

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

UNITED STATES SECURITIES
AND EXCHANGE COMMISSION,

Plaintiff,

Case No. 12-cv-12109

v.

Hon. Victoria A. Roberts

KWAME M. KILPATRICK,
ET AL.,

Magistrate Judge R. Steven Whalen

Defendants.

PLAINTIFF U.S. SECURITIES AND EXCHANGE COMMISSION'S
MOTION FOR FINAL JUDGMENT BY DEFAULT
AGAINST DEFENDANTS KWAME KILPATRICK AND JEFFREY BEASLEY

Plaintiff U.S. Securities and Exchange Commission (the "SEC"), pursuant to Rules 55 and 65 of the Federal Rules of Civil Procedure, hereby moves for the entry of default judgments against Defendants Kwame M. Kilpatrick and Jeffrey W. Beasley based on their failure to answer, plead, or otherwise defend the Complaint filed in this action.

May 23, 2014

Respectfully submitted,

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PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S MEMORANDUM
IN SUPPORT OF MOTION FOR FINAL JUDGMENT BY DEFAULT
AGAINST DEFENDANTS KWAME KILPATRICK AND JEFFREY BEASLEY

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ISSUE PRESENTED

Whether the Court should grant the SEC's request for the entry of default judgments against Defendants Kilpatrick and Beasley due their failure to answer, plead, or otherwise defend against the Complaint filed in this action.

The SEC's answer: "Yes."

MOST APPROPRIATE AUTHORITY

<i>CFTC v. Marquis Fin. Mgmt. Sys., Inc.</i> , 2005 U.S. Dist. LEXIS 41440, *5 (E.D. Mich. June 8, 2005).....	12
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INTRODUCTION

Former Detroit Mayor Kwame Kilpatrick and his City Treasurer, Jeffrey Beasley, sat on the governing boards of two large public employee pension funds: (1) the Police and Fire Retirement System of the City of Detroit (the “PFRS”) and (2) the General Retirement System of the City of Detroit (the “GRS”) (together, the “Pension Funds”). Plaintiff U.S. Securities and Exchange Commission (the “SEC” or “Commission”) alleges that Kilpatrick and Beasley engaged in a brazen “pay to play” scheme where they solicited over \$122,000 worth of luxury travel – including flights on private jets – from Mayfield Gentry Realty Advisors (“MGRA”), one of the Pension Funds’ investment advisers. At the same time as it was plying Kilpatrick and Beasley with lavish gifts, MGRA was recommending that the Pension Funds buy more than \$115 million in securities from an entity controlled by MGRA. Despite pending Board votes on massive investments by the Pension Funds with MGRA, neither Kilpatrick nor Beasley told their fellow trustees that they were receiving tens of thousands of dollars in free travel and entertainment from MGRA. As detailed in the Complaint, the receipt of the gifts, the failure to disclose the gifts, and the resulting conflicts of interest constituted a fraud on the Pension Funds -- violating the antifraud provisions of the Securities Act, the Exchange Act, and the Advisers Act.

Rather than answer the charges against them, Kilpatrick and Beasley remained silent. They failed to answer or otherwise respond to the SEC’s Complaint. The SEC, therefore, respectfully requests that the Court enter final judgments against them by default, and enter an Order that (a) permanently enjoins them from further violations of the securities laws identified in the SEC’s Complaint, (b) permanently enjoins them from participating in

any investment decisions by public pensions as a trustee, officer, employee or agent, (c) requires them to disgorge their ill-gotten gains plus prejudgment interest and (d) requires them to pay a third-tier civil penalty in an amount to be determined by the Court.

I. PROCEDURAL HISTORY

On May 9, 2012, the SEC sued Kilpatrick, Beasley, Chauncey Mayfield and MGRA for securities fraud.¹ (Dkt. #1.) The SEC properly served each defendant. On May 16, 2012, the Commission's process server served the Summons and Complaint on Defendant Kilpatrick at his home in Grand Prairie, Texas. (Dkt. #10.) Kilpatrick's Answer, therefore, was due on June 6, 2012. *See* FRCP 12(a)(1)(A)(i). On July 10, 2012, the Commission's process server served the Summons and Complaint on Defendant Beasley at his home in Chicago, Illinois by leaving copies with his son, Chase Beasley. (Dkt. #20.) Beasley's Answer was, therefore, due on July 31, 2012. *See id.*

Kilpatrick and Beasley failed to answer the SEC's Complaint or otherwise appear in this case. On the SEC's application, the Clerk of Court entered defaults against Kilpatrick and Beasley on July 13, 2012 and August 31, 2012 respectively. (Dkt. #12 and 22.)

On March 11, 2013, Kilpatrick was convicted on federal charges of racketeering, conspiracy, fraud, extortion, and tax crimes. On October 10, 2013, he was sentenced to 28 years in prison. Beasley is currently awaiting trial for bribery, conspiracy, fraud, and extortion. His trial is scheduled to begin on October 7, 2014.

II. STATEMENT OF FACTS

The SEC's allegations as to Kilpatrick and Beasley – which are accepted as true for purposes of this Motion – are as follows:

¹ The SEC's claims against Mayfield and MGRA in this case have settled. Resolution of this Motion will resolve all remaining claims in this case.

A. Background: MGRA's Business with the Pension Funds

During Kilpatrick's tenure as Detroit's Mayor, MGRA – headed by Chauncey Mayfield – had a long and profitable relationship with the Pension Funds. MGRA and its predecessors performed services for the PFRS from 2002 until 2012. (Dkt. #1, Compl. at ¶ 26.) In 2004, MGRA's business expanded greatly when the PFRS selected it to manage \$140 million in properties owned by the PFRS. (*Id.* at ¶ 27.) In May 2005, MGRA and the PFRS formalized their relationship by entering into a Real Estate Investment Advisory and Asset Management Agreement (the "PFRS MGRA Advisory Agreement"). (*Id.* at ¶ 28.) That Agreement remained in effect until 2012. (*Id.* at ¶ 32.)

