APPENDIX

TABLE OF APPENDICES

Appendix A

FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 15-55506
D.C. No. 8:11-cv-01962-JVS-AN

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

v.

MITCHELL J. STEIN.

Defendant-Appellant.

Appeal from the United States District Court for the
Central District of California
James V. Selna, District Judge, Presiding

OPINION

Filed: Oct. 11, 2018

Argued and Submitted March 13, 2018

Before: J. Clifford Wallace, Marsha S. Berzon,
and Consuelo M. Callahan, Circuit Judges.

WALLACE, Circuit Judge:

Mitchell Stein, an attorney, appeals from the district court's summary judgment in favor of the Securities and Exchange Commission (SEC) on the SEC's claims that Stein violated various federal securities laws. The district court entered summary judgment on six of the SEC's claims on the ground that Stein's prior criminal conviction precluded him from contesting the allegations at issue in the civil case. We have jurisdiction under 28 U.S.C. § 1291, and we affirm.

I.

In December 2011, the SEC brought a civil enforcement action against Stein alleging that Stein, while acting as purported outside counsel to co-defendant Heart Tronics, engaged in a series of frauds designed to inflate the company's stock price so that he could profit from selling its securities to investors. The alleged scheme was wide ranging, but centered on allegations that Stein concocted three false purchase orders with fictitious companies, and used these orders as the basis for SEC filings and press releases touting bogus sales of Heart Tronics' "Fidelity 100" heart-monitoring system.

The purchase orders at issue ostensibly were agreed to during September and October 2007. The first purchase order reflected a sale of 180 units of the Fidelity 100 for $1.98 million. The SEC alleges that an individual later identified as Thomas Tribou signed the purchase order and sent Heart Tronics $50,000 as a deposit. However, the copy of the order that was counter-signed by the then-CEO of Heart Tronics and returned to Tribou identified the customer as "Cardiac Hospital Management" (CHM). The SEC maintained

that CHM was a fictitious entity not known to Tribou. The second and third purchase orders reflected sales to a fictional Israeli company called "IT Healthcare" for $3.3 million and $564,000, respectively.

Stein went to great lengths to make the purchase orders appear legitimate. Specifically, the SEC alleges that Stein and his personal assistant, co-defendant Martin Carter, created letters and documents purportedly originating from CHM and IT Healthcare to create the appearance of communication between Heart Tronics and its "customers." One such letter was from a purported CHM purchasing agent named "Toni Nonoy" asking for products to be sent to a "new address" in Japan. Other documents were from fictitious people supposedly affiliated with IT Healthcare confirming sales orders and providing updated shipping instructions. The SEC alleges that all these documents were fraudulent and that Stein simply made up the names.

During the same period in which Stein drew up the alleged fraudulent purchase orders, he also orchestrated the dissemination of press releases reporting the sales. The SEC alleges that based on information provided by Stein, John Woodbury, Heart Tronics' securities lawyer, published three press releases touting the more than $5 million in purported sales to CHM and IT Healthcare. The SEC also alleged that Stein caused the fraudulent sales orders to be incorporated into Heart Tronics' SEC filings from approximately September 2007 through August 2008.

Based on these and other allegations, the SEC asserted various claims against Stein, including

securities fraud in violation of Section 10(b) of the Securities Exchange Act (Exchange Act), Exchange Act Rule 10b-5, and Section 17(a) of the Securities Act; aiding and abetting violations of Section 10(b) and Rule 10b-5; selling or offering for sale unregistered securities in violation of Section 5(a) and 5(c) of the Securities Act; falsifying books and records in violation of Exchange Act Rule 13b2-1; knowingly falsifying books and records in violation of Section 13(b)(5) of the Exchange Act; and aiding and abetting Heart Tronics' violations of the reporting, record-keeping, and internal controls provisions of the Exchange Act (Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B)) and Exchange Act Rules (Rules 13a-1, 13a-11, 13a-13, and 12b-20).

Concurrent with the SEC's case against Stein, the Department of Justice (DOJ) filed a criminal case against him in the Southern District of Florida arising out of the same fraudulent conduct alleged in the civil case. The fourteen-count indictment charged Stein with three counts of securities fraud (18 U.S.C. § 1348), three counts of wire fraud (18 U.S.C. § 1343), three counts of mail fraud (18 U.S.C. § 1341), one count of conspiracy to commit mail and wire fraud (18 U.S.C. § 1349), three counts of money laundering (18 U.S.C. § 1957), and one count of conspiracy to obstruct justice (18 U.S.C. § 371). The DOJ eventually moved to intervene and stay discovery in the SEC action pending the outcome of the criminal proceeding. The district court granted the unopposed motion and stayed the civil case in April 2012.

The DOJ's case against Stein tracked the main allegations asserted in the SEC's complaint. During a

twoweek trial, the DOJ presented evidence that Stein created three fraudulent purchase orders for CHM and IT Healthcare; that he orchestrated the publication of press releases touting the fraudulent purchase orders; that he made up documents purported to be from employees of CHM and IT Healthcare to create the impression the purchase orders were legitimate; and that he caused the false information to be incorporated into Heart Tronics' SEC filings. During closing arguments, the prosecution focused the jury's attention on the "false purchase orders," "false press releases," and "false SEC filings" that underpinned Stein's scheme. At the end of trial, the jury returned guilty verdict against Stein on all counts. The district court sentenced Stein to 17 years' imprisonment, and ordered him to forfeit over $5 million and pay over $13 million in restitution.

Stein appealed from his judgment of conviction and sentence, arguing, among other things, that the DOJ failed to produce material, exculpatory evidence in violation of *Brady v. Maryland*, 373 U.S. 83 (1963), and that the DOJ knowingly relied on false testimony in violation of *Giglio v. United States*, 405 U.S. 150 (1972). The Eleventh Circuit rejected the *Brady* and *Giglio* claims, affirmed Stein's conviction, but vacated and remanded Stein's sentence for a recalculation of actual losses attributable to his fraud. *See United States v. Stein*, 846 F.3d 1135 (11th Cir. 2017).

Following Stein's conviction, the SEC moved for summary judgment, arguing that Stein's conviction precluded him from contesting the SEC's allegations in the civil proceeding. The district court concluded that Stein's criminal conviction "necessarily decided"

the facts needed to establish his liability in the civil case, and entered summary judgment in favor of the SEC on the following claims: securities fraud in violation of Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and Section 17(a) of the Securities Act; aiding and abetting violations of Section 10(b) and Rule 10b-5; falsifying books and records in violation of Exchange Act Rule 13b2-1; knowingly falsifying books and records in violation of Section 13(b)(5) of the Exchange Act; and aiding and abetting Heart Tronics' violations of the reporting and internal controls requirements of the Exchange Act and Exchange Act Rules. This appeal followed.

II.

We review a district court's summary judgment de novo. *Branch Banking & Trust Co. v. D.M.S.I., LLC*, 871 F.3d 751, 759 (9th Cir. 2017). We also review de novo whether issue preclusion is available. *Dias v. Elique*, 436 F.3d 1125, 1128 (9th Cir. 2006). If issue preclusion is available, the district court's decision to apply the doctrine is reviewed for abuse of discretion. *Id*.

III.

Issue preclusion bars parties from relitigating an issue if the same issue was adjudicated in prior litigation. *Resolution Tr. Corp. v. Keating*, 186 F.3d 1110, 1114 (9th Cir. 1999). The form of the doctrine at issue here is "offensive nonmutual issue preclusion," which prevents "a defendant from relitigating the issues which a defendant previously litigated and lost against another plaintiff." *Syverson v. IBM Corp.*, 472 F.3d 1072, 1078 (9th Cir. 2007) (quoting *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 329 (1979)). A party

invoking a defendant's prior criminal conviction as the basis for offensive preclusion must demonstrate: (1) the prior conviction was for a serious offense; (2) the issue at stake in the civil proceeding is identical to the issue raised in the prior criminal proceeding; (3) there was a full and fair opportunity to litigate the issue at the prior trial; and (4) the issue on which the prior conviction is offered was actually litigated and necessarily decided at trial. *Ayers v. City of Richmond*, 895 F.2d 1267, 1271 (9th Cir. 1990); *see also Syverson*, 472 F.3d at 1078.

We typically look to four factors (sometimes referred to as the Restatement factors) to determine whether two issues are "identical" for purposes of issue preclusion:

> (1) Is there a substantial overlap between the evidence or argument to be advanced in the second proceeding and that advanced in the first?
>
> (2) Does the new evidence or argument involve the application of the same rule of law as that involved in the prior proceeding?
>
> (3) Could pretrial preparation and discovery related to the matter presented in the first action reasonably be expected to have embraced the matter sought to be presented in the second?
>
> (4) How closely related are the claims involved in the two proceedings?

Howard v. City of Coos Bay, 871 F.3d 1032, 1041 (9th Cir. 2017); *see* Restatement (Second) of Judgments § 27 cmt. C (Am. Law Inst. 1982). These factors "are not applied mechanistically." *Howard*, 871 F.3d at 1041; see Jack H. Friedenthal, Mary Kay Kane & Arthur R. Miller, *Civil Procedure* § 14.10 (5th ed. 2015) ("The assessment of the similarity of issues necessary to decide whether collateral estoppel should preclude relitigation of a particular issue varies with the facts of each case.").

IV.

We begin our analysis by comparing the record in the DOJ's criminal case with the allegations in the SEC's enforcement action, to determine whether the issues actually litigated and determined in the criminal proceeding are identical to those raised in the civil proceeding.[1]

As outlined above, the DOJ's criminal case against Stein focused on his scheme to inflate Heart Tronics' stock price by creating false purchase orders, and using those purchase orders as the basis for false press releases and SEC filings. The evidence presented at the criminal trial was that Stein drafted one purchase order attributed to CHM for $1.98

[1] Stein's argument that issue preclusion is inapplicable due to a lack of identity of issues is apparently limited to the SEC's claims for violations of Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and Section 17(a) of the Securities Act. We therefore do not consider the identity of issues between Stein's criminal proceeding and the SEC's other claims. *Brownfield v. City of Yakima*, 612 F.3d 1140, 1149 n.4 (9th Cir. 2010) ("We review only issues which are argued specifically and distinctly in a party's opening brief") (quoting *Greenwood v. FAA*, 28 F.3d 971, 977 (9th Cir. 1994)).

million, two false purchase orders attributed to IT Healthcare for $3.3 million, and three false press releases; and then he profited from selling Heart Tronics' securities to investors while materially false information was in the market. In light of this evidence, the jury found Stein guilty of (among other offenses) three counts of securities fraud in violation of 18 U.S.C. § 1348, which means it found the following facts proved beyond a reasonable doubt, as instructed by the trial judge: (1) Stein "knowingly executed or attempted to execute a scheme or artifice to defraud;" (2) Stein "did so with intent to defraud;" and (3) "[t]he scheme to defraud was in connection with any security of Heart Tronics, Inc." *See Emich Motors Corp. v. Gen. Motors Corp.*, 340 U.S. 558, 569 (1951) (explaining that trial courts assessing the preclusive effect of a prior criminal conviction based on a general verdict determine which issues were necessarily decided by examining the pleadings, evidence submitted, jury instructions, and other parts of the record).

