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6 **IN THE UNITED STATES DISTRICT COURT**
7 **FOR THE DISTRICT OF ARIZONA**

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9 Strategic Diversity, Inc., a Massachusetts
10 corporation; and Kenneth P. Weiss, an
unmarried man,

11 **Plaintiffs,**

12 v.

13 Alchemix Corporation, an Arizona
14 corporation; and Robert R. Horton and
Cheryl Halota Horton, husband and wife,
15 Medici Associates, LLC, a Delaware
limited liability company,

16 **Defendants.**

No. CV-07-00929-PHX-GMS

**FINDINGS OF FACT AND
CONCLUSIONS OF LAW**

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18 On March 28, 2013, the issue of damages relating to Plaintiff Kenneth P. Weiss's
19 securities fraud claims was tried to the Court without a jury. (Doc. 269.) This Order
20 constitutes the Court's findings of fact and conclusions of law under Federal Rule of
21 Civil Procedure 52(a).

22 **BACKGROUND**

23 This case involves a \$500,000 loan by Plaintiff Strategic Diversity, Inc.
24 ("Strategic") to Defendant Robert R. Horton's company, Defendant Alchemix
25 Corporation ("Alchemix"). Also at the center of this case is the subsequent and separate
26 purchase by Weiss, the sole owner of Strategic, of 250,000 shares of Alchemix stock at
27 the price of \$1.00 per share. In their operative Amended Complaint (the "Complaint")
28 both Weiss and Strategic bring claims for equitable relief and damages.

FINDINGS OF FACT

I. Strategic's Note with Alchemix

Horton is the founder and CEO of Alchemix, an alternative fuels start-up company. (Doc. 203, Final Pretrial Order ¶ B(1)(c)–(d).) Sometime after their first meeting, Horton offered Weiss an investment opportunity with Alchemix. (*Id.* at 19:7–9.) On July 2, 2001, Weiss's investment company, Strategic, agreed to loan \$500,000 to Alchemix. Strategic and Alchemix consummated the loan through a Convertible Promissory Note (the "Note"), payable after five years at ten-percent interest, or convertible to stock at a price of \$2.00 per share. (Doc. 127-2, Ex. 1.) In exchange for consummating the Note, Strategic was given a security interest in Alchemix's patents and Weiss was given a seat on Alchemix's Board of Directors (the "Board") until the Note was repaid. (Doc. 127-4, Ex. 18 at 90; Doc. 129-2, Ex. B at ALCHX00156 ¶ 4.) The agreements provided that the security interest and Weiss's seat on the Board endured "until the Note [h]as been satisfied or converted" into stock. (Doc. 127-2, Ex. 2; Doc. 129, Ex. B at ALCHX00156 ¶ 4.)

In addition, the Note granted Alchemix the right to prepay its debt after one year. The conditions on Alchemix's right to prepay were that Alchemix had to: (1) give Strategic thirty days advanced written notice before prepayment; (2) pay a \$10,000 prepayment penalty; and (3) during the notice period, give Strategic the option to convert the Note into 250,000 shares of Alchemix stock at the lower of \$2.00 per share or such price as offered to other investors at the time. (Doc. 127-2, Ex. 1 at 2–3.) Alchemix further provided Strategic with a Stock Purchase Warrant, whereby Alchemix was required to obtain Strategic's consent before increasing the number of capitalized shares beyond 40 million because of the dilutive nature of such an increase in shares. (*See* Doc. 129-2, Ex. B at ACLHX00165 ¶ 4c.)

II. Western's Investment in Alchemix

Approximately one year later, in the Spring and Summer of 2002, Horton sought to raise additional capital to develop Alchemix's technology. (*See* Doc. 127-4, Ex. 15,

1 June 11, 2002 Board Minutes at ALCHX00605-04; Doc. 203, Final Pretrial Order ¶
2 B(1)(i).) In cooperation with Horton, a group of investors called the Alchemix Funding
3 Group (“AFG”) sought to obtain additional investment capital for Alchemix through
4 additional sales of stock. Horton, however, began investment discussions with Western
5 Oil Sands (“Western”), a large Canadian energy company. In June 2002, Horton and
6 Alchemix received an investment proposal from Western.

7 Horton initially met with Western’s Chairman and CEO, Guy Turcotte, on June
8 12, 2002. (Doc. 224, Jury Trial Tr. at 147:10–148:1.) On June 17, 2002, Western sent a
9 Memorandum of Understanding (the “Memorandum”) which described the terms of the
10 investment and a wire transfer of \$3 million to Horton. (*Id.* at 148:2–6.) The
11 Memorandum granted Western 1.5 million shares of Alchemix stock at a price of \$2.00
12 per share. (Doc. 127-2, Ex. 9, Memorandum at SDI000080.) The Memorandum further
13 granted Western the “right to purchase” up to an additional \$33 million in Alchemix
14 stock in the subsequent months conditioned on Alchemix meeting benchmarks. (*Id.*) The
15 Memorandum referred to these rights to purchase stock as “options.” (*Id.*) Alchemix
16 consummated the Western investment on June 18, 2002. (Doc. 203, Final Pretrial Order ¶
17 B(1)(n).)

18 On June 18, 2002, Horton announced the Western investment and sent the
19 Memorandum to Weiss and the rest of the members of the Board. (Doc. 203, Final
20 Pretrial Order ¶ B(1)(m).) On June 24, 2002, Horton contacted Weiss to discuss
21 Western’s investment. Horton told Weiss that Western was a multibillion dollar Canadian
22 company with expertise in energy and would be a good strategic partner for Alchemix.
23 (Doc. 224, Jury Trial Tr. at 42:24–43:3.)

24 Alchemix decided to repay the Note from Strategic, including the early payment
25 penalty. Strategic elected to waive the 30-day notice provision. In the subsequent weeks,
26 Weiss and his executive assistant, Arthur Hagopian, worked with Alchemix’s CFO,
27 Richard Armstrong, to execute a series of documents reflecting the repayment of the Note
28 to Strategic, Strategic’s relinquishment of its security interest in Alchemix’s patents and

1 Weiss's resignation from the Board. (*See* Pls. Exs. 7–10, 13–14, 17; Doc. 129-3, Ex. G at
2 SDI000069.) On July 2, 2002, Strategic accepted \$560,832 from Alchemix as repayment
3 of principal, interest, and prepayment penalties under the Note. (Pls. Ex. 10; Doc. 136-12,
4 Ex. K.) Weiss formally resigned from the Board on July 11, 2002. (Doc. 203, Final
5 Pretrial Order ¶ B(1)(t).) Finally, on August 5, 2002, Strategic released its security
6 interest in Alchemix's patents. (Pls. Ex. 19.)

7 **III. Weiss's Stock Purchase From Medici**

8 In late June or early July 2002, Horton made an offer to sell shares at a favorable
9 price to members of AFG for their ultimately unused efforts to raise investment capital
10 for Alchemix. (Doc. 224, Jury Trial Tr. at 107:25–108:21.) In conjunction with that offer,
11 Horton offered Alchemix stock held by his holding company, Medici Associates, LLC
12 ("Medici"), to Weiss at the same price of \$1.00 per share. (*Id.* at 45:16–46:5.) Weiss
13 accepted Horton's offer to invest in Alchemix. On July 8, 2002, Weiss signed a
14 subscription agreement and purchased 250,000 shares of Alchemix stock for \$250,000
15 from Medici. (Pls. Exs. 15, 17; Doc. 127-2, Ex. 11 (Subscription Agreement); Doc. 203
16 (Final Pretrial Order) ¶¶ 1(r)–(s).) Weiss's stock purchase from Medici was wholly and
17 entirely separate from Strategic's Note to Alchemix.