Beginning in 2006, MGRA began serving as a real estate advisor, managing the real estate investments of the GRS. (*Id.* at ¶ 33.) The relationship between MGRA and the GRS was formalized in a Real Estate Investment Advisory and Asset Management Agreement (the "GRS MGRA Advisory Agreement"). (*Id.* at ¶ 34.) The GRS Agreement also remained in effect until 2012. (*Id.* at ¶ 38.)

B. State Law and Pension Fund Policies Barred Kilpatrick and Beasley's Conduct

While Kilpatrick was Mayor of Detroit, both he and Beasley were trustees of the PFRS and the GRS. Their duties and responsibilities as trustees were defined, in part, by Michigan state law and by GRS ethics policies, each of which were designed to prevent precisely the sort of scheme that the SEC alleged in its Complaint.

The Public Employee Retirement System Investment Act ("PERSIA"), the Michigan state law that governs the administration and investment of the assets of the Pension Funds, defines trustees such as Kilpatrick and Beasley as investment fiduciaries. (*Id.* at ¶ 39.) PERSIA prohibits an investment fiduciary from receiving "any consideration

for his or her own personal account from any party dealing with the [the pension fund] in connection with a transaction involving the assets of the [the pension fund].” (*Id.*)

The GRS had an ethics policy in place during the relevant period. (*Id.* at ¶ 40.) The policy stated that “[c]onflicts of interest, bribes, gifts or favors which subordinate fund trustees to private gains are unacceptable.” (*Id.*) Furthermore, the policy addressed conflicts of interest by dictating that:

A pension board must discharge all its duties solely in the interest of the participants and beneficiaries for the exclusive purpose of (1) providing benefits to participants and their beneficiaries; and (2) defraying reasonable expenses of administering the retirement system or pension fund. A trustee must act honestly and with undivided loyalty to the trust and must serve the interest of all beneficiaries excluding self interest...

The trustee must not deal with the pension system assets for the individual benefit of the trustee. (*Id.* at ¶ 41.)

During the relevant time period, the Pension Funds did not monitor receipt of consideration by trustees. (*Id.* at ¶ 42.) Rather, the Funds relied on the trustees (like Kilpatrick and Beasley) to self-report any conflicts of interest. (*Id.*)

C. Mayfield “On the Outs” with the Kilpatrick Administration

Kilpatrick was first elected Mayor of the City of Detroit in 2001. (Dkt. #1 at ¶ 43.) In his 2005 re-election bid, Kilpatrick faced off against Deputy Mayor Freman Hendrix (“Hendrix”). (*Id.*) After supporting Kilpatrick in his first run for Mayor, Chauncey Mayfield switched his allegiance to Hendrix in the 2005 election: Mayfield (a) personally donated \$3,400, the maximum allowable individual contribution, to Hendrix’s campaign and (b) hired Hendrix’s daughter to work at MGRA. (*Id.* at ¶ 44-45.)

Mayfield had a lot at stake at the time of the 2005 election. By the Fall of 2005, MGRA, with Mayfield at its helm, was managing millions of dollars in real estate

investments for the Pension Funds. (*Id.* at ¶ 46.) The Pension Funds were MGRA's largest client and Mayfield, who owned more than 70 percent of MGRA, was the biggest beneficiary of that relationship. (*Id.*)

MGRA also had potential new business on the line. In September 2005, MGRA received conditional, preliminary approval from the GRS Board for a \$10 million investment in the MGRA Genesis Fund. (*Id.* at 47.) The deal, however, was far from complete: the GRS Board's preliminary approval specifically stated that (a) there was no obligation of the GRS Board to make the investment, (b) there was a possibility of changes to the proposal, and (c) final documents were subject to approval as to form and content by the GRS Board and its legal counsel. (*Id.*) In other words, the deal's fate was still in the hands of a Board that would be led by whoever won Detroit's mayoral election.

Ultimately, Kilpatrick won a second term as Mayor of Detroit. As part of his second-term administration, Kilpatrick appointed Beasley, his college fraternity brother, as City Treasurer. (*Id.* at 48.) In that position, Beasley also was a trustee to the Pension Funds. (*Id.*)

While final approval of the GRS \$10 million investment with MGRA was pending, members of Kilpatrick's administration began to exert pressure on Mayfield. (*Id.* at 49.) First, at a January 2006 dinner, Deputy Mayor Anthony Adams ("Adams") told Mayfield that Mayfield was "on the outs with the Kilpatrick administration" because of Mayfield's support of Hendrix in the 2005 election. (*Id.* at 50.) Adams also told Mayfield that they needed to figure out a way to "get this cleared up" and then proposed that he fire Hendrix's daughter. (*Id.*) Mayfield refused. (*Id.*)

In February 2006, Beasley invited Mayfield to meet for drinks. (*Id.* at 51.) At that

meeting, Beasley reiterated Mayfield's need to make amends with the Kilpatrick administration. (*Id.* at 52.) Beasley warned that Mayfield was "in the dog house" with Kilpatrick and offered to help him "clear the air" with the administration. (*Id.* at 52.)

