

14-2301-cv(L), 14-2937-cv(XAP), 15-3978-cv
SEC v. Surlis

1 UNITED STATES COURT OF APPEALS

2 FOR THE SECOND CIRCUIT

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4 August Term, 2015

5 (Submitted: April 27, 2016

Decided: December 6, 2016)

6 Docket Nos. 14-2301-cv(L), 14-2937-cv(XAP), 15-3978-cv

7
8 SECURITIES AND EXCHANGE COMMISSION,

9 *Plaintiff-Appellee-Cross-Appellant,*

10 - v. -

11 VIRGINIA K. SOURLIS,

12 *Defendant-Cross-Claimant-Appellant-Cross-*
13 *Appellee,*

14 JOHN B. FROHLING, HISAO SAL MIWA,

15 *Defendants-Cross-Claimants-Cross-Defendants,*

16 DANIEL D. STARCZEWSKI, THOMAS F. PIERSON,

17 *Defendants-Cross-Defendants,*

18 GREENSTONE HOLDINGS, INC., JOE V. OVERCASH, JR., FRANK J. MORELLI, III,
19 JAMES S. PAINTER, III,

20 *Defendants,*

21
22 ACTIVE STEALTH, LLC, BAF CONSULTING, INC., BLUEWATER EXECUTIVE
23 CAPITAL, LLC, EMERGING MARKETS CONSULTING, LLC, KCS REFERRAL
24 SERVICES, LLC, MBA INVESTORS, LTD., NEW AGE SPORTS, INC., POWER
25 NETWORK, INC., PROJECT DEVELOPMENT, INC., SEVILLE CONSULTING, INC.,

1 STARR CONSULTING, INC., TUSCANY CONSULTING, INC., YT2K, INC.,

2 *Relief-Defendants.**
3

4 Before: KEARSE, POOLER, and DRONEY, *Circuit Judges.*

5 Appeals in Nos. 14-2301 and 15-3978 by defendant attorney from a November 25,
6 2015 final judgment of the United States District Court for the Southern District of New York, Miriam
7 G. Cedarbaum, *Judge*, granting plaintiff Securities and Exchange Commission's motion for summary
8 judgment in this enforcement action, holding defendant liable for securities laws violations (§ 5 of the
9 Securities Act of 1933, 15 U.S.C. § 77e; and, as both a primary actor and an aider and abetter, § 10(b)
10 of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R.
11 § 240.10b-5) in connection with a false opinion letter she wrote, enabling an impermissible public
12 offering of unregistered shares of stock of defendant Greenstone Holdings, Inc.; ordering her to pay
13 a total of \$57,284.83 as a civil penalty, disgorgement, and prejudgment interest; and permanently
14 barring her from participating in certain stock offerings. Defendant contends principally that she did
15 not have a duty to protect the interests of the investing public, and she challenges the imposition of
16 a civil penalty and an injunction.

17 In Nos. 14-2301 and 15-3978, we affirm the final judgment. The cross-appeal by the
18 SEC, No. 14-2937, challenging a 2012 interlocutory order that was superseded by the final judgment,
19 is dismissed as moot.**

* The Clerk of Court is directed to amend the official caption in these appeals to conform with the above.

** Originally filed as a summary order on July 8, 2016, this decision is now being published as an opinion on motion of the Securities and Exchange Commission dated November 14, 2016, granted on December 1, 2016.

1 ALLAN A. CAPUTE, Special Counsel to the Solicitor,
2 Washington, D.C. (Anne K. Small, General Counsel,
3 Michael A. Conley, Deputy General Counsel, Jacob H.
4 Stillman, Solicitor, Securities and Exchange
5 Commission, Washington, D.C., on the brief), *for*
6 *Plaintiff-Appellee-Cross-Appellant*.

