UNITED STATES
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November 10, 2009

Via CM/ECF

The Honorable William C. Griesbach
United States District Court Judge
United States District Court
Eastern District of Wisconsin
125 South Jefferson Street
Green Bay, WI 54305-2490

Re: SEC v. Wealth Management LLC, et al., Case No. 09-C-506

Dear Judge Griesbach:

Pursuant to the Court's minute order entered on November 4, 2009, plaintiff, the United States Securities and Exchange Commission ('SEC') submits this letter brief to address a handful of issues raised at the hearing held on that date by Bruce Arnold, counsel for the Bender Trusts and IRA and Wilson IRA.[1] Specifically, the SEC respectfully disagrees with Mr. Arnold's statements suggesting that: (i) the WM Funds were not "securities," and (ii) even if his clients investments in the WM Funds were investment in securities, once they requested redemptions, they became creditors entitled to a priority over non-redeeming investors, by operation of the operating agreements and Wisconsin and Delaware state law; and (iii) in a federal equity receivership such as this, the Receiver is obligated to abide by these state statutes in fashioning its plan of distribution of funds, and to treat his clients as creditors.

The WM Funds' "Membership" Interests Are Securities.

At the hearing, Mr. Arnold suggested that because the operating agreements and offering memoranda for the WM Funds' described investors' interest as "memberships" and provided a mechanism whereby on the redemption of their interests they would be treated as a creditor, the WM Funds were not actually investments in securities, at least for purposes of the federal securities laws. Contrary to these suggestions, Mr. Arnold's clients, like all other investors in the WM Funds, were plainly investing in securities, and

[1] The SEC's arguments herein apply to all WM Fund investors who seek some priority status as a "creditor" by virtue of redemption requests made after February 18, 2008.

that fact that they are termed "members" rather than shareholders or investors in the offering memoranda and operating agreements does not alter that fact.

Under the Securities Act, "security" has a "broad" definition sufficient "to encompass virtually any instrument that might be sold as an investment." *See SEC v. Edwards,* 540 U.S. 389, 393, 124 S.Ct. 892 (2004) (citation omitted). Section 2(a)(1) of the Securities Act of 1933 and Section 3(a)(10) of the Securities Exchange Act define securities to include a broad range of instruments, including "any note, stock . . . debenture, investment contract, [or any] instrument commonly known as a security." 15 U.S.C. § 77(b)(a)(1); 15 U.S.C. § 78c(a)(10).

The cover page to the offering memoranda for each of the WM Funds make evident that these instruments were securities, providing that the membership interests "were being offered pursuant to Section 4(2) of the Securities Act and Regulation D promulgated thereunder." (*See* Exs. 14-17 contained in the SEC's Compendium of Exhibits filed on May 20, 2009, Docket Nos. 4, 5). The fact that the Wealth Management LLC and the WM Funds themselves considered what they were selling to be securities subject to the federal securities law should be dispositive of the issue. But even if it were not, it is clear that the particular investments at hand are "investment contracts" under the *Howey* test, as each WM Fund involves "an investment of money in a common enterprise with profits [that] come solely from the efforts of [Defendants]." *SEC v. W.J. Howey Co.,* 328 U.S. 293, 301, 66 S.Ct. 1100 (1946). The offering memoranda make clear that the subscribers were making investments, in a pooled fund, with the expectation of profits to be made solely from the efforts of the general manager of the fund, Wealth Management LLC. The fact that the WM Funds' offering documents term the investments as "memberships" does not alter the fact that they are securities within the definition of the Securities Act. *See, e.g., SEC v. Seaforth Meridian, Ltd.,* 2007 WL 3238584, at *6 (D. Kan. 2007) (holding that sale of "limited partnership interests" are investment contracts); *SEC v. International Loan Network, Inc.*, 770 F.Supp. 678 (D.D.C. 1991) (finding that "memberships" in a pyramid scheme were securities); *SEC v. Jet Travel Services, Inc.*, 1975 WL 422 (M.D. Fla. Aug. 29, 1975) (holding that instruments referred to as "Executive Memberships" were securities).

Perhaps most helpful to this analysis is *Goodman v. Epstein*, 582 F.2d 388 (7th Cir. 1978), another case involving the sale of limited partnership interests. Following the dictates of the Supreme Court in *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967), the court in *Goodman* held that such interest were securities, reaffirming that the "substance of the transaction must be elevated over the form" and noting that numerous courts had also determined that a limited partner's interest in a limited partnership is an "investment contract" or security, "even though it does not have the normal trappings of what a lay person may think of as a security." *Goodman*, 582 F.2d at 406-409.

B. A Federal Equity Receiver in an SEC Enforcement Action Is Not Required to Apply State Law or Even the Federal Bankruptcy Code In Fashioning a Plan of Distribution Under Equitable Principles of Fairness

At the hearing, Mr. Arnold argued that even if his clients' investments in the WM Funds were securities, once they made redemption requests, they ceased to be investors and instead became creditors of the WM Funds entitled under Wisconsin and Delaware state law to a priority over WM Fund investors who did not make similar redemption requests prior to the institution of this lawsuit. Mr. Arnold further argued that a federal equity receiver in an SEC enforcement action must adhere to state law in fashioning a plan of distribution, including determining whether investors are similarly situated, or whether certain investors, by virtue of their conduct, are entitled to a priority over other investors. The SEC respectfully disagrees with all of Mr. Arnold's arguments.