By April 2006, the economic stakes for MGRA had grown. That month, Mayfield and MGRA appeared before the PFRS Board and proposed that the PFRS invest \$20 million in the MGRA Genesis Fund – an investment that would generate substantial fees for MGRA. (*Id.* at ¶ 53.) In June 2006, the PFRS Board gave preliminary approval for that investment. (*Id.* at ¶ 54.) But, again, the PFRS approval was not final: the Board's approval stated that (a) the PFRS Board was not obligated to make the investment, (b) the proposal would likely change, and (c) final documents were subject to approval as to form and content by the PFRS Board and its legal counsel. (*Id.*)

D. The Fraudulent Scheme Begins: The Bogus "Building Inspection" in Charlotte, North Carolina

In 2007, Mayfield and MGRA sought to increase and finalize approval of the Pension Funds' new investments with MGRA. (*Id.* at ¶ 55.) At the same time, Kilpatrick and Beasley began soliciting – and Mayfield began providing – a series of expensive trips that were never disclosed to the Pension Funds which Kilpatrick and Beasley helped run. First, Mayfield paid to send Kilpatrick and his cohorts on a trip to Charlotte, North Carolina under the guise of a "building inspection."

The "building inspection" was a well-designed cover story. As part of its advisory relationship with the Pension Funds, MGRA managed and acquired properties on their behalf. (*Id.* at ¶ 56.) MGRA employees usually conducted annual inspections of buildings MGRA managed for the Pension Funds, and often invited trustees of the Pension Funds to accompany them free of charge. (*Id.* at ¶ 57.)

In January 2007, MGRA acquired a new building for the PFRS in Charlotte, North Carolina. (*Id.* at ¶ 58.) Shortly thereafter, Beasley called Mayfield and told him that Beasley and Kilpatrick wanted to travel to Charlotte to inspect that building. (*Id.* at ¶ 59.) Mayfield agreed to Beasley's request that MGRA pay for the hotel stay. (*Id.* at ¶ 60.)

Beasley told an MGRA employee that four people would join Kilpatrick and Beasley on the trip: Duane Love (Kilpatrick's bodyguard), Marc Cunningham (Special Assistant to Kilpatrick), Bobby Ferguson (a city contractor and close friend of Kilpatrick), and Derrick Miller (Kilpatrick's Chief Information Officer). (*Id.* at ¶ 61.) MGRA made the hotel reservations and paid in excess of \$3,000 for the hotel rooms. (*Id.* at ¶ 62.)

There was no apparent business purpose to the trip. No trustees other than Kilpatrick and Beasley were informed of the purported Charlotte "inspection" and no MGRA employees joined Kilpatrick and Beasley on the trip. (*Id.* at ¶¶ 63-64.) Kilpatrick, Beasley, and their companions travelled to Charlotte and stayed overnight on January 22, 2007, but they never inspected the building while they were there. (*Id.* at ¶¶ 65-67.)

E. Leaving for Las Vegas

For his second gift to Kilpatrick, Mayfield upped the ante: he led Kilpatrick and his friends on an all-expense paid trip to Las Vegas.

In April 2007, Mayfield chartered a flight to Las Vegas for himself and a few friends. (*Id.* at ¶ 68.) He invited Beasley on the trip. (*Id.*) Before Mayfield had an opportunity to invite anyone else, Beasley called Mayfield and told him that he would be coming on the Las Vegas trip, along with Kilpatrick and several members of Kilpatrick's inner circle: Derrick Miller, Duane Love, Marc Cunningham, and Lucius Vassar (Kilpatrick's Chief Administrative Officer). (*Id.* at 69.) Beasley told Mayfield that the Las

Vegas trip would be a good opportunity to “clear the air” with Kilpatrick. (*Id.* at ¶ 70.)

On the morning of Friday, April 13, 2007, Kilpatrick, Beasley, their friends, and Mayfield flew by private jet from Pontiac, Michigan to Las Vegas for an extravagant three-day vacation. (*Id.* at ¶ 71.) A private limousine whisked Kilpatrick, Beasley, and their entourage to their VIP rooms at the Venetian Resort Hotel Casino. (*Id.* at ¶ 72.) They received massages, attended exclusive concerts by Toni Braxton and Prince, and played three rounds of golf. (*Id.*) When it came time to go home, they were picked up by private limousine, and the private jet returned them to Detroit. (*Id.*)

The trip was solely for pleasure: Mayfield was the only person from MGRA on the trip and there were no discussions of business between Mayfield and Kilpatrick or Beasley. Nevertheless, MGRA picked up the \$60,259.30 tab which included:

- Chartered flights on private jet (\$43,632.18)
- 7 VIP hotel rooms at the Venetian Resort Hotel Casino (\$4,375.90)
- Toni Braxton tickets (\$974.30)
- Prince tickets (\$2,175.44)
- Dinner at McCormick & Schmick (\$800.48)
- Golfing fees (\$2,712.00)
- Private limousine charges (\$5,289.00)
- Massages at Canyon Ranch Spa for Kilpatrick and Mayfield (\$300.00)

MGRA accounted for these expenditures as business expenses.

Mayfield’s attempt to “clear the air” with Kilpatrick was spectacularly successful. In May 2007, just weeks after the Las Vegas vacation, Mayfield and MGRA sought to finalize the PFRS investment in the Genesis Fund. (*Id.* at ¶ 77.) However, instead of the \$20 million investment originally proposed for each fund, MGRA now proposed that the PFRS transfer \$55 million worth of the PFRS’s properties to the Genesis Fund, in addition to a \$25 million cash investment. (*Id.* at ¶¶ 77-78.) This ballooning of the proposed investment meant increased fees for MGRA. (*Id.* at ¶ 79.) On May 10, 2007, the PFRS

Board approved this expanded proposal by a vote of 9 to 2; both Kilpatrick's designee to the PFRS Board and Beasley voted in favor of the proposal. (*Id.* at ¶ 80.)

Neither Kilpatrick nor Beasley informed anyone associated with the Pension Funds about the Las Vegas trip. (*Id.* at ¶ 81.) The Board thus voted to dramatically increase its business with Mayfield and MGRA without the knowledge that their advisers had just wooed Kilpatrick and Beasley with a \$60,000 vacation. (*Id.* at ¶ 82.)