7 VIRGINIA K. SOURLIS, *pro se*, Red Bank, New Jersey,
8 *Defendant-Cross-Claimant-Appellant-Cross-Appellee*.

9 KEARSE, *Circuit Judge*:

10 In these consolidated appeals, filed or reinstated following a remand for final resolution
11 of pending claims, *see SEC v. Frohling*, 614 F. App'x 14 (2d Cir. 2015), defendant-cross-claimant-
12 appellant-cross-appellee Virginia K. Sourlis *pro se* appeals from a November 25, 2015 Superseding
13 Final Judgment of the United States District Court for the Southern District of New York, Miriam G.
14 Cedarbaum, *Judge*, in this enforcement action brought by the Securities and Exchange Commission
15 ("SEC") in connection with public offerings of unregistered shares of stock of defendant Greenstone
16 Holdings, Inc. ("Greenstone"). The district court granted a motion by the SEC for summary judgment
17 on issues of liability, holding Sourlis--an attorney who wrote a January 11, 2006 opinion letter
18 ("Sourlis Letter") relating to one of the offerings--liable for violating § 5 of the Securities Act of 1933
19 ("Securities Act"), 15 U.S.C. § 77e; violating § 10(b) of the Securities Exchange Act of 1934
20 ("Exchange Act"), 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5; and aiding
21 and abetting violations of § 10(b) and Rule 10b-5, in violation of § 20(e) of the Exchange Act,
22 15 U.S.C. § 78t(e). The Superseding Final Judgment orders Sourlis to pay a total of \$57,284.83 as
23 a civil penalty, disgorgement, and prejudgment interest, and permanently bars her from participating
24 in so-called "penny stock" offerings, *i.e.*, offerings of "any equity security that has a price of less than

1 five dollars, except as provided in Rule 3a51-1 under the Exchange Act," Superseding Final Judgment
2 at 4.

3 In Nos. 14-2301 and 15-3978, Sourlis principally contends that she was entitled to
4 summary judgment in her favor, arguing that she "did not owe a duty to protect the interests of the
5 investing public" (*e.g.*, Sourlis brief on appeal at 1, 26), and that the actual offering of the stock that
6 was the subject of her opinion letter was intervening fraudulent conduct by other defendants that
7 relieved her of responsibility. She also challenges the court's imposition of a civil penalty and its
8 injunctive order. For the reasons that follow, we find no error in the district court's determinations of
9 liability and no abuse of discretion in its remedial order. We assume the parties' familiarity with the
10 underlying facts and procedural history of the case.

11 *A. Liability*

12 Section 5 of the Securities Act makes it unlawful, directly or indirectly, to publicly offer or sell
13 unregistered stock, *see* 15 U.S.C. § 77e, unless the offering is covered by an exemption. The stock
14 certificate for unregistered shares not covered by an exemption--"restricted" stock--normally bears a
15 legend stating that the shares have not been registered and cannot lawfully be sold until they are
16 registered. The pertinent exemption in this case, as it existed at the relevant time, allowed stock to
17 be issued without the restricted-stock legend if the recipients were persons unaffiliated with the stock's
18 issuer, and if at least two years had elapsed since the shares were owned by the issuer or a person
19 affiliated with the issuer, *see* SEC Rule 144(k), 17 C.F.R. § 230.144(k) (2005). The two-year
20 requirement was satisfied if unaffiliated persons acquired the shares in exchange for "consideration
21 consisting *solely* of other securities of the same issuer" that had been received at least two years
22 earlier, as the shares were deemed to have been acquired from the issuer at the time the surrendered

1 securities had been acquired. *Id.* § 230.144(d)(3)(ii) (2005) (emphasis added). "To state a cause of
2 action under Section 5, one must show '(1) lack of a [required] registration statement as to the subject
3 securities; (2) the offer or sale of the securities; and (3) the use of interstate transportation or
4 communication and the mails in connection with the offer or sale.'" *SEC v. Cavanagh*, 445 F.3d 105,
5 111 n.13 (2d Cir. 2006) (quoting *Europe & Overseas Commodity Traders, S.A. v. Banque Paribas*
6 *London*, 147 F.3d 118, 124 n.4 (2d Cir. 1998)). A person not directly engaged in transferring title of
7 the security can be held liable under § 5 if he or she "engaged in steps necessary to the distribution of
8 [unregistered] security issues." *SEC v. Chinese Consolidated Benevolent Ass'n*, 120 F.2d 738, 741
9 (2d Cir. 1941).

10 Section 10(b) of the Exchange Act and Rule 10b-5, which prohibit fraud in the
11 purchase or sale of a security, are violated if a person has "(1) made a material misrepresentation or
12 a material omission as to which he had a duty to speak, or used a fraudulent device; (2) with scienter;
13 (3) in connection with the purchase or sale of securities." *SEC v. Pentagon Capital Management*
14 *PLC*, 725 F.3d 279, 285 (2d Cir. 2013) (quoting *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308
15 (2d Cir. 1999)), *cert. denied*, 134 S. Ct. 2896 (2014). A false statement was made with the requisite
16 scienter if it was made with the "intent to deceive, manipulate, or defraud." *SEC v. Obus*, 693 F.3d
17 276, 286 (2d Cir. 2012) (internal quotation marks omitted). "[S]cienter may be established through
18 a showing of reckless disregard for the truth, that is, conduct which is highly unreasonable and which
19 represents an extreme departure from the standards of ordinary care." *Id.* (internal quotation marks
20 omitted).