The same fraudulent scheme that underpinned Stein's criminal conviction served as the basis for the SEC's claims that Stein violated Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and Section 17(a) of the Securities Act. "Section 17(a) of the Securities Act, and the SEC's other claims. *Brownfield v. City of Yakima*, 612 F.3d 1140, 1149 n.4 (9th Cir. 2010) ("We review only issues which are argued specifically and distinctly in a party's opening brief") (quoting *Greenwood v. FAA*, 28 F.3d 971, 977 (9th Cir. 1994)). Section 10(b) of the Exchange Act and Rule 10b-5, prohibit fraudulent conduct or practices in connection with the offer or sale of securities." *SEC v.*

Dain Rauscher, Inc., 254 F.3d 852, 855 (9th Cir. 2001). These antifraud provisions prohibit schemes to defraud, and they prohibit "making a material misstatement or omission in connection with the offer or sale of a security by means of interstate commerce." *Id.* at 855–56. Securities fraud in violation of Section 17(a)(1), Section 10(b), and Rule 10b-5 require a showing of scienter, while violations of Sections 17(a)(2) and (3) require a showing of negligence. *Id.* at 856.

Having considered the records in the criminal and civil proceedings in light of the relevant Restatement factors, we conclude that Stein's conviction determined the identical issues the SEC was required to prove to establish Stein's liability for securities fraud. First, both the criminal and civil case involve the same fraudulent scheme carried out by Stein: an effort to inflate Heart Tronics' stock price by using false purchase orders and false press releases to profit from the sale of the company's securities. A review of the civil complaint, the criminal indictment, and the trial transcript indicates there is a "substantial overlap" between the evidence and argument to be advanced in the SEC's enforcement action and that advanced by the DOJ at trial, and that the claims involved are "closely related." Restatement (Second) of Judgments § 27 cmt. c; *see Howard*, 871 F.3d at 1041. Therefore, these factors support the conclusion that the issues previously decided in the criminal trial are identical to those at issue in the civil case.

Second, the SEC's securities fraud claims involve "the application of the same rule of law" as

that involved in the criminal case. Restatement (Second) of Judgments § 27 cmt. c. Stein's conviction required the jury to find (1) a scheme or artifice to defraud, (2) with fraudulent intent, (3) in connection with any security. *See* 18 U.S.C. § 1348. These findings encompass the SEC's claims, which require proof of the same elements except that Section 17(a) prohibits fraud "in the offer or sale of any securities," which was what was at stake in the criminal trial, and Sections 17(a)(2) and (3) do not require scienter. Therefore, the DOJ proved beyond a reasonable doubt the same issues the SEC needed to prove only by a preponderance of the evidence. There is no difference in the applicable legal standards that would affect the outcome of the civil case.

Finally, pretrial preparation and discovery related to the criminal proceeding could "reasonably be expected" to have embraced the issues sought to be presented in the SEC's civil case. Restatement (Second) of Judgments § 27 cmt. c. The DOJ's prosecution of Stein involved the same fraudulent scheme—including the same false purchase orders, fictitious companies, made-up names, and false press releases—at issue in the civil action. Given the nearly complete overlap of facts, there is no issue of significance presented by the SEC's action that could be expected to fall outside pretrial preparation and discovery related to the criminal proceeding.

In sum, the issues the SEC seeks to preclude Stein from litigating in the civil action are identical to the issues litigated and decided in the DOJ's criminal case. Accordingly, the district court did not err in

entering summary judgment based on the preclusive effect of Stein's conviction.

V.

Stein disagrees, and we turn now to his arguments. Stein first contends that the precise issue as to why the $1.98 million CHM purchase order was fraudulent at issue in this action was not actually litigated and decided in his criminal case. Stein argues that the DOJ's position in the criminal case was that the CHM purchase order was "all made up" and "never happened," while the SEC's position in this case is that Tribou signed the CHM order. Stein contends that because the SEC alleges that Tribou signed the CHM order, the SEC in effect admits that the order was not fraudulent.

This argument fails. The DOJ's position regarding the fraudulent CHM purchase order is, in fact, consistent with the SEC's allegations. In the criminal case, the DOJ argued before the jury that the CHM purchase order was "made up" on the grounds that CHM was a fictitious company with no connection to Tribou, and that Stein arranged for Carter to send fabricated documents from Japan to create the impression the CHM sales order was real. Likewise, the SEC alleged that although Tribou contracted to purchase a certain number of units from Heart Tronics in his personal capacity, the purchase order counter-signed by Heart Tronics and returned to Tribou identified the customer as CHM, "a fictitious entity that was not known to [Tribou]." The SEC further alleged that Stein "orchestrated an elaborate scheme"—having a fabricated letter sent from Japan—to create the illusion that the CHM order was

viable. Therefore, in both the criminal and civil proceedings the underlying theory was that the CHM purchase order was fraudulent because CHM was not a real company and was not connected to Tribou. Accordingly, the issue of whether the CHM purchase order was fraudulent was actually litigated and decided at Stein's criminal trial.

Stein next argues the district court abused its discretion in applying issue preclusion because its application was "unfair" under *Parklane Hosiery*. In Parklane Hosiery, the Supreme Court explained that although trial courts have "broad discretion" to determine whether to apply offensive issue preclusion, the doctrine should not be applied when doing so "would be unfair to a defendant." 439 U.S. at 331. Stein contends that because this circuit would have resolved his *Giglio* claim differently than the Eleventh Circuit did, issue preclusion was unfair under the circumstances.

Under *Giglio v. United States*, 405 U.S. 150 (1972), a conviction must be set aside if the prosecution knowingly uses false testimony, or fails to correct false testimony, and that testimony was "material." *See Jackson v. Brown*, 513 F.3d 1057, 1071–72 (9th Cir. 2008); *Hayes v. Brown*, 399 F.3d 972, 984 (9th Cir. 2005). False testimony is "material" if "there is any reasonable likelihood that [it] could have affected the judgment of the jury." *Dow v. Virga*, 729 F.3d 1041, 1048 (9th Cir. 2013) (emphasis omitted) (quoting *United States v. Agurs*, 427 U.S. 97, 103 (1976)).

After his conviction, Stein argued on appeal that the DOJ violated *Giglio*, partly because it

knowingly relied on false testimony by Tracey Jones (the assistant to the then-Heart Tronics CEO) and Woodbury. The Eleventh Circuit rejected this argument, concluding that because Stein was at the time of the testimony in possession of the evidence needed to demonstrate the alleged falsity of the testimony, there could be no *Giglio* violation. Stein, 846 F.3d at 1150. Stein argues that the Eleventh Circuit's resolution of his *Giglio* claim is at odds with this circuit's rule that "the government's duty to correct perjury by its witnesses is not discharged merely because defense counsel knows, and the jury may figure out, that the testimony is false." *United States v. LaPage*, 231 F.3d 488, 492 (9th Cir. 2000). On the basis of this purported split in circuit court authority, Stein contends that our court would have concluded that the DOJ's failure to correct the testimony at issue entitled him to a new trial.

Assuming Stein is correct that the Eleventh Circuit treats *Giglio* claims differently than we do—which we need not determine—the supposed circuit split does not help him here. This is because the testimony Stein alleges was false is not "material," a concept defined consistently across circuits. *Compare Reis-Campos v. Biter*, 832 F.3d 968, 976 (9th Cir. 2016), *with Guzman v. Sec'y, Dep't of Corr.*, 663 F.3d 1336, 1348 (11th Cir. 2011). Stein contends that because Jones and Woodbury received an October 24, 2007 email with a copy of a $50,000 check from Tribou attached, Jones testified falsely when she stated that she "never received any backup" on the purchase orders, and Woodbury testified falsely when he said he "got all [his] information from . . . Stein" in preparing the SEC filings. But in light of the evidence that CHM

did not exist, that there was no connection between CHM and Tribou, and that Stein engaged in an extensive effort to fabricate supporting documentation for the CHM purchase order, there is no "reasonable likelihood" that Jones and Woodbury's allegedly false testimony "could have affected the judgment of the jury." *Dow*, 729 F.3d at 1048. The case against Stein was overwhelming, and the prosecution's correction of the allegedly false testimony would not have cast meaningful doubt on Stein's guilt.

Stein also argues the district court's application of issue preclusion was "unfair" because the SEC action affords him "procedural opportunities unavailable in the first action that could readily cause a different result." *Parklane Hosiery*, 439 U.S. at 331. Specifically, Stein contends that the SEC action presents him with his "first opportunity" to review nearly 200 million documents contained in an SEC database. Stein asserts that reviewing these documents will allow him to determine whether DOJ prosecutors spoke to an individual named "Yossi Keret," who was listed in a public SEC filing as CFO of an Israeli company, before telling the jury that Yossi Keret was a fabricated name.

Stein's argument is baseless. The record indicates that Stein did, in fact, have access to the 200 million-document database during his criminal trial. At a pre-trial hearing before the district judge on April 3, 2013, Stein indicated he was working his way through the documents to determine which documents might be relevant for him to use at trial. Transcript of Hearing Proceeding at 38, *United States v. Stein*, No. 11-cr-80205-KAM, ECF No. 146 (Stein stating to trial

judge: "That database, which I've given the Court the address to, is – has 200 million documents. Obviously, all of those documents are not relevant. . . . However, some of the documents as I go through them are relevant."); *see also id*. at 43–44. Therefore, the SEC action does not mark Stein's "first opportunity" to review the database in question; Stein, in fact, was reviewing the database in preparation for his criminal trial.

Moreover, even if Stein did not have access to the database until after his trial, reviewing the database was not an opportunity "that could readily cause a different result." *Parklane Hosiery*, 439 U.S. at 331. The individual that prosecutors argued did not exist was "Yossie" (with an "e") Keret, not "Yossi" Keret. "Yossie" Keret, argued the DOJ, was affiliated with a phony company called "IT Healthcare," while "Yossi" Keret was in 2004 apparently the CFO of a real company called Pluristem Life Systems, Inc. Therefore, confirmation that the SEC did, or did not, talk to "Yossi Keret" of Pluristem Life Systems would not likely undermine the DOJ's argument that "Yossie Keret" of "IT Healthcare" was fabricated to make fraudulent purchase orders appear legitimate.

