial Services when an issuer refused to honor his redemption request. He did not try to fly below issuers' radar screens. Rather, he bombarded the same issuer with multiple, high-value redemption requests from different Participant accounts in short periods of time, virtually guaranteeing scrutiny. He did this because he believed that that the issuers were obligated under the language of the governing documents to redeem the bonds, even if they did not like it. When issuers disputed their redemption obligation, Mr. Lathen, rather than just selling the bonds back in to the market, engaged with the issuer, explained his strategy and attempted to demonstrate that they had a contractual obligation to honor his redemption request. When the relatives of Participants told him that the Division had contacted them, Mr. Lathen told them to speak freely with the Division because he had nothing to be afraid of or hide.

Mr. Lathen's actions are wholly inconsistent with what one would expect of an individual who believes that he is engaging in a fraudulent enterprise, and, more particularly, a fraudulent investment strategy. His conduct powerfully negates the intent element of the Division's claim – that is, the intent that the Division must establish before any of the Eden Arc Respondents could be held liable for any of the fraud violations alleged in the OIP. When presented at the hearing herein, we are confident that this Court will conclude that Mr. Lathen's

acted with due care and in good faith and that he lacked the state of mind necessary to have violated the antifraud provisions of the federal securities laws.

At its heart, this is not a case about fraud. It is a case about the legal interpretation of language in bond offering documents and differing opinions on joint tenancy law. The operative contracts were drafted by the alleged "victims"– entities like Goldman Sachs, GECC, JPMorgan and others – some of the most sophisticated players in the capital markets who are more than capable of protecting their own interests. Indeed, once issuers became aware of Mr. Lathen's strategy, many of them revised their governing documents to foreclose it. For example, they changed their prospectuses to state that they would only redeem survivor's option bonds if joint tenants lived in the same house and/or were blood relatives.

While some may find Mr. Lathen's investment strategy distasteful, several truths associated with it are not in dispute. None of the terminally ill Participants were harmed. Not even the Division alleges that they were harmed. None of the issuers were harmed. They were merely required to accelerate redemption of the bonds they had issued and ultimately would have to redeem. And to the extent that a dispute exists as to whether Mr. Lathen should have been permitted to redeem those bonds, it is a contractual dispute between two sophisticated parties over the meaning of the legal documents by which issuers sold their survivor's option bonds, the implications and import of the contractual arrangements that facilitated Mr. Lathen's investment strategy and the interpretation of state joint tenancy law. In other words, any such dispute is a commercial dispute between two sophisticated parties - a fact recognized by New York State banking regulators who examined Mr. Lathen's investment strategy with respect to bank certificates of deposit. The issues presented herein should not be the subject of a regulatory enforcement proceeding.

FACTUAL BACKGROUND

A. Donald Lathen

Mr. Lathen, age 48, graduated from Rice University in 1989 with a B.A. in Economics and earned an M.B.A. with distinction from the University of Michigan in 1993. Before starting his current business, Mr. Lathen had a successful fifteen-year career as an investment banker on Wall Street, primarily as a mergers and acquisitions specialist at Lehman Brothers and Citicorp, where he served as Managing Director and co-head of that firm's U.S. Energy mergers and acquisition business. Since approximately 2009 he has been a full-time investor and fund manager. In light of his broad experiences over more than two decades in the financial services industry, Mr. Lathen fully appreciates and understands the importance of ensuring full and firm legal grounding for transactions in which he is involved.

B. The Genesis of Mr. Lathen's Investment Strategy

Mr. Lathen conceived of his investment strategy in early 2009, following the death of his aunt in November 2008. He discovered that there were hundreds of billions of dollars' worth of survivor's option bonds (and CDs) trading in the secondary market at significant discounts to par – that is, bonds and brokered CDs issued by large corporations and financial institutions which provide that a surviving joint owner may redeem such security from the issuer at par upon the death of another joint owner.[1] Mr. Lathen also realized, through his experience with his aunt, that those with terminal illnesses often face acute financial demands on top of the heavy emotional and physical burdens present in end-of-life situations.

[1] The benefit associated with survivor's option bonds and CDs is obvious – guaranteed payment of par to an investor's successor following his/her death, whether a family member, philanthropic organization, joint owner or other surviving person. Like any benefit, however, the survivor's option comes at a cost. Issuers of bonds and CDs featuring a survivor's option pay a lower coupon than they otherwise would if no such benefit existed.

Following a lengthy review of issuers' bond indentures in the survivor's option marketplace, and consultation with legal counsel – detailed below – Mr. Lathen developed the basic contours of his investment strategy. He would offer financial assistance (typically $10,000) to terminally ill individuals (who would come to be known as "Participants") in return for an agreement to open a joint tenancy with rights of survivorship (JTWROS) account (a "Joint Tenancy Account") with Mr. Lathen (or, as in Mr. Lathen testified, with himself and other individuals like David Jungbauer, his step-father, who the Division plans to call as a witness herein). Mr. Lathen, in turn, funded the Joint Tenancy Accounts, into which survivor's option securities were purchased or, in certain circumstances, into which survivor's option securities were transferred from pre-existing accounts. Upon the death of a Participant, Mr. Lathen (and, if applicable, the aforementioned other individuals), as the surviving joint tenant(s) on that Joint Tenancy Account, would, pursuant to the survivor's option provisions of those securities, redeem same from their issuers at par.

Mr. Lathen funded Joint Tenancy Accounts created between approximately August 2009 and August 2010. Between approximately September 2010 and March/April 2011 Mr. Lathen and Gary Rosenbach (a private investor acting in his individual capacity) funded Joint Tenancy Accounts. In or about May 2011 Mr. Lathen created and raised money for Eden Arc Capital Partners, LLC ("EACP" or the "Fund") as a funding source for the Joint Tenancy Accounts.[2] Thus, since approximately May 2011 the Fund has funded all Joint Tenancy Accounts.

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[2] Eden Arc Capital Partners, LP is a Delaware LLP formed in May 2011 to raise funds from qualified investors. Eden Arc Capital Management, LLC ("EACM") is the Fund's Investment Advisor and Mr. Lathen is its sole owner and Chief Investment Officer. EACM was registered with the SEC as a Registered Investment Advisor with the SEC until February 2016.

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C. The Vigorous Vetting of and Disclosure to Potential Participants

Mr. Lathen realized early on that the success of his investment strategy depended in part on a vigorous vetting of, and disclosure to, prospective participants. He therefore developed a robust process for assuring that prospective participants (or their legal representatives)[3] were legally capable of entering into such a transaction and that prospective participants fully understood his investment strategy. In particular, before entering into a transaction with a prospective participant, Mr. Lathen (or Mr. Robinson) explained a number of facts and issues relating to Mr. Lathen's business to prospective participants so that they were fully informed. All of those relevant details were then more formally disclosed in writing to Participants and memorialized in a written contract between Mr. Lathen and a Participant (the "Participant Agreement"). There can therefore be no doubt but that Participants entered into transactions with Mr. Lathen (as evidenced by the Participant Agreement) on a fully informed and voluntary basis. Relevant details disclosed to prospective participants include the following:

First, Mr. Lathen and/or Mr. Robinson explained to prospective participants how Mr. Lathen's business worked, including that it is a for-profit operation, not a charitable organization, and that its profits likely would exceed the payment that prospective participants would receive. As described by Mr. Robinson: "I explain that this is a profit making enterprise" and "that by agreeing to become a joint tenant in this account, they are enabling the – Eden Arc

(... continued)

Eden Arc Capital Advisors, LLC is the general partner of the fund, which is also solely owned by Mr. Lathen.

3 The term "legal representative" refers to individuals who have been granted a general power of attorney by a Participant at a time when such Participant was competent to do so. For the sake of simplicity, "Participants" herein incorporates both individuals who themselves opened Joint Tenancy Accounts with Mr. Lathen and terminally ill individuals whose legal representatives opened Joint Tenancy Accounts with Mr. Lathen pursuant to a general power of attorney.

generally" to "realize or unlock value in securities purchased at a discount because when your relative passes away, this – this enables us to do the – puts – and that's how we make money. And most people say, oh, yeah, I get that." He also stated that "I always make it very clear what – you know, sort of what we are about. That this is not – you know, again, it's not a gift. It's not a charity. This is at some level a business transaction." And Mr. Robinson confirmed that he "describe[d] to people that – that the fund was profiting from this strategy."