18 **IV. Western's Decision Not to Exercise its Options**

19 Three to four weeks after their initial meeting on June 12, 2002, Turcotte informed
20 Horton that Western's Board of Directors had decided that Western would not invest
21 further in any ventures outside of their immediate projects. (Doc. 224, Jury Trial Tr. at
22 176:1–11; Doc. 127-4, Ex. 19 (Gregory Depo.) at 50:9–13.) Turcotte further told Horton
23 that Western would not exercise its options to purchase Alchemix shares, though Western
24 would retain its initial investment of \$3 million. (Doc. 224, Jury Trial, Tr. at 184:24–
25 185:2; 244:3–245:9.)

26 Immediately after Western's decision was communicated to him, Horton convened
27 a meeting with the Board to apprise it of the development. (*Id.* at 185:21–25.) Horton did
28 not inform Weiss because Weiss was no longer on the Board and Alchemix had 500 other

1 shareholders. (*Id.* at 186:1–4.) Horton did not contact Weiss at any time after that
2 meeting to inform him of Western’s decision. (*Id.* at 186:20–25.)

3 In late 2005, Weiss met with Horton to discuss his investment in and the corporate
4 health of Alchemix since he had not received regular updates as a shareholder of the
5 company. (*Id.* at 57:4–19.) It was at this meeting that Weiss first learned from Horton that
6 Western had not exercised its options. (*Id.* at 58:11–13.)

7 **V. The Complaint and Summary Judgment**

8 On May 7, 2007, Weiss and Strategic brought suit against Alchemix, Robert and
9 Cheryl Horton, and Medici. In their Complaint, Plaintiffs alleged the following counts: 1)
10 federal securities fraud (15 U.S.C. § 78j and Rule 10b-5); 2) state securities fraud in
11 violation of the Arizona Securities Act (the “ASA”) (A.R.S. § 44-1991); 3) common law
12 fraud; 4) statutory fraud (A.R.S. § 44-1521, et seq.); 5) negligent misrepresentation; 6)
13 mistake/rescission; 7) failure of condition precedent; 8) equitable restitution; and 9)
14 punitive damages. (Doc. 54.) Plaintiffs requested the Court to provide the equitable relief
15 of (1) reinstating Strategic’s Note to Alchemix and its security interest in Alchemix’s
16 patents; (2) reinstating Weiss to the Board; and (3) voiding Weiss’s purchase of
17 Alchemix stock and restoring all consideration given by Weiss for that stock. (*Id.* at 21.)
18 Plaintiffs further requested compensatory and actual damages, interest, punitive damages,
19 and taxable costs and reasonable attorneys’ fees incurred in this action. (*Id.*)

20 Initially, the Court dismissed the statutory fraud claim (count four) as time-barred.
21 (Doc. 29 at 1; Doc. 148 at 7 n.4.) The Court then granted summary judgment to
22 Defendants on all of Plaintiffs’ remaining claims. (Doc. 148 at 19.) To the extent that
23 Plaintiffs’ federal and state securities fraud claims were based on Horton’s omission
24 regarding Western’s investment, the Court held that those claims were barred under the
25 statute of limitations. (*Id.* at 8.)

26 To the extent Plaintiffs’ fraud claims were not time-barred, the Court held that
27 they failed because Plaintiffs had not demonstrated economic loss or other injury. (*Id.* at
28 13.) At the outset, the Court made clear that although Plaintiffs alleged that the stock

1 purchase was part of a two-pronged, but single “debt-equity swap,” the undisputed facts
2 demonstrated that Alchemix’s repayment of the Note to Strategic was separate from
3 Weiss’s purchase of the 250,000 shares from Horton. (*Id.* at 5.) Strategic could not have
4 entered into a “debt-equity swap” as Weiss obtained the equity rather than Strategic and
5 Strategic made the Note rather than Weiss. Accordingly, Weiss’s purchase of the 250,000
6 shares must have been separate from Strategic’s accepting repayment of the Note

7 Defendants had a unilateral right to pay off the Note to Strategic one year from
8 origination. That right to prepayment was based on three conditions as described above.
9 Defendants did not fulfill the conditions of notifying Strategic thirty days in advance and
10 providing Strategic the option to convert the Note into shares of Alchemix stock.
11 Plaintiffs, however, did not prove that Strategic suffered injury as a result. They conceded
12 to the lack of injury at oral argument. Further, Weiss, the owner of Strategic, purchased
13 Alchemix shares after the Note was prepaid by Defendants. Plaintiffs also did not prove
14 that Weiss was somehow damaged by the purchase price of Alchemix stock of \$1.00 per
15 share. Thus, the Court held that Plaintiffs failed to show injury.

16 As to the Plaintiffs’ equitable claims, the Court first held that there was no claim
17 for rescission based on mutual mistake because there was no mistake of fact. (*Id.* at 17.)
18 Although it is not clear that Arizona recognizes a claim for failure of condition precedent,
19 that claim also failed as a matter of law because the conditions were fulfilled. (*Id.* at 18).
20 Upon accepting repayment, Strategic was required to release its security interest in
21 Alchemix’s patents and Weiss was required to resign from the Board. Finally the
22 equitable restitution/unjust enrichment claim failed because Plaintiffs failed to show any
23 element of “impoverishment” or injury as discussed above. (*Id.*)

24 **VI. Appeal**

25 Plaintiffs appealed all of the Court’s rulings including the grant of summary
26 judgment to Defendants. (Doc. 152 at 1.) The Ninth Circuit did not address the Court’s
27 dismissal of the statutory fraud claim (count four). It affirmed judgment for Defendants
28 as to Plaintiffs’ state law claims of common law fraud (count three), negligent

1 misrepresentation (count five), mutual mistake (count six), failure of a condition
2 precedent (count seven), and unjust enrichment (count eight), but reversed and remanded
3 the federal and state securities fraud claims (counts one and two) for consideration under
4 a “rescissionary measure of damages.” *Strategic Diversity, Inc. v. Alchemix Corp.*, 666
5 F.3d 1197, 1211 (9th Cir. 2012).

6 Those claims were apparently reversed as to both Strategic’s and Weiss’s claims.
7 The Ninth Circuit did not address this Court’s determination that Strategic could show no
8 damage and that the transaction between Strategic, Weiss and the Defendants could not
9 have been a “debt-equity swap” as the transactions were between separate parties.¹
10 Instead, the Ninth Circuit determined that while Weiss could tender his 250,000 shares to
11 rescind his purchase of Alchemix stock, it would not be possible to return to Strategic the
12 rights it had received from Alchemix pending the complete repayment of its Note which
13 occurred in June 2002. These rights included Strategic’s security interests in Alchemix’s
14 intellectual property and right to name a director, Weiss, to the Board. The Ninth Circuit
15 reasoned:

16 Although Weiss stands ready to tender the 250,000 shares of Alchemix for
17 the consideration he offered (\$250,000) The Note has long since
18 expired, coming due in July 2006. We doubt that Weiss’s demand for his
19 seat on the Alchemix Board is even possible when there does not appear at
20 present to be an existing board. In addition, true rescission would also
involve the unfurling of security interests that are currently held as
collateral on other debts.