The district court's application of issue preclusion was not unfair.

VI.

We turn now to Stein's claim that the district court erred in denying his request to continue the summary judgment motion to allow for additional discovery pursuant to Federal Rule of Civil Procedure 56(d). "A district court's refusal to continue a hearing on summary judgment pending further discovery is

reviewed for an abuse of discretion." *Swoger v. Rare Coin Wholesalers*, 803 F.3d 1045, 1047 (9th Cir. 2015).

A party requesting a continuance pursuant to Rule 56(d) must identify by affidavit "the specific facts that further discovery would reveal, and explain why those facts would preclude summary judgment." *Tatum v. City & County of San Francisco*, 441 F.3d 1090, 1100 (9th Cir. 2006). The facts sought must be "essential" to the party's opposition to summary judgment, Fed. R. Civ. P. 56(d), and it must be "likely" that those facts will be discovered during further discovery, *Margolis v. Ryan*, 140 F.3d 850, 854 (9th Cir. 1998).

In his declaration in opposition to the SEC's motion for summary judgment, Stein stated that additional discovery would allow him to confirm or deny the existence of Yossi Keret and other allegedly made up individuals. Stein asserted that if he could find Keret, and others, he could ask them questions about their involvement in the fraudulent purchase orders.

Stein did not satisfy Rule 56(d). For one thing, he failed to identify with specificity facts "likely to be discovered" that would justify additional discovery. *Margolis*, 140 F.3d at 854. Rather, the evidence Stein sought was "the object of mere speculation," which is insufficient to satisfy the rule. *Ohno v. Yasuma*, 723 F.3d 984, 1013 n.29 (9th Cir. 2013); *see also Margolis*, 140 F.3d at 854 (affirming district court's denial of Rule 56(d) motion where assertions regarding the evidence that would result from additional discovery were "based on nothing more than wild speculation"). Furthermore, Stein did not explain how additional

facts would preclude summary judgment. Stein stated in his declaration that he "cannot possibly oppose the Motion for Summary Judgment in an effective manner without complete and truthful answers to all outstanding discovery." But this conclusory assertion is not enough. Stein did not, for example, point out how particular evidence not yet discovered was "essential" to his argument that issue preclusion was inapplicable or unfair. Accordingly, the district court did not abuse its discretion in denying Stein's request for a continuance pending further discovery.

VII.

Finally, Stein contends the district court erred in denying his motion for summary adjudication with respect to Paragraph 77 of the SEC's complaint. Paragraph 77 alleges in relevant part: "Stein falsely told Rauch [a stock promoter] that Heart Tronics would imminently announce up to $100 million in sales and that the Company's stock price was artificially depressed by naked short sellers." Stein argues he was entitled to summary adjudication on this allegation because he presented evidence that the SEC confirmed naked short selling of Heart Tronics stock, which means he could not have lied about the short selling.

The district court did not err. First, Stein's "evidence" that the SEC confirmed naked short selling of Heart Tronics stock was a broken link to an SEC web page. Like the district court, we could not access the link, nor otherwise confirm its contents. Absent any evidence negating the SEC's allegation, or a demonstration by Stein that the SEC lacks sufficient evidence to carry its burden, Stein has not

demonstrated the absence of a genuine dispute of material fact. *Nissan Fire & Marine Ins. Co., Ltd. v. Fritz Cos., Inc.*, 210 F.3d 1099, 1102 (9th Cir. 2000). Therefore, the district court did not err in denying Stein's motion for summary adjudication on this allegation. *Id.* at 1102–03 ("If a moving party fails to carry its initial burden of production, the nonmoving party has no obligation to produce anything, even if the nonmoving party would have the ultimate burden of persuasion at trial.").

Second, even if Stein produced evidence of naked short selling of Heart Tronics stock, such evidence would not demonstrate the absence of a genuine dispute as to the truth of the SEC's allegation in Paragraph 77. This is because the falsity of the statement alleged by the SEC stemmed from both Stein's assertions of naked short selling and his representation that Heart Tronics "would imminently announce up to $100 million in sales." A reasonable jury presented with evidence of naked short selling of Heart Tronics stock could still decide that Stein's statement was materially false based on Stein's false assertion that Heart Tronics' would imminently announce up to $100 million in sales. Accordingly, the district court did not err in denying Stein's motion for summary adjudication. *See S. Cal. Darts Ass'n v. Zaffina*, 762 F.3d 921, 925 (9th Cir. 2014) ("A dispute is 'genuine' if 'a reasonable jury could return a verdict for the nonmoving party.'" (quoting *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986))).

VIII.

Stein's criminal conviction conclusively established all of the facts the SEC was required to

prove with respect to the specified securities fraud claims. Accordingly, we **AFFIRM** the district court's summary judgment. All pending motions are denied as moot.

Appendix B

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 15-55506
D.C. No. 8:11-cv-01962-JVS-AN
Central District of California, Santa Ana

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

v.

MITCHELL J. STEIN.

Defendant-Appellant.

(Filed: Feb. 21, 2019)

ORDER

Before: WALLACE, BERZON, and CALLAHAN, Circuit Judges.

Stein's petition for panel rehearing is **DENIED**. The full court has been advised of the petition for rehearing en banc and no judge of the court has requested a vote on en banc rehearing. Stein's petition for rehearing en banc is therefore **DENIED**.

Appendix C

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 15-55506
D.C. No. 8:11-cv-01962-JVS-AN
Central District of California, Santa Ana

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

v.

MITCHELL J. STEIN.

Defendant-Appellant.

Filed: Jan. 4, 2019

ORDER

Before: WALLACE, BERZON, and CALLAHAN, Circuit Judges.

Plaintiff-Appellee is directed to file a response to Defendant-Appellant's petition for panel rehearing or rehearing en banc. The response shall be filed within 21 days from the filing of this order and shall comply with Federal Rule of Appellate Procedure 32 and Ninth Circuit Rule 40-1.

Appendix D

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

Case No. SACV11-1962-JVS(ANx)

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

HEART TRONICS, INC., MITCHELL JAY STEIN, WILLIE JAMES GAULT, J. ROWLAND PERKINS, II, MARTIN BERT CARTER, MARK CROSBY NEVDAHL, and RYAN ALLAN RAUCH,

Defendants,

TRACEY HAMPTON-STEIN, ARC FINANCE GROUP, LLC, ARC BLIND TRUST, THS BLIND TRUST, JAYMI BLIND TRUST, OAK TREE INVESTMENTS BLIND TRUST, WBT INVESTMENTS BLIND TRUST, CATCH 83 GENERAL PARTNERSHIP, and FIVE INVESTMENTS PARTNERSHIP,

Relief Defendants.

(Filed: Mar. 3, 2015)

FINAL JUDGMENT AGAINST DEFENDANT STEIN IMPOSING PERMANENT INJUNCTIONS, PERMANENT OFFICER AND DIRECTOR BAR, PERMANENT PENNY STOCK BAR, DISGORGEMENT WITH PREJUDGMENT INTEREST, AND A CIVIL PENALTY

Consistent with the Court's Order Granting in Part and Denying in Part of Plaintiff's Motion for Summary Judgment Against Defendant Mitchell J. Stein as to Claims One, Two, Three, Five, Seven, Eight and Nine (Docket No. 255) pursuant to Fed. R. Civ. P. 56, and the Plaintiff's request for leave to voluntarily dismiss with prejudice all other claims of the Complaint against this Defendant:

I.

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that Defendant Stein and Defendant's agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Judgment by personal service or otherwise are permanently restrained and enjoined from violating, directly or indirectly, Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") [15 U.S.C. § 78j(b)] and Rule 10b-5 promulgated thereunder [17 C.F.R. § 240.10b-5], by using any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, in connection with the purchase or sale of any security:

(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 the 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.

II.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant Stein and Defendant's agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Judgment by personal service or otherwise are permanently restrained and enjoined from violating, directly or indirectly, Section 17(a) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. § 77q(a)] in the offer or sale of any security by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails:

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

(b) to obtain money or property by means of any untrue statement of a material fact or any omission of 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 transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

III.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED THAT Defendant Stein and Defendant's agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Judgment by personal service or otherwise are permanently restrained and enjoined from violating, directly or indirectly, Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] by knowingly circumventing or failing to implement a system of internal accounting controls or knowingly falsifying any book, record, or account described in Section 13(b)(2) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)].

IV.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant Stein and Defendants' agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Judgment by personal service or otherwise are permanently restrained and enjoined from violating, directly or indirectly, Rule 13b2-1 of the Exchange Act [17 C.F.R. § 240.13b2-1] by falsifying, or causing to be falsified, any book, record, or account described in Section 13(b)(2)(A) of the Exchange Act [15 U.S.C § 78m(b)(2)(A)].

V.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant Stein and Defendant's agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of this Judgment by personal service or otherwise are permanently restrained and enjoined from aiding and abetting any violation of Sections 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1and 13a-13 of the Exchange Act [17 C.F.R. §§ 240.12b-20, 240.13a-1and 240.13a-13], including by knowingly providing substantial assistance to an issuer who files or causes to be filed with the Commission any periodic or current report pursuant to Section 13(a) and the rules and regulations promulgated thereunder, which contains any untrue statement of a material fact, or which omits to state a material fact necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, or which fails to comply in any material respect with the requirements of Section 13(a) of the Exchange Act and the rules and regulations thereunder.

VI.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Defendant Stein and Defendant's agents, servants, employees and attorneys-infact, and all persons in active concert or participation with any of them, who receive actual notice of this Final Judgment, by personal service or otherwise, and each of them, are permanently enjoined and restrained from aiding and abetting any

violation of Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)], by knowingly providing substantial assistance to any issuer which has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l], or Section 15(d) of the Exchange Act [15 U.S.C. § 78o], in failing to make or keep books, records or accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer.

VII.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Defendant Stein and Defendant's agents, servants, employees and attorneys-infact, and all persons in active concert or participation with any of them, who receive actual notice of this Final Judgment, by personal service or otherwise, and each of them, are permanently enjoined and restrained from aiding and abetting any violation of Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)], by knowingly providing substantial assistance to any issuer which has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l], or Section 15(d) of the Exchange Act [15 U.S.C. § 78o], in failing to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or other applicable criteria, and to maintain accountability for assets.

