

[Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION—N.D. III.: Biofuel company founder ordered to disgorge \\$700,000 for pump and dump scheme, \(Sept. 22, 2016\)](#)

Securities Regulation Daily Wrap Up

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By [Kevin Kulling, J.D.](#)

The founder of a company purportedly in the business of making and selling biofuels has been ordered to disgorge more than \$700,000 in ill-gotten gains in connection with a pump and dump scheme that allegedly cost investors more than \$4 million. Meanwhile, an attorney who was found liable for her role in the scheme that included advising the company about a reverse merger that resulted in the sale of unregistered securities will be afforded a hearing before a civil penalty is assessed (*SEC v. Zenergy International, Inc.*, September 20, 2016).

Pump and dump scheme. The SEC alleged that Zenergy International, Inc. (Zenergy), founded by defendants Bosko Gasich and Robert Luiten, entered into a reverse merger with a publicly traded shell entity, Paradigm Tactical Products, Inc. (Paradigm). Prior to the merger, Gasich prepared a backdated convertible note for a \$300,000 debt purportedly owed to him by Zenergy. Paradigm agreed to assume the debt and issued shares of its common stock to settle the debt as partial consideration for the reverse merger. The underlying "debt" never existed, according to the SEC's complaint.

Gasich allegedly assigned the debt to several family, friends, stock promoters, associates of Paradigm, and Zenergy's counsel Diane Dalmy. The assignees immediately exercised an option to convert the debt into shares of Paradigm stock, according to the SEC. Gasich assignees and their transferees obtained total trading profits of at least \$4.4 million, the SEC alleged. No registration statement was filed or in effect for the transactions, according to the SEC.

Promotional activity. The SEC alleged that Zenergy, Gasich, and Luiten engaged in a number of promotional activities, including the issuance of misleading press releases about the reverse merger. The press releases did not disclose that Zenergy's operations and assets were nonexistent nor did they disclose the material terms of the reverse merger or the assignment of convertible debt to family, friends, and promoters. Zenergy stock was touted on message board posts, emails, and Twitter. As the result of this promotional activity, Zenergy's stock price increased dramatically, according to the SEC.

Counsel opinion letters. The SEC also alleged that Dalmy's opinion letters incorrectly represented that the shares being issued in connection with the Gasich assignment could be issued to and sold by the assignees without restriction pursuant to Rule 144 under the Securities Act. Her opinion letters were also incorrect in representing that the Gasich debt was reflected Zenergy's financial statements, and, when the one-year holding period for the "debt" began. Dalmy failed to conduct any reasonable inquiry to prepare her opinions, the SEC alleged.

Settlement and sanctions. The SEC previously settled with several defendants, who agreed to penny stock bars, permanent injunctions, and monetary relief. Gasich had previously agreed to a partial settlement imposing disgorgement and penalties, a penny stock bar, an officer and director bar, and a permanent injunction. At issue before the court was the amount of monetary sanctions.

Disgorgement. The court ordered Gasich to disgorge \$633,518 plus \$79,732 in prejudgment interest; Luiten to disgorge \$11,800 in profits and \$1,709 in prejudgment interest; and attorney Dalmy to disgorge \$43,995 in profits and \$9,877 in prejudgment interest.

Civil penalties. Before imposing Tier 3 civil penalties against Gasich, the court first looked at several factors, including the seriousness of the violations, scienter, the repeated nature of the violations, whether Gasich

admitted wrongdoing, the losses or risk of losses caused by the conduct, any cooperation provided to enforcement authorities and his ability to pay.

The court found his conduct to be egregious, resulting in a loss of \$4 million to investors. The SEC established that Gasich's conduct was fraudulent, deceitful, and manipulative and resulted in his gain of more than \$600,000. Furthermore, the SEC proved that he acted with scienter and that his scheme spanned over six months, involved numerous acts and resulted in multiple violations of federal securities laws. The court assessed a civil penalty equal to the gross amount of gain, \$633,518 as an appropriate amount.

Luiten, although a founder of Zenergy, was less involved in the scheme and his profits were less than Gasich's. But the court found it significant that he reviewed and approved Zenergy's false press releases and false disclosure statement. His actions, and inactions as corporate officer and director, contributed to the losses suffered by investors. The court ordered a Tier one penalty of \$7,500.

As to Attorney Dalmy, the court noted that she argued that her only transgression was opining incorrectly that the shares at issue did not need registration. Therefore, the court ordered a hearing on the matter of scienter and reserved the ruling on the motion for civil penalties against her until the hearing was conducted.

The case is [No. 13-cv-5511](#).

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