Second, Mr. Lathen and Mr. Robinson confirmed that prospective participants had the requisite mental and physical capacity to enter into a contract with Mr. Lathen. As described by Mr. Lathen: "[I]f there's any doubt about the mental capacity usually we will just pass. Unless they have put in place a durable power of attorney with someone prior to their incapacitation." And, as described by Mr. Robinson: "[I]n the process of vetting the participant, you know, that involving a social worker, doctor, whatever relative, one of the questions I asked always, and of various parties, is do you believe this person, the would be participant, is mentally competent to sign a legal document. I mean, that's a question I ask. And the answer could be, yes, absolutely. Or they'd say, oh, no, she's physically incapable or mentally incapable. And then I'd ask, well, is there – is there a power of attorney. And if the answer was yes, I'd say, well, send it to me. And if the answer is no, but I'll get one right now, and I'll say, no, sorry. . . . [T]hey can't do it."

Third, Mr. Lathen and Mr. Robinson fully informed prospective participants as to Mr. Lathen's investment strategy and how profits from that strategy would be generated, including how the Joint Tenancy Accounts would be opened and the purpose of doing so.

Fourth, Mr. Lathen and Mr. Robinson explained the terms under which prospective participants would receive compensation, including how it likely is, but is not definitively, the only compensation they would receive.

Fifth, Mr. Lathen and Mr. Robinson informed prospective participants that they would be required to disclose personal information (such as their social security number and date of birth) and that Mr. Lathen would use that information to open Joint Tenancy Account(s).

Sixth, Mr. Lathen and Mr. Robinson explained what would happen if the prospective participant dies before Mr. Lathen, including, but not limited to, that the Joint Tenancy Account and the assets therein would pass by operation of law to Mr. Lathen and would not be part of the prospective participant's estate.

Finally, Mr. Lathen and Mr. Robinson explained what would happen if Mr. Lathen dies before a prospective participant, including, but not limited to, that the Joint Tenancy Account would pass by operation of law to the prospective participant and would not be part of Mr. Lathen's estate, and that the prospective participant would be contractually obligated to repay any loan received from EACP

Simply put, Mr. Lathen operated his business so as to achieve full disclosure to all prospective participants and total transparency with regard to his investment strategy. Not even the Division alleges that the disclosures that Mr. Lathen and/or Mr. Robinson made to prospective participants was anything other than fulsome and complete.

D. The General Method By Which Mr. Lathen's Business Operates

Once a prospective participant is fully vetted and he/she decided to move forward with a transaction, Mr. Lathen or Mr. Robinson sent a Participant Agreement for signature. Pursuant to the terms of the Participant Agreement, the Participant was also required to execute a

limited power of attorney authorizing Mr. Lathen to open and manage one or more Joint Tenancy Accounts using the applicable account opening documents required by the brokerage firm at which a Joint Tenancy Account is to be opened (the "Account Agreement"). Both the Participant Agreement and the Account Agreement clearly stated that Mr. Lathen and the Participant were establishing a "joint tenancy with rights of survivorship" account. Pursuant to New York Banking Law § 675 (as detailed below), establishing such an account by those means constituted *prima facie* evidence of a lawful, statutory joint tenancy.

After the Participant Agreement was signed and the Joint Tenancy Account opened and funded (and certain other conditions satisfied), Mr. Lathen or the Fund (depending on the time of the transaction) paid the Participant (or any person or entity the Participant designates) an agreed-upon amount (typically $10,000). And, following execution of the Participant Agreement, Mr. Lathen, on behalf of both joint tenants (pursuant to the authority granted to him by the aforementioned limited power of attorney), purchased survivor's option bonds and/or CDs (or transferred such positions into the Joint Tenancy Account) for the benefit of the Joint Tenancy Account (that is, for the benefit of himself and the Participant).

Upon the Participant's demise (assuming his/her death before Mr. Lathen's), the Joint Tenancy Account and all assets therein passed by operation of law to Mr. Lathen as the surviving joint tenant. Pursuant to the indentures and disclosure statements that govern securities in the survivor's option marketplace (as detailed below), a surviving joint owner of a Joint Tenancy Account may make a redemption request for any survivor's option bonds and/or CDs in such an account upon the death of a joint tenant. Such redemption requests were made through Mr. Lathen's brokerage firm pursuant to the instructions contained in the issuer's governing documents.

The governing documents associated with survivor's option bonds and CDs set forth the information that must be submitted in support of a redemption request, which typically includes: (A) a redemption request letter from the account holder or his/her authorized representative; (B) a certified death certificate; (C) a brokerage account statement from the date of death of one of the joint tenants demonstrating that the deceased joint tenant owned the security at the time of death; (D) the most recent month's account statement demonstrating that the bond and/or CD is still held in the account and that the deceased joint tenant's name is still on the account; (E) an older account statement demonstrating that the holding period for the bond and/or CD had been met if a holding period requirement for such security exists; and (F) a letter from the brokerage firm attesting to the requestor's authority to make the request.

Under the bond prospectus, Mr. Lathen is not permitted to make a redemption request to the issuer. Only a brokerage firm that is associated with the Depository Trust Corporation (which is the legal holder of the bonds) is authorized to make a redemption request. Thus, upon the death of a Participant, Mr. Lathen submitted a written request to the brokerage firm where the Joint Tenancy Account is held, informing the broker that the Participant has died, and asking it to redeem the bonds and CD's identified in the letter. Along with that letter, Mr. Lathen provided his broker with a copy of the deceased Participant's death certificate. The brokerage firm then added whatever other documentation from its records required by the issuer pursuant to its governing documents. Upon determining that the combined records satisfactorily substantiate a claim for redemption, the brokerage firm then prepared a letter to the issuer requesting the redemption of the bond and submits its letter along with the aforementioned documents to the issuer (or the issuer's designated agent). Absent a request for additional

information by the issuer, at no point in this process did Mr. Lathen have any contact with the issuer or engaged in any communications with the issuer.

Occasionally a trustee or issuer requested additional information not specified in those governing documents (such as the Participant Agreement). Mr. Lathen always provided whatever information was requested, and occasionally communicated directly with the issuer in doing so. The Division has not alleged that any of these communications were in any way false. In the normal course, the issuer redeemed the bond or CD at par and transferred those funds into the Joint Tenancy Account. In a handful of instances (with seven out of roughly eighty issuers), the issuer asserted that under the terms of the governing instrument, they were not obliged to fulfill a redemption request and refused to pay. Significantly, several issuers changed the survivor's option language in their governing documents after learning of Mr. Lathen's strategy, effectively acknowledging the validity of that investment strategy.

Issuers of survivor's option bonds and CDs were well aware of Mr. Lathen's investment strategy, even if they were not specifically aware of Mr. Lathen. The strategy was highlighted in a March 10, 2010 front-page story in *The Wall Street Journal*, which reported that "[i]n a little-known practice, investors can recruit a terminally ill person and together they can scoop up these bonds on the open market at a discount. When the ailing bondholder dies, the surviving co-owner can then redeem them at face value and potentially turn a quick profit . . . . Legal and financial experts say there is nothing to prevent investors from buying the bonds with a dying relative or even a stranger who is terminally ill." See Mark Maremont and Aparajita Saha-Bubna, "Investors Tap Into Deathbed Bond Deal," *The Wall Street Journal* (March 10, 2010). *The New York Times* mentioned *The Wall Street Journal* story in its own coverage of the investment strategy. See "Making a Killing on 'Death Bonds'?," *The New York Times* (March

10, 2010). Mr. Lathen also read this article when it was published and observed a quote in it from an attorney who worked on bond offerings that there is "nothing in a typical prospectus that would prohibit such deals" and a quote from AIG that "the bonds' fine print doesn't prohibit such activity." A number of other publications also highlighted the investment strategy, including *CNN Money*, *ProPublica* and *Index Fund Advisors*.

ARGUMENT

I.

MR. LATHEN AND PARTICIPANTS FORMED TRUE AND LEGALLY VALID JOINT TENANCIES WITH RIGHTS OF SURVIVORSHIP

Given the current state of the law, there can be no doubt but that Mr. Lathen and Participants formed true and legally valid joint tenancies with rights of survivorship.

A. The Presumption of Validity Under New York Law

Pursuant to the terms of the Participant Agreements, Mr. Lathen and the Participants (and sometimes others) opened JTWROS brokerage accounts. The act of doing so creates a presumptively valid joint tenancy with rights of survivorship. In particular, N.Y. Banking Law § 675 provides that a joint tenancy with rights of survivorship is formed:

> When a deposit of cash . . . has been made . . . in the name of [the] depositor . . . and another person and in form to be paid or delivered to either, or the survivor of them, such deposit . . . and any additions thereto made, by either of such persons, . . . shall become the property of such persons as joint tenants and the same, together with all additions and accruals thereon, . . . may be paid or delivered to either during the lifetime of both or to the survivor after the death of one of them.

