UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, **Plaintiff,** **v.** **LONGFIN CORP. and VENKATA S. MEENAVALLI,** **Defendants.**	**Case No.: 19-cv-5296-DLC** **MEMORANDUM IN SUPPORT OF MOTION FOR AN ORDER ESTABLISHING A FAIR FUND AND AUTHORIZING DISTRIBUTION OF COLLECTED FUNDS THROUGH A RELATED ACTION**

I. INTRODUCTION

Plaintiff, the Securities and Exchange Commission (the "SEC"), respectfully submits this memorandum in support of: (i) establishing a Fair Fund pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002 ("Section 308(a)") for all funds under the Court's jurisdiction in the captioned matter (the "Present Action"); and (ii) combining those funds, currently comprised of approximately $300,000 in disgorgement, prejudgment interest, and civil penalty collected from the defendants in the Present Action, plus accrued interest, with the Fair Fund established in the related action before this Court, *SEC v. Longfin, et al.,* 18-cv-2977-DLC (the "Related Action"), for distribution to harmed investors pursuant to the Court-approved distribution plan[1] in that case.

The SEC is simultaneously seeking, by the accompanying motion (the "Motion"), the entry of an Order to Show Cause so that interested parties have the opportunity to object to this

[1] 18-CV-2977, ECF No. 134.

proposal for the disposition of collections in the Present Action (the "SEC Proposal"). If the Court grants the Motion and enters the proposed Order to Show Cause, upon the completion of the steps set forth in the Order to Show Cause, the SEC will file a notice (the "Notice") and/or a response, so notifying the Court and responding to any objections, and provide a proposed Order approving the SEC Proposal or an amended proposal, as appropriate.

By this memorandum, and subject to the Notice, the SEC provides to the Court the factual and legal basis for approving the SEC Proposal. A Fair Fund is a prerequisite to including in any distribution the collected civil penalties with the remainder of collections in the Present Action. Combining the funds collected in the Present Action with the Fair Fund established in the Related Action (the "2018 Fair Fund") is appropriate for several reasons. First, there is significant overlap between the harm being addressed in the two cases. Second, there are insufficient collections in the Present Action to make a stand-alone distribution feasible. Third, combining the collections in the two actions will ensure that the collections in the Present Action are used to benefit investors.

II. RELEVANT BACKGROUND

A. The Present Action

The SEC filed the Present Action on June 5, 2019, alleging that defendants Longfin Corp. ("Longfin") and Venkata S. Meenavalli ("Meenavalli") (collectively, the "Defendants") engaged in a scheme to obtain a Nasdaq listing through a fraudulent public offering under Regulation A+ of the JOBS Act. ECF No. 1. The SEC further alleged that, during 2017 and 2018, Longfin and Meenavalli perpetrated an accounting fraud by reporting fictitious revenue from commodity transactions that resulted in a materially false annual report filed April 2, 2018 on Form 10-K for the year ended December 31, 2017 (the "Annual Report"), and a materially false quarterly report

filed August 13, 2018 on Form 10-Q for the quarter ended March 31, 2018 (the "Quarterly Report").

The Court has since entered final judgments against Longfin and Meenavalli, ordering them to pay combined disgorgement and prejudgment interest of $3,532,235 and $168,000, respectively; and civil penalties of $3,243,613 and $232,000, respectively. *See* ECF Nos. 36, 46. Of this amount, the SEC has collected approximately $300,000 from Meenavalli, held in an interest bearing account at the U.S. Treasury's Bureau of Fiscal Service ("BFS"). Each of the final judgments provides that the SEC may propose a plan to distribute the collected funds that may provide for the distribution pursuant to the Fair Fund provisions of Section 308(a). *Id.*

B. The Related Action

By action instituted on April 4, 2018, unsealed on April 6, 2018, the SEC charged Longfin, Meenavalli, Amro Izzelden Altahwi, Suresh Tammineedi, and Dorababu Penumarthi, with distributing over $26 million in Longfin securities in violation of the registration requirements of Section 5 of the Securities Act of 1933, 15 U.S.C. § 77(e).[2] The Court has since entered final judgments against all of the defendants, ordering them, in the aggregate, to pay disgorgement of $22,862,377.23 and civil penalties of $3,582,941.97, for a total monetary liability of $26,445,319.20.[3] Of this amount, the defendants have paid, approximately, $26.1 million, held in an interest-bearing account at BFS.

On April 15, 2020, this Court established the 2018 Fair Fund so that civil penalties can be distributed to harmed investors; appointed Miller Kaplan Arase LLP as the tax administrator for

[2] *See* Related Action, ECF Nos. 1-6.

