

[Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION](#) [—D.Mass.: SEC charges in priest's short-and-distort scheme survive dismissal, \(Apr. 8, 2021\)](#)

Securities Regulation Daily Wrap Up

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By [Rodney F. Tonkovic, J.D.](#)

The hedge fund adviser, who was also an Orthodox priest, was charged with scheming to drive down the price of a pharmaceutical company's shares.

The SEC's fraud claims against a hedge fund adviser charged with engaging in a short-and-distort scheme have survived summary judgment. The Commission accused the adviser of taking a short position in a pharmaceutical company and then issuing a series of reports spreading false claims, including that the company was on the verge of bankruptcy. After the company's share price dropped, the adviser reaped the gains. The court found that the SEC adequately showed at this stage that Lemelson knowingly made materially false statements. The court also rejected Lemelson's affirmative defense that he suffered bias due to his religion ([SEC v. Lemelson](#), April 6, 2021, Saris, P.).

Short-and-distort. The Commission [charged](#) hedge fund adviser Gregory Lemelson and his investment advisory firm, Lemelson Capital Management, with [scheming](#) to drive down the price of a pharmaceutical company's stock. In May 2014, Lemelson took a short position in Ligand Pharmaceuticals Inc. on behalf of a hedge fund he advised and partly owned.

According to the SEC, after establishing his short position, Lemelson made a series of false statements intended to shake investor confidence in Ligand, lower its stock price, and increase the value of his position. At issue are statements made by Lemelson after taking his short position. First, Lemelson published a 25-page report explaining that in his opinion, Ligand's stock was overvalued. This theory was based on Lemelson's belief that Ligand's main product would soon be replaced by drugs from competitors. In a later report, Lemelson said that Ligand was insolvent. Lemelson also participated in live and written interviews in which he made additional false statements, including that Ligand representatives agreed with his analysis. By October 2014, Lemelson had covered his short position and generated approximately \$1.3 million in illegal profits.

Summary judgment denied. The court denied Lemelson's motion for summary judgment, which argued that the challenged statements were immaterial, made without scienter, and were either true or protected opinion. Lemelson argued that his statements were not material because they had no demonstrable effect on Ligand's stock price. In support of its allegations, the Commission put forth evidence of stock price drops during the time Lemelson was publishing his reports, and Lemelson himself attributed price drops to his statements. This was sufficient for the court to find that the challenged statements altered the "total mix" of available information. The court also found that the Commission adequately alleged scienter by showing that Lemelson was at least reckless and aware that his statements could mislead investors. Lemelson then argued that his statements were opinions protected by the First Amendment but the court disagreed, finding that the statements were statements of fact, not opinion. Finally, the court found that the SEC provided evidence supporting its claim under the Investment Advisers Act that Lemelson made false statements in emails to prospective and current investors.

Selective enforcement. In his defense, Lemelson claimed an equal protection violation based on selective enforcement. Lemelson pointed out that Ligand's lead outside counsel was once employed by the SEC and was friends with Commissioner Hester Peirce (the SEC testified that Peirce and Bondi never discussed this case, or any other SEC business). Also, as an Orthodox priest, Lemelson cited evidence that Ligand employees mocked his vocation; among other items, Ligand argued before the SEC that Lemelson was engaged in an "affinity

fraud." During the investigation, Lemelson was asked about an email in which he appeared to compare himself to activist investors and religious and civil rights leaders: "Did Socrates, Martin Luther King, Ghandi or the son of God have a financial incentive to cause investors to sell stock in a particular company to bring the price down?"

The court granted the Commission's motion for partial summary judgment and dismissed the affirmative defense of selective enforcement. Lemelson pointed to others who published reports critical of Ligand, but none of these entities were alleged to have made false statements about Ligand or to have short positions in the company. The defendants also accused the SEC of impermissibly considering Lemelson's religion, but the court found no evidence of bias—there was no link between the statements by Ligand employees and the SEC, for example. There was also no evidence that Ligand's attorney had any influence over the SEC commissioners or that Ligand received any preferential treatment.

The case is [No. 18-11926](#).

Attorneys: Alfred A. Day, for the SEC. Douglas S. Brooks (Libby Hoopes Brooks, P.C.) for Gregory Lemelson, Lemelson Capital Management, LLC and Amvona Fund, LP.

Companies: Lemelson Capital Management, LLC; Amvona Fund, LP

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