It is well established under New York Law that "[w]here an account has been formed in compliance with [§ 675], it is presumed, absent a showing of fraud or undue influence, that the depositors intended to create a joint tenancy with rights of survivorship." In re Estate of

Farrar, 129 A.D.3d 1261, 1263 (3d Dep't 2015) (quoting In re Estate of Stalter, 270 A.D.2d 594, 595 (3d Dep't 2000). This presumption applies equally whether the account is a standard joint savings account or a joint brokerage or investment account. In re Estate of Corcoran, 63 A.D.3d 93, 97 (3d Dep't 2009). Moreover, the case law makes clear that there are only very limited – indeed the case law enumerates only four – bases by which the statutory presumption of a valid joint tenancy with rights of survivorship can be overcome, which must be accomplished through the presentation of clear and convincing evidence.

Here, there is ample evidence to show that the Joint Tenancy Accounts were created and funded in the names of both Mr. Lathen and a Participant with the intent that the surviving joint tenant – either Mr. Lathen or the Participant – would be entitled to the assets of the account upon the death of the other joint tenant, commonly referred to as "bilateral survivorship." Mr. Lathen and Participants entered into the Participant Agreement, which expressly provided that a JTWROS brokerage account would be opened and that JTWROS would appear on the face of those accounts, thereby establishing by operation of law that they are joint tenancy with rights of survivorship brokerage accounts.

Once the facts giving rise to the presumption of validity are established, "the burden then shifts to the party challenging the survivorship rights 'to establish – by clear and convincing evidence – fraud, undue influence, lack of capacity or . . . that the account[] [was] only opened as a matter of convenience and [was] never intended to be [a] joint account[].'" Farrarr, 129 A.D.3d at 1264 (quoting Corcoran, 63 A.D.3d at 93). The concept of convenience accounts in the case law is unrelated to issues of how the joint tenants funded their accounts or how, if at all, they agreed to monitor the accounts or dispose of proceeds. The Division's

contemplated arguments about why these JTWROS are supposedly invalid simply are not reflected in the existing case law.

With respect to the formation of the JTWROS between Mr. Lathen and Participants, no evidence exists that there has been fraud, undue influence or lack of capacity in the formation of the Joint Tenancy Accounts. Proving invalidity therefore hinges on proving that the Joint Tenancy Accounts were convenience accounts. But they were not.

A convenience account is an account established for the convenience of the holders – typically, for example, a grandparent, say, adding a grandson to an account for the convenience of having the grandson write checks and pay bills on the grandparent's behalf – and is not intended to create a right of survivorship. Here, the opposite circumstances exist. The Participant Agreements expressly provided for bilateral rights of survivorship and those survivorship rights were integral to why the accountholders established the accounts. Moreover, in the "convenience account" cases, no document exists specifying survivorship, contrary to the circumstances here. See, e.g., Farrar, 129 A.D.3d at 1264; Stalter, 270 A.D.2d at 597.

As Mr. Lathen testified, he intended for the Joint Tenancy Accounts and the assets therein to pass to Participants upon his death, subject only to the contractual obligation to repay loans to the Fund. Mr. Lathen also disclosed this survivorship intent (and the risk associated with it) to the Fund's investors. For instance, the July 2013 Private Placement Memorandum for the Fund states in relevant part:

> If [Mr. Lathen] predeceases one or more Participants any profits in those Joint Accounts would go to the Participant and not the Partnership. The Partnership would only be entitled to receive funds loaned to those Joint Accounts plus interest. As such, the Partnership's returns would be adversely affected by the death of the [Mr. Lathen] and there is an increased risk of loss on any Joint Accounts where the Participant has outlived [Mr. Lathen].

No legal precedent exists for the proposition that a separate contract between two joint owners of a JTWROS account specifying survivorship eviscerates the presumption of validity or otherwise vitiates the intent of the parties to create a JTWROS. And, although New York courts have not squarely addressed the facts at issue herein, one consistent theme in the existing case law is that the presumption of validity prevails without clear and convincing evidence to rebut an expressed intent to create a lawful JTWROS.

This is true regardless of the particular details of how the accounts were funded. See Corcoran, 270 A.D.2d at 596 (concluding that circumstantial proof such as the fact that only one tenant contributed money to the account "hardly is conclusive" as to the intent of the parties); In re Estate of Grancaric, 91 A.D.3d 1104, 1105-06 (3d Dep't 2012) (finding no convenience account where third party funded the account, and neither joint owner had true economic interest in account, because intent to create JTWROS was demonstrated). Indeed, the "distinguishing feature" of cases in which courts have found sufficient proof to rebut the statutory presumption is "record evidence that the [party] in question did not intend to create a joint tenancy." Corcoran, 270 A.D.2d at 596 (collecting cases). Here, the evidence points strongly in the other direction: Mr. Lathen intended to create a JTWROS (the success of his strategy depended on it) and so did Participants (who so specified by contract).

B. The Interests of Participants in the Joint Tenancy Accounts Are Real

The Participants' rights to the assets in the accounts are not, as the Division asserts, merely hypothetical. Although the assets held in the Joint Tenancy Accounts were financed by the Fund, the account – and the assets therein – were jointly held by Mr. Lathen and the Participant from the date upon which the account was opened to the date upon which one of the joint tenants dies. The Participant Agreements, in their various forms, provided for the

disposition of the assets after one of the joint tenants dies. Until that point, though, legal title to the account is held jointly by both Mr. Lathen and a Participant (and occasionally a third joint tenant). This is made no less so by the fact that the Fund loaned money to the Joint Tenancy Account to purchase securities or by the fact that the Participant Agreement provided that the Fund's loan be repaid prior to the disposition of any profits to the owners of the Joint Tenancy Account. The same arrangements apply regardless of whether Mr. Lathen or the Participant dies first.

In every conceivable joint account, one owner having the benefits that flow from survivorship is necessarily hypothetical. That is so because there is no way to know with any degree of certainty which joint tenant will die first. This is true whether the account is opened by a husband and wife or by two people who are not related. New York case law on joint tenancies does not have any concept of "hypothetical" survivorship, and it makes no difference which of the joint tenants is more likely to die first. Indeed, there is no requirement in the case law that there be only two joint tenants or that joint tenants be related or have any particular health status. These are matters that the state courts could refine in the future, but there is nothing in the case law today that would support a finding by this Court on that basis.

C. Mr. Lathen's Management of the Assets in the Joint Tenancy Accounts Does Not Vitiate the Ownership Interests of Participants to Those Assets

We expect that the Division will argue that Participants never had a true ownership interest in the assets in the Joint Tenancy Accounts because Mr. Lathen moved assets into and out of accounts based on the relative health of the various Participants and because Participants were not informed about the particular investments made or given updates on the accounts. In fact, the Participants were informed in writing at the outset via the Participant Agreement that Mr. Lathen would use the accounts as part of an investment strategy, which he

was entitled to do as a joint owner. The Participants had no expectation of receiving updates via monthly statements or otherwise as to the particular investments made or account balances. Moreover, joint tenancy law does not require that both joint tenants be equally active in the management of the account. Even where two spouses own the account, often only one manages the accounts' assets – a fact that does not in any way undermine the validity of the joint tenancy. If it did, the surviving spouse on a joint tenancy account would never be entitled to the assets of the account unless both spouses had been fully involved in its management. That is simply not the law.[4]

D. All Other Attributes of the Joint Tenancy Accounts Are Consistent With Lawful Joint Tenancies With Rights of Survivorship

That Mr. Lathen never disbursed account profits to Participants, never issued 1099s to them, never sent them account statements and never discussed or advised them of the impact that additional income from the Joint Tenancy Accounts could have on their Medicaid eligibility does not mean that these were not valid joint tenancies. Rather, the Participant Agreements explicitly informed Participants that investments would be made in the Joint Tenancy Accounts and that Participants were unlikely to receive additional distributions unless they outlived Mr. Lathen. No case law exists requiring that each joint tenant notify the other any time there is a change in the account balance or that both joint tenants have equal involvement in

[4] In fact, the circumstances here starkly contrast with the typical convenience account, in which the decedent had primary control of the account and the court is tasked with determining whether the decedent intended to have the assets of the account flow to the purported joint owner or to the decedent's estate. See Corcoran, 63 A.D.3d at 97. Here, however, there is no claim that Mr. Lathen or the Fund attempted to lay claim to assets rightfully belonging to the Participants or their estates. Moreover, the Participants' intent to convey survivorship to Mr. Lathen was manifestly clear in both the Participant Agreement and the Account Agreement.

the management of the account to preserve their clearly expressed intent to form a joint tenancy. In any event, the facts are these:

- Participants received a 1099 with respect to the up-front $10,000 payment. Issuing them a 1099 for additional income beyond the $10,000 would make little sense because receipt of additional distributions from the Joint Tenancy Account would be conditioned on them outliving Mr. Lathen. Issuing Participants a 1099 in such a circumstance would improperly impose a tax liability on them for income that they had not yet received.