F. The Tallahassee Trip

A few months after the Las Vegas junket, Mayfield again provided a private jet for Kilpatrick's personal use in response to a request from Beasley. In July 2007, Beasley asked Mayfield to charter a private jet, at MGRA's expense, to fly Kilpatrick to Tallahassee, Florida. (*Id.* at ¶ 84.) Beasley told Mayfield that Kilpatrick was going to Tallahassee to raise money for the Kilpatrick Civic Fund and that a private jet was necessary to get Kilpatrick "in and out" of Tallahassee quickly. (*Id.* at ¶ 85.) Mayfield agreed to make the arrangements and to have MGRA foot the bill. (*Id.* at ¶ 86.)

On July 20, 2007, the Kilpatrick entourage flew to Tallahassee on a private jet which cost MGRA \$24,725.65. (*Id.* at ¶ 87.) The passengers were Kilpatrick, Connor Beasley (Beasley's son), and two other individuals with the last name "Kilpatrick." (*Id.*)

Contrary to Kilpatrick's purported need for a private jet to get "in and out" of Tallahassee quickly, the trip lasted three days. (*Id.* at ¶ 92.) Coincidentally, Kilpatrick and his wife had purchased a second home in Tallahassee in June 2007, just weeks before the trip. (*Id.* at ¶ 93.)

Again, it seems that Mayfield successfully "cleared the air" with the Kilpatrick administration. In August 2007, shortly after the trip to Tallahassee, the GRS Board voted

to enter into the GRS MGRA Advisory Agreement, cementing the relationship between MGRA and the GRS. (*Id.* at ¶ 94.) Both Kilpatrick's designee to the GRS Board and Beasley voted in favor of the Agreement. (*Id.*) Neither Kilpatrick nor Beasley informed anyone associated with the Pension Funds about the trip to Tallahassee. (*Id.* at ¶ 96.) In other words, the GRS Board voted to formalize its business relationship with MGRA without the knowledge that the advisers had just provided Kilpatrick and his associates a \$25,000 private jet trip. (*Id.* at ¶ 97.)

G. The Weekend in Bermuda

Kilpatrick and Beasley were not done with their "pay to play" scheme. In September 2007, Beasley asked Mayfield to charter yet another private jet at MGRA's expense – this time to fly Kilpatrick and his wife to Bermuda. (*Id.* at ¶ 98.) Beasley again told Mayfield that Kilpatrick was going to Bermuda to raise money for the Kilpatrick Civic Fund and that a private jet was necessary to get Kilpatrick in and out of Bermuda quickly. (*Id.* at ¶¶ 99-100.) Mayfield made the arrangements, and MGRA paid for the jet. (*Id.* at ¶ 100.) The trip took place on October 4-7, 2007, and the private jet cost MGRA \$34,604.90. (*Id.* at ¶ 101.)

Mayfield sent an email shortly before the trip stating that the passengers on the private jet would include not just Kilpatrick and his wife, but also Bobby Ferguson (Kilpatrick's friend and city contractor), Beasley, Beasley's wife, and another individual. (*Id.* at ¶ 102.) The return flight carried Kilpatrick, Kilpatrick's wife, Kilpatrick's father, and Kilpatrick's father's girlfriend. (*Id.* at ¶ 103.)

During their weekend in Bermuda, Kilpatrick and his father played golf with comedian Steve Harvey and Bermuda's Premier and Minister of Tourism and Transport.

(*Id.* at ¶ 104.) Kilpatrick and his wife also attended the Bermuda Music Festival where they were photographed with celebrities including members of the band Earth, Wind & Fire and actresses Gabrielle Union and Regina King. (*Id.*) The Kilpatrick Civic Fund's records do not reflect the receipt of any donations on or around the dates of the Bermuda trip. (*Id.* at ¶ 108.)

Neither Kilpatrick nor Beasley informed anyone associated with the Pension Funds about the trip to Bermuda. (*Id.* at ¶ 109.)

H. The Final Votes to Invest Over \$115 Million with MGRA

By November 2007, the relationship between Mayfield and the Kilpatrick administration was fully healed. Just weeks after the trip to Bermuda, at its November 14, 2007 meeting, the GRS Board considered a proposed \$10 million investment in common shares of the MGRA Genesis REIT which, in turn, would be invested in the MGRA Genesis Fund. (*Id.* at ¶ 110.) The GRS Board approved the investment by a unanimous vote of 8 to 0. (*Id.*) Both Kilpatrick's designee to the GRS Board and Beasley voted in favor of the proposal. (*Id.*)

Also in November 2007, the PFRS Board voted on an extraordinary increase in its investment in MGRA's funds. On November 15, 2007, the PFRS Board voted to contribute approximately \$67 million worth of PFRS properties, and approximately \$15 million in proceeds from the sale of another property, to the MGRA Genesis REIT in return for securities issued by the REIT. (*Id.* at ¶ 111.) The PFRS also made a capital commitment of \$25 million in cash to the MGRA Genesis REIT. (*Id.*) The PFRS Board approved the investment by a vote of 8 to 1 with both Kilpatrick's designee to the PFRS Board and Beasley voting in favor of the proposal. (*Id.*)

Neither Kilpatrick nor Beasley told anyone associated with the Pension Funds about the trip to Bermuda, which had taken place just weeks earlier. (*Id.* at ¶ 112.) The Boards thus voted to invest over \$115 million with MGRA without the knowledge that over the preceding ten months, Mayfield and MGRA had supplied Kilpatrick, Beasley, and their associates with over \$122,000 in extravagant gifts. (*Id.* at ¶ 113.)