21 (*Id.* at 1207–08.)

22 While the panel opinion did not explain why Weiss could not tender the stock to
23 rescind his stock purchase, it apparently held that because tender was impossible for both
24 Weiss and Strategic neither was entitled to rescission, but both might be entitled to the

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28 ¹ As discussed above, the Note was between Strategic and Alchemix while the
Stock Purchase Agreement was between Weiss and Medici.

1 equitable remedy of rescissionary damages upon reconsideration by this Court.²

2 Nevertheless, on remand, Strategic acknowledged that it had no claims against the
3 Defendants. Thus, regardless of whether the Ninth Circuit reversed this Court's holding
4 *sub silentio* that, as a matter of law, Alchemix's repayment of the Note to Strategic and
5 Weiss's subsequent purchase of Alchemix stock from Medici could not have been a debt
6 equity swap, Weiss's tender of the stock as a condition of the rescission which he sought
7 was no longer either difficult or impossible. As the Ninth Circuit noted, the only facts
8 that made tender impossible arose from Strategic's request to rescind Alchemix's
9 repayment and reinstate its Note and security interest. (*Id.*) Once that request was
10 dropped, tender of the stock for the amount claimed became possible because, as it noted
11 in its opinion, Weiss could still tender his stock³ as a condition precedent to rescission.

12 In fact, during a status conference after remand, Plaintiff's counsel agreed that
13 Strategic no longer had a remedy and the remaining issue was whether Horton and/or
14 Alchemix made a misrepresentation or omission that caused Weiss to invest in Alchemix.
15 (March 2, 2012, Hearing Tr. at 5:20–6:17, 7:5–9, 10:16–18.) Plaintiff's counsel also
16 agreed that there was no difficulty with a rescission remedy as to Weiss's investment.
17 (*Id.*) Rescission is the only claim Weiss sought for the stock purchase in his Complaint,
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19 ² On appeal, Plaintiffs continued to assert that the repayment of the Note to
20 Strategic and the subsequent stock purchase by Weiss constituted a debt-equity swap that
21 inextricably combined the interests of Weiss and Strategic as it related to the Defendants.
22 (Opening Brief of Plaintiffs-Appellants, 2010 WL 6415455, *21) (“As noted above, the
23 gravamen of the District Court's errors in this matter was its conclusion that the
24 repayment of the Note and concurrent purchase of Alchemix stock ‘must have been
25 separate’ and unrelated transactions.”). The undisputed facts, however, were actually to
26 the contrary.

24 The Ninth Circuit may not have observed that this Court held that the transaction
25 could not have involved a debt-equity swap as a matter of law. Thus, the Ninth Circuit
26 may not have perceived any need to offer explanation as to how the transaction could
27 have constituted a debt-equity swap and thus why it would not have been possible for
28 Weiss to tender his stock as a necessary condition to rescinding his stock purchase, even
if tender would have been difficult at best for Strategic in its attempt to rescind
Alchemix's repayment of its Note.

³ As this Court is aware or can recall, Weiss has not yet tendered his Alchemix
stock to the Defendants.

1 (see Doc. 54 (Compl.) at 21), and hence, the only claim to which he is entitled. The
2 Ninth Circuit's opinion that the Plaintiffs could seek rescissionary damages as opposed to
3 rescission was explicitly based on its assumption that Weiss could no longer tender the
4 stock he had received from Medici. *Strategic Diversity*, 666 F.3d at 1208.

5 **VII. Trial on Remand**

6 After remand, the issue of fact of whether Horton made a material
7 misrepresentation or omission to Weiss in relation to Weiss's stock purchase from Medici
8 was tried to a jury. (Docs. 209, 211.) At trial, the Court granted judgment as a matter of
9 law against Strategic because, as Plaintiffs conceded, Strategic did not have a claim for
10 damages in this case. (Doc. 211.) Because the remaining relief requested by Weiss was
11 equitable relief that depended on the resolution of certain issues of fact the jury verdict
12 consisted of answers to several special interrogatories in a special verdict form.

13 On August 30, 2012, the jury found that (1) Horton made a misrepresentation or
14 omission of fact to Weiss in connection with the sale of 250,000 shares of Alchemix
15 stock to Weiss; (2) the misrepresentation or omission was material to Weiss's decision to
16 purchase the shares; (3) Weiss justifiably relied on the misrepresentation or omission in
17 making the decision to purchase the shares; (4) the misrepresentation or omission caused
18 Weiss to purchase the shares; (5) Weiss should not have discovered the facts underlying
19 the misrepresentation or omission prior to discovering it on May 7, 2005; and (6) Horton
20 learned that Western was not going to exercise its options before Weiss purchased shares
21 on July 8, 2002. (Doc. 218, Jury Verdict.)

22 On December 3, 2012, the Court denied the Defendants' Motion for Judgment
23 Renewed and Motion for New Trial. (Doc. 248.) At the Plaintiffs' request the Court
24 conducted a bench trial on March 28, 2013, regarding damages. (Doc. 269.)

25 **VIII. Value of Alchemix Stock in Years Subsequent to the Omission**

26 At trial and the subsequent hearing, evidence was introduced from which the
27 Court makes the following findings. The value of Alchemix stock for the period
28 following Horton's omission in July 2002 is opaque. There is no evidence of additional

1 sales of Alchemix stock until 2006. In September 2003, Horton had taken the position
2 that Alchemix stock was “worthless” because there was no market for the stock at the
3 time. (Doc. 224, Jury Trial Tr. at 267:4–13.) Horton testified that not obtaining the
4 additional investment from Western was “bad news” for Alchemix. (*Id.* at 185:12.)
5 Horton testified, however, that six months after Western’s decision, Alchemix formed a
6 joint venture with a large mining and minerals processing company in which the
7 company contributed \$2 million, which may have brought value to Alchemix stock. (*Id.*
8 at 264:5–10.)

9 During the period after late 2005 when Weiss discovered Horton’s omission,
10 Horton sold Alchemix stock to a few private investors at the price of \$2.00 per share.
11 (Bench Trial Tr. at 164:13–15.) In the fall of 2006, Horton sold shares to a wealthy
12 widow, Mary Menk, a shareholder whom Horton had known for a long time. (*Id.* at
13 177:17–25.) Menk approached Horton to purchase shares for herself and as a gift for her
14 employee, Patricia Townsend. (*Id.* at 178:1–9.) In the fall of 2008, Horton sold shares to
15 another shareholder, Paul Schilling, a senior citizen and “big supporter” of Horton. (*Id.* at
16 177:12–178:23.) Because of the “collapse of the gas market” in 2008, Schilling knew that
17 Horton “needed some help” and was willing to invest in Alchemix to help it through
18 difficult times. (*Id.*) Schilling purchased 100,000 shares at the price of \$2.00 per share.
19 (*Id.* at 165:19–24.)

20 In addition to these sales to individuals, Alchemix entered into a partnership with
21 Diversified Energy Corporation (“Diversified”), a company that invests in a diversified
22 portfolio of energy technologies. (*Id.* at 178:13–19.) In April 2006, Alchemix executed a
23 stock purchase agreement with Diversified. (*Id.*) The agreement was for a purchase of 2.5
24 million shares of Alchemix stock at the price of \$2.00 per share (*Id.* at 164:21–165:2.)
25 Diversified provided a \$600,000 down payment and \$4.4 million via promissory note.
26 (*Id.* at 178:20–179:3.) Alchemix purchased also an unspecified number of shares of
27 Diversified stock. (*Id.* at 182:9–11.) Around the same time, the parties entered into a
28 management consulting, marketing, and advocacy arrangement. (*Id.* at 181:17–20.)

