

IN THE UNITED STATES DISTRICT COURT FOR THE  
NORTHERN DISTRICT OF ILLINOIS  
EASTERN DIVISION

UNITED STATES,	)	
	)	
Plaintiff,	)	No. 07 CR 227
vs.	)	
	)	Judge George W. Lindberg
JOHN TOMKINS,	)	
Defendant.	)	

**DEFENDANT TOMKIN'S MOTION TO DISMISS**

NOW COMES defendant John Tomkins, by his attorney John M. Beal, and respectfully moves this Court, pursuant to Fed.R.Crim.P. 12(b)(3)(B), to dismiss Counts One through Ten of the Indictment in this case for failure to state an offense, and in support thereof states as follows:

1. The indictment in this case charges defendant Tomkins with, *inter alia*, ten counts of securities fraud under 15 U.S.C. §78j(b). The common paragraphs applicable to Counts One through Ten allege that the defendant "employed a manipulative device or contrivance in contravention of Rule 10b-5," referring to Securities and Exchange Commission Rule 10b-5. Indictment, ¶2. Paragraph 2 further states that the defendant employed such manipulative device or contrivance, "in that defendant (a) did employ a device, scheme and artifice to defraud and (b) did engage in acts, practices and a course of business which would operate as a fraud and deceit upon shareholders and potential shareholders of Navarre and 3COM, in connection with the purchase and sale of common stock and options contracts of Navarre and 3COM..." The indictment specifically states

in paragraph 3 that the scheme utilized by the defendant "was to induce, by threats of violence, certain third party investors and executives, through false information and trading activities, to manipulate and cause the common stock of Navarre and 3COM to trade at artificially high prices that did not reflect the unfettered supply of and demand for such stocks, thereby artificially and fraudulently increasing the market value of defendant's investment positions."

2. The indictment proceeds to allege that defendant Tomkins purchased common stock of Navarre and 3COM corporations, and call option contracts for the stock of these companies. It is further alleged that the defendant intended to sell the aforesaid stock and exercise the option contracts when the market price had been increased. Indictment, ¶4.

3. It is further alleged that defendant Tomkins sent threatening and extortionate letters to senior officials of investment management firms that traded in the national securities markets and who exercised investment discretion over the assets entrusted to their management. Indictment, ¶5.

4. In particular, with respect to 3COM stock, defendant Tomkins is alleged to have "attempted to manipulate the price of 3COM stock to reach \$6.66 by October 31, 2005," by mailing at least five letters to persons employed by Yacktman Asset Management Company, Friess Associates, and Broadview Advisors LLC, which letters contained threats of violence and bodily injury if the 3COM stock price did not reach the target price. Indictment, ¶6. That paragraph further alleges that

it was "defendant's purpose and intent to cause the recipients of the letters to execute trades and to take such manipulative and fraudulent actions as may have been required to increase the price of 3COM stock to defendant's target price."

5. Five such letters are identified in paragraph 7 and 8 of the indictment.

6. It is then alleged that the defendant "intended to sell 3COM common stock and 3COM call options after the price of 3COM was fraudulently, artificially and manipulatively increased pursuant to defendant's communications." Indictment, ¶9. To that end, it is alleged that the defendant acquired 3COM stock options.

7. Paragraphs 10 through 17 allege a virtually identical scheme with respect Navarre Corporation. Defendant Tomkins is alleged to have mailed threatening letters to persons associated with Wallace R. Weitz & Company; Nicolas Company, Inc.; Thompson Investment Management; First Pacific Advisors; Schwartz Investment Counsel, Inc.; Ave Maria Mutual Funds; Calamos Investments; Diamond Hill Investments; Bidgeway Funds; American Century Investments; and Janus Small Cap Value Funds. The letters are alleged to have contained threats of violence and bodily injury if the Navarre stock price did not reach a certain specified price on or before May 1, 2006, June 13-17, 2006, July 4, 2006, August 1, 2006, and/or February 7-9, 2007. Indictment, ¶10.

8. It is also alleged that on March 13, 2006, defendant Tomkins mailed threatening letters to three individuals associated with Wallace R. Weitz & Company, Nicolas Company, Inc., and Thompson Investment Management

demanding that they begin purchasing stock of Navarre and increase the Navarre stock price to \$6.66 by May 1, 2006. Indictment, ¶12.

9. In paragraphs 13 through 15, additional threatening letters are alleged to have been sent to Individuals 8 through 15, all demanding that the price of Navarre stock be increased.

10. It is then alleged that on January 26, 2007, two parcels were mailed to individuals 16 and 17, which contained "an improvised explosive weapon, also known as a pipe bomb," with one wire left intentionally unattached, and a letter demanding that the price of Navarre stock be increased.

11. In paragraph 17, it is alleged that the defendant purchased Navarre common stock and call option contracts in Navarre stock.

12. Finally, in paragraph 18, it is alleged that the defendant executed that charged scheme by sending eight specified letters and two specified parcels, each of which forms the basis of Counts One through Ten of the indictment.