21 Summary judgment may be granted "if the movant shows that there is no genuine
22 dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ.
23 P. 56(a). A genuine dispute exists when the evidence is such that, if the party against whom summary

1 judgment is sought is given the benefit of all permissible inferences and all credibility assessments,
2 a rational factfinder could resolve all material factual issues in favor of that party. *See, e.g., Anderson*
3 *v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). Summary judgment is appropriate when "there can
4 be but one reasonable conclusion as to the verdict," *id.* at 250, *i.e.*, "it is quite clear what the truth is,"
5 *Poller v. Columbia Broadcasting System, Inc.*, 368 U.S. 464, 467 (1962) (internal quotation marks
6 omitted), and no rational factfinder could find in favor of the nonmovant. We review the district
7 court's grant of summary judgment *de novo*, applying the same standards that govern the district
8 court's consideration of the motion. *See, e.g., Aulicino v. New York City Department of Homeless*
9 *Services*, 580 F.3d 73, 79 (2d Cir. 2009).

10 The district court concluded that there was no genuine issue of material fact as to
11 Sourlis's liability under § 5 of the Securities Act with respect to more than 6 million Greenstone shares
12 to which her January 11, 2006 opinion letter pertained. It is undisputed that the Greenstone shares in
13 question were not registered. Sourlis opined that shares could lawfully be issued as unrestricted shares
14 to recipients who were acquiring them in exchange for certain convertible notes. The Sourlis Letter
15 stated that she was relying on "information and representations furnished by . . . the Original Note
16 Holders to me," and that "I have been informed by the Original Note Holders" that none of them were
17 affiliated with the issuer and that the Original Note Holders had owned the notes for at least two years.
18 (Sourlis Letter at 2.) The record established, however, that "the convertible notes described by Sourlis
19 did not even exist." *SEC v. Greenstone Holdings, Inc.*, 954 F.Supp.2d 211, 213 (S.D.N.Y. 2013).
20 Accordingly, many of the statements in the Sourlis Letter were necessarily false. *See id.* On the basis
21 stated in the Sourlis Letter, which was approved by defendant John B. Frohling, Greenstone's
22 securities counsel, 6,150,000 Greenstone shares were issued in February 2007 as unrestricted shares,
23 allowing them to be sold to the public despite the fact that they were unregistered. The court

1 concluded that Sourlis's role

2 satisfie[d] the requirement that she directly or indirectly offered to sell
3 securities. [Greenstone's transfer agent] required a legal opinion letter
4 providing the authority to issue the unregistered shares without a restrictive
5 legend. It would not have issued the shares without Sourlis's letter. This is
6 sufficient to hold an attorney liable under Section 5.

7 *Id.* at 214. We see no error in this conclusion.

8 The district court also found Sourlis liable under § 20(e) of the Exchange Act because
9 her letter aided and abetted violations of § 10(b) and Rule 10b-5 by others. *See* Order dated November
10 16, 2012, entered November 20, 2012 ("November 20 Order"), incorporated in the Superseding Final
11 Judgment. Sourlis challenges this conclusion, arguing, as she did in the district court, that she had no
12 actual knowledge that her January 2006 letter would be used for the issuance of unrestricted stock a
13 year later, and that she had no knowledge of the exhibit that was eventually attached to the letter. The
14 court found that the attachment (which specified the persons who were to receive the shares and the
15 number of shares each was to receive) was not the problem; the problem "was the contents of the
16 letter" (Hearing Transcript, November 16, 2012 ("Tr."), at 32). Although § 20(e) as it existed at the
17 time of the Sourlis Letter pertained to "any person that knowingly provide[d] substantial assistance"
18 to a primary violator of the securities laws, 15 U.S.C. § 78t(e) (2000), it did not, unlike certain other
19 sections of the Exchange Act, state that in order to be liable the person must have had actual
20 knowledge, *see, e.g.*, Exchange Act § 21E, 15 U.S.C. § 78u-5(c)(1)(B) (for claims of fraud in forward-
21 looking statements, requiring proof that the statements were made with "actual knowledge" of falsity).
22 *See generally SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786, 798-801 (11th Cir. 2015). The
23 district court concluded that the requirements of § 20(e) were met because Sourlis's election not to
24 insist on seeing the notes discussed in her opinion letter was at the very least reckless (*see* Tr. 36-37
25 ("even if it were not intentionally done, it was so reckless," in light "of its importance to the

1 transaction")), and that her misrepresentations that she had spoken to the original note holders were
2 misrepresentations as to her knowledge and hence were knowingly false (*see id.* at 35-36).