[3] *See* Related Action, ECF Nos. 100-102, 117-18.

the 2018 Fair Fund; and appointed Epiq Class Action & Claims Solutions, Inc. as distribution agent to oversee the administration of the 2018 Fair Fund pursuant to the terms of a court-approved distribution plan and related Court Orders.[4]

By Order entered June 30, 2020, after completion of procedures set forth in an Order to Show Cause, the Court approved a proposed plan for the distribution of the 2018 Fair Fund to harmed investors (the "Related Action Plan").[5]

C. The Related Action Plan

The goal of the Related Action Plan is to compensate those investors harmed by the unregistered offering of Longfin common stock. Under the Related Action Plan, the Recovery Period[6] -- June 16, 2017 through April 6, 2018, inclusive -- begins on the day that Longfin common stock was first offered to the public under SEC Regulation A[7] and goes through the date that the SEC complaint against Longfin was made public and trading was temporarily halted.[8] In order to be considered for distribution eligibility under the Related Action Plan, investors must have invested in Longfin common stock during the Recovery Period.[9]

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[4] Related Action, ECF No. 125.

[5] Related Action, ECF No. 134.

[6] Related Action Plan, ¶5.s. Capitalized terms not otherwise defined in this memorandum have the meanings ascribed to them in the Related Action Plan. The Related Action Plan is available at https://longfinfairfund.com/ .

[7] Regulation A – Conditional Small Issues Exemption, 17 C.F. R. §§ 230.241-263.

[8] *See, e.g.,* https://www.marketwatch.com/story/longfins-stock-halted-for-additional-information-as-sec-freezes-stock-sales-2018-04-06 . The Recovery Period is appropriate in the context of the Related Action. Specifically, after the SEC's complaint in that action and the temporary trading halt, investors were on notice of unregistered nature of the common stock. The Related Action does not include the fraud allegations related to the quarterly filings and, accordingly, collections in that case should not be distributed to compensate investors for the unalleged misconduct.

[9] Related Action Plan, ¶5.q.

The SEC now proposes to distribute the collections in the Present Action through the Related Action Plan because there is significant, albeit incomplete, overlap between the investors harmed in the Present Action and the Related Action; an independent distribution of the approximately $300,000 in collections in the Present Action would not be feasible; and combining the collections in the two actions will ensure that the collections in the Present Action are used to benefit investors.

D. The Overlap of the Pools of Harmed Investors in the Two Actions.

There is a substantial, although incomplete, overlap in the allegations of the Present Action and the Related Action, and those harmed investors that are common to both actions will be eligible to file claims under the Related Action Plan. In sum, most of the investors potentially harmed by the violations alleged in the Present Action are eligible to file claims under the Related Action Plan.

1. Investors in Both Actions Potentially Harmed by the Alleged Registration Violations Coincide and Will Be Eligible to File Claims Under the Related Action Plan.

In both the Present Action and the Related Action, the SEC has asserted claims against Longfin and its agents for violation of registration requirements of federal securities laws in connection with its offering of over $27 million in Longfin securities. All those who purchased the unregistered securities during the Recovery Period – which ends upon the date of filing of the Related Action and the imposition of a temporary trading halt – would be eligible to file a claim under the Related Action Plan. Thus, there is complete coincidence between those potentially harmed by the registration violations in the Related Action and those potentially harmed by those same violations in the Present Action.

2. Most of the Investors Potentially Harmed by the Fraud Allegations in the Present Action Will Be Eligible to File Claims Under the Related Action Plan.

The Present Action includes not only charges based on registration violations but also includes fraud charges for the filing of the fraudulent Annual Report and Quarterly Report on April 2, 2018 and August 13, 2018, respectively. But the inclusion of those fraud charges in the Present Action does not result in a significant number of additional harmed investors.

Those investors potentially harmed by the fraudulent April 2, 2018 Annual Report largely coincide with those harmed by the registration violations and will be eligible to file claims under the Related Action Plan. Specifically, because of the trading suspension beginning on April 6, 2018, and continuing through May 24, 2018, most, if not all, investors potentially influenced by the April 2, 2018 Annual Report would have purchased Longfin common stock on or before April 6, 2018, thus falling with the Recovery Period.

In contrast, those affected (only) by the fraudulent August 13, 2018 Quarterly Report will be ineligible to file claims under the Related Action Plan.[10] This subset of investors represents a small percentage of purchasers of Longfin common stock; records indicate relatively few shares were purchased after that report.[11] Moreover, some of the investors who purchased after the

[10] Investors who, despite the SEC's enforcement action and the temporary trading halt of the trading in Longfin common stock, purchased that stock after the August 13, 2018 publication of the Quarterly Report, and who do not otherwise fall within the parameters described in D.1., above, will fall outside of the Recovery Period and will be ineligible to file a claim under the Related Action Plan.