III. ARGUMENT

The SEC requests that this Court enter an order of permanent injunction against Kilpatrick and Beasley to enjoin them (a) from future violations of the federal securities laws identified in the Complaint and (b) from participating in any investment decisions by public pensions. A permanent injunction will protect the investing public by deterring future violations. The SEC also seeks an order requiring Kilpatrick and Beasley, jointly and severally, to disgorge \$122,922.87 -- the proceeds that they received from Mayfield and MGRA by violating federal securities law as alleged in the Complaint -- plus prejudgment interest. The SEC also moves the Court for an order directing Kilpatrick and Beasley to pay a civil monetary penalty -- \$390,000 for Kilpatrick and \$130,000 for Beasley.

A. Default Judgments Against Kilpatrick and Beasley Are Warranted.

The decision to grant a default judgment rests within the discretion of the district court. *J & S Construction Co., Inc. v. Rush*, 633 F.2d 215 (6th Cir. 1980). “In the context of a default judgment, the district court is obliged to accept as true all facts alleged by the plaintiff and all reasonable inferences contained therein.” *CFTC v. Marquis Fin. Mgmt. Sys., Inc.*, 2005 U.S. Dist. LEXIS 41440, *5 (E.D. Mich. June 8, 2005) (citing *Thomson v. Wooster*, 114 U.S. 104 (1885)); *CFTC v. Millenium Trading Group, Inc.*, 2007 U.S. Dist. LEXIS 65784, *13 (E.D. Mich. Sept. 6, 2007) (“if a district court determines that a

defendant is in default, then the factual allegations of the complaint, except those relating to the amount of damages, will be taken as true"). Moreover, as "a general rule, a default judgment establishes, as a matter of law, that a defendant is liable to a plaintiff as to each cause of action alleged in the complaint." *CFTC v. Marquis Fin. Mgmt. Sys., Inc.* at *5 (citing *Thomson*). Additionally, "a judgment by default may be entered without a hearing on damages when ... the amount claimed is liquidated or capable of ascertainment from the definite figures contained in the documentary evidence or in detailed affidavits." *Id.* at *6 (citations omitted). In this case, an evidentiary hearing on monetary relief is not necessary as the evidence in the attached declaration of SEC Accountant Ann M. Tushaus sufficiently establishes the nature and need for the relief that the SEC seeks, as well as the sums for which computations for monetary relief can be made.²

B. Securities Law Violations By Kilpatrick and Beasley

The SEC is requesting that the Court enter judgment based on Defendants' default – *i.e.*, their failure to answer the Complaint or otherwise participate in this litigation. That said, it is important to note that the allegations of the SEC's Complaint – which are taken as true for purposes of this Motion – establish that Kilpatrick and Beasley violated the securities laws as charged in the Complaint.

1.) Kilpatrick and Beasley Committed Fraud

Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit any person, in connection with the purchase or sale of any security, from directly or indirectly: (1) employing any device, scheme or artifice to defraud; (2) making any untrue statement of material fact or omitting to state a material fact necessary in order to make the statements

² Exhibit A to this motion, the declaration of Ann M. Tushaus, details the SEC's disgorgement and prejudgment interest calculations against Kilpatrick and Beasley.

made, in the light of circumstances under which they were made, not misleading; or (3) engaging in any act, practice, or course of business that operates as a fraud or deceit upon any person. Scienter – *i.e.*, knowing or reckless misconduct – is an element of Section 10(b) of the Exchange Act, and Rule 10b-5. *Aaron v. SEC*, 446 U.S. 680, 695 (1980); *Miller v. Champion Enter., Inc.*, 346 F.3d 660, 672 (6th Cir. 2003); *SEC v. Blavin*, 760 F.2d 706, 711 (6th Cir. 1985).

The SEC's allegations establish that Kilpatrick and Beasley violated each of these antifraud provisions. First, Kilpatrick and Beasley made material omissions when they failed to disclose to the Pension Funds almost \$125,000 in gifts from MGRA. To be actionable under 10b-5(b), an omission must involve information the defendant had a duty to disclose. *See In re Time Warner Inc. Sec. Litig.*, 9 F.3d 259, 267 (2d Cir. 1993). Kilpatrick and Beasley had a duty to disclose the gifts they received to the other trustees of the Pension Funds because they were fiduciaries to the Pension Funds as designated by Michigan State law.

Second, Kilpatrick and Beasley participated in a fraudulent scheme in violation of Exchange Act Section 10(b) and Rules 10b-5(a) and 10b-5(c) by extracting secret payments in connection with the Pension Funds' purchase of securities. From January 2007 through October 2007, Kilpatrick and Beasley requested personal gifts of private jet flights and entertainment from Mayfield and MGRA, which Mayfield and MGRA provided. Kilpatrick and Beasley knew, or recklessly disregarded, that the solicitation and provision of the gifts was inherently improper, and in violation of PERSIA and GRS ethics policy.

2.) Kilpatrick and Beasley Aided and Abetted MGRA's Violations of the Investment Advisers Act

The Advisers Act prohibits fraudulent conduct by investment advisers. Section

206(1) of the Advisers Act makes it unlawful for any investment adviser, directly or indirectly, to employ any device, scheme, or artifice to defraud any client or prospective client. Section 206(2) of the Advisers Act makes it unlawful to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client. Scienter is an element of a Section 206(1) violation, but is not an element of a Section 206(2) violation. *Capital Gains*, 375 U.S. at 195. Under Section 206(2), all that need be shown is that there is a “non-disclosure of material facts.” *Id.* at 186. Section 206(2) “simply requires proof of negligence by the primary violator.” *SEC v. PIMCO Advisors Fund Mgmt LLC*, 341 F. Supp. 454, 470 (S.D.N.Y. 2004).