- As set forth above, the fact that the Participants did not actively monitor the accounts or make investments themselves does not mean that they had no ownership interests in the assets in the Joint Tenancy Accounts. Even though the Participant Agreements limited the Participants' involvement in the Joint Tenancy Accounts, the agreements also expressly preserved the Participants' survivorship rights as joint tenants of the accounts.

- The Participants were advised that the payments they received under the Participant Agreement could affect Medicaid eligibility. As a practical matter, it was unlikely that Participants would receive any further payments – as Mr. Lathen disclosed in the Participant Agreement. It is therefore irrelevant that Mr. Lathen did not warn Participants of the risk that, in the unlikely event that he predeceased them, their Medicaid eligibility could be affected.

E. Changes to the Participant Agreement Reflected the Normal Evolution of Mr. Lathen's Business and Investment Strategy

That Mr. Lathen changed the form of the Participant Agreement over time does not support the conclusion that Participants were not rightful owners of the Joint Tenancy Accounts. Rather, the Participant Agreements evolved over time to reflect various changes to Mr. Lathen's investment strategy, including attempts to further strengthen his joint tenancies to more forcefully rebut potential issuer challenges. At the same time, the Participant Agreements evolved to protect the Fund, which came to provide the financing for the Joint Tenancy

Accounts. These changes evidence only Mr. Lathen's intent to preserve and strengthen the validity of the Joint Tenancy Accounts and the investment strategy overall.

The basic features of the Participant Agreement – i.e., that the investments are financed by an investment loan from the Fund and are made through the Joint Tenancy Accounts without the involvement of the Participants – do not negate the Participants' interests in those accounts as joint tenants with rights of survivorship. The Participant Agreement specifically advises the Participant of both the risks and potential benefits of the Joint Tenancy Accounts, including the potential for margin call liability and the fact that the account will pass to the Participant if Mr. Lathen dies first.

F. Providing for the Repayment of the Loan From the Fund Does Not Vitiate the Validity of the Joint Tenancy Accounts

Nor are the Joint Tenancy Accounts invalid because Mr. Lathen's assistant would be responsible for making sure all loans were repaid to the Fund if Mr. Lathen predeceased a Participant. Under the terms of the Participant Agreements, the Fund was entitled to repayment out of the proceeds of the redemption of the bonds or CDs purchased into the Joint Tenancy Account. That repayment provision, however, applied equally to Mr. Lathen and the Participant. The provision does not negate the Participant's right to the ultimate residual of the account should Mr. Lathen die first. In this way the provision is akin to a mortgage or other contractual encumbrance on any asset held in joint tenancy: the loan is repaid first and the remaining assets are disbursed to the surviving joint tenant. That encumbrance, however, does not vitiate or invalidate the joint tenancies. See Smith v. Bank of America, 103 A.D.3d 21, 27 (2d Dep't 2012) (holding that mortgage encumbrance does not invalidate a joint tenancy); Ehrlich v. Wolf, 2011 WL 197821 (N.Y. Sup. Ct. Jan. 11, 2011) (finding side agreement insufficient to invalidate

a joint tenancy). It is of no consequence that an Eden Arc employee ensures that the loan repayment requirement is fulfilled.

II.

MR. LATHEN AND PARTICIPANTS ARE BENEFICIAL OWNERS OF THE ASSETS IN THE JOINT TENANCY ACCOUNTS

The governing documents for the bonds and CDs purchased into the Joint Tenancy Accounts do not provide identical definitions of "beneficial owner." Rather, they vary from issuer to issuer, and even from deal to deal. Indeed, some of the governing documents – including many CD disclosure statements – provide no definition whatsoever. Where no definition is provided, state law presumably applies and, depending on choice of law provisions, that law may vary. These variations make the requisite legal standard for beneficial ownership a moving target and demonstrate the considerable challenges of premising the Division's material omission allegations on a theory of lack of beneficial ownership.

But even applying basic, common understandings of beneficial ownership, there can be no doubt but that both Mr. Lathen and the Participants are beneficial owners of the bonds and CDs in the Joint Tenancy Accounts and that Mr. Lathen is entitled to redeem them upon a Participant's death. As the Second Circuit explained, "in the absence of a statutory definition, a beneficial owner would be a person who does not have the legal title to the securities but who is, nevertheless, the beneficiary of a trust or a joint venture, or is a shareholder in a corporation which owns the shares." Whiting v. Dow Chem. Co., 523 F.2d 680, 686 (2d Cir. 1975) (citation omitted). Typical descriptions of "beneficial owner" in the governing documents of the bonds and CDs at issue herein are not inconsistent. Definitions range from "a person who, during his lifetime, was entitled to substantially all of the rights of a beneficial owner of an interest in the

notes" to a "person who has the right to sell, transfer or otherwise dispose of notes and the right to receive the proceeds from that sale, as well as the interest thereon and principal thereof."

Under this framework, Mr. Lathen and Participants – as joint tenants – are beneficial owners. In fact, the governing documents for the bonds and CDs purchased into the Joint Tenancy Accounts typically provide that the death of "a tenant by the entirety, joint tenant or tenant in common will be considered the death of a beneficial owner."

Nevertheless, the Division posits that the Fund – not Mr. Lathen or a Participant – is the beneficial owner of the bonds and CDs because it is entitled to repayment of the loan it made to the Joint Tenancy Account and a share of the profits generated in those accounts. But as even the Division must concede, only Mr. Lathen and the Participant – not the fund – are authorized to sell, transfer or otherwise dispose of assets in the Joint Tenancy Accounts because they are the only individuals with actual legal title to the assets in those accounts. Any brokerage firm at which a Joint Tenancy Account was held simply would not recognize or act upon an instruction given by the Fund as to assets within such an account. Thus, only Mr. Lathen and Participants may be considered the beneficial owners of the assets in the Joint Tenancy Account. Simply put, Mr. Lathen and Participants – not the Fund – hold legal title to the securities in the Joint Tenancy Accounts.[5] And, as detailed herein, that legal distinction is significant and has meaning.

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[5] Although there is no fixed definition of 'beneficial ownership," it is often an *inclusive* rather than *exclusive* construct. For instance, as defined in Section 13(d) of the Securities Exchange Act, a "beneficial owner" of a security includes "any person who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise has or shares: (1) Voting power which includes the power to vote, or to direct the voting of, such security; and/or (2) Investment power which includes the power to dispose, or to direct the disposition of, such security." 17 C.F.R. § 240.13d–3a. Significantly, for purposes of liability, delegating voting and investment authority to a third party does not strip beneficial ownership; a

(continued ...)

Nevertheless, the Division appears to view the Fund as the sole beneficial owner of the securities in the Joint Tenancy Accounts in part because the Division construes various features of the Participant Agreement as restricting the Participants' rights to the accounts such that they do not constitute "beneficial owners."

To the contrary, the Participant Agreement affirmatively preserves the beneficial ownership interests of both the Participants and Mr. Lathen in the accounts. The agreement expressly provides that the Joint Tenancy Account will pass to Mr. Lathen at the time of the Participant's death or to the Participant if Mr. Lathen dies first. Additionally, if the Participant survives Mr. Lathen, the Participant is entitled to all profits and proceeds in excess of the loan amount (plus interest) that is repaid to the Fund.

Moreover, nothing in the Participant Agreement negates the beneficial ownership of either Mr. Lathen or the Participant. Rather, the agreement – along with the Profit Sharing Agreement and Line of Credit Agreement – affect the management of the accounts and the final disposition of any proceeds earned from the bonds and CDs once they redeemed. Pursuant to the operative Participant Agreement, for example, the Participant agrees to execute a limited power of attorney in favor of Mr. Lathen to execute the account opening paperwork, secure financing for the account by executing the Line of Credit Agreement and facilitate modifications to the account as necessary. None of these features strip the Participant of his or her beneficial interest in the account.

Likewise, what Mr. Lathen and the Participant agree to do with the proceeds or a bond or CD after redemption has no bearing whatsoever on whether Mr. Lathen or the

(... continued)

beneficial owner may merely "indirectly share[] or possess[] voting and investment power." Greenberg v. Hudson Bay Master Fund Ltd., 14-CV-5226 DLC, 2015 WL 2212215, at *8 (S.D.N.Y. May 12, 2015).