1 Alchemix paid Diversified \$1.5 million in exchange for Diversified’s assistance in
2 demonstrating Alchemix’s technology, obtaining access to government funding, and
3 soliciting the Department of Energy. (*Id.* at 179:4–180:25.) Alchemix paid Diversified
4 \$18,500 and \$83,330 per month for these services pursuant to two separate agreements.
5 (*Id.* at 182:12–25.) In the fall of 2012, Alchemix and Diversified unwound and rescinded
6 the entire arrangement and both parties divested their stock investment in the respective
7 companies. (*Id.* at 184:2–16.) Diversified retains a limited license to use Alchemix’s
8 Hydromax technology in the United States that it received in connection with these
9 dealings, for which Diversified does not pay fees to Alchemix. (*Id.* at 184:21–23.)

10 CONCLUSIONS OF LAW

11 I. Federal Securities Fraud Claim

12 “The elements of a private action under Rule 10b–5 are (1) a material
13 misrepresentation or omission by the defendant; (2) scienter; (3) a connection between
14 the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon
15 the misrepresentation or omission; (5) economic loss; and (6) loss causation.” *Janus*
16 *Capital Group, Inc. v. First Derivative Traders*, ___ U.S. ___, ___, n.3, 131 S.Ct.
17 2296, 2301, n.3, 180 L.Ed.2d 166 (2011) (citing *Stoneridge Investment Partners, LLC v.*
18 *Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008)). Rescission is an available remedy for
19 federal securities fraud claims. *See Ah Moo v. A.G. Becker Paribas, Inc.*, 857 F.2d 615,
20 623 (9th Cir. 1988) (internal citations omitted).

21 In a 10b-5 action, the Court must consider “whether the plaintiff has shown some
22 causal connection between the fraud and the securities transaction in question.” *In re*
23 *Daou Sys., Inc.*, 411 F.3d 1006, 1025 (9th Cir. 2005). The causation requirements
24 comprised of both reliance and proximate cause or “loss causation.” *Id.* To establish
25 transaction causation, the plaintiff must show that but for the material misrepresentation
26 or omission, he would not have engaged in the transaction. *Stoneridge*, 552 U.S. at 171.
27 To establish the necessary elements of loss a party must show both economic loss and
28 loss causation. To prove loss causation, the plaintiff must demonstrate that the

1 defendant's deceptive acts proximately caused the plaintiff's loss. *Dura Pharm., Inc. v.*
2 *Broudo*, 544 U.S. 336, 346 (2005).

3 When evaluating evidence as to loss causation, the Supreme Court has held that
4 "to touch upon a loss is not to *cause* a loss." *Dura Pharm.*, 544 U.S. at 336 (emphasis in
5 original); see *Metzler Inv. GMBH v. Corinthian Colleges, Inc.*, 540 F.3d 1049, 1064 (9th
6 Cir. 2008) ("Loss causation requires more."). Yet, a plaintiff is not required to show "that
7 a misrepresentation was the *sole* reason for the investment's decline in value" in order to
8 establish loss causation. *Daou Sys.*, 411 F.3d at 1025 (citation omitted) (emphasis in
9 original). "[A]s long as the misrepresentation is one substantial cause of the investment's
10 decline in value, other contributing forces will not bar recovery under the loss causation
11 requirement" but will play a role "in determining recoverable damages." *Id.*

12 Although the jury found transaction causation based on a special interrogatory in
13 the jury verdict form, Plaintiff did not request that the jury answer an interrogatory as to
14 whether Defendants' acts caused Weiss to suffer economic losses. Thus, the Court is left
15 to determine loss causation based on the evidence in the record. On appeal, the Ninth
16 Circuit noted that Weiss's request for relief "does not relieve [him] of demonstrating loss
17 causation." *Strategic Diversity*, 666 F.3d at 1209 (citing 15 U.S.C. § 78bb (limiting
18 recovery to damages "on account of the act complained of"))).

19 One manner in which Weiss may establish loss causation is by proving that the
20 price of his shares declined after the facts underlying Horton's omission or
21 misrepresentation became known, otherwise known as a "fraud on the market" theory.
22 *Metzler*, 540 F.3d at 1062. Weiss purchased 250,000 Alchemix shares at the price of
23 \$1.00 per share. To recover damages based on a "fraud on the market" theory, the
24 relevant time period during which Weiss must show loss is soon *after* he and/or other
25 investors learned of the omission. Weiss did not provide sufficient evidence at trial that
26 the share price declined soon after it was revealed to him or other investors that Western
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1 had decided not to exercise its options.⁴

2 A decline in stock price is not the only method through which Weiss may show
3 loss causation. “With a privately held company, a comparison of market stock price to
4 establish loss causation has less relevance because market forces will less directly affect
5 the sales prices of shares of a privately held company.” *WPP Luxembourg Gamma Three*
6 *Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1053 (9th Cir. 2011) *cert. denied*, 132 S. Ct.
7 2713, 183 L. Ed. 2d 68 (2012) (internal citations omitted). In these cases, plaintiffs more
8 commonly prove loss causation by showing that a misrepresentation or omission caused
9 them to engage in a transaction and that the revelation of the truth is directly related to
10 their economic loss. *Id.* (citing *Livid Holdings Ltd. v. Salomon Smith Barney, Inc.*, 416
11 F.3d 940, 949 (9th Cir. 2005)).

12 In *Livid Holdings*, the plaintiff purchased several million dollars’ worth of shares
13 in a closely-held company based on an offering memorandum authored by the
14 defendants. The memorandum stated that a large private equity fund-raising had been
15 completed when only a fraction of it had, in fact, been completed. 416 F.3d at 944–45.
16 The company then entered bankruptcy proceedings at which time the plaintiff discovered
17 that the memorandum was false. *Id.* at 950–51. The Ninth Circuit held that the plaintiff
18 had pled loss causation because the defendants’ alleged misrepresentation concealed the
19 company’s financial situation and “[a]s a result of its dire financial situation, [the
20 company] eventually went bankrupt, which caused [the plaintiff] to lose the entire value
21 of its investment in [the company].” 416 F.3d at 949. The court did not require the
22 plaintiff to allege variation in the stock price to plead loss causation, holding that
23 “[u]nder these circumstances, *Dura* is not controlling.” *Id.* at 949 n.2. Rather, to find that

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25 ⁴ Weiss contends that Horton’s “anecdotal testimony” of a “handful of isolated
26 sales to private individuals in 2006 and 2008” and “opaque” sales of stock to Diversified
27 Energy in 2007 do not provide reliable evidence upon which to conclude that the price of
28 Alchemix shares remained at or above \$2.00 per share after 2005. (Doc. 276 at 3.) But it
is Weiss’s burden to prove, if at all, that his shares declined in value below \$1.00 per
share after it became apparent that Western was not going to make further investments in
Alchemix. See *Metzler*, 540 F.3d at 1062. It is not sufficient to carry such a burden by
attacking the reliability of Defendants’ evidence.

1 loss causation was properly pled, the court relied upon the reduction in value of the
2 plaintiff's investment as a result of the truth concealed by the misrepresentation.