[11] The aggregate number of shares of Longfin common stock affected by the August 13, 2018 Quarterly Report is likely to be a small percentage of the number of shares affected by the remainder of the misconduct, for which investors will be eligible to file claims. Specifically, whereas the average daily volume of trading in Longfin common stock was 1.2 million shares from the time it began trading on the public market through April 6, 2018, the average daily trading after the filing of the Quarterly Report on August 13, 2018 through the November 21, 2018 filing of an 8-K report referencing an orderly liquidation of assets was just under 28,000 shares—approximately 2% of the trading volume on the public market through April 6, 2018.

August 13, 2018 Quarterly Report may also have holdings in Longfin common stock acquired on or before April 6, 2018, for which they will be eligible to seek compensation under the Related Action Plan.

In short, the universe of investors potentially harmed by the violations covered by the Present Action and those potentially harmed by the violations covered by the Related Action would be largely the same.

III. DISCUSSION OF THE RELIEF REQUESTED

A. The Court Must Establish a Fair Fund in Order to Distribute the Collected Civil Penalty.

The SEC has collected approximately $300,000 from Meenavalli, of which approximately $131,000 is collected civil penalty. In order to include the civil penalty in any distribution, including a transfer to the Related Action for distribution to harmed investors through the Related Action Plan, a Fair Fund pursuant to Section 308(a) must be established.

Section 308(a) provides, in relevant part:

> If in any judicial or administrative action brought by the [SEC] under the securities laws, the [SEC] obtains a civil penalty against any person for a violation of such laws, or such person agrees, in settlement of any such action, to such civil penalty, the amount of such civil penalty shall, on the motion or at the direction of the [SEC], be added to and become part of a disgorgement fund or other fund established for the benefit of the victims of such violation.

15 U.S.C. § 7246(a).

The SEC brought the Present Action under the federal securities laws and, in relevant part, this Court has ordered Meenavalli to pay a $232,000 civil penalty in addition to disgorgement and prejudgment interest. Of that amount, the SEC has collected approximately $131,000 of the ordered civil penalty. Section 308(a)'s requirements have thus been satisfied

and the creation of a Fair Fund for the benefit of harmed investors is appropriate so that the entirety of the collections in this case can benefit harmed investors.

B. Combining the $300,000 paid by Meenavalli with the Fair Fund in the Related Action for Distribution Pursuant to the Related Action Plan is Fair and Reasonable.

A district court has broad discretion in approving a plan of distribution, and that determination is reviewed for abuse of discretion. *Official Comm. Of Unsecured Creditors of WorldCom, Inc. v. SEC*, 467 F.3d 73, 84 (2d Cir. 2006). *See also SEC v. Loewenson*, 290 F.3d 80, 84 (2d Cir. 2002) (in the context of approval of a plan presented by a receiver). District courts review distribution plans proposed by the SEC to determine whether the plan fairly and reasonably distributes limited funds among the potential claimants. *See WorldCom*, 467 F.3d at 81-82, 84; *SEC v. Wang,* 944 F.2d 80, 85 (2d Cir. 1991); *SEC v. CR Intrinsic Investors, LLC*, 164 F. Supp. 3d 433, 435-36 (S.D.N.Y. 2016). *See also SEC v. Amerindo Inv. Advisors*, 639 F. App'x 752, 755 (2d Cir. 2016) (quoting *Wang*, finding adequate the district court's finding that the receiver's proposed distribution was fair and reasonable).

Nearly every plan to distribute funds obtained in an SEC enforcement action requires choices to be made regarding the allocation of funds between and among potential claimants within the parameters of the amounts recovered. As the Court of Appeals for the Second Circuit has explained, "[t]his kind of line-drawing – which inevitably leaves out some potential claimants – is . . . appropriately left to the experience and expertise of the SEC in the first instance." *See Wang,* 944 F.2d at 88.

Under the SEC Proposal, collections in this matter will be aggregated with other funds that will be used to compensate most of the investors harmed by the conduct underlying the Present Action. Although not a perfect solution, the execution of a separate plan by which

unknown investors could be compensated is not feasible with a fund of approximately $300,000. Even assuming the sharing of costs with the Related Action, the administrative costs would leave little, if anything, for distribution. Accordingly, the SEC respectfully submits that the SEC Proposal is both fair and reasonable and should be approved. It is the best way to ensure that the collections in this case are used for the benefit of investors.

II. Conclusion

For all of the foregoing reasons, the SEC respectfully requests that the Court establish a Fair Fund pursuant to Section 308(a) for all funds under the Court's jurisdiction in the Present Action; approve the SEC Proposal by which the Fair Fund will be combined with the 2018 Fair Fund for distribution to harmed investors pursuant to the Related Action Plan; and grant such other relief as the Court deems appropriate.

Dated: August 13, 2020

Respectfully submitted,

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