Participant were beneficial owners of the bonds and CDs from the time they were purchased those securities until after they were redeemed. The Participant Agreement and Line of Credit Agreement contemplate the repayment of the loan to the Fund, and, if Mr. Lathen survives the Participant, the Line of Credit Agreement and Profit Sharing Agreement provide for the assignment of profits to the Fund. These provisions simply evidence contractual obligations to repay the loan amount to the Fund and, in the event that Mr. Lathen survives his joint tenant and redeems under the survivor's options, for Mr. Lathen to share his profits with the fund. No provision in any of the agreements, however, provides for the Fund to supplant the Participant or Mr. Lathen as beneficial owner of the Joint Tenancy Accounts. Indeed, the Participant Agreement expressly states with regard to the Fund that the assets in the account are simply "security for payment of the [loan]." And although the ownership interests of both Mr. Lathen and the Participant are subordinated to the loan obligation, they are not subordinated to any other general interest held by the Fund.

Earlier versions of the Participant Agreement did contain greater restrictions on the Participants' rights to access the assets in the Joint Tenancy Account both while it was jointly held and in the event that Mr. Lathen predeceased the Participant. No version of the Participant Agreement, however, invalidated the Participants' beneficial ownership interest. Similarly, the Investment Management Agreement did not transfer ownership to the Fund nor negate Participants' ownership and survivorship interests. But while the Participants' interests were nonetheless kept intact irrespective of which version of Participant Agreement was in use, Mr. Lathen and the Fund revised the Participant Agreement and replaced the Investment Management Agreement in 2013 with the Profit Sharing Agreement and Discretionary Line Agreement to avoid any suggestion to the contrary.

In sum, the Participants' beneficial ownership is not vitiated by any of the agreements used in Mr. Lathen's investment strategy. There is no authority for the proposition that these or other forms of side agreements and estate planning mechanisms – which merely provide for the assignment of proceeds from already monetized assets to a third party – strip beneficial ownership from the named joint owners of the accounts. If that were the effect of these types of forward-looking arrangements, the availability of the survivor's option would be strained to the point of absurdity. Whenever a brokerage account was included in a final will and testament, the prospective heir rather than the current owner would be considered the beneficial owner of the instruments in that account.

More generally, adopting the Division's anticipated position would baselessly restrict individuals from disposing of their property as they see fit. Not only, as relevant here, would the theory bar Mr. Lathen from exercising his survivor's option, but it also would prohibit an estate from exercising the survivor's option anytime the asset is subject to a separate side agreement or where it is subject to a creditor dispute. Even with regard to a standard margin account, under the Division's anticipated theory, beneficial ownership would be invalidated because the brokerage firm was owed repayment of its loans. These types of restrictions would seriously and needlessly infringe on freedom of contract in the financial planning context.

Finally, even if the Division were to establish that Mr. Lathen and/or the Fund somehow infringed upon the Participants' beneficial ownership interests, any such infringement would be inadvertent and at odds with the intent expressed in the agreements governing the investment strategy – not probative of any fraud. For these reasons, the Division's beneficial ownership theory fails to establish a basis for any alleged securities fraud.

III.

THE FUND DOES NOT OWN THE ASSETS IN THE JOINT TENANCY ACCOUNTS

Notwithstanding that the Joint Tenancy Accounts are legally titled in the names of Mr. Lathen and Participants, the Division asserts that the Fund is the true owner of the assets in the Joint Tenancy Accounts, and that the contracts underlying and facilitating Mr. Lathen's investment strategy are mere "window dressing" to disguise the Fund's ownership of those assets. No reason exists, though, for disregarding the legal form of ownership associated with the Joint Tenancy Accounts. Indeed, doing so would be akin to saying that it is mere "window dressing" to call a corporation a corporation when it has only one shareholder. Likewise, doing so is tantamount to the circumstances in which a private equity firm loans money to a company so that it can hire new employees. Those new employees obviously work for the company, not the private equity firm.

Individuals have every right to use contractual arrangements and corporate and other entities to arrange their business affairs. See Neill A. Helfman, Establishing Elements for Disregarding Corporate Entity and Veil Piercing, 114 Am. Jur. Proof of Facts 3d 403 ("A fundamental principle of Anglo-American law is that a business operating as a legally recognized entity is separate and distinct from its owners."); Krivo Indus. Supply Co. v. Nat'l Distillers and Chem. Corp., 483 F.2d 1098, 1102 (5th Cir. 1973) ("Basic to the theory of corporation law is the concept that a corporation is a separate entity, a legal being having an existence separate and distinct from that of its owners.").

Here, Mr. Lathen and Participants (and occasionally a third individual) opened the Joint Tenancy Accounts into which survivor's bonds were purchased. Mr. Lathen himself, pursuant to the limited power of attorney granted to him by the Participants, purchased those

bonds. In doing so, Mr. Lathen did not simply withdraw money from the Fund's bank account. Rather, the Fund loaned Mr. Lathen the money to purchase those survivor's option bonds in the Joint Tenancy Accounts pursuant to a written agreement and secured by the assets in those accounts themselves. These secured loans from the Fund to Mr. Lathen were fully documented. And, profits arising from transactions in the Joint Tenancy Accounts were shared with the Fund pursuant to the terms of another written agreement. They were never deposited directly into a Fund bank account.

Additionally, the Division contends that the Fund's financial statements record the assets held in the Joint Tenancy Accounts as the Fund's assets. The Division is wrong. In fact, that particular line item on the Fund's balance sheet is stated and reflected as "Due from Joint accounts, at fair value" – not as the underlying assets themselves. This accounting treatment reflects the reality of the contractual relationship between the Fund, on the one hand, and Mr. Lathen and Participants, on the other hand – to wit, it simply reflects the fair value that the Fund expected to realize from its loans to and profit-sharing arrangements with Mr. Lathen, coupled, of course, with the assumption that Mr. Lathen would outlive Participants. Likewise, that the terms of the Investment Management Agreement provide that Mr. Lathen is a "nominee" for the Fund simply reflects the most likely outcome of the contractual arrangements – that the Participant will predecease Mr. Lathen and the proceeds of the Joint Tenancy Accounts will flow to the Fund pursuant to the terms of the contracts between Mr. Lathen and the Fund. The Fund's outside auditors approved of this accounting method and, since its inception, the Fund has received unqualified audit opinions for each of its yearly audited financial statements.

Simply put, the foregoing facts do not support an alter ego, veil piercing or other theory that would permit this Court to ignore the corporate form. No evidence exists that Mr. Lathen and the Fund commingled Fund assets, failed to adhere to corporate formalities or otherwise abused the corporate form. Absent any of these legal or equitable bases for disregarding the corporate form that Mr. Lathen and investors in the Fund chose, it is Mr. Lathen and the Participants – not the Fund – who own the bonds and CDs in the Joint Tenancy Accounts. See Pearson v. Component Tech. Corp., 80 F. Supp. 2d 510, 524 (W.D. Pa. 1999) (no disregarding of corporate form absent allegations of commingling of funds or failure to follow corporate formalities); Island Seafood Co. v. Golub Corp., 303 A.2d 892, 895 (3d. Dep't 2003) (no evidence of owner's "personal use of corporate funds" or that company was undercapitalized with alleged "purpose of rendering uncollectable any money judgment"). The fact that the Fund receives the profits from Mr. Lathen's investment strategy changes nothing and the existence of the Profit Sharing Agreement is not a basis to disregard the corporate form. See, e.g., Goodman v. H.I.G. Capital, LLC (In re Gulf Fleet Holdings, Inc.), 491 B.R. 747 (Bankr. W.D. La. 2013) (funds paid to secured lender pursuant to contractual arrangement could not as a matter of law count as "siphoning of funds" under corporate veil piercing test).

In a word, the foregoing evidences a classic secured lending arrangement, akin to a private equity firm owning and funding a portfolio company through secured loans. This Court should not disregard the corporate separateness of a secured lender and borrower absent some showing of a fraudulent use of the corporate form, which is clearly absent here. See, e.g., In re Fundamental Long Term Care, 507 B.R. 359 (Bankr. M.D. Fla. Mar. 14, 2014); Pearson, 80 F. Supp. 2d at 522.

Finally, the Division's assertion that the Fund is the true owner of the Joint Tenancy Accounts and/or the securities held therein is belied by the scenario in which Mr. Lathen predeceases a Participant. Under such circumstances, a Participant would not and would not be required to turn over the assets or even all of the proceeds from the Joint Tenancy Account to the Fund, as would be the case if the Fund were the owner. Rather, the Joint Tenancy Account passes to a Participant by operation of law (just as it would if the Participant died before Mr. Lathen) and s/he would owe a contractual sum (e.g., principal plus interest) to the Fund – a contractual obligation that the Participant may fulfill or may breach.