3 Weiss has not established that Western's decision not to exercise its options was a
4 "substantial cause of [his] investment's decline in value." *Daou Sys.*, 411 F.3d at 1025.
5 The company in *Livid Holdings* had a "negative net worth" of several hundreds of
6 thousands of dollars and the unsuccessful private equity fund raising was the decisive
7 blow to its financial viability. 416 F.3d at 947. The company went bankrupt soon after
8 plaintiff invested in it based on the misrepresentation regarding the company's
9 fundraising. *Id.* at 949. Weiss, conversely, did not present sufficient evidence to show
10 that in July 2002 or soon thereafter, his investment in Alchemix was reduced in value as a
11 result of Western's decision not to exercise its options.

12 The jury found that Horton omitted to inform Weiss that Western would not
13 exercise its options before Weiss purchased Alchemix stock. Although it is possible that
14 the value of Alchemix stock declined as a result of Western's decision, Weiss did not
15 show that it declined below \$1.00 a share at the time he purchased it for that price. Three
16 weeks before Weiss purchased 250,000 shares of Alchemix stock, Western purchased 1.5
17 million shares for \$2.00 per share. Even if Western decided not to exercise its subsequent
18 options, it had just invested \$3 million in the enterprise. Therefore, it is also possible that
19 Weiss received an advantageous price per share and that even if the stock declined in
20 value, it was not to a level below \$1.00 per share. Thus, Weiss did not show that he was
21 harmed by the omission.

22 Nor did Weiss show that the value of the stock declined below \$1.00 per share
23 soon after he purchased it in July 2002. Weiss points to Horton's testimony that he
24 considered Alchemix stock to be worthless as of September 2003 insofar as there was no
25 market for the stock. Weiss further contends that because Western decided not to exercise
26 its options, Alchemix was not able to build a demonstration plant to prove the
27 commercial viability of its Hydromax technology, which Horton estimated would cost
28 \$35 million to build. Western's decision was, according to Horton, "bad news" for

1 Alchemix as an early-stage technology company. As a result, Weiss argues, Alchemix
2 could not conduct business operations, raise operating revenues, or attract additional
3 investors, ultimately reducing the value of Weiss's investment to a penny per share.

4 Alchemix did not attract another investment capable of funding its Hydromax
5 technology in order to develop revenue. But Weiss did not show that it was not possible
6 for Alchemix to attract investment and that therefore Western's decision not to invest was
7 damaging to Alchemix's financial viability and as a result, to Weiss's stock value. In fact,
8 Weiss testified that six months after Western's decision, Alchemix formed a joint venture
9 with a large mining and minerals processing company in which the company contributed
10 \$2 million. Further, Weiss did not provide evidence that he could not have resold his
11 shares for at least \$1.00 per share.

12 Although the jury found that Weiss relied upon Horton's assurances regarding
13 Western's investment and that Weiss would not have invested otherwise, "establishing
14 'loss causation' is a more difficult task." *Daou Sys.*, 411 F.3d at 1025. Weiss has not
15 carried his burden prove loss causation and thus may not get rescission for securities
16 fraud pursuant to 10b-5.

17 **II. State Securities Fraud Claim**

18 In his Complaint, Weiss alleged that in making material misrepresentations or
19 omissions regarding the Western investment, Defendants violated the ASA. This statute
20 states, in relevant part,

21 A. It is a fraudulent practice and unlawful for a person, in connection with a
22 transaction or transactions within or from this state involving an offer to
23 sell or buy securities, or a sale or purchase of securities, . . . directly or
indirectly to do any of the following:

24 1. Employ any device, scheme or artifice to defraud.

25 2. Make any untrue statement of material fact, or omit to state any
26 material fact necessary in order to make the statements made, in the
27 light of the circumstances under which they were made, not
28 misleading.

1 3. Engage in any transaction, practice or course of business which
2 operates or would operate as a fraud or deceit.

3 A.R.S. § 44-1991(A). Weiss alleged that Defendants violated all three of these
4 subsections.⁵ Rescission is an available remedy under the ASA:

5 A sale or contract for sale of any securities to any purchaser in violation of .
6 . . . [Section 44-1991] is voidable at the election of the purchaser, and the
7 purchaser may bring an action . . . to recover the consideration paid for the
8 securities, with interest, taxable court costs and reasonable attorney fees,
9 less the amount of any income received by dividend or otherwise from
10 ownership of the securities, on *tender* of the securities purchased

11 A.R.S. § 44-2001(B) (emphasis added).

12 **A. Joint and Several Liability**

13 Pursuant to the ASA, “an action brought under § 44-2001 . . . may be brought
14 against any person, including any dealer, salesman or agent, who made, participated in or
15 induced the unlawful sale or purchase, and such persons shall be jointly and severally
16 liable to the person who is entitled to maintain such action.” A.R.S. § 44-2003. The relief
17 requested in this action, however, is rescission, not damages. “The contractual remedy of
18 rescission abrogates the contract and undoes it from the beginning; that is, not merely to
19 release the parties from further obligation to each other in respect to the subject of the
20 contract, but to annul the contract and restore the parties to the relative positions which
21 they would have occupied if no such contract had ever been made.” *Hall v. Read Dev.,*
22 *Inc.*, 229 Ariz. 277, 285, 274 P.3d 1211, 1219 (Ct. App. 2012), *review denied* (Aug. 28,
23 2012), *as amended* (Apr. 26, 2012). (internal quotation marks and citation omitted). As
24 rescission is primarily a remedy between principals, an agent that “was not a party to the
25 contract and received nothing from the other party, . . . is subject only to an action of

26 ⁵ The Complaint alleges that Defendants “made untrue statements of material fact,
27 or omitted to disclose material facts, which, in light of the circumstances under which
28 they occurred, were materially misleading, and Defendants further employed a device,
scheme or artifice to defraud Plaintiffs in connection with said transactions, or otherwise
engaged in a course or practice which operated as a fraud and deceit upon Plaintiffs
within the meaning of A.R.S. § 44-1991.” (Doc. 54 ¶ 41.)

1 tort,” not an action for rescission. Restatement (Second) of Agency § 348 (1958). Weiss
2 purchased the 250,000 shares of Alchemix stock from Medici, Horton’s personal holding
3 company and paid \$250,000 to that entity. The contract was between Weiss and Medici.
4 Thus, if Weiss succeeds on his claim, Medici is the party liable for restoring the
5 consideration Weiss paid for Alchemix stock.

6 **B. Loss Causation**

7 Arizona’s loss causation requirement is contained in Section 44–2082(E). That
8 Section “requires any plaintiff who brings an action to ‘recover damages’ for a violation
9 of Section 44-1991(A)(1) or (A)(3) to prove ‘that the act or omission of the defendant
10 alleged to violate the section under which the private action is brought caused the loss.’”
11 *Grand*, 214 Ariz. at 27. Section 44–2082(E), however, “does not apply to a rescission
12 claim.” *Id.* at 24. “If tender is possible, proof of proximate cause is not required for
13 traditional rescission relief.” *Id.* at 24, 28. *Id.*

14 Further, Weiss has not proven a claim under subsections (A)(1) or (A)(3) to which
15 the loss causation requirement attaches.⁶ He has proven a claim under subsection (A)(2)
16 insofar as the jury found that Horton made a material omission to Weiss regarding
17 Western’s investment. That subsection does not require a plaintiff to show loss causation.
18 *Grand*, 214 Ariz. at 25.