VIII.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, pursuant to Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)] and Section 20(e) of the Securities Act [15 U.S.C. § 77t(e)], Defendant Stein is permanently barred from: (i) acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)]; and (ii) from participating in an offering of penny stock, including engaging in activities with a broker, dealer, or issuer for purposes of issuing, trading, or inducing or attempting to induce the purchase or sale of any penny stock. A penny stock is any equity security that has a price of less than five dollars, except as provided in Rule 3a51-1 under the Exchange Act [17 C.F.R. 240.3a51-1].

IX.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant Stein is liable for disgorgement of $5,378,581.61, representing profits gained as a result of the conduct alleged in the Complaint, together with prejudgment interest thereon in the amount of $697,833.91; and that he is further liable for a civil penalty in the amount of $5,378,581.61, pursuant to Section 20 of the Securities Act [15 U.S.C. § 77t(d)(2)] and Section 21 of the Exchange Act[15 U.S.C. § 78u(d)(3)]. Defendant shall satisfy this obligation by paying $11,454,997.13 to the Securities and Exchange Commission within 14 days after entry of this Judgment.

Defendant may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request. Payment may also be made directly from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm. Defendant may also pay by certified check, bank cashier's check, or United States postal money order payable to the Securities and Exchange Commission, which shall be delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

and shall be accompanied by a letter identifying the case title, civil action number, and name of this Court; Mitchell J. Stein as a defendant in this action; and specifying that payment is made pursuant to this Judgment.

Defendant shall simultaneously transmit photocopies of evidence of payment and case identifying information to the Commission's counsel in this action. By making this payment, Defendant relinquishes all legal and equitable right, title, and interest in such funds and no part of the funds shall be returned to Defendant. The Commission shall send the funds paid pursuant to this Judgment to the United States Treasury. Defendant shall pay post-judgment interest on any delinquent amounts pursuant to 28 USC § 1961.

X.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that this Court shall retain

jurisdiction of this matter for the purposes of enforcing the terms of this Judgment and all order and decrees which may be entered herein and to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

XI.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, there being no just reason for delay, pursuant to Rule 54(b) of the Federal Rules of Civil Procedure, the Clerk of the Court is ordered to enter this Judgment forthwith and without further notice. Any remaining claims against the Defendant are dismissed with prejudice pursuant to Rule 42(a)(2) of the Federal Rules of Civil Procedure.

Dated: March 03, 2015 [handwritten: signature]
HONORABLE JAMES V. SELNA
UNITED STATES DISTRICT JUDGE

Appendix E

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

Case No. SACV11-1962-JVS(ANx)
The Honorable James V. Selna

SECURITIES AND EXCHANGE COMMISSION,
Plaintiff,
v.
HEART TRONICS, INC., et al.,
Defendants.

(Filed: Feb. 18, 2015)

Civil Minutes

Deputy Clerk: Karla J. Tunis
Court Reporter: Not Present
Attorneys Present for Plaintiffs: Not Present
Attorneys Present for Defendants: Not Present

Proceedings: Order Granting in Part and Denying in Part Plaintiff's MOTION for Summary Judgment Against Defendant Stein as to Claims One, Two, Three, Five, Seven, Eight, and Nine [175] and Denying Defendant Stein's Motion for Summary Adjudication [221]

Plaintiff Securities and Exchange Commission ("SEC") moves for summary judgment against Defendant Mitchell J. Stein ("Stein") as to the first, second, third, fifth, seventh, eighth, and ninth claims for relief. (Docket No. 175.) Stein opposes (Docket No. 220) and the SEC has replied. (Docket No. 221.)

Stein also moves the court for summary adjudication with respect to Paragraph 77 of the SEC's Complaint. (Docket No. 186) The SEC addresses and opposes this motion in its reply to Stein's opposition to its motion for summary judgment. (Docket No. 221.)

For the following reasons, the Court GRANTS IN PART and DENIES IN PART the SEC's motion for summary judgment. Stein's motion is DENIED.

I. BACKGROUND

The facts of this case are familiar to both parties and the Court, so the Court will provide a brief overview of those facts relevant to Stein and the present motions. Stein is the purported outside counsel of co-defendant Heart Tronics, Inc. (Compl. ¶¶ 1, 17.) Between December 2005 to December 2008, Stein allegedly orchestrated a series of frauds designed to manipulate the price of Heart Tronics stock in order to profit from the sale of its securities to investors. (Id. ¶¶ 33.) In furtherance of this scheme, Stein allegedly submitted false and misleading filings to the SEC, concealed his ownership of Heart Tronics stock through the use of brokerage accounts and blind trusts over which he and false and misleading press releases in order to inflate the price of stock. (See id. ¶¶ 4, 6, 40-50, 52-62, 79-82, 85, 87, 93, 95-103.)

Based on the foregoing, the SEC filed this civil action against Stein and other defendants on December 11, 2011, asserting claims against Stein for violations of federal securities laws. (Docket No. 1).

On December 13, 2011, a federal grand jury in the Southern District of Florida returned a fourteen-count indictment charging Stein with crimes based on the same conduct alleged in the Complaint. (*See* SEC's Mot. Summ. J. 3; Eisner Decl., Ex. 1.) This Court stayed discovery in this action on April 4, 2012, pending resolution of the parallel criminal matter, United States v. Stein. (*See* Docket Nos. 36, 37.)

On May 20, 2013, the jury in the criminal matter returned a guilty verdict against Stein on all fourteen counts in the Indictment, establishing that Stein committed one count of conspiracy to commit mail fraud and wire fraud (18 U.S.C. § 1349), three counts of mail fraud (18 U.S.C. § 1341), three counts of wire fraud (18 U.S.C. § 1343), three counts of securities fraud (18 U.S.C. § 1348), three counts of money laundering (18 U.S.C. § 1957), and one count of conspiracy to obstruct justice (18 U.S.C. § 371). (SEC's Statement of Uncontroverted Facts ("SUF") 15-17.) On December 5, 2014, the court in the criminal matter entered judgment against Stein and sentenced him to seventeen years in custody. (*Id*. at 16-17.)

The SEC now moves for summary judgment in this action based on the collateral estoppel effect of Stein's criminal conviction. (SEC's Mot. Summ. J. 1.) The SEC requests permanent injunctive relief, disgorgement of ill-gotten gains, and civil penalties against Stein. (*Id*. at 2.)

II. LEGAL STANDARD

Summary judgment is appropriate where the record, read in the light most favorable to the nonmovant, indicates "that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a); *see also Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). Summary adjudication, or partial summary judgment "upon all or any part of [a] claim," is appropriate where there is no genuine dispute as to any material fact regarding that portion of the claim. Fed. R. Civ. P. 56(a); *see also Lies v. Farrell Lines, Inc.*, 641 F.2d 765, 769 n.3 (9th Cir. 1981) ("Rule 56 authorizes a summary adjudication that will often fall short of a final determination, even of a single claim . . . .") (internal quotation marks omitted).

Material facts are those necessary to the proof or defense of a claim, and are determined by referring to substantive law. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). In deciding a motion for summary judgment, "[t]he evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in his favor." *Anderson*, 477 U.S. at 255.[1]

The moving party has the initial burden of establishing the absence of a material fact for trial. *Anderson*, 477 U.S. at 256. "If a party fails to properly

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[1] "In determining any motion for summary judgment or partial summary judgment, the Court may assume that the material facts as claimed and adequately supported by the moving party are admitted to exist without controversy except to the extent that such material facts are (a) included in the 'Statement of Genuine Disputes' and (b) controverted by declaration or other written evidence filed in opposition to the motion." L.R. 56-3.

support an assertion of fact or fails to properly address another party's assertion of fact . . . , the court may . . . consider the fact undisputed." Fed. R. Civ. P. 56(e)(2). Furthermore, "Rule 56[(a)][2] mandates the entry of summary judgment . . . against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Celotex Corp.*, 477 U.S. at 322. Therefore, if the nonmovant does not make a sufficient showing to establish the elements of its claims, the Court must grant the motion.

III. DISCUSSION

A. Collateral Estoppel

Collateral estoppel is appropriate when (1) "the issue at stake is identical to an issue raised in the prior litigation;" (2) "the issue was actually litigated in the prior litigation;" and (3) "the determination of the issue in the prior litigation must have been a critical and necessary part of the judgment in the earlier action." *Littlejohn v. United States*, 321 F.3d 915, 923 (9th Cir. 2003). In the Ninth Circuit, the following criteria are used to analyze the collateral effect of a prior criminal conviction:

> (1) the prior conviction must have been for a serious offense so that the defendant was motivated to fully litigate the charges;

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[2] Rule 56 was amended in 2010. Subdivision (a), as amended, "carries forward the summary-judgment standard expressed in former subdivision (c), changing only one word — genuine 'issue' becomes genuine 'dispute.'" Fed. R. Civ. P. 56, Notes of Advisory Committee on 2010 amendments.

> (2) there must have been a full and fair trial to prevent
>
> convictions of doubtful validity from being used; (3) the issue on which the prior conviction is offered must of necessity have been decided at the criminal trial; and (4) the party against whom collateral estoppel is asserted was a party or in privity with a party to the prior trial.

Ayers v. City of Richmond, 895 F.2d 1267, 1271 (9th Cir. 1990).

Stein argues that collateral estoppel is not appropriate because "the specific issues in this case were not decided in the criminal case."[3] (Stein's First Am. Opp'n 1). While Stein correctly notes that only the identical issues necessarily decided in the criminal case may be given collateral effect, when a jury returns a general verdict a court may determine what was necessarily decided by the criminal judgment "upon an examination of the record, including the pleadings, the evidence submitted, [the jury instructions], and any opinions of the court." *See Emich Motors Corp. v. Gen. Motors Corp.*, 340 U.S.

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[3] Stein does not appear to dispute that the first, second, and fourth factors necessary to give preclusive effect to a criminal judgment are satisfied in this case. (*See* Stein's First Am. Opp'n 1.) The prior conviction was clearly for serious offenses warranting heavy penalties (Stein was ultimately sentenced to 17 years in custody based on the conviction), so Stein had a strong incentive to fully litigate the charges. There is nothing in the record to indicate that Stein received anything other than a fair and full trial or that the validity of the conviction is doubtful. Finally, Stein was the sole defendant in the prior criminal proceeding and is the party against whom the SEC now asserts collateral estoppel.

558, 569 (1951). Issues "essential to the verdict must be regarded as having been determined by the judgment." *Id*. The Court will discuss the identity of issues necessarily decided in its discussion of the SEC's claims, infra Parts B and C.