MGRA was an investment adviser to both the PFRS and GRS.³ MGRA provided advice to its clients regarding the purchase of securities, and was paid for that advice. Also, both the Advisory Agreements between MGRA and the Pension Funds expressly defined MGRA as an investment adviser to the Pension Funds. As an Investment Adviser, MGRA had a fiduciary duty to act in its clients’ best interests, including “an affirmative duty of utmost good faith, and full and fair disclosure of all material facts.” *Capital Gains*, 375 U.S. at 191-92.

Mayfield and MGRA violated their fiduciary duty to the Pension Funds when they failed to disclose that MGRA, at Mayfield’s direction, had given lavish gifts to Kilpatrick and Beasley coinciding with MGRA’s provision of fee-generating investment advisory services to the Pension Funds. This conduct compromised the fiduciary obligations

³ Specifically, MGRA provided advice to the Pension Funds regarding the purchase of shares of the MGRA Genesis REIT. The MGRA Genesis REIT issued shares of common stock, which are securities. All of the capital invested in the MGRA Genesis REIT was contributed to the MGRA Genesis Fund, which was controlled by Mayfield and MGRA. MGRA earned a management fee based on the amount of assets held by the MGRA Genesis Fund. (*E.g.*, Dkt. #1 at ¶¶ 110-16.)

investment advisers owe their clients. *See SEC v. DiBella*, Civil Action No. 3:04cv1342 (EBB) (D.Conn. Oct. 3, 2007).

Kilpatrick and Beasley aided and abetted those violations. Individuals aid and abet violations of the Advisers Act when: (1) there has been commission of an underlying securities violation; (2) the alleged aider-abettor had general knowledge that his role was part of overall activity that is improper; and (3) the aider-abettor knowingly and substantially assisted the violation. *SEC v. Washington County Utility Dist.*, 676 F.2d 218, 224 (6th Cir. 1982) (citing *SEC v. Coffey*, 493 F.2d 1304, 1316 (6th Cir. 1974)).

Kilpatrick and Beasley's conduct meets that standard. Beasley personally solicited, and Beasley and Kilpatrick personally received, gifts from Mayfield and MGRA. Neither Kilpatrick nor Beasley disclosed the gifts to other trustees of the Pension Funds, and they knew that the gifts had not been disclosed by Mayfield or MGRA. Kilpatrick's designee and Beasley participated in deliberations and allowed the votes on investments in the MGRA Genesis REIT to go forward, all while concealing knowledge of their own, and Mayfield's and MGRA's, conflicts of interest. Kilpatrick and Beasley knew what they were doing, and they knew what they were doing was wrong. Accordingly, Kilpatrick and Beasley aided and abetted the violations of Sections 206(1) and 206(2).

C. Permanent Injunctions are Warranted Against Kilpatrick and Beasley.

The SEC requests that this Court enter a permanent injunction against Kilpatrick and Beasley to deter them from future violations of federal securities law. SEC can obtain a permanent injunction upon showing that a person has engaged, is engaged or is about to engage in acts or practices constituting a violation of the federal securities laws. 15 U.S.C. § 77t(b); 15 U.S.C. § 78u(d). To obtain a permanent injunction, the SEC must establish

that a violation has occurred and that there is a reasonable likelihood of future violations.

SEC v. Youmans, 729 F.2d 413, 415 (6th Cir. 1984).

In assessing whether there is a likelihood of future violations, Courts weigh the following factors: (1) the egregiousness of the violations; (2) the isolated or repeated nature of the violations; (3) the degree of scienter involved; (4) the sincerity of the defendant's assurances, if any, against future violations; (5) the defendant's recognition of the wrongful nature of his conduct; (6) the likelihood that the defendant's occupation will present opportunities (or lack thereof) for future violations; and (7) the defendant's age and health. *Youmans*, 729 F.2d at 415.

Here, each of those factors weighs in favor of a permanent injunction against Kilpatrick and Beasley. As pled in the SEC's Complaint, Kilpatrick and Beasley repeatedly violated the Exchange Act and the Advisers Act by engaging in a corrupt scheme to defraud the Pension Funds. They each acted with a high degree of scienter, with no concern for their own culpability and a high likelihood of future violations. Moreover, neither Kilpatrick nor Beasley has provided any assurances against future violations or recognized their wrongful conduct. To the contrary, in investigative testimony with the Commission, Kilpatrick and Beasley each exercised their Fifth Amendment right and refused to answer the staff's questions. Even with the imposed criminal relief for Kilpatrick – and the potential criminal liability for Beasley – Kilpatrick and Beasley both have the desire and political connections to work with local or state governments in the future. In fact, Kilpatrick has stated publicly that – even with his criminal record – if he ran for Mayor of the City of Detroit again, he would be elected. For his part, after he left city government, Beasley worked as the director of investor and

client services at a New York class action securities litigation law firm – a firm that represents the Pension Funds.