IV.

MR. LATHEN MADE NO MISSTATEMENTS TO ISSUERS WHEN REDEEMING SURVIVOR'S OPTION BONDS AND CDS

The Division's core allegation is that Mr. Lathen defrauded issuers of survivor's option bonds and CDs by misrepresenting that he was entitled to redeem such bonds and CDs as a surviving joint owner of a JTWROS brokerage account. Mr. Lathen, however, made no such misstatements to any issuer. Rather, the issuers required certain information, which Mr. Lathen duly provided. The information he provided was accurate and responsive to the issuers' specific requirements. And if issuers requested additional information, Mr. Lathen provided that information, too.

In particular, the issuers, in drafting their offering documents, made clear what information was necessary and material to any redemption request. Each issuer provided a list (largely similar from issuer to issuers) of the materials they wanted to review, that is, what was material to their determination as to eligibility for redemption. It is well established, though, that "an omission is actionable under the securities laws only when the [party] is subject to a duty to disclose the omitted facts." Stratte-McClure v. Morgan Stanley, 776 F.3d 94, 101 (2d Cir. 2015).

See also Chiarella v. U. S., 445 U.S. 222, 230 (1980). As Mr. Lathen had no fiduciary duty to the issuers, he had no affirmative duty to disclose details about his relationship with Participants, including the Participant Agreements or other details regarding the Joint Tenancy Accounts or the financing arrangement between the Joint Tenancy Accounts and the Fund. See Chiarella, 445 U.S. at 235.

That Mr. Lathen did not disclose to issuers all of the circumstances of his relationship with the Participants where he was not required to do so does not render the information he did provide misleading. Disclosure is required under Section 10(b) and Rule 10b-5 "only when necessary 'to make . . . statements made, in the light of the circumstances under which they were made, not misleading.'" Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 44–45 (2011) (citing 17 CFR § 240.10b–5(b)). Here, the information Mr. Lathen provided to issuers was tailored to the particular information they requested in the offering documents they (or their high-priced lawyers) drafted. Put differently, Mr. Lathen gave issuers exactly what they asked for purposes of processing a redemption request. And when issuers asked Mr. Lathen for more information, he gave them that additional information, too.

Given the foregoing, it goes without saying that Mr. Lathen never tried to hide or disguise his ownership in the Joint Tenancy Accounts when redeeming survivor's option bonds and CDs. Mr. Lathen's name, address and social security number were on all of the accounts. The account statements and letters of authorization were all in his name. His profile and professional background as a Wall Street investor and fund professional have been readily available through basic Internet research or social media. He made multiple redemption requests to multiple issuers, representing that he was a surviving joint owner. Over the years, he held multiple joint accounts with multiple deceased joint owners, none of whom shared his last name.

There was no artifice whatsoever. Mr. Lathen represented to issuers exactly who he is and gave issuers exactly the information that they specified themselves, in full and accurately.

V.

EVEN IF MR. LATHEN MADE MISSTATEMENTS OR OMISSIONS, THEY WERE NOT MATERIAL

Even if the Division can establish that Mr. Lathen made misrepresentations or omissions to issuers it will not be able to establish that such misrepresented and/or omitted information was material to issuers or their validity determination agents. As discussed herein, the only misstatements or omissions identified by the Division are statements contained in letters sent by Mr. Lathen to his brokers stating that the joint tenant on the account with him had passed away and asking the broker to submit survivor's option bonds held in the account for redemption. The only purpose of this letter is to request redemption. Mr. Lathen had no expectation that any issuer would look to this letter to determine if he and the Participant were in fact joint tenants on the account and there is no indication that issuers relied upon the letter for that purpose. The brokerage account statements (which the brokerage firms provide to the issuers) are the documentary evidence used by issuers to substantiate ownership of the bonds. As set forth in the bond offering documents, beneficial ownership of the bonds could only be established by reference to the brokerage firm's books and records. Thus, Mr. Lathen's representations in his redemption request letters regarding his joint ownership of the Joint Tenancy Accounts are entirely superfluous to the determinations agent's redemption decision. The only relevant information on this point was in the brokers books and records. Mr. Lathen's redemption letters are *per se* immaterial.

The best evidence of this is Mr. Lathen's 100% success rate in redeeming instruments with thirty-three different issuers under the expanded disclosure regime he adopted

after he received the Division's Wells Notice. In particular, Mr. Lathen changed the redemption letter he used to address the issues that the Division had raised. Under this revised letter, Mr. Lathen, though he did not believe he was required to do so, voluntarily disclosed the supposedly crucial information that the Division alleges he fraudulently omitted in his prior submissions -- namely the existence of a side agreement between him and the deceased Participant and the fact that the Fund financed the Joint Tenancy Account. Instead of denying Mr. Lathen's claims or asking for additional information after being provided this supposedly "material" new information, issuers instead uniformly honored all of his post-Wells redemption requests without incident. It seems reasonable to conclude that such information was not material to these issuers in the "total mix of information" they considered in evaluating his redemption requests.

VI.

MR. LATHEN SOUGHT AND RECEIVED LEGAL COUNSEL SINCE THE INCEPTION OF HIS INVESTMENT STRATEGY

From his days as Wall Street investment banker Mr. Lathen has known of the need for legal counsel in connection with an investment strategy of this nature. Before undertaking a single investment, Mr. Lathen brought his idea to counsel and asked if it could be done.

A. Katten Muchin Rosenman LLP

Before doing anything with survivor's option bonds, Mr. Lathen retained Katten Muchin Rosenman LLP ("Katten") to provide him with legal advice about whether his idea was legally viable. He made full disclosure concerning his proposed investment strategy to the Katten attorneys with whom he was working and asked them to identify legal issues they perceived to be implicated by that strategy. The Katten lawyers stressed the importance of disclosures to prospective participants and of having valid joint tenancies. They assisted Mr.

Lathen in creating an agreement that he could use with Participants with whom he would form joint tenancies with rights of survivorship. At no time did any Katten attorney ever advise Mr. Lathen that his proposed investment strategy was fraudulent or that it violated any securities law.

B. Gersten Savage LLP

Mr. Lathen engaged Gersten Savage LLP ("Gersten") to oversee formation of the Fund and to draft all of the controlling documents related thereto. Mr. Lathen told Gersten his investments strategy and asked them if could be lawfully implemented using money raised by an investment fund. Gersten advised him that it could.

Gersten created each of the Eden Arc entities and Gersten drafted the Investment Management Agreement, pursuant to which the Fund advanced funds to Mr. Lathen as one of two joint tenants of the Joint Tenancy Accounts. Gersten changed and updated the Participant Agreement to reflect the implications of the new formant of Mr. Lathen investment strategy, in which the Fund, not Mr. Lathen, financed the purchase of survivor's option bonds in the Joint Tenancy Accounts.

Having created this structure, Gersten knew that Mr. Lathen would be using money raised by the Fund to buy survivor option bonds that would be held in the Joint Tenancy Accounts with a Participant, and that Mr. Lathen, as the likely (but not definitively) surviving joint tenant, would redeem these bonds from those JTWROS accounts upon the Participant's death. Gersten never informed Mr. Lathen of any risk that this arrangement, which it created, might be fraudulent or violate the securities law. Rather, Gersten advised Mr. Lathen, and Mr. Lathen believed (and continues to believe), that it was a lawful means of implementing the investment idea Mr. Lathen brought to Gersten.

C. Hinckley Allen & Snyder LLP

After the retirement of the Gersten attorney with whom he had worked, Mr. Lathen sought advice from Hinckley Allen & Snyder LLP ("Hinckley Allen"). Hinckley Allen identified what it expressed as a vulnerability of Gersten's structure, and that issuers might use it to challenge the validity of the Joint Tenancy Accounts. In other words, Hinckley Allen believed that Mr. Lathen's investment strategy was legally valid, albeit potentially subject to challenge by issuers of survivor's option bonds. Hinckley Allen also suggested replacing the contractual regime created by Gersten with a new regime that it believed better protected Mr. Lathen's investment strategy from the risk of challenge by issuers following redemption requests. No Hinckley Allen attorney ever suggested to Mr. Lathen that his investment strategy might be construed as a violating any federal securities law and certainly no Hinckley Allen lawyer ever communicated such a concern to Mr. Lathen.

VII.