### **Legal Standard**

13. The statute, 15 U.S.C. §78j(b) states that:

It shall be unlawful for any person...by the use of any means or instrumentality of interstate commerce or of the mails...--

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange...any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission [the Securities and Exchange Commission or " SEC"] may prescribe...

14. The indictment proceeds to allege that the SEC rule that defendant violated

is Rule 10b-5 (17 C.F.R. 240.10b-5), which states, in pertinent part,

It shall be unlawful for any person..., by use of any means or instrumentalities of interstate commerce, or of the mails...

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Defendant Tomkins is charged under subsections (a) and (c) of Rule 10b-5.

15. One court has helpfully summarized the conduct prohibited by Rule 10b-5 as follows:

By its terms, Section 10(b) prohibits using any manipulative or deceptive device in connection with the purchase or sale of any security....The forbidden act may take the form of a fraudulent scheme, a false statement of material fact or material omission, or a fraudulent act or practice....The allowable unit of prosecution under section 78j(b) is...the use of a manipulative device or contrivance.

*United States v. Rigas*, 281 F.Supp.2d 660, 666-667 (S.D.N.Y. 2003).

### **Argument**

16. The problem with Count One through Ten in this case is that, fundamentally, the government has charged a case of mailing threatening communications, not

securities fraud. The same threats are directly charged in Counts Eleven and Twelve. Defendant Tomkins did not mislead any stock market investors, which is the essential requirement in a securities fraud.

17. The Supreme Court has interpreted the core concept of the use of a manipulative or deceptive device or contrivance as follows: "'Manipulation' is 'virtually a term of art when used in connection with the securities markets. It connotes intentional or wilful conduct designed to deceive or defraud investors...'" *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 at 199, 96 S.Ct. at 1384 (1976). "The term refers generally to practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity....Section 10(b)'s general prohibition of practices deemed by the SEC to be 'manipulative' in this technical sense of artificially affecting market activity *in order to mislead investors* is fully consistent with the fundamental purpose of the 1934 Act..." *Santa Fe Industries v. Green*, 430 U.S. 462, 476-477, 97 S.Ct. 1292, 1302-1303 ((1977)(emphasis added). The Supreme Court has further required "manipulative" in the Rule 10(b) context "to require misrepresentation...All three species of misconduct, *i.e.*, 'fraudulent, deceptive or manipulative,' listed by Congress are directed at failures to disclose. The use of the term 'manipulative' provides emphasis and guidance to those who must determine which types of acts are reached by the statute;" *Schreiber v. Burlington Northern, Inc.*, 472 U.S. 1, 7-8 (1985). The Supreme Court has also stated that section 10b "must not be

construed so broadly as to convert every common law fraud that happens to involve securities into a violation of §10b." *SEC v. Zanford*, 535 U.S. 813, 820, 122 S.Ct. 1899 (2002). As one district court has concluded, "This term of art cannot be extended to cover every form of unfair dealing which appears to the lay person to be manipulative." *Billard v. Rockwell International Corporation* 526 F.Supp. 218, 222. (S.D.N.Y. 1981). The Supreme Court has echoed this in stating, "We cannot amend the statute to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute." *Central Bank of Denver, N.A. v. First Interstate Bank*, 511 U.S. 164, 177, 114 S.ct. 1439 (1994).

18. The Second Circuit has applied the Supreme Court's requirement in *Santa Fe Industries, supra*, that there must be market activity before there can be securities fraud, stating, "A market manipulation claim...cannot be based solely upon misrepresentations or omissions...There must be some market activity." *ATSI Communications, Inc. v. Shaar Fund Ltd.*, 493 F.3d 87, 101 (2<sup>nd</sup> Cir. 2007). In defendant Tomkins case, there was no market activity at prices based upon any misrepresentations.

19. The Second Circuit also recently reversed a conviction in a case brought under section 78(j)(b) and Rule 10b-5 involving an allegation of stock market fraud. In that case, a New York Stock Exchange specialist engaged in "interpositioning." This means that he received separate buy and sell orders for

a particular stock. If he had executed the buy and sell orders against each other, it would have resulted in the best financial result for the customers. Instead, he bought the buy order on his own account and sold the sell order from his own account. This resulted in more money to him, and less advantageous trades for the investors. The Second Circuit ruled that this constituted criminal conversion, but not fraud under section 78(j)(b) and Rule 10b-5. The Second Circuit stated, "The language of 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception.....Broad as the concept of deception may be, it irreducibly entails some act that gives the victim a false impression....The government has identified no way in which Finnerty communicated anything to his customers, let alone anything false. Rather, viewing the evidence in the light most favorable to the government, the government undertook to prove no more than garden variety conversion." *United States v. Finnerty*, 533 F.3d 143, 148-9 (2<sup>nd</sup> Cir. 2008)(internal quotations omitted). See also, *United States v. Hayward*, 2008 WL 2926828 (2<sup>nd</sup> Cir. July 30, 2008). In this case, mailing threatening communications has been sufficiently alleged, analogously to criminal conversion in *Finnerty*, but securities fraud has not in this case, just as it was not in *Finnerty*.