19 Although Weiss does not have to prove loss causation under subsection (A)(2),
20 Defendants retain a “loss causation affirmative defense provided in § 44-1991(B).”
21 *Grand*, 214 Ariz. at 24. The affirmative defense is stated as follows:

22
23 ⁶ “The subsections of § 44–1991(A) address different violations, and it is not
24 unreasonable for the legislature to require different proof for each.” *Id.* at 26. Liability
25 under subsections (A)(1) or (A)(3) must be premised on more than just an omission of
26 material fact. *See Red River Res., Inc. v. Mariner Sys., Inc.*, CV 11-02589-PHX-FJM,
27 2012 WL 2507517, *10 (D. Ariz. June 29, 2012) (“To permit liability under § 44–
28 1991(A)(1) or (3) solely on the basis of misstatements and omissions would conflate the
three subsections.”). “Manipulative conduct must be distinct from omissions and
misrepresentations under state law as well in order to give meaning to every provision of
§ 44–1991(A).” *Id.* (citing *Grand v. Nacchio*, 225 Ariz. 171, 175–76, 236 P.3d 398, 402–
03 (2010) (“We ordinarily do not construe statutes so as to render portions of them
superfluous.”)). Weiss did not prove that Defendants employed a scheme to defraud or
engaged in a transaction or course of business which would operate as a fraud.

1 B. In a private action brought pursuant to subsection A, paragraph 2 of this
2 section or § 44-1992, if the person who offered or sold the security proves
3 that *any portion or all of the amount recoverable* under subsection A,
4 paragraph 2 of this section or § 44-1992 *represents an amount other than*
5 *the depreciation in value of the subject security* resulting from the part of
6 the prospectus or oral communication, with respect to which the liability of
the person is asserted, not being true or omitting to state a material fact
required to be stated or necessary to make the statement not misleading,
then the amount shall not be recoverable.

7 A.R.S. § 44-1991(B) (emphasis added). In other words, if a defendant proves that a
8 plaintiff's stock did not decline in value as a result of the defendant's omission, then the
9 plaintiff is not entitled to rescission.

10 Arizona courts have not addressed the issue of whether the affirmative defense
11 applies to claims for rescission based on subsection (A)(2). Unlike the loss causation
12 requirement in Section 44-2082(E) which language limits it to claims for damages, the
13 affirmative defense in Section 44-1991(B) refers to "the amount recoverable" which
14 suggests that it is not so limited. In *Grand*, the court referred to that difference in
15 statutory language between "damages" and "the amount recoverable" to determine that
16 Section 44-2082(E) applied only to claims for damages. *See* 214 Ariz. at 24 ("This
17 difference in language shows the legislature's intent to distinguish between a claim for
18 damages and a claim for rescission."). Here, the "amount recoverable" is the
19 consideration Weiss paid for Alchemix stock. Although it is possible Arizona courts
20 would find an affirmative defense unavailable for a rescission claim "if the defendant's
21 intentional fraud can be understood as inducing a transaction that the plaintiff would not
22 have entered at any price if he had known the truth," *Id.* at 25, the Court assumes without
23 holding that an affirmative defense is available in this case.

24 **1. Waiver of Affirmative Defense**

25 Weiss contends that Defendants have waived their affirmative defense because
26 Defendants did not assert it in their Answers, (see Doc. 63, Alchemix and Horton Ans. at
27 6-8; Doc. 64, Medici Ans. at 9-10), raise it in the Parties' Joint Pretrial Order, (see Doc.
28

1 193 at 6–12), or raise it through the filing of a supplemental Final Pretrial Memorandum
2 pursuant to Fed. R. Civ. P. 26(a)(3)(B). The Federal Rules of Civil Procedure control the
3 timing of the assertion of defenses and when waiver occurs. *Han v. Mobil Oil Corp.*, 73
4 F.3d 872, 877 (9th Cir. 1995) (citations omitted). Rule 8(c) requires affirmative defenses
5 to be pleaded in the answer. The Ninth Circuit has held, however, that a defendant’s
6 failure to raise an affirmative defense in its answer does not necessarily waive the
7 defense. *Owens v. Kaiser Foundation Health Plan, Inc.*, 244 F.3d 708, 713 (9th Cir.
8 2001); *see Han*, 73 F.3d at 877–78. The defense may be raised later if the delay in raising
9 it does not prejudice the plaintiff. *Owens*, 244 F.3d at 713 (allowing an affirmative
10 defense for the first time in a motion for judgment on the pleadings); *Camarillo v.*
11 *McCarthy*, 998 F.2d 638, 639 (9th Cir. 1993) (allowing an affirmative defense for the
12 first time in a motion for summary judgment). That is because “[t]he purpose of Rule 8(c)
13 is simply to guarantee that the opposing party has notice of any additional issue that may
14 be raised at trial so that he or she is prepared to properly litigate it.” *Hassan v. U.S. Postal*
15 *Serv.*, 842 F.2d 260, 263 (11th Cir. 1988) (citing *Blonder-Tongue Labs., Inc. v. Univ. of*
16 *Illinois Found.*, 402 U.S. 313, 350 (1971)); *see In re Sterten*, 546 F.3d 278, 285 (3d Cir.
17 2008).

18 Defendants first raised the Section 44-1991(B) affirmative defense in their trial
19 brief filed on the day of the bench trial. (Doc. 267 at 4.) But Defendants did not waive
20 their defense. There was no unfair surprise to Weiss as a consequence of Defendants’
21 failure to plead specifically this defense. Weiss already had the burden to prove loss
22 causation at trial to establish that he was entitled to damages under his federal securities
23 fraud claim. Similarly, Defendants had to establish a lack of loss causation to prove their
24 affirmative defense against Weiss’s state securities fraud claim. *See* § 44-1991(B); *see*
25 *also Sterten*, 546 F.3d at 285 (holding that defendant did not waive its defense because
26 the analysis involved in proving plaintiff’s claim and defendant’s defense were
27 substantially similar). Weiss argued that his Alchemix stock never recovered from the
28 impact of Alchemix losing the Western investment and put on evidence to prove that his

1 stock declined in value. Defendants proffered evidence that the stock was worth more
2 than \$1.00 per share for a period of years after Weiss learned of Horton's omission. It
3 was not unexpected to Weiss for Defendants to do so. The Court does not find any
4 prejudice from allowing Defendants to argue their affirmative defense.

5 **2. Value of Alchemix Stock After Horton's Omission**

6 At trial, the jury found that Horton had made a material omission to Weiss
7 regarding Western's investment. Therefore, Defendants have the burden to show that
8 Weiss's Alchemix stock did not depreciate in value below \$1.00 per share as a result of
9 the subject of the omission: Western's decision not to exercise its options. *See* A.R.S. §
10 44-1991(B).

11 Defendants have not carried their burden. Defendants proffered sales of stock
12 several years after Horton's omission to show that the value of Alchemix stock was
13 greater than \$1.00 per share.⁷ But these isolated sales took place several years after
14 Horton's omission. Further, the stock sales to individuals were based on Horton's
15 personal relationships and the third sale to Diversified was in the context of other
16 agreements through which Alchemix remitted to Diversified much of the funds Alchemix
17 received. They do not rebut Horton's statement in September 2003 that at the time, the
18 stock did not have value. Although that statement was not sufficient for Weiss to prove
19 loss causation, it is relevant to Defendants' affirmative defense.