The SEC is unaware of any reported decision in which an SEC receiver has been required to apply state law in determining whether one class of investors is differently situated from another, or entitled to a priority, in connection with the formulation of a plan of distribution. To the contrary, in *SEC v. Credit Bancorp, Ltd.*, the Second Circuit expressly declined to require a receiver to adhere to state law governing priority among various claimants where such law conflicted with what the court considered to be a more appropriate pro rata distribution. 290 F. 3d 80, 90, n.10 (2d Cir. 2002). Even with respect to the federal Bankruptcy Code, courts have not required the SEC (or by extension, an SEC receivership) to follow Bankruptcy Code priorities "when developing a distribution plan." *SEC v. Cobalt Multifamily Investor I*, 2009 WL 1808980 (S.D.N.Y. June 24, 2009) (quoting *Official Committee of Unsecured Creditors of WorldCom, Inc. v. SEC*, 467 F.3d 73, 85). In *Official Committee*, the court noted that district courts possess "broad equitable discretion to craft remedies for violations of the Exchange Act" and applied a "fair and reasonable" standard for disgorgement plans in SEC cases. *Id.* at 81-83. (citing *SEC v.* Wang, 944 F.2d 80, 84-85 (2d Cir. 1991). So too has this Circuit embraced this approach to giving deference to "sensible" claim classifications in receivership proceedings. *SEC v. Enterprise Trust Co.*, 559 F.3d 649, 652 (7th Cir. 2009).[2]

When applied to the facts of this case, any "fair and reasonable" standard for a plan of distribution must take into account that fact that Wilson, and others who claim a priority over other investors by virtue of their making a redemption request prior to the commencement of this action, made such request only *after* all WM Fund investors had received a written communication from the WM Funds on February 15, 2008 informing them of the WM Funds' decision to "temporarily limit redemptions from the Fund" based on Wealth Management LLC's belief that "to manage the Fund in the best interests of all

[2] Contrary to Mr. Arnold's assertion at the November 4 hearing, nothing in the *Enterprise* decision suggests that the Circuit would require a receiver to follow the absolute priority rule set out in the Bankruptcy Code. At best, the decision stands for the proposition that a district court may look to the Bankruptcy Code for guidance in establishing an "appropriate" distribution plan. *SEC v. Enterprise Trust Co.*, 559 F.3d at 653.

members, it is prudent to temporarily restrict redemptions to a maximum of 2% of an investor's capital basis as determined at the beginning of each calendar quarter . . . effective immediately." (*See, e.g.*, Ex. 54 filed as Docket Entry No. 6 on May 20, 2009).[3] The Receiver believes, and the SEC agrees, that it would be unfair to give an investor who requested a redemption subsequent to the dissemination of this February 15, 2008 letter over any investor who did not make such request, since the clear message to all investors was that the WM Funds would not honor any such request. The SEC is not aware of any subsequent communication from the WM Funds or Wealth Management that lifted this stated 2% restriction.

For these reasons, and all of the reasons set forth by the Receiver in her various filings in support of her Plan of Allocation, the SEC continues to believe that the Receiver's Plan of Allocation is fair and reasonable and should be approved by the Court.

Respectfully submitted,

/s/ *Steven J. Levine*
Steven Levine
Senior Trial Counsel
Securities and Exchange Commission

Encl. Exhibit 54 to TRO Compendium of Exhibits

cc: All Counsel and parties per ECF Service List,
James Putman via U.S. Mail

[3] For ease of reference, we have attached a copy of this exhibit to this letter.

WML GRYPHON FUND LLC

February 15, 2008

REDACTED

Dear REDACTED

I am writing to you on behalf of the Managing Member (Wealth Management LLC) of the WML Gryphon Fund LLC to inform you of a decision to temporarily limit redemptions from the Fund. The Managing Member believes that in order to manage the Fund in the best interests of all members, it is prudent to temporarily restrict redemptions to a maximum of 2% of an investor's capital base as determined at the beginning of each calendar quarter. This policy is effective immediately. For the majority of current investors, this is consistent with how the Fund has operated in the past to provide periodic liquidity and represents no significant change. We are currently exploring all possible sources of liquidity consistent with acting in the best interest of all Members.

It is important to understand that this temporary limitation is not correlated with our outlook for the Fund's performance. We remain confident in our ability to achieve the Fund's stated objectives. We have continued to receive capital account statements from all managers and have appropriate documentation on those investments. We have checked in with all the managers and all are proceeding with audits of their books for 2007.

For those members who have previously submitted either full or partial redemption requests, those requests have been grouped by accepted quarterly redemption date (e.g., March 31, June 30, etc.) and members of those groups will be treated equally as liquidity becomes available.

Enclosed with this letter is an election form to indicate if you wish to redeem up to 2% of your capital balance. To ensure payment it is imperative that we receive this signed form no later than February 29, 2008. If you prefer to remain fully invested in the Fund you do not need to return the form to us. Note that this form is only effective for the quarter ending March 31, 2008, and you will be receiving similar election forms each quarter.

As always, we value your trust and confidence in our ability to assist you in achieving your financial goals. Please feel free to call or e-mail with any questions or concerns.

Simone Fevola, CFA, CAIA
President of the Managing Member

Enclosure(s)

Exhibit 54