Stein also argues that the application of collateral estoppel would be inequitable because the Government in the criminal proceeding and the SEC in this proceeding maintain distinguishable theories on one aspect of the case: the Government argued that the names of individuals on or in connection with allegedly fraudulent purchase orders were invented by Stein, while here the SEC implicitly acknowledges that at least two of the people may exist but argues that they were not the actual signatories on documents related to the purchase orders in question. (Stein First Am. Opp'n 2-3.) This is a difference that is immaterial to the jury's ultimate findings of material facts supporting their conviction of Stein for securities, mail, and wire fraud. The jury need not have found that the individuals in question did or did not exist. Moreover, given that Stein's position at trial was that the signatures were genuine, Stein had a full and fair opportunity to rebut the Government's evidence on this point.

Stein particularly takes issue with difference between the SEC's and the Government's theories regarding the Cardiac Hospital Management purchase order (see Stein First Am. Opp'n 11), which formed the basis of his conviction for one count of wire fraud. (*See* Eisner Decl, Ex. 1, Ex. 3 at Gov't Ex. 129.) For the reasons discussed supra, the difference in the SEC's and Government's theories regarding the

existence of the order's signatory does not affect the jury's ultimate finding that there was fraud in connection with this order, and it does not affect whether the issue was actually litigated in the prior case. Furthermore, even if Stein were correct that the SEC's different position destroys the identity of issues related to this particular count of fraud, the Court's analysis would be unaffected because Stein was convicted of two additional counts of fraud based on two other purchase orders. Stein does not argue that the SEC and the Government have different positions with respect to those orders.

Stein also argues that collateral estoppel is inappropriate because the SEC's Complaint alleges additional wrongful conduct that was not discussed or decided at the criminal trial and is not discussed in their motion for summary judgment. (Stein's First Am. Opp'n 7.) However, the relevant inquiry is not whether the Complaint and the Indictment are identical in all respects; rather, the Court considers whether the issues sought to be precluded are identical to those previously litigated. The presence of allegations in the Complaint that were not previously litigated cannot defeat the summary judgment motion when the SEC is arguing that at a minimum the issues decided at the criminal proceeding establish Stein's civil liability. Obviously, if the issue here was not address in the criminal case, that has no bearing on the issue.

Finally, Stein argued at the hearing that the Court should defer ruling on the SEC's motion for summary judgment pursuant to Federal Rule of Civil Procedure 56(d) because Stein has pending discovery

motions. The Court declines to defer its ruling because Stein has now shown how discovery would change the result of collateral estoppel.

B. Stein's Principal Violations

I. First and Second Claims: Securities Fraud

Section 10(b) of the Exchange Act makes it unlawful "to use or employ any stoploss order in connection with the purchase or sale, of any security other than a government security, in contravention of such rules and regulations as the [SEC] may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78j(a)(1). Rule 10b-5 makes it unlawful

> (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 the 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.

17 C.F.R. § 240.10b-5. Section 10(b) and Rule 10b-5 together prohibit "(1) using any deceptive device (2) in connection with the purchase or sale of securities." *United States v. O'Hagan*, 521 U.S. 642, 651 (1997). Section 17(a) prohibits the same fraudulent conduct in the offer or sale of any security. *See* 15 U.S.C. § 77q(a).

The antifraud provisions may be violated either (1) by proof of misrepresentations or omissions of material fact, or (2) by proof that the defendant engaged in a scheme to defraud. *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 152-53 (1972). Under either theory, the SEC must also establish that the defendant's actions or representations were (1) material, (2) made with scienter,[4] and (3) in connection with the purchase or sale of securities. *See Gebhart v. SEC*, 595 F.3d 1034, 1040 n.8 (9th Cir. 2010).

Stein's criminal conviction clearly establishes his liability for securities fraud in this action. The jury in the criminal proceedings found that based on evidence presented at trial, Stein was guilty of three counts of securities fraud. The district court judge instructed the jury that to find Stein guilty of securities fraud, it must find the following facts are proved beyond a reasonable doubt: (1) Stein "knowingly executed or attempted to execute a scheme or artifice to defraud;" (2) Stein "did so with the intent to defraud . . . the specific intent to deceive or cheat someone, usually for personal gain or to cause financial loss to someone else;" and (3) "the scheme to defraud was in connection with any security of Heart Tronics, Inc., collectively Signalife, and Signalife had a class of securities registered under Section 12 of the Securities Exchange Act of 1934." (SEC's SUF ¶ 7.)

The jury also found that Stein was guilty of three counts of mail fraud. The district court judge instructed the jury that to find Stein guilty of mail

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[4] Scienter is not an element of violations of subsections 17(a)(2) or 17(a)(3). *Aaron v. SEC*, 446 U.S. 680, 697 (1980).

fraud, it must find that the following facts are proved beyond a reasonable doubt: (1) Stein "knowingly devised or participated in a scheme to defraud someone, or to obtain money or property using false or fraudulent pretenses, representations or promises;" (2) "the false or fraudulent pretenses, representations or promises were about a material fact;" (3) Stein "did so with an intent to defraud someone;" and (4) Stein "used a private or commercial interstate carrier by depositing or causing to be deposited with the carrier something meant to help carry out the scheme to defraud."[5] (SEC's SUF ¶ 8.) The district court judge instructed the jury that it must make the first three findings as well as a finding that Stein "transmitted or caused to be transmitted by wire some

[5] The district court further instructed:

> A scheme to defraud includes any plan or course of action intended to deceive or cheat someone out of money or property using false or fraudulent pretenses, representations or promises. A statement or representation is false or fraudulent if it is about a material fact, it is made with intent to defraud, and the speaker either knows it is untrue or makes it with reckless indifference to the truth. It may be false or fraudulent if it is made with the intent to defraud and is a half-truth or effectively conceals a material fact. A material fact is an important fact that a reasonable person would use to decide whether to do or not do something. A fact is material if it has the capacity or natural tendency to influence a person's decision. It does not matter whether the decision-maker actually relied on the statement or knew or should have known that the statement was false.

(SEC's SUF ¶ 8.)

communication in interstate commerce to help carry out the scheme to defraud" in order to find Stein guilty of wire fraud. (*See* SEC's SUF ¶ 9.) The jury convicted Stein of three counts of wire fraud.

Accordingly, Stein is estopped from challenging the facts found by the jury in convicting him. Given that the Complaint describes a scheme identical to the scheme described in the Indictment and at trial, there is no dispute of material fact that Stein is guilty of securities fraud under Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and Section 17(a) of the Securities Act.

ii. Eighth and Ninth Claims: Falsifying Records

In its eighth and ninth claims for relief, the SEC alleges that Stein violated Exchange Act Rule 13b2-1 and Exchange Act 13(b)(5). (Compl. ¶¶ 158-163.) Rule 13b2-1 provides that "[n]o person shall directly or indirectly, falsify or cause to be falsified, any book, record or account subject to section 13(b)(2)(A) of the . . . Exchange Act." 17 C.F.R. § 240.13b2-1. Rule 13(3)(b)(5) provides that "no person shall . . . knowingly falsify any book, record or account described in [Section 12(b)(2)(A) of the Exchange Act]." 15 U.S.C. § 78m(b)(5). It is not disputed that at the relevant time Heart Tronics was a reporting company subject to Section 13(b)(2)(A) of the Exchange Act, requiring it to "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer." *See* 15 U.S.C. § 78m(b)(2)(A). Here, as discussed supra, Stein is estopped from contesting the issues necessarily determined by the

jury in his criminal conviction, including that he committed securities, mail, and wire fraud in connection with a scheme to artificially inflate the price of Heart Tronics stock. Given that Stein is estopped from challenging the foregoing facts, Stein cannot reasonably dispute that his knowingly fraudulent activity was included in Heart Tronics' books, records, and accounts, which caused falsification of those books, records, and accounts. Accordingly, summary judgment is appropriate on the SEC's eighth and ninth claims for relief.

iii. Fifth Claim: Section 5 Violations

The SEC seeks summary judgment on its fifth claim for relief that Stein violated Exchange Acts Sections 5(a) and 5(c). (SEC's Mot. Summ. J. 15-17.) Section 5(a) prohibits the direct or indirect sale of unregistered securities through the mail or interstate commerce. 15 U.S.C. § 77e(a). Section 5(c) prohibits the interstate offer for sale of unregistered securities. 15 U.S.C. § 77e(c). Liability pursuant to Section 5 extends to one who has a "significant" role in the transaction, which includes one who is a "necessary participant" and a "substantial factor" in the transaction. *S.E.C. v. Phan*, 500 F.3d 895, 906 (9th Cir. 2007).

After a review of the trial record, the Court is unable to conclude that the jury necessarily decided that Stein failed to properly register securities given to contractors as compensation. Although Stein does not appear to dispute that the securities in question were unregistered (*see* Stein's Statement of Genuine Issues in Opp'n Mot. Summ J., ¶ 6g), Stein is not collaterally estopped from challenging the SEC's

assertion that he played a significant role in the transaction. The SEC argues that Stein was significantly involved in the prior proceeding, with reference to testimony and evidence developed at trial. (*See* SEC's SUF ¶ 6g.) However, viewing the evidence in the light most favorable to the nonmoving party, the Court cannot conclude that the SEC has shown that no genuine dispute of material fact remains. Accordingly, summary judgment is not appropriate on the SEC's fifth claim.

C. Stein's Liability as Aider and Abettor to Heart Tronics' Principal Violations

The SEC seeks summary judgment on its third and seventh claims for relief in the Complaint, specifically alleging that Stein aided and abetted Heart Tronics' principal violations of securities laws (Exchange Act Section 10(b), Rule 10b-5, Securities Act Section 17(a)) and financial reporting requirements (Exchange Act Section 13(a), 13(b)(2)(A), 13(b)(2)(B), Rules 12b-20, 13a-1, 13a-11, and 13a-13). (*See* Compl. ¶¶ 133-140, 155-157.) To establish a defendant's liability for aiding and abetting violations of these provisions, the SEC must show that a defendant knowingly provided substantial assistance to a primary violation of the securities laws by another. *See SEC v. Todd*, 642 F.3d 1207, 1225 (9th Cir. 2011); 15 U.S.C. § 78t(e).

The Court finds that it cannot be disputed that Stein aided and abetted Heart Tronics' primary violations of the securities laws and financial reporting requirements. Stein was operating as Heart Tronics' general counsel during the time of his fraudulent actions. (SEC's Mot. Summ. J. 11.)

Furthermore, it cannot be genuinely disputed that Heart Tronics had scienter with respect to these fraudulent transactions, because a corporation's scienter is "necessarily derived from its employees." *Brown v. China Integrated Energy, Inc.*, 875 F. Supp. 2d 1096, 1120 (C.D. Cal. 2012). Thus, for the purposes of this motion, Stein cannot dispute that Heart Tronics committed a primary violation of the securities laws, because the issues necessarily determined by the jury in convicting Stein of securities fraud are identical to the issues necessary to find a primary violation of the securities laws by Heart Tronics in this instance.