21 ⁷ Horton testified about three sales of stock that he made to private individuals and
22 an entity between 2006 and 2008 at \$2.00 per share. In the fall of 2006, Horton sold
23 Alchemix stock to Mary Menk, a wealthy shareholder whom Horton had known for a
24 long time. Menk contacted Horton to purchase shares for herself and her employee,
25 Patricia Townsend. In the fall of 2008, Horton sold Alchemix stock to a senior citizen
26 and supporter of Horton, Paul Schilling. Due to the decline in the gas market in 2008,
27 Schilling wanted to help Horton by investing in Alchemix to get it through tough times.
28 Further, as part of a partnership, Diversified agreed to purchase \$5 million worth of
shares in Alchemix at \$2.00 per share in April 2006. The Diversified purchase was
completed in the context of terms and conditions, and other agreements including
Alchemix's purchase of Diversified stock, a consulting agreement through which
Alchemix paid Diversified \$1.5 million in fees, and a licensing arrangement for
Alchemix's Hydromax technology without royalty fees.

1 Defendants did not provide a valuation of Alchemix stock as of July 2002 or
2 shortly thereafter to show that Weiss's stock did not decline in value as a result of
3 Horton's omission. Because Defendants did not prove their affirmative defense, Weiss is
4 entitled to rescission of his stock purchase under Section 44-1991(A)(2).

5 **C. Tender**

6 "[T]ender of the securities purchased" is a required element of Weiss's ASA claim
7 for rescission. *See* A.R.S. § 44-2001(B). As mentioned above, Weiss has not yet tendered
8 his shares of Alchemix stock to Medici. In light of Plaintiffs' renunciation of Strategic's
9 claims after remand, tender is possible even acknowledging the Ninth Circuit's apparent
10 acceptance of the Plaintiffs' characterization of the two transactions as being intertwined.
11 Because Weiss seeks only rescission in his claim, tender is possible, and tender is a
12 requirement to rescission, and because Weiss has not yet tendered his stock, he has not
13 established his claim. In fairness, however, the Ninth Circuit's opinion may have led
14 Weiss to think he was obliged to prove and recover only rescissionary damages, even
15 after Strategic confirmed the dismissal of its claims and tender became possible for
16 Weiss. The Court proceeded on that assumption in granting Weiss's request for a
17 damages hearing.

18 After considering the equities, the Court does not see the fairness in permitting
19 Weiss to both retain the stock and recover damages that would virtually be the value that
20 he paid for the stock. On the other hand, the Court sees no fairness in denying Weiss's
21 claims in light of the confusion over the requirement to tender. In light of the multiple
22 permutations that Weiss made of his own case up to this stage of the litigation, the Court
23 will provide Weiss thirty days to tender his stock. If he does, he will have established his
24 claim for the reasons detailed above, and be entitled to judgment for the restoration of the
25 \$250,000 consideration he paid for the stock. If he does not, the Defendants will prevail
26 on all of Plaintiff's claims.

27 **D. Prejudgment Interest**

28 The ASA provides for the recovery of "consideration paid for the securities, with

1 interest” if a “contract for sale of any securities to any purchaser” is found to be in
2 violation of Section 44-1991. A.R.S. § 44-2001(A). “The general rule in Arizona is that
3 a liquidated claim entitles its holder to prejudgment interest.” *Trimble v. Am. Sav. Life*
4 *Ins. Co.*, 152 Ariz. 548, 557, 733 P.2d 1131, 1140 (Ct. App. 1986). “[I]f one accepts the
5 evidence and can calculate exactly the amount of damages without relying on the opinion
6 or discretion of a judge or jury, the claim is liquidated.” *Scottsdale Ins. Co. v. Cendejas*,
7 220 Ariz. 281, 288, 205 P.3d 1128, 1135 (Ct. App. 2009) (citing *Canal Ins. Co. v. Pizer*,
8 183 Ariz. 162, 164, 901 P.2d 1192, 1194 (Ct. App.1995)). Further, a claim is liquidated if
9 “the amount of damages can be computed with exactness.” *Interstate Markings, Inc. v.*
10 *Mingus Constructors, Inc.*, 941 F.2d 1010, 1014 (9th Cir. 1991) (applying Arizona law).
11 A good faith dispute over liability will not defeat a recovery of prejudgment interest on a
12 liquidated claim. *Id.*

13 Weiss’s claim for rescission may be liquidated once he tenders his stock, which is
14 a prerequisite to rescission. A.R.S. § 44-2001(B). As of yet, Weiss has not tendered his
15 stock to Defendants. Because of the lack of tender, no interest is accruing on that amount.
16 Such a result is not inequitable in this case because Weiss did not bring this claim until
17 2007, two years after he discovered in 2005 that Horton had made an omission in 2002.
18 When he did bring the claim he erroneously characterized the two separate transactions
19 underlying his claims as a “debt-equity swap.” That mischaracterization made it seem to
20 the Ninth Circuit as though a rescission remedy was not possible. It was only after
21 remand that Weiss acknowledged Strategic did not have a claim for damages or
22 rescission and clarified that a rescission remedy was practical as to Weiss, making tender
23 a possibility for the first time. Yet, insofar as the Court is aware he has never tendered the
24 stock to Medici. In light of the relief Weiss sought, the lack of any right to rescind the
25 repayment of the Strategic Note, and the lack of tender, it is not appropriate to award
26 prejudgment interest to Weiss, and the Court declines to do so.

27 **E. Punitive Damages**

28 Arizona law permits an award of punitive damages “to punish the wrongdoer and

1 to deter others from emulating his conduct.” *Linthicum v. Nationwide Life Ins. Co.*, 150
2 Ariz. 326, 330, 723 P.2d 675, 679 (1986) (internal citations omitted). The Arizona
3 Supreme Court has held that punitive damages are available in a suit involving
4 rescissionary damages.⁸ *Medasys Acquisition Corp. v. SDMS, P.C.*, 203 Ariz. 420, 424,
5 55 P.3d 763, 767 (2002) (“No reason justifies distinguishing between rescissory damages
6 and compensatory damages as a basis for allowing or denying an award of punitive
7 damages.”); see *Sec. Title Agency, Inc. v. Pope*, 219 Ariz. 480, 499, 200 P.3d 977, 996
8 (Ct. App. 2008). Punitive damages are allowed in such a case “to facilitate judicial
9 administration, to deter misconduct, and to completely serve justice” which “comports
10 with the Arizona policy of providing complete relief to injured parties.” *Medasys*
11 *Acquisition*, 203 Ariz. at 424 (internal citations omitted).

12 Defendants contend that punitive damages are not an available remedy under the
13 ASA. The statute states that the purchaser of securities “may bring an action . . . to
14 recover the consideration paid for the securities, with interest, taxable court costs and
15 reasonable attorney fees, less the amount of any income received by dividend or
16 otherwise from ownership of the securities” § 44-2001(A). Nevertheless, § 44-2005
17 states that “[n]othing in this article shall limit any statutory or common law right of any
18 person in any court for any act involved in the sale of securities.” Punitive damages are a
19 common law remedy in Arizona. See *Wyatt v. Wehmuller*, 167 Ariz. 281, 285, 806 P.2d
20 870, 874 (1991). Further, Arizona courts have held that “if a party has pursued a course
21 of conduct knowing that it created a substantial risk of significant harm to others and its
22 conduct was guided by evil motives, punitive damages should be available to punish such
23 behavior.” *Medasys Acquisition*, 203 Ariz. at 424 (internal quotation marks omitted)
24 (collecting Arizona cases). Consequently, punitive damages are an available remedy for

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26 ⁸ Defendants contend that punitive damages are not recoverable in this action as a
27 matter of law. They cite to *Grand*, in which the court states that “a claim for rescission
28 could not encompass compensatory or punitive damages.” 214 Ariz. at 9. But the Arizona
Supreme Court has held that punitive damages are available where rescissionary damages
have been awarded to a plaintiff. See *Medasys Acquisition*, 203 Ariz. at 424.