C. Disgorgement and Prejudgment Interest Should be Ordered Against Kilpatrick and Beasley.

The SEC respectfully requests that this Court order Kilpatrick and Beasley to disgorge (on a joint and several basis) the ill-gotten gains received from their fraudulent scheme, plus prejudgment interest on those amounts. “The purpose of disgorgement is to force a defendant to give up the amount by which he was unjustly enriched rather than to compensate the victims of fraud.” *SEC v. Blavin*, 760 F.2d 706, 713 (6th Cir. 1985) (quotations omitted). Joint and several liability is appropriate in cases where two or more individuals or entities have close relationships in engaging in illegal conduct ... This holds true even where one defendant is more culpable than another.” *S.E.C. v. Calvo*, 378 F.3d 1211, 1215 (11th Cir.2004) (*Citing S.E.C. v. Hughes Capital Corp.*, 124 F.3d 455 (3rd Cir.1997); *S.E.C. v. First Pac. Bancorp*, 142 F.3d 1186, 1191 (9th Cir.1998)). “Calculation of the defendant’s economic gain need not be exact, and determination of the appropriate amount is left to the sound discretion of the trial court.” *SEC v. Conaway*, 2010 U.S. Dist. LEXIS 17057, *34 (E.D. Mich. Feb. 25, 2010). “All doubts concerning the determination of disgorgements are to be resolved against the defrauding party.” *SEC v. Great Lakes Equities Co.*, 775 F. Supp. 211, 214 (E.D. Mich. 1991), *aff’d* 1993 U.S. App. LEXIS 29509 (6th Cir. 1993) (quotations omitted). Once the SEC shows that its disgorgement figure is a “reasonable approximation of the profits causally connected to the violation,” the burden then shifts to the defendant to show that this approximation is inaccurate. *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989). Additionally, the Court “may add prejudgment interest to the disgorgement amount to avoid a defendant benefitting for the

use of his ill-gotten gains interest free.” *Id.* (citing *SEC v. Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978)).

Here, Kilpatrick and Beasley reaped over \$125,000 in free travel and entertainment in the course of their illegal “pay to play” scheme, including:

TRIP	EXPENSES PAID FOR KILPATRICK AND BEASLEY
North Carolina	\$3,333.02
Las Vegas, Nevada	\$60,259.30
Bermuda	\$34,604.90
Tallahassee, Florida	\$24,725.65
TOTAL:	\$122,922.87

Using the IRS rate for the underpayment of income taxes, prejudgment interest on that total, measured from the date the gift was conferred through the end of May 2014 is \$39,939. (*See* Ex. A, Tushaus Decl. ¶¶ 6-7.)

D. Civil Penalties are Warranted Against Kilpatrick and Beasley.

The SEC respectfully requests that this Court order Kilpatrick and Beasley to pay a civil penalty – of \$390,000 and \$130,000 respectively – for their violations of the anti-fraud provisions of federal securities law. The imposition of such penalties are “necessary for the deterrence of securities law violations that otherwise would provide great financial returns to the violator.” *SEC v. Conaway*, 2010 U.S. Dist. LEXIS 17057, *36-37 (quotations omitted). The standard for determining a penalty is based upon the Court’s discretion in light of the facts and circumstances of each case. 15 U.S.C. § 77t(d)(2). Under the Exchange Act, there is a three tier system for assessing civil penalties. A “third

tier” penalty is appropriate where, as here, (1) the defendant’s violation “involved fraud, deceit, manipulation” and (2) the defendant’s “violation directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons.” 15 U.S.C. § 77t(d)(2)(C); 15 U.S.C. § 78u(d)(3)(B)(iii). For a natural person, the maximum third tier penalty is the higher of (1) \$130,000 per violation; or (2) the gross amount of pecuniary gain to such defendant as a result of the violation. *Id.*

The conduct alleged here meets the standard for a third-tier penalty. Kilpatrick and Beasley engaged in a course of conduct that involved fraud, deceit, manipulation, and deliberate or reckless disregard of regulatory requirements. The risk of loss to pensioners was potentially catastrophic as their violations corrupted the integrity of the Pension Funds’ investment process. The SEC requests that the Court impose a \$390,000 civil penalty against Defendant Kilpatrick reflecting that he violated the antifraud provisions on multiple occasions. While the SEC could seek a civil penalty for each of the four trips that Kilpatrick received from MGRA, the SEC – in an abundance of caution, recognizing the relatively small benefit conveyed for the North Carolina trip – asks that Kilpatrick be assessed a maximum third-tier penalty for each of the three major trips that he received (Las Vegas, Bermuda, and Florida). The SEC requests that the Court impose a \$130,000 civil penalty against Defendant Beasley, reflecting that his fraud was serious enough to warrant a maximum third-tier penalty, but that he received a lesser benefit from the fraud than Kilpatrick.

CONCLUSION

For the reasons stated above, the SEC respectfully requests that the Court grant this motion in its entirety, and enter an order as to Defendants Kilpatrick and Beasley (1)

enjoining each of them from future violations of the provisions of federal securities law identified in the Commission's Complaint; (2) enjoining them from participating in any investment decisions by public pensions as a trustee, officer, employee or agent (3) requiring each of them to disgorge their ill-gotten gains plus prejudgment interest; and (4) requiring each of them to pay a civil penalty.

May 23, 2014

Respectfully submitted,

s/ **Timothy S. Leiman**
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Eric A. Celauro
U.S. Securities and Exchange
Commission
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Chicago, IL 60604
Tel. (312) 353-8642
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CERTIFICATE OF SERVICE

Timothy S. Leiman, an attorney, hereby certifies that on May 23, 2014, I caused the foregoing *Plaintiff U.S. Securities and Exchange Commission's Motion for Final Judgments of Permanent Injunction and Other Relief by Default* to be filed with the Clerk of Court using the CM/ECF system, and have served a copy of the same, via overnight delivery, upon:

Kwame Kilpatrick, #44678-039
FCI El Reno
Federal Correctional Institution
P.O. Box 1500
El Reno, Oklahoma 73036

Jeffrey Beasley
4315 S. Cottage Grove Ave. 2N
Chicago, IL 60653

s/ Timothy S. Leiman

EXHIBIT A

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

UNITED STATES SECURITIES
AND EXCHANGE COMMISSION,

Plaintiff,

Case No. 12-cv-12109

v.

Hon. Victoria A. Roberts

KWAME M. KILPATRICK,
ET AL.,

Magistrate Judge R. Steven Whalen

Defendants.