Similarly, as discussed supra, Stein is estopped from disputing that his knowingly fraudulent activity was included in Heart Tronics' books, records, and accounts, which necessarily served as the basis of Heart Tronics' inaccurate SEC filings. Thus, it cannot be disputed that Heart Tronics violated the financial reporting requirements of the Exchange Act and Rules, as scienter is not an element of a primary violation of these provisions. *See SEC v. McNulty*, 137 F.3d 732, 740-41 (2d Cir. 1998). Based on the foregoing, Stein substantially assisted Heart Tronics in its primary violation.

Accordingly, summary judgment is appropriate on the SEC's third and seventh claims for relief.

D. Permanent Injunction

The SEC seeks an order permanently enjoining Stein from future violations of the securities laws pursuant to Section 20(b) of the Securities Act and Section 21(d) of the Exchange Act. See 15 U.S.C. § 77t(b); 15 U.S.C. § 78u(d); (SEC's Mot. Summ. J. 17).

It is within the Court's discretion to issue an injunction permanently enjoining a defendant from future violations of securities laws when the Court finds a defendant liable for securities violations and there is a reasonable likelihood that violations may be repeated. *SEC v. Murphy*, 626 F.2d 633, 655 (9th Cir. 1980). The court may consider the following factors in determining whether injunctive relief is appropriate:

> [T]he degree of scienter involved; the isolated or recurrent nature of the infraction; the defendant's recognition of the wrongful nature of his conduct; the likelihood, because of [the] defendant's professional occupation, that future violations might occur; and the sincerity of [the defendant's] assurances against future violations.

Id. The SEC notes that Stein's fraudulent conduct was egregious, intentional, and recurrent. (*See* SEC's Mot. Summ J. 18-20.) Based on this conduct, Stein was convicted guilty of securities fraud, mail fraud, wire fraud, money laundering, and obstruction of justice. (*Id*. at 19.) The SEC also argues that Stein has not shown any remorse or acceptance of responsibility for his actions. (*Id*. at 20.) The Court concludes that the SEC adequately supports its request for a permanent injunction and also notes that Stein has failed to reply to the SEC's arguments on this point. (*See* SEC's Reply 6.) Consequently, the Court finds a permanent injunction warranted in this case.

E. Bar of Service as Officer or Director

A court may bar an individual from serving as an officer or director of a publicly reporting company

upon sufficient showing that the person committed a scienter-based fraud violation and his conduct demonstrates unfitness to serve as an officer or director of public company. *See* 15 U.S.C. § 77t(e); 15 U.S.C. § 78u(d)(2). The following factors are relevant to a determination that an individual should be barred from serving as an officer or director

> (1) the "egregiousness" of the underlying securities law violation; (2) the defendant's "repeat offender" status; (3) the defendant's "role" or position when he engaged in the fraud; (4) the defendant's degree of scienter; (5) the defendant's economic stake in the violation; and (6) the likelihood that misconduct will recur.

S.E.C. v. First Pac. Bancorp, 142 F.3d 1186, 1193 (9th Cir. 1998). The SEC notes that Stein's offense was egregious and "his fraudulent scheme was systematic, multi-faceted, and long-running." (SEC's Mot. Summ. J. 20.) Stein occupied a central role in the scheme, served as general outside counsel of Heart Tronics, and gained over $5 million as a result of his fraudulent conduct. (*Id*.) Stein makes no argument in response. (*See* SEC's Reply 6.) Accordingly, the Court concludes that an order barring Stein from serving as an officer or director of a publicly reporting company is warranted in this case.

F. Bar of Trading in Penny Stock

A court is authorized to bar an individual from trading in "penny stock," an equity security with a price of less than $5.00, when it is shown that the person was participating in an offering of penny stock

at the time of the alleged misconduct. *See* 15 U.S.C. § 78u(d)(6)(A); 15 U.S.C. § 77t(g). The court may consider a conditional, unconditional, temporary, or permanent bar considering the facts and circumstances of the case. Id. The court considers "essentially the same factors that govern the imposition of an officer or director bar" when imposing a penny stock bar. *SEC v. Abella*, 674 F. Supp. 2d 1213, 1223 (W.D. Wash. 2009.)

Here, the SEC notes that Heart Tronics was a penny stock when Stein sold millions of dollars worth of Heart Tronics' stock after issuing false press statements and SEC filings that artificially inflated the price of shares in the market. (SEC's Mot. Summ. J. 22.) The SEC argues that the egregiousness of Stein's conduct justifies a permanent bar on trading penny stock. (*Id.*) Again, Stein makes no argument in response. (*See* SEC's Reply 6.) Accordingly ,the Court finds that an order permanently barring Stein from trading in penny stock is warranted in this case.

G. Civil Penalties

The SEC requests that the Court impose civil penalties pursuant to Section 20(d) of the Securities Act and Section 21(d)(3) of the Exchange Act. *See* 15 U.S.C. § 77t(d); 15 U.S.C. § 78u(d)(3). "Third tier" penalties in the gross amount of pecuniary gain are warranted when a violation "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement" and "such 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).

Here, Stein is liable for securities fraud. The SEC maintains that evidence presented at trial shows that Stein's fraudulent scheme directly or indirectly resulted in substantial losses to investors (Mot. Summ. J. 23), and Stein does not present any argument in opposition. (*See* SEC's Reply 6.) After a two day evidentiary hearing in connection with sentencing, the district court judge found that the gross amount of pecuniary gain as a result of Stein's violations was $5,378,581.61. (Eisner Decl., Exs. 6, 7.) The Court finds that imposing a civil penalty for this amount is warranted under the law.

H. Disgorgement

Finally, the SEC seeks an order of disgorgement of ill-gotten gains from Stein. (SEC's Mot. Summ. J. 23.) When a defendant is found liable for securities violations, he Court has broad equitable power to order disgorgement of all gains, including prejudgment interest, flowing from that illegal activity. *See First Pac. Bancorp*, 142 F.3d at 1191; *SEC v. Cross Fin. Servs., Inc.*, 908 F. Supp. 718, 734 (C.D. Cal. 1995).

Here, the SEC requests the Court order Stein to pay in disgorgement a total of $6,076,415.52, which is the sum of $5,378,581.61 in illegal gain and $697,833.91 in interest calculated using the post-judgment interest rate set forth in 28 U.S.C. § 1961. (SEC's Mot. Summ. J. 24-25; Eisner Decl., Ex. 8.) Stein does not reply to the SEC's arguments on this point. (*See* SEC's Reply 6.) Accordingly, Stein is ordered to pay in disgorgement $6,076,415.52.

I. Stein's Motion for Summary Adjudication

Stein requests summary adjudication with respect to Paragraph 77 of the Complaint, which alleges in relevant part that

> Stein falsely told Rauch that Heart Tronics would imminently announce up to $100 million in sales and that the Company's stock price was artificially depressed by naked short sellers.

(Compl. ¶ 77.) Stein argues that because the SEC acknowledged the existence of naked short selling, Stein could not have lied about it. (*See* Stein's Mot. Summ. Adjudication 1.) As evidence, Stein submits a broken link to an SEC web page. (*Id.*) Stein claims, but the Court is unable to confirm, that the web page shows that the SEC publicly acknowledged naked short selling of Heart Tronics stock. (*Id.*) It is not clear to the Court that the SEC's and Stein's positions are in tension, as the sentence does not clearly state that Stein was lying about the artificial depression. In any event, Stein fails to carry his initial *Celotex* burden; Stein's motion for summary adjudication on this issue is not supported with evidence and consequently is denied.

IV. CONCLUSION

For the foregoing reasons, the SEC's motion for summary judgment is GRANTED IN PART with respect to the first, second, third, and seventh claims and DENIED IN PART with respect to the fifth claim. Stein's motion is DENIED.

IT IS SO ORDERED.

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Initials of Preparer kjt

Appendix F

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CERTIFIED TRANSCRIPT

Case No. SACV11-1962-JVS(ANx)

The Honorable James V. Selna, Judge Presiding

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

HEART TRONICS, INC., et al.,

Defendants.

February 17, 2015

REPORTER'S TRANSCRIPT OF PROCEEDINGS

SANTA ANA, CALIFORNIA; TUESDAY, FEBRUARY 17, 2015; 10:35 A.M.

THE CLERK: Item No. 3, SACV-11-01962-JVS, SEC versus Heart Tronics, Inc., et al. Counsel, please state your appearance for the record.

MR. DONNELLY: Good morning. I'm Ken Donnelly. I am here for the Securities and Exchange

Commission, and with me is my colleague, Melissa Armstrong.

THE COURT: Good morning.

MR. NEWHOUSE: Good morning, Your Honor. George Newhouse on behalf of defendant Willie Gault. Although it's not our motion, I thought I would be present.

THE COURT: Good morning. At Docket 228 --

(Court and clerk conferring.)

THE COURT: Well, apparently Mr. Stein is trying to call in on Ms. Tunis's number. So we are just going to recess briefly and see if she can't link up with him and put him on the phone here.

MR. DONNELLY: All right.

(Recess.)

THE CLERK: Item No. 3, SACV-11-01962-JVS, SEC versus Heart Tronics, Inc., et al. Parties, please state your appearances for the record.

MR. DONNELLY: Good morning. My name is Ken Donnelly for the Securities and Exchange Commission, and with me is my colleague Melissa Armstrong.

MR. NEWHOUSE: Good morning, Your Honor. George Newhouse on behalf of Mr. Gault.

MR. STEIN: Good morning, Your Honor. Mitchell Stein, pro se, appearing by telephone.

THE COURT: Mr. Stein, were you able to obtain a copy of the tentative ruling?

MR. STEIN: Yes, I was Your Honor.

THE COURT: Okay, sir, then I think I would like to begin with you.

MR. STEIN: Thank you, Your Honor. I appreciate the Court allowing me to argue telephonically. I have read the tentative carefully, and I understand and am mindful that the Court has reviewed the record carefully.

I have a few things I would like to address. The first will be the one SEC admission at Paragraph 40 of the Complaint that I believe is fatal to the application of offensive collateral estoppel, and it's regarding one of three allegedly false purchase orders.

I will then speak briefly about Rule 56(d) and about my cross-motions for partial summary judgment.

Turning to the argument, Your Honor, if the Court could please pull up Trial Exhibit 64, which is docket entry 175-6, Exhibit 3 to the Eisner declaration. Again, it's 175-6, the docket entry.

THE COURT: Is it in your responding papers?