1 Weiss's ASA claim.

2 Defendants further assert that the Court previously denied Weiss's claim for
3 punitive damages and the Ninth Circuit did not disturb that decision upon appeal. The
4 Ninth Circuit did not address the availability of punitive damages when remanding
5 Weiss's securities fraud claims but because it reversed as to those claims, the Court
6 assumes that it *sub silentio* reversed the denial of punitive damages. *See Strategic*
7 *Diversity*, 666 F.3d at 1211. Thus, punitive damages are still available as a common law
8 remedy in this case.

9 Punitive damages are awarded only "in the most egregious of cases, where a
10 plaintiff proves by clear and convincing evidence that the defendant engaged in
11 reprehensible conduct and acted with an evil mind." *Medasys Acquisition*, 203 Ariz. at
12 424 (internal quotation marks and alterations omitted) (citing *Linthicum v. Nationwide*
13 *Life Ins. Co.*, 150 Ariz. 326, 331–32, 723 P.2d 675, 680–81 (1986)). Clear and
14 convincing evidence means "that which may persuade that the truth of the contention is
15 highly probable." *Thompson v. Better-Bilt Aluminum Prods. Co.*, 171 Ariz. 550, 557, 832
16 P.2d 203, 210 (1992) (internal quotation marks and citations omitted). "While the
17 necessary 'evil mind' may be inferred, it is still this 'evil mind' in addition to outwardly
18 aggravated, outrageous, malicious, or fraudulent conduct which is required for punitive
19 damages." *Linthicum*, 150 Ariz. at 331.

20 The court empaneled the jurors to answer factual predicates necessary to the
21 Court's consideration of equitable relief. At trial, the Parties did not request the jury to
22 determine, by special interrogatory, whether Horton acted with an evil mind in making an
23 omission to Weiss. (*See* Docs. 191 (Pl.'s Proposed Verdict Form), 194 (D.'s Proposed
24 Verdict Form).) At the hearing before the bench trial on damages, Weiss's counsel
25 acknowledged that the issue of punitive damages was for the Court to resolve.
26 (September 21, 2012, Hearing Tr. at 6:25–7:3.) Therefore, the Court will determine
27 whether punitive damages are warranted based on the facts ascertained at trial.

28 There is insufficient evidence that Horton had a malicious intent to secure Weiss's

1 investment and then deny him a return. Even assuming that Horton knew prior to the time
2 that Weiss purchased the stock that Western had decided not to exercise its options and
3 that he should have disclosed that information to Weiss, there is no evidence that he
4 withheld that information with an evil hand. Western made the \$3 million dollar
5 investment on June 18, 2002; only three weeks prior to Weiss's investment. The
6 Memorandum contained the option but not the obligation for Western to purchase up to
7 an additional \$33 million of stock over time, and was distributed to Weiss and all
8 members of the Board on the same date of June 18.

9 Weiss does not challenge Horton's testimony that Horton learned as early as three
10 to four weeks after June 18 that Western would not exercise its options. It is thus
11 possible, sufficient to support the jury's verdict, that Horton could have been aware
12 Western would not exercise its options before Weiss purchased his stock. The Court
13 assumes that the jury concluded either that Horton had represented to Weiss that Western
14 would exercise its options or that he should have informed Weiss about Western's
15 decision not to do so. Even still, Weiss testified that he received a copy of the
16 Memorandum from Horton on June 18 that specified that the additional investment was
17 merely an option held by Western. Further, Weiss does not question Horton's testimony
18 that he informed members of the Board about Western's decision shortly after it was
19 made and that Weiss was not a member of the Board at this time, but simply one
20 shareholder among five hundred others.

21 Weiss points to Horton's other conduct with Alchemix investors to show that
22 Horton engaged in egregious conduct warranting punitive damages. For example, Horton
23 did not inform Alchemix investors that some of his earlier ventures had not succeeded
24 financially and had filed for bankruptcy, a fact he did not disclose on his annual reports to
25 the Arizona Corporation Commission. (*See* Doc. 224, Jury Trial Tr. at 147:5–150:16.)
26 Weiss also asserts that Horton misled the Court at trial when Horton contended that the
27 so-called "China deal" was a legitimate current project contributing value to Alchemix
28 stock. Nevertheless, such conduct, even if less than forthcoming, is not relevant to

1 whether Horton had an “evil mind” at the time he made the omission to Weiss.

2 There is not clear and convincing evidence in the record that Horton operated with
3 an “evil mind” when omitting to inform Weiss about Western’s decision not to exercise
4 its options. *See Dawson v. Withycombe*, 216 Ariz. 84, 112, 163 P.3d 1034, 1062 (Ct.
5 App. 2007) (finding that although the defendant made fraudulent statements to the
6 plaintiff there was “little if any indication of any ‘evil motive’ on [the defendant’s] part
7 when he made the misrepresentation.”). To the extent that Weiss argues that Defendants’
8 fraudulent conduct by itself may justify an award of punitive damages, that argument
9 “extends this concept beyond the basis for punitive damages.” *Id.* As the Arizona
10 Supreme Court has stated, “punitive damages are not recoverable in every fraud case,
11 even though fraud is an intentional tort.” *Rawlings v. Apodaca*, 151 Ariz. 149, 162, 726
12 P.2d 565, 578 (1986). Punitive damages are not warranted in this case.

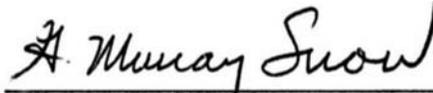
13 CONCLUSION

14 Because Weiss did not show that Horton’s omission caused Weiss’s loss in
15 relation to his Alchemix stock, he failed to prove his federal securities fraud claim under
16 10b-5. Upon tender of the Alchemix stock to Medici, however, Weiss may prevail on his
17 state securities fraud claim under the ASA because loss causation is an affirmative
18 defense pursuant to Section 44-1991(A)(2) and Defendants did not prove that Weiss did
19 not suffer economic loss as a result of Horton’s omission. Plaintiffs will be granted
20 rescission of the stock purchase upon tender. If Weiss does not accomplish tender within
21 thirty days, he will retain his stock and Defendants will prevail on all of his claims. Even
22 if Weiss prevails, however, he is denied prejudgment interest and punitive damages.

23 **IT IS THEREFORE ORDERED** that Plaintiff Weiss shall have **thirty (30) days**
24 in which to tender his 250,000 shares of Alchemix stock to Medici and apprise this Court
25 that he has done so. If **within fourteen (14) days** after the notice has been filed, Medici
26 has not challenged the existence or adequacy of Weiss’s tender, the Court shall enter
27 judgment against Medici. Should this Court not receive notice of Weiss’s tender **within**
28 **thirty (30) days** of the date of this Order, then this suit will be dismissed with prejudice,

1 with Weiss possessing his Alchemix stock, but no judgment against the Defendants.

2 Dated this 23rd day of August, 2013.

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5 _____
6 G. Murray Snow
7 United States District Judge
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