THE GUIDANCE AND ADVICE THAT MR. LATHEN RECEIVED FROM COUNSEL VITIATES ANY CLAIM OF FRAUDULENT INTENT

The Division alleges that Mr. Lathen made false statements to issuers by representing that he and the Participants held bonds as joint tenants. The evidence will demonstrate that Mr. Lathen never made any false or misleading statements to any issuer. Mr. Lathen, in fact, made virtually no statements at all to issuers, and those that he did make were true and not at all misleading. In addition, the evidence will demonstrate that Mr. Lathen, in fact, did hold the bonds in valid JTWROS accounts with the Participants.

No matter what the Division thinks about the validity of the joint tenancies that Mr. Lathen formed with Participants, however, the evidence is overwhelming that Mr. Lathen did not act with scienter. Mr. Lathen believed in good faith that he was entitled to redeem the

bonds under the terms of their governing instruments. He did not believe that he had any legal duty to make a pre-emptive voluntary disclosure to issuers when redeeming a bond. Mr. Lathen sought advice from reputable law firm that understood his business. He told his lawyers his investment strategy and asked them if it would work. Each firm identified potential issues which they addressed. His lawyers advised him of the importance of disclosure to the Participants – and he made full disclosure to Participants. His lawyers advised him of the importance of full disclosure to investors – and he made full disclosure to investors. Although every lawyer he dealt with understood that he would be submitting redemption requests, not a single lawyer ever advised him that he was required to provide issuers with information about his investment strategy when making a redemption. Based on his experience on Wall Street, Mr. Lathen understood that in a transaction between sophisticated parties, if a party wants to know something, they ask for it. As he understood his obligation, he had to provide issuers with the information they asked for, nothing more, nothing less. No attorney ever told him otherwise.

A. Mr. Lathen Reasonably Relied on the Advice of His Counsel

The Division is required to establish that Mr. Lathen acted with scienter to establish the securities fraud claims it has alleged. To meet this burden, the Division must show that Mr. Lathen intentionally and deliberately, or with a reckless disregard for the truth, made a material misstatement or omission. The only material misstatement or omission identified by the Division is Mr. Lathen's statement in the redemption request he sent to his brokers in which he stated that he and the Participant were joint owners of the account in which the bonds were held. After alleging, incorrectly, that Mr. Lathen made this statement to issuers, the Division asserts the following in the OIP:

> Lathen knew, or was reckless in not knowing, that those representations were false. Lathen, EACM, and EACA also omitted to disclose material information, such details of EACA and EACM's relationship to the investments, and documents, such as the PPM, Participant Agreements, the Investment Management Agreement, the Profit Sharing Agreement, and the Discretionary Line Agreement, that would have disclosed the falsity of the ownership language in his redemption letters.

The Division's case thus rests upon its ability to establish that Mr. Lathen had the requisite level of intent to deceive issuers by stating in the redemption letters he sent to his broker that he and the Participants were joint tenants. Mr. Lathen's dealings with his attorneys are evidence that he lacked any such intent.

A good faith reliance on the advice of counsel is "simply a means of demonstrating good faith and represents possible evidence of an absence of any intent to defraud." United States v Peterson, 101 F.3d 375, 381 (5th Cir 1996). "Reliance on the advice of counsel need not be a formal defense; it is simply evidence of good faith, a relevant consideration in evaluating a defendant's scienter." Howard v SEC, 376 F.3d 1136, 1147-1148 (D.C. Cir. 2004). As one former SEC commissioner put it, the "reliance defense ... is not really a defense at all but simply some evidence tending to support a defense based on due care or good faith." Bevis Longstreth, *Reliance on Advice of Counsel as a Defense to Securities Law Violations,* 37 BUS. LAW. 1185, 1187 (1982). "For example, a defendant might testify that he negligently, but not intentionally, failed to provide a complete set of facts to the lawyer, or that he received accurate advice but innocently misinterpreted it. That would not qualify for an advice-of-counsel defense in the formal sense; nonetheless, such evidence would surely be admissible on the issue of defendant's state of mind." United States v Gorski, 36 F Supp. 3d 256, 268 (D Mass 2014).

Mr. Lathen sought the advice of counsel almost immediately after conceiving of his investment strategy and continued to receive guidance from attorneys – who were fully apprised of his investment strategy – throughout the evolution of his investment strategy from self-funding to funding by the Fund. Simply put, Mr. Lathen sought in good faith to execute his investment strategy – at all times – in full compliance with the law. For example, Katten warned about issues relating to Participant disclosures. Mr. Lathen carefully followed that counsel. Likewise, Hinckley Allen advised Mr. Lathen concerning vulnerabilities associated with use of the Investment Management Agreement. Again, Mr. Lathen carefully followed that counsel. Moreover, none of the lawyers with whom Mr. Lathen consulted ever suggested that his investment strategy even came close to violating the antifraud provisions of the federal securities laws. Mr. Lathen's relied on his attorney to identify the legal risks that he needed to navigate and he relied on his attorneys to tell him how to navigate those risks. None of the attorneys with whom he consulted suggested that he would be making a false statement if he redeemed bonds under the contractual regimes they established for him. And none of those attorneys ever told him that he needed to provide extra information about the joint tenancies to issuers when he redeemed survivor's option bonds. Mr. Lathen's reliance on this advice (or the absence of such advice) was perfectly reasonable,

Notably, the Division has repeatedly challenged the Eden Arc Respondents' advice of counsel defense. Among other things, the Division has asserted that the advice Mr. Lathen received is irrelevant because it did not involve advice concerning disclosures to issues. Initially, the Division is in no position to unilaterally declare what is and what is not relevant or, for that matter, what this case is about. In any event, the Division misses the point – to wit, Mr. Lathen acted in good faith at all times, which good faith is evidenced by, among other things, his

reliance on the advice he received from his attorneys after making full disclosure to them concerning his investment strategy. It is that good faith that vitiates the Division's case in that it will not be able to establish the requisite level of intent required for a finding against Mr. Lathen for having violated federal securities law. And that good faith applies to any claim the Division makes with respect to what it thinks Mr. Lathen was supposed to have done, including claims of insufficient disclosures to issuers.

B. Mr. Lathen's Good Faith Belief as to the Sufficiency, Truth and Accuracy of His Disclosures to Issuers Vitiates the Division's Claim that He Intentionally Deceived Issuers

Mr. Lathen had a good faith belief as to the validity of the JTWROS that he formed with Participants and, thus, a good faith belief that his disclosures to issuers when redeeming survivor's option bonds were sufficient, truthful and accurate – which good faith "represents possible evidence of an absence of any intent to defraud." See In the Matter of the Robare Group, 2015 SEC LEXIS 2248 (2015) at *97 (quoting United States v. Peterson, 101 F.3d 375, 381 (5th Cir. 1996) ("A good faith reliance on the advice of counsel is not a defense to securities fraud. It is simply a means of demonstrating good faith and represents possible evidence of an absence of any intent to defraud"); Howard v. SEC, 376 F.3d 1136, 1147 (D.C. Cir. 2004) ("[R]eliance on the advice of counsel need not be a formal defense; it is simply evidence of good faith, a relevant consideration in evaluating a defendant's scienter").

First, Mr. Lathen's attorneys knew (from Mr. Lathen's fulsome disclosures) that the strength and validity of his joint tenancies with Participants was critical to the success of his investment strategy. Yet none of those attorneys ever suggested that those joint tenancies were not valid. Rather, the most that can be said about the legal advice he received was that his joint tenancies were subject to potential challenge (just as any other feature of his investment strategy

could be challenged). Thus, in the absence of advice to the contrary, it was perfectly reasonable for Mr. Lathen to have believed in good that his joint tenancies were valid and legally effective and, thus, that his disclosures to issuers when redeeming survivor's option bonds were sufficient, truthful and accurate.

Second, Mr. Lathen studied N.Y. Banking Law § 675, which provides that the simple act of two (or more) individuals jointly opening a bank or brokerage account using the relevant survivorship language – "JTWROS" or "joint tenancy with right of survivorship" – constitutes *prima facie* evidence of a valid and legally effective JTWROS.[6] He also studied the case law interpreting N.Y. Banking Law § 675 and challenges to the validity of joint tenancies under that statute, learning that New York courts understood the statute the same as he did.[7] He also discussed all of his reading with counsel. Given the foregoing, it was perfectly reasonable for Mr. Lathen to believe in good faith that his joint tenancies were valid and legally effective and, thus, that his disclosures to issuers when redeeming survivor's option bonds were sufficient, truthful and accurate.

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6 See In the Matter of the Estate of Catherine K. Corcoran, 63 A.D.3d 93, 96 (N.Y. App. Div. 2009) (New York Banking Law § 675's presumption applies equally to investment accounts and traditional deposit accounts).