MR. STEIN: I'm sorry. No, Your Honor. It's attached to the declaration of Mr. Eisner from the SEC, Docket 175-6. It's a trial exhibit from the criminal trial, Exhibit 64.

THE COURT: Just a minute, please.

MR. STEIN: Thank you.

THE COURT: Okay, Docket No. 175.

MR. STEIN: Exhibit 64, Docket 175-6, Trial Exhibit 64 from the criminal trial.

THE COURT: Okay.

MR. STEIN: Thank you, Your Honor.

Just so we are talking about the same thing, on the top it should say Purchase Order No. 2003-001. This is the Cardiac Hospital Management purchase order, one of the three purchase orders that I was convicted of fabricating.

In the criminal case, government witnesses and the prosecution said this purchase order was not signed by Thomas Tribou and thus not a binding purchase order, that the $50,000 check was not delivered under this purchase order.

In this case, Your Honor, at Paragraph 40, the SEC alleges and admits the opposite, that not only does the signatory, Thomas Tribou, exist, but that he signed this document and entered in into this deal.

THE COURT: Sir, let me make sure I have the right document.

MR. STEIN: Yes, Your Honor.

THE COURT: -6 is part of Exhibit 3 to the Eisner declaration. It's 255 pages. And I am looking at Government's Exhibit 68, which is --

MR. STEIN: I believe it's 64.

THE COURT: 64, okay.

MR. DONNELLY: Yes, Your Honor. I'm sorry.

THE COURT: Okay.

MR. STEIN: Your Honor, it says 2003-001, the purchase order at the top.

THE COURT: Okay, I'm with you.

MR. STEIN: Thank you, Your Honor.

In the criminal case, government witnesses and the prosecution said this was not signed by Thomas

Tribou and thus not binding, that the $50,000 called for under it was not delivered.

In this case, Your Honor, the SEC alleges the exact opposite. They allege at Paragraph 40 of their Complaint and in their separate statement that this purchase order was entered into, that Mr. Tribou does exist, and that he signed this document and entered into this deal. That's at Paragraphs 40 through 43 of the Complaint, as well as separate statement 6-C.

I have laid this out very simply on page 11 of the amended opposition in a simple chart that shows the difference between the criminal trial, where this purchase order simply was never entered, and this case, where it was entered into.

Now, Your Honor, to be fair to the Securities and Exchange Commission, they do allege that there was a fraud regarding this purchase order, but the fraud is completely different. The fraud they allege in this case is that the purchase order was entered into, but if you read Paragraphs 40 through 43, that there was a lie regarding whether the products could be delivered and a fraud after the purchase order.

Page 7 of the text of the tentative ruling, which I have reviewed carefully, says that, quote: "Given the Complaint describes a scheme identical to the scheme described at trial," meaning the criminal trial. But respectfully, Your Honor, that's inaccurate. The criminal trial has this purchase order as never having been entered into, and this case has the purchase order as being entered into. It's the opposite. Littlejohn versus United States, which I know this Court is well familiar with, requires that the issues be identical.

I have been sentenced to 17 years based on three purchases orders. This is one of the three. And contrary -- this is not identical. This is completely the opposite.

The criminal jury needed to know that this purchase order was signed by Mr. Tribou and that he delivered $50,000 under it, but the DOJ actually objected to the check on hearsay grounds. I am not -- I have reviewed that in my papers. Judge Marra ruled that the check was excludable because it's hearsay, but U.S. versus Williams says says checks aren't hearsay. That's besides the point. The matters are completely different regarding one of the core purchase orders.

I would also like to cite Security and Exchange Commission versus Reyes, Judge Breyer of the Northern District of California, 2008 Lexis 65895. In that case, Judge Breyer wrote -- I am paraphrasing -- "If there is a doubt that the issue was not litigated in the earlier case, the identical issue, offensive collateral estoppel cannot be applied." It is beyond dispute that of this one purchase order out of the three the identical issue was not litigated.

I am very mindful of the heavy presumption against me, and I have been convicted and my life is essentially over. But, Your Honor, I respectfully submit we have got to face the reality that the criminal trial theory that Exhibit 64 was not signed by Thomas Tribou and he did not deliver a $50,000 check -- that theory has been admitted in this case by the SEC to have been false.

Paragraph 40 says it specifically. It says, quote: "On approximately September 14, 2007" -- and I ask

the Court to note that that is the date on the purchase order -- continuing: "Heart Tronics contracted to sell $2 million of its Fidelity 100 product to an individual located in Portland, Oregon, the customer, who had a prior relationship with Lowell Harmison, then CEO of Heart Tronics. More specifically, the customer signed an order to purchase 180 units of the Fidelity 100 for $1.98 million. Stein negotiated and drafted the purchase order with the customer, and it was signed on behalf of Heart Tronics by Harmison. The customer sent Heart Tronics a personal check for $50,000 as a deposit for the units."

The criminal jury, Your Honor, was given none of these facts. They were given the opposite facts. Once it is understood that one of three purchase orders said to be fictitious at the criminal trial is admitted by the SEC not to be fictitious, I argue, Your Honor, the entire case here is thrown into a different light, because that's what is required under the equitable prong of offensive collateral estoppel. That's been heavily briefed, I see that the Court has reviewed it carefully. There is no need to go into the equitable prong.

If this Court is -- nevertheless -- and I pointed out it's one of the key differences, but here are many more that have been pointed out. The issues are not identical because of this. But if this Court is inclined to say the issues are similar enough or whatever the standard is, then, Your Honor, I think it underscores the importance of the outstanding discovery, and I believe that the discovery should be ruled upon prior to this motion being granted, not vice-versa.

Once we know that Thomas Tribou not only existed -- and I think the Court has correctly in the tentative said just the fact that people exist and they said at trial they didn't exist may not be enough. Presuming that that is the standard, that should be the ruling, and that is this Court's ruling. That wasn't what happened.

In this case, it's not about Thomas Tribou existing, which it turns out he does exist. He signed the purchase order, and they told the criminal jury he didn't sign the purchase order. He delivered a $50,000 check, and they told the jury he didn't deliver a $50,000 check.

So, Your Honor, in the event -- in the discovery -- now we turn to Yossi Keret. In the discovery -- and I understand the Court has not reviewed that matter yet, and I'm not going to go into it in any great detail. But the SEC objected that it's burdensome to tell us what Yossi Keret said about the purchase orders if in fact he said something. They objected, the SEC, on the grounds of investigatory privilege and that it's burdensome to tell me if Yossi Keret told them on the telephone or in person that these purchase orders were real.

Your Honor, there is additional doubt from the record -- and I argue that once we see that the issues are not identical -- in fact, the polar opposite -- I believe that the Court is obligated at that point and should make a more probing review of the record.

If it did that, Your Honor, and if it felt it was appropriate to do that, I think the Court would see at docket entry -- the Court can take a note and review this later. I don't want to belabor the point. Docket

entry 185-3 at 8, Exhibit 10 to my declaration dated January 12 is a 302 from the only witness who testified that I made these things up, which I did not. That witness's name is Martin Carter, and he testified clearly that I made these people's names up as did the government. They said the same thing. But in his 302 with the postal inspector, Mr. Carter said that he -- not me -- made these people's names up.

Your Honor, I'm now going -- unless the Court has any questions about this -- I would like to also cite Ismail versus Ford, which is April 2014, Central District of California. It's Ismail, 2014 Westlaw 168 (1993). At 7, it says that a request, Your Honor, under -- for discovery under subsection (d) is to be liberally applied on Motions for Summary Judgment. I know that law is well settled.

The SEC investigated these people because they are citing the investigative privilege in the discovery, but it refuses to tell us the content of those discussions or to produce any documents citing investigatory privilege. As I said, I don't think it's appropriate, unless the Court wants me to, to go into the discovery motions. But the investigatory privilege under the case law has lapsed. I have already been convicted.

So I respectfully submit the discovery should be ruled upon first before summary judgment is granted if the Court is still inclined to do so under 56(d).

THE COURT: You don't have a formal 56(d) application before the Court do you?

MR. STEIN: No, I don't, but under the case law that we've cited, including Ismail versus Ford, the

affidavit that I have submitted, as well as the request in the brief, is more than enough because the discovery is pending. If the Court felt that it was not enough, I would like to have an opportunity to file that, but I think the case law is clear that by the outstanding discovery motions -- and we cited 56(d) in our opposition. But, obviously, the Court will make whatever ruling it makes there.

Your Honor, with respect to the Cross-Motion for Summary Judgment, the correct link to the SEC website was always on Exhibit 4, and I apologize that it was broken as the Court pointed out in the brief. We have resubmitted it this morning in an errata. But, Your Honor, this should not be disputed. There was adjusted for the split over one billion shares, naked short sold, during the year when this fraud happened in a company that had 60 million shares outstanding. Everything -- to the extent there is a trial, everything that I will prove will have to be in the light of these short sales, because every board member was talking about it, and everything the company did had something to do with it.

I request, Your Honor, that if the SEC denies that this is the truth that they simply be required to do what I have had to do, submit a separate statement and say denied.

The evidence is this. They didn't deny it. All they did in their response on that issue is say that -- and then I am basically through. They said that they are at a loss for what I desire other than mentioning the relief in the first and last paragraphs of my opposition, that I, quote, "do not address the legal or factual basis for my cross-motion," but I filed a

separate motion which they haven't referenced. They then say the motion is untimely, which I pointed out it wasn't, but they never denied the facts.

I understand this case may never be tried for me, but to the extent it is, I don't know why I should be put to the burden of having to establish the fundamental fact behind why the company did everything it did through expert testimony and the rest when there can be no dispute as to the SEC's website.

Your Honor, I would like to reserve one minute to formally request a continuance on a 56(d) if the Court is still inclined to grant the motion, but I appreciate the Court allowing me to argue so long.

THE COURT: Mr. Donnelly.

MR. DONNELLY: Your Honor, Mr. Stein's argument is basically just an attack on what occurred in his criminal case. We think that the Court got it right in the tentative.

We do note that on Page 2 there is a typographical error, and it could have been from us. We apologize. At the very top, on December 13, 2012, it should say I think 2011. That's when Mr. Stein was indicted.

Just to the point about the purchase orders, that's one of three purchase orders, Your Honor, that's at issue. He was criminally convicted of falsifying these purchase orders, and that's what's relevant. Our allegations are what our allegations are. They are not admissions. That's what frames what is to be litigated.

Most of what Mr. Stein has argued is simply an attack on the fairness of his trial in the Southern

District of Florida. There is no evidence that he received an unfair trial. There is no evidence that he was railroaded there. He was properly convicted, and we believe that that conviction supports collateral estoppel here.