DECLARATION OF ANN M. TUSHAUS

1. I, Ann M. Tushaus, am a Staff Accountant with the United States Securities and Exchange Commission (the "Commission") in its Chicago Regional Office, located at 175 West Jackson Boulevard, Suite 900, Chicago, Illinois, 60604. I have been employed as a Staff Accountant by the Commission since July 2007. My official duties include participating in fact-finding inquiries and investigations to determine whether the federal securities laws have been, are presently being, or are about to be violated, and assisting in the Commission's litigation of enforcement actions.

2. I received a B.A. degree in Accounting from Illinois Wesleyan University. I have been a Certified Public Accountant since October 2004. Prior to joining the Commission, I was an auditor in the private sector.

3. In connection with the Commission's above-captioned litigation against Kwame M. Kilpatrick ("Kilpatrick") and Jeffrey W. Beasley ("Beasley"), I have reviewed documents relating to the benefits given by MayfieldGentry Realty Advisors, LLC ("MGRA") to Kilpatrick, Beasley, and their associates.

4. Specifically, I have reviewed:

- (a) the Complaint filed by the Commission in this matter;
- (b) invoices from Pentastar Aviation for charter flights to Las Vegas, Tallahassee, and Bermuda;
- (c) bank statements showing wire transfers from MGRA's bank accounts to Pentastar Aviation; and
- (d) emails, credit card statements, and expense reports showing payments by MGRA for entertainment and travel expenses.

5. Based on my review and analysis of the records referenced above and conversations with Commission staff, Kilpatrick, Beasley, and their associates received \$122,923 in ill-gotten gains from MGRA.

6. Exhibit 1 attached hereto is a schedule I prepared reflecting calculations I performed for prejudgment interest on the \$122,923 in ill-gotten gains described above. The prejudgment interest was calculated applying the interest rate, adjusted quarterly, used by the IRS for computation of interest on the underpayment of taxes.

7. Prejudgment interest on the \$122,923 of ill-gotten gains totals \$39,939. (Ex. 1)

I, Ann M. Tushaus, do hereby declare under penalty of perjury, in accordance with 28 U.S.C. § 1746, that the foregoing is true and correct. Executed on the 23rd day of May 2014.


ANN M. TUSHAUS

EXHIBIT 1

PREJUDGMENT INTEREST CALCULATION
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
v.
KWAME M. KILPATRICK, ET AL

PERIOD		(1) ANNUAL RATE	(2) PERIOD RATE	(3) PERIOD INTEREST	(4) PERIOD PROCEEDS	(5) TOTAL
	to 31-Mar-07	8%	2.00%	-	3,333	3,333
01-Apr-07	to 30-Jun-07	8%	2.00%	67	60,259	63,659
01-Jul-07	to 30-Sep-07	8%	2.00%	1,273	24,726	89,658
01-Oct-07	to 31-Dec-07	8%	2.00%	1,793	34,605	126,056
01-Jan-08	to 31-Mar-08	7%	1.75%	2,206	-	128,262
01-Apr-08	to 30-Jun-08	6%	1.50%	1,924	-	130,186
07-Jan-08	to 30-Sep-08	5%	1.25%	1,627	-	131,813
01-Oct-08	to 31-Dec-08	6%	1.50%	1,977	-	133,790
01-Jan-09	to 31-Mar-09	5%	1.25%	1,672	-	135,463
01-Apr-09	to 30-Jun-09	4%	1.00%	1,355	-	136,817
01-Jul-09	to 30-Sep-09	4%	1.00%	1,368	-	138,185
01-Oct-09	to 31-Dec-09	4%	1.00%	1,382	-	139,567
01-Jan-10	to 31-Mar-10	4%	1.00%	1,396	-	140,963
01-Apr-10	to 30-Jun-10	4%	1.00%	1,410	-	142,373
01-Jul-10	to 30-Sep-10	4%	1.00%	1,424	-	143,796
01-Oct-10	to 31-Dec-10	4%	1.00%	1,438	-	145,234
01-Jan-11	to 31-Mar-11	3%	0.75%	1,089	-	146,324
01-Apr-11	to 30-Jun-11	4%	1.00%	1,463	-	147,787
01-Jul-11	to 30-Sep-11	4%	1.00%	1,478	-	149,265
01-Oct-11	to 31-Dec-11	3%	0.75%	1,119	-	150,384
01-Jan-12	to 31-Mar-12	3%	0.75%	1,128	-	151,512
01-Apr-12	to 30-Jun-12	3%	0.75%	1,136	-	152,648
01-Jul-12	to 30-Sep-12	3%	0.75%	1,145	-	153,793
01-Oct-12	to 31-Dec-12	3%	0.75%	1,153	-	154,947
01-Jan-13	to 31-Mar-13	3%	0.75%	1,162	-	156,109
01-Apr-13	to 30-Jun-13	3%	0.75%	1,171	-	157,280
01-Jul-13	to 30-Sep-13	3%	0.75%	1,180	-	158,459
01-Apr-13	to 30-Jun-13	3%	0.75%	1,188	-	159,648
01-Oct-13	to 31-Dec-13	3%	0.75%	1,197	-	160,845
01-Jan-14	to 31-Mar-14	3%	0.75%	1,206	-	162,051
01-Apr-14	to 31-May-14	3%	0.50%	810	-	162,862

TOTAL PROCEEDS	\$ 122,923
TOTAL INTEREST	39,939
	\$ 162,862

NOTES

- (1) Interest rate published by the Internal Revenue Service obtained from Rev. Rul 2014-11; 2014 IRB Lexis 218; 2014-14 I.R.B. 906.
- (2) Interest rate to be used in the calculation. For example, the rate for the period ending June 30, 2007, is 8% divided by 4.
- (3) The interest amount calculated for the period which equals the preceding period total multiplied by the period interest rate.
- (4) Period Proceeds equals the benefits to Kilpatrick, Beasley, and their associates.
- (5) Total is the preceding period total plus the interest calculated for the period.