7 See Kleinberg v. Heller, 38 N.Y. 2d 836, 840 (1976) ("[T]he opening of an account in the names of two people in facial form to be paid or delivered to either, or the survivor of them, evinces an intention to create a joint tenancy, thereby placing the burden of refutation on anyone who challenges it.") (internal quotations and citations omitted) (Fuchsberg, J., concurring); In re Matter of Nino Grancaric, 91 A.D. 3d 1104, 1105 (N.Y. App. Div. 2012) ("When a bank account is opened in two names, in form to be paid or delivered to either, or the survivor of them and survivorship language appears on a joint account's signature card, a statutory presumption arises that the parties intended to create a joint account with rights of survivorship") (internal quotations and citations omitted).

Third, Mr. Lathen's also learned from his study of New York joint tenancy law that any party seeking to invalidate a joint tenancy bears a "heavy burden" and that they are only limited grounds for invalidating presumptively valid joint tenancies (fraud, undue influence, lack of capacity or a determination that the joint tenancy is a so-called "convenience account").[8] Moreover, Mr. Lathen discussed the foregoing with counsel. Given the foregoing, it was perfectly reasonable for Mr. Lathen to believe in good faith that his joint tenancies were valid and legally effective and, thus, that his disclosures to issuers when redeeming survivor's option bonds were sufficient, truthful and accurate.

Fourth, Mr. Lathen's review of the Grancaric case – standing alone – caused Mr. Lathen to conclude that his joint tenancies were valid and legally effective and, thus, that his disclosures to issuers when redeeming survivor's option bonds were sufficient, truthful and accurate. In particular, Grancaric upheld the presumption of validity of a JTWROS account where both joint tenants were acting as *de facto* nominees for a third party "true owner" who funded the JTWROS account, just as the Fund finances the Joint Tenancy Accounts.

Even if the Division goes to the mat on Mr. Lathen's interpretation of New York joint tenancy law – which they must to satisfy the burden of proving that Mr. Lathen had the requisite intent to defraud – the Division will have missed the point. It matters not whether the Division or Mr. Lathen is "right" with respect to New York joint tenancy law. Rather, what

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[8] See Grancaric, 91 A.D.3d at 1105 (the only bases for vacating a joint tenancy are fraud, undue influence, lack of capacity or . . . that the accounts were only opened as a matter of convenience and were never intended to be joint accounts"); In the Matter of the Estate of Richard N. Coddington, 56 A.D.2d 697 (N.Y. App. Div. 1971) (noting the "heavy burden" borne by_those trying to rebut the statutory presumption of a valid joint tenancy supported by *prima facie* evidence).

matters is Mr. Lathen's good faith belief in the accuracy of his interpretation of New York joint tenancy law and that which supports his good faith belief.

VIII.

OTHER EVIDENCE OF MR. LATHEN'S GOOD FAITH BELIEF AS TO THE LEGALITY OF HIS INVESTMENT STRATEGY

Even beyond the foregoing, abundant and wide-ranging indicators exist of Mr. Lathen's good faith – indicators that further undermine any claim that Mr. Lathen acted with the requisite level of scienter required to sustain a finding that he violated any federal securities law.

First, Mr. Lathen worked with and sought assistance from a bevy of financial professionals, including lawyers, compliance professionals, auditors and brokerage firms. All of these professionals were fully aware of the details of Mr. Lathen's investment strategy. Several, in fact, examined the investment strategy before agreeing to do business with Mr. Lathen. None ever even hinted that Mr. Lathen's investment strategy might violate the federal securities laws.

Second, not even the Division alleges that investors in the Fund or Participants were defrauded. Rather, Mr. Lathen was completely transparent with both categories of individuals, including with respect to the risks associated with the investment strategy. None questioned the legality of the investment strategy.

Finally, Mr. Lathen operated in the public spotlight and openly invited regulatory scrutiny. In particular, Eden Arc Capital Management LLC ("EACM") was registered with the SEC as an investment advisor. As such, EACM made regular filings with the SEC and was subject to review and inspection by the SEC. What's more, when Mr. Lathen had a dispute with Goldman after it refused to redeem a survivor's option bond presented for redemption, Mr. Lathen went so far as to invite further governmental scrutiny by filing complaints with the New York State Financial Authority and Consumer Financial Protection Board. Nobody engaged in

an ongoing fraud would be thoughtless or brazen enough to invite regulatory scrutiny into their business practices.

IV.

NEITHER MR. LATHEN NOR EDEN ARC CAPITAL MANAGEMENT, LLC VIOLATED THE CUSTODY RULE

Rule 206(4)-2 prohibits investment advisers from having custody of client funds or securities unless the adviser maintains those assets "[i]n a separate account for each client under that client's name" or "[i]n accounts that contain only [his] clients' funds and securities, under [his] name as agent or trustee for the clients." 17 C.F.R. § 275.206(4)-2(a). Custody is defined as "holding, directly or indirectly, client funds or securities, or having any authority to obtain possession of them." 17 C.F.R. § 275.206(4)-2. Additionally, Rule 206(4)-2 prescribes a variety of other requirements pertaining to matters such as bookkeeping, provision of notice to clients and auditing, which are meant to ensure effective safekeeping of client funds and securities.

Rule 206(4)-2(a)(1) does not apply to the Joint Tenancy Accounts. As detailed above, the Fund does not own these accounts or the securities in them. Rather, the Fund owned loans made to Mr. Lathen (i.e., debt instruments) in his personal capacity (and in some cases to Mr. Lathen and Participants jointly) and profit-sharing rights in the Joint Tenancy Accounts. The Joint Tenancy Accounts themselves and the assets therein were merely collateral to secure Mr. Lathen's contractual obligation to the Fund and the Fund's profit-sharing rights, not assets owned by the Fund itself. As such, from the Fund's perspective, the Custody Rule does not require that the Joint Tenancy Accounts, or the bonds and CDs in them, be held in the name of the Fund. The loans and profit-sharing rights owned by the Fund, if securities at all, are best considered "privately offered securities" that are exempt from the Custody Rule.

Notwithstanding the inapplicability of the Custody Rule to the Joint Tenancy Accounts, Eden Arc Capital Management, LLC employs numerous safekeeping procedures consistent with the Custody Rule, including the following:

- All accounts were maintained at a Qualified Custodian;
- All accounts were reconciled on a monthly basis by the Fund's administrator, Integrated Investment Solutions;
- The Fund was audited on an annual basis by Eisner Amper, a PCAOB registered accounting firm, with such audited financials delivered to Fund investors within 120 days of year end; and
- No Eden Arc Capital Management, LLC employee other than Mr. Lathen, a joint owner of the Joint Tenancy Accounts, had access to those accounts.

Furthermore, we note that Mr. Lathen's access to the underlying Joint Tenancy Accounts' collateral by virtue of his individual ownership in the accounts is not substantively different from a risk perspective than his deemed custody of the entirety of the Fund's assets by virtue of his role as general partner of the Fund. Under the Custody Rule, the annual audit requirement is deemed a cure for this risk with respect to pooled investment vehicles such as the Fund. Thus, regardless of whether the Custody Rule is deemed applicable to the Joint Tenancy Accounts, Eden Arc Capital Management, LLC is substantively complying with it.[9]

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[9] The SEC website's explains this concept. *See* "Staff Responses to Questions About the Custody Rule," dated September 1, 2013 (found at http://www.sec.gov/divisions/investment/custody_faq)030510.hrm (explaining that if an adviser manages client assets that are not funds or securities, Rule 206(4)-3 does not apply, as it only applies to clients' funds and securities.

CONCLUSION

Accordingly and for all of the foregoing reasons, respondents Donald F. Lathen, Jr., Eden Arc Capital Management, LLC and Eden Arc Capital Advisors, LLC respectfully submit that this Court should: (1) dismiss the Order Instituting Proceedings and all the charges contained therein with prejudice; and (2) grant the Eden Arc Respondents such other and further relief as this Court deems just and appropriate.

Dated: New York, NY
January 20, 2017

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned attorney hereby certifies that on January 21, 2017 I caused a true and correct copy of the attached PRE-HEARING BRIEF OF RESPONDENTS DONALD J. LATHEN, JR., EDEN ARC CAPITAL MANAGEMENT, LLC AND EDEN ARC CAPITAL ADVISORS, LLC, dated January 20, 2017, to be served upon the individuals listed below via e-mail and UPS Overnight Mail:

Honorable Jason S. Patil
Administrative Law Judge
U.S. Securities and Exchange Commission
100 F. Street, N.E.
Washington, DC 20549-2557

Brent Fields, Secretary
Office of the Secretary
U.S. Securities and Exchange Commission
100 F. Street, N.E.
Washington, DC 20549-2557

Judith Weinstock, Esq.
U.S. Securities and Exchange Commission
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