3 We see no error in the district court's rejection of Sourlis's arguments. Sourlis's letter
4 began by stating that her "opinion has been requested with respect to the issuance of shares (the
5 'Shares') . . . upon the conversion of [certain] . . . Convertible Notes" (Sourlis Letter at 1), and it
6 concluded that "the Shares underlying the Note [*sic*] may be issued . . . *without a legend* pursuant to
7 the Securities Act" (*id.* at 2 (emphasis in original)). Between stating its purpose and its legal
8 conclusion, the "letter represented as fact matters that were contrary to fact"; Sourlis represented in
9 the letter more than once that she "had spoken to the original note-holders," a representation as to her
10 own "knowledge," although "there is no dispute that in fact she did not speak to those original note-
11 holders"; thus, a "critical statement of fact underpinning the opinion" was false because "no original
12 note-holders existed and indeed no notes existed" (Tr. 35). The Sourlis Letter itself makes clear that
13 its purpose was to state whether unrestricted stock could be issued in exchange for the supposed notes.
14 Its misrepresentations underlying its conclusion that such shares could, consistent with the Securities
15 Act, be issued without a restrictive legend plainly enabled Frohling to instruct Greenstone's transfer
16 agent to issue, in exchange for nonexistent notes, unrestricted stock that was then sold by the
17 recipients. The district court did not err in ruling as a matter of law that Sourlis, in violation of
18 § 20(e), aided and abetted violations of § 10(b) and Rule 10b-5.

19 The district court subsequently ruled that Sourlis's knowingly false statements that she
20 had spoken to the note holders, along with her misrepresentations as to facts she had not verified, also
21 warranted holding her liable as a primary violator of § 10(b) and Rule 10b-5. (*See* Hearing Transcript
22 July 21, 2015, at 4, 21-22.) That ruling, reflected in the Superseding Final Judgment, is amply
23 justified by the record described above.

1 In No. 14-2937, the SEC cross-appealed to challenge so much of the district court's
2 November 20 Order as had denied its motion for partial summary judgment holding Sourlis liable
3 under § 10(b) and Rule 10b-5 as a primary violator. Since the Superseding Final Judgment holds
4 Sourlis liable under those provisions as a primary violator, the SEC's cross-appeal is moot.

5 B. *Relief*

6 "Once the district court has found federal securities law violations, it has broad
7 equitable power to fashion appropriate remedies," *SEC v. First Jersey Securities, Inc.*, 101 F.3d 1450,
8 1474 (2d Cir. 1996) ("*First Jersey*"), *cert. denied*, 522 U.S. 812 (1997), and its choice of remedies is
9 reviewable for abuse of discretion, *see, e.g., id.* at 1474-77; *SEC v. Contorinis*, 743 F.3d 296, 301 (2d
10 Cir. 2014), *cert. dismissed*, 136 S. Ct. 531 (2015). Sourlis, in addition to denying any responsibility
11 in connection with the unlawful issuance of the 6,150,000 shares to which her opinion letter pertained,
12 argues that that letter was a one-time occurrence that did not warrant a civil penalty or injunctive
13 relief.

14 Civil monetary penalties are authorized by the Securities Act and the Exchange Act for
15 both deterrent and punitive purposes. *See, e.g., SEC v. Razmilovic*, 738 F.3d 14, 38-39 (2d Cir. 2013).

16 And injunctive relief is

17 particularly within the court's discretion where a violation was founded on
18 systematic wrongdoing, rather than an isolated occurrence, . . . and where the
19 court views the defendant's degree of culpability and *continued protestations*
20 *of innocence* as indications that injunctive relief is warranted, since "*persistent*
21 *refusals to admit any wrongdoing ma[k]e it rather dubious that [the offenders]*
22 *are likely to avoid such violations of the securities laws in the future in the*
23 *absence of an injunction.*"

24 *First Jersey*, 101 F.3d at 1477 (quoting *SEC v. Lorin*, 76 F.3d 458, 461 (2d Cir. 1996) (other internal
25 quotation marks omitted) (emphases ours)).