20. Moreover, in the district court In *Finnerty*, the government also argued that the defendant utilized a manipulative, as well as deceptive, device. It abandoned that argument in the Court of Appeals. *Finnerty*, 533 F.3d at 148. The district

court ruled that, "In the securities context, manipulation still requires misleading or deceiving someone...The government essentially argues that because Finnerty interpositioned, he therefore manipulated the prices of the stock so that the principal account could earn an unlawful profit.....This argument is rejected....The fact that Finnerty may have 'manipulated' prices says nothing about whether interpositioning misled or deceived customers." *United States v. Finnerty*, 474 F.Supp.2d 530, 542-543 (S.D.N.Y. 2007). Similarly in this case, there is no evidence of defendant Tomkins misleading stock market investors.

21. Thus, in order to violate the securities fraud statute, defendant Tomkins must have employed a manipulative device or contrivance to defraud investors with respect to the stock of Navarre and 3COM; in the course doing so, there must have been: (1) misrepresentations and (2) intent on the part of defendant Tomkins to mislead the investors; and there must have been market activity based upon the misrepresentations.

22. What defendant Tomkins is alleged to have actually done is to have made threats to officers of various investment companies, seeking to cause them to purchase additional shares of Navarre and 3COM common stock at market prices. This did not involve misrepresentations. As for the common stock and stock options that are alleged to have been acquired by defendant Tomkins himself, they are alleged to have been purchased at legitimate market prices and, to the extent they were sold or exercised, they were sold or exercised at legitimate market

prices.

23. The course of conduct alleged in the indictment does not constitute a scheme by defendant Tomkins to defraud investors. Rather, it alleges threats by defendant Tomkins aimed at investment company executives. The executives themselves did not take any action or have any intent to defraud investors. They did not scheme with defendant Tomkins in any way. Since no misleading statements were made by anyone and no investors were, in fact, deceived or defrauded, the requisites of a securities fraud charge have not been met.

24. The Rule of Lenity also supports this motion. "(T)he scope of a criminal statute, unless it is clear and unambiguous...is to be strictly and not expansively construed." *United States v. Spruill*, 292 F.3d 207, 220 (7th Cir. 2002). In this case the government is seeking to do exactly that, namely to expansively interpret 15 U.S.C. §78j and Rule 10b-5. The Seventh Circuit has also stated, "In interpreting the reach of a criminal statute, the purpose of this court's review is to determine the intent of Congress as reflected in the language, structure, and legislative history of the statute..If these manifestations of Congressional intent are ambiguous, leaving us unable to define the ambit of the criminal statute, the Rule of Lenity requires that we strictly construe the statute in favor of the defendant." *United States v. Lowe*, 860 F.2d 1370, 1376 (7<sup>th</sup> Cir. 1988). Accord, *United States v. Santos*, \_\_ U.S. \_\_, 128 S.Ct. 2020, 2025 (2008). As quoted above in *SEC v. Zanford*, the Supreme Court has explicitly warned against the type of

broad interpretation of the statute sought by the government in this case.

25. It should also be recognized that under Rule 10(b)-5, civil private actions, as well as criminal prosecutions, may be brought. Thus, expansion of the basis of criminal liability under the rule also expands the grounds for shareholder derivative suits. See, *e.g.*, *Securities Class Actions on the Upswing: Report*, Chicago Daily Law Bulletin, Aug. 1, 2008, p.1. This is one reason that the courts have constrained the limits of liability under Rule 10(b)-5. If mere threats sufficed to state a cause of action, without misrepresentations to investors actually being made or market activity actually occurring, then it could be expected that private securities actions would proliferate based upon, *inter alia*, threats made by or to investment company officials and corporate officers (as are alleged in this case). They could include, for example, threats to publicly disclose either accurate (but non-public) or inaccurate information about a public corporation, if certain demands were not met. Such threats would be intended to induce a fear that the corporation's stock price would be adversely affected if they were carried out. It is hard to imagine the appellate courts opening the Pandora's box of such an expanded basis for Rule 10(b)-5 liability.

26. Defendant Tomkins is not asserting that the facts alleged by the government, if proven, do not constitute a crime. But they do not constitute the highly technical offense of securities fraud. Thus, the indictment does not allege an offense under 15 U.S.C. §78j(b) and Rule 10(b)-5 in Counts One through Ten.

WHEREFORE, defendant Tomkins respectfully moves this Court to dismiss Counts One through Ten of the indictment.

Respectfully submitted,

S/ John M. Beal  
Attorney for Defendant

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#### **CERTIFICATE OF SERVICE**

I, John M. Beal, attorney, certify that I caused a copy of **DEFENDANT TOMKIN'S MOTION TO DISMISS** to be served on January 6, 2009, in accordance with Fed.R.Crim.P. 49, Fed.R.Civ.P. 5, LR 5.5, and the General Order on Electronic Case Filing (ECF) pursuant to the district court's system as to ECF filers.

Executed on January 6, 2009

S/ John M. Beal  
John M. Beal