To his request suddenly for Rule 56(d), it's far to late to grant such a request, Your Honor. That's about all I have, unless the Court has any questions.

THE COURT: Well, did the SEC take two different positions with regard to this purchase order?

MR. DONNELLY: Your Honor, we made allegations in Paragraph 40 of the Complaint. There was really no discovery done in this case to flush out what the truth was with respect to those allegations because Mr. Stein was criminally convicted, and our plan all along was to move for collateral estoppel for that, so I can't tell you sitting here today what the truth is.

We are not truth-finders as the SEC. We make allegations. The jury obviously found a truth that's applicable here, and it's only one of three purchase orders. The other two are still in play. Even assuming that this is irrelevant, he was still convicted of fraud with respect to those other two purchase orders in the criminal case, and that has application here as well.

THE COURT: But come back to my question: Were two different positions taken as to whether this purchase order, Exhibit 64, in the criminal trial was real or not real?

MR. DONNELLY: Well, Your Honor, we do allege in Paragraph 42 of the Complaint that this entity, Cardiac Hospital Management, is a fictitious

entity. So it was our position in this case that the entity itself was fictitious. It may have been signed by this individual, but Mr. Stein completed this purchase order, and the entity that it was completed for was a fictitious entity. There was no sale.

THE COURT: What was the result of the purchase order in the criminal case?

MR. DONNELLY: What's that, Your Honor?

THE COURT: What did jury do with this purchase order in the criminal case?

MR. DONNELLY: Your Honor, I don't know if the jury did anything specific with this purchase order. There wasn't like a special verdict directed to just this purchase order. So I don't know what the jury found with respect to this purchase order.

We do know that he was criminally convicted. At issue in the criminal case was the were these purchase orders? And he was found guilty of securities fraud and wire fraud and mail fraud as it related to the purchase orders.

THE COURT: But how did the government present the case in the criminal case with regard to this purchase order?

MR. DONNELLY: They alleged -- as Mr. Stein is saying, they alleged that the signatures were false, Your Honor, and they also alleged that the entity itself was false, Cardiac Hospital Management.

Mr. Stein is seizing on an allegation in Paragraph 40 that we made very early on in this case before Mr. Stein was indicted. So, I mean -- again, as I said, sure we haven't amended Paragraph 40, but it's sort of beside the point at this point.

And as my colleague points out, if the entity doesn't exist, Your Honor, the signature has to be false, even if a real person signed it.

THE COURT: Understood.

MR. DONNELLY: Okay.

THE COURT: Anything further?

MR. DONNELLY: No, Your Honor.

THE COURT: Mr. Stein.

MR. STEIN: Yes, Your Honor. Unfortunately, Your Honor, I hate to say I am dumbfounded. The SEC -- first of all, are they claiming this purchase order was not signed by Mr. Tribou because he testified in their investigation that he signed it?

And at trial in the criminal case, the prosecutor said to the jury: If Tom Tribou is Cardiac Hospital Management, where is his name? Where is his name? Does it say sold to Tom Tribou? Take a look at Government's Exhibit 64, the $1.98 million purchase order. See if his name or signature appears on there. It's on Page 11.

The jury believed because they told them – as this Court has pointed out under Emich Motors, the Court can review the record and see -- and that's, by the way, Your Honor, Government's Exhibit 2 to the Summary Judgment Motion what I just quoted -- and you can see from the record that this jury necessarily found that this purchase order was forged, that the signature did not exist. The issues have to be identical.

I understand I have been convicted and this might be it for me. All I ask is an opportunity to follow

the law regarding the identicality of issues that were necessarily decided.

And I think the Court is supposed to ask itself, under Emich Motors and under Littlejohn, if the criminal jury had been told that Thomas Tribou not only existed but signed this purchase order and agreed to pay $1.98 million and delivered a $50,000 check, and with all the other impeachment of Martin Carter, would they have still convicted me?

This civil case -- it's a different case. This is a completely different case. Your Honor, that's -- that's my first response. By the way, that's on Page 11 where the government made their argument to the jury. It's in a chart referencing the portion of that transcript.

But, Your Honor, it's actually much worse than that. Because with $1.98 million of legitimate sales, no matter what happened afterwards, there is colloquy between Judge Marra and I and the prosecutors where I said -- and I quote: "This idea of fake people" -- I was completely shocked at trial when they started talking about fake people. They never told me they were going to do that. I understand they have no obligation to. I just didn't – I couldn't believe it.

There is no allegation that I ever touched these purchase orders, put my hands on them, or that actually I'm the one that signed it. I wasn't an officer or director of the company.

Martin Carter is the only one that alleged it, Your Honor. He's the only one. The SEC will not tell you to the contrary. It was one person, and it turns out he is wrong. And it turns out the SEC and DOJ have different theories and different facts.

To say that Paragraph 40 is not a judicial admission, Your Honor, runs counter to the controlling law in the Eleventh Circuit and the Ninth Circuit. The admission at Paragraph 40 is an admission particularly for purposes of applying offensive collateral estoppel in which the law is very clear that the Court has to be very careful.

So I would again request that the motion be denied. If it's denied without prejudice and the Court wants to -- I understand they need to get to trial. If Court would streamline the discovery perhaps just to produce those documents related to these people or -- we would streamline the motion -- then it would be fair.

Right now the Court is about to enter judgment against me if it follows what the SEC is requesting that necessarily includes a fact that it knows is probably untrue, that this purchase order was forged and that the $50,000 was not delivered. It was delivered. It was a $1.98 million purchase order. I have been sentenced to 17 years because it wasn't and yet it was.

I would ask the Court if there is any inclination to grant the motion to please carefully review the case law regarding a continuance for the discovery, because I believe that I have done more than is necessary in the opposition to qualify for such a continuance.

THE COURT: Mr. Donnelly.

MR. DONNELLY: Your Honor, if I may just add to the point I was making earlier. This is one of three purchase orders. This one purchase order is a red herring.

Let's assume for the sake of argument that there is not a perfect alignment between the allegations made in the criminal case on this one purchase order and the allegations made in this case. Let's assume for purpose of argument that there is not a perfect alignment in exactly the facts that each -- that the government alleged and the SEC alleged. There are two still other purchase orders. He was criminally convicted on those as well. Those are also in our Complaint here.

The government in the criminal case charged him with obstruction of justice. We don't charge him with obstruction of justice. That's not a reason to not apply collateral estoppel. Collateral estoppel still applies.

If Your Honor wants to for safety purposes or whatever carve out one of these purchase orders, it really doesn't matter. I mean, he has been criminally convicted of securities fraud. He should be civilly found liable for the securities fraud.

THE COURT: As the Court reviews the record in the criminal case, there is no finding with respect to each contract, correct?

MR. STEIN: That's correct.

THE COURT: There is simply a finding, a general verdict, he violated the statute?

MR. STEIN: That's correct.

MR. DONNELLY: Right.

THE COURT: I'm talking to Mr. Donnelly now.

MR. STEIN: I'm sorry, Your Honor.

THE COURT: So in theory, the jury could have found one contract violative, and that would have been sufficient to support its various verdicts; isn't that true?

MR. DONNELLY: Yes, Your Honor, that's true.

THE COURT: I guess what I am saying in a roundabout way does disregarding this one contract really work given the nature of the verdict?

MR. DONNELLY: I don't know the answer to that, Your Honor.

THE COURT: Assuming I hold to the tentative, I assume the SEC would not wish to proceed further against Mr. Stein.

MR. DONNELLY: Your Honor, as soon as there is a final ruling, we will seek our client's permission to drop the other claims against Mr. Stein, and we will hopefully have that permission within a matter of a few days. We are already working to get that permission now on the assumption that the tentative stands.

THE COURT: Have you had any further discussions with Mr. Gault?

MR. DONNELLY: No, Your Honor, we have not. I will let Mr. Gault's counsel speak to that, though.

MR. NEWHOUSE: Your Honor, it would appear that Mr. Gault will proceed to trial, which is -- that's the reason I'm here -- that is scheduled to begin in two weeks.

Of course we have the pretrial conference next week, and it makes a big difference. If Mr. Stein is part

of our trial, then our trial will be much more complicated than the Gault case.

THE COURT: Well, I want to take one more look at this, so the matter will stand submitted. We'll try and get it out promptly.

MR. DONNELLY: Thank you.

* * *

CERTIFICATE

I hereby certify that pursuant to Section 753, Title 28, United States Code, the foregoing is a true and correct transcript of the stenographically reported proceedings held in the above-entitled matter and that the transcript page format is in conformance with the regulations of the Judicial Conference of the United States.

Date: March 30, 2015

/s/ Sharon A. Seffens 3/30/15

SHARON A. SEFFENS, U.S. COURT REPORTER

Appendix G

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

Case No. SACV11-1962-JVS(ANx)

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

HEART TRONICS, INC., MITCHELL JAY STEIN, WILLIE JAMES GAULT, J. ROWLAND PERKINS, II, MARTIN BERT CARTER, MARK CROSBY NEVDAHL, and RYAN ALLAN RAUCH,

Defendants,

TRACEY HAMPTON-STEIN, ARC FINANCE GROUP, LLC, ARC BLIND TRUST, THS BLIND TRUST, JAYMI BLIND TRUST, OAK TREE INVESTMENTS BLIND TRUST, WBT INVESTMENTS BLIND TRUST, CATCH 83 GENERAL PARTNERSHIP, and FIVE INVESTMENTS PARTNERSHIP,

Relief Defendants.

Filed: Dec. 20, 2011

COMPLAINT

Plaintiff Securities and Exchange Commission (the "Commission") alleges:

SUMMARY

1. Between December 2005 and December 2008, defendant Mitchell J. Stein ("Stein"), the purported outside counsel of defendant Heart Tronics, Inc. (f/k/a Signalife, Inc. and Recom Managed Systems, Inc.) ("Heart Tronics" or the "Company") and husband of its majority shareholder, orchestrated a brazen series of frauds designed to inflate the price of Heart Tronics stock so that he could profit from selling its securities to investors.

2. Stein held himself out as Heart Tronics' outside counsel and claimed not to be a Company officer or director; however, in practice, Stein was a *de facto* officer who controlled many of Heart Tronics' business decisions and public disclosures. In that capacity, Stein orchestrated the repeated announcement of fictitious sales orders for Heart Tronics' products in public filings with the Commission, press releases, and other public broadcasts, all designed to make it appear that Heart Tronics was more successful than it actually was. Stein also installed former professional football player Willie Gault ("Gault") as a figurehead co-CEO along with former Hollywood executive J. Rowland Perkins ("Perkins") in order to generate publicity for the company and foster investor confidence. Through this and other fraudulent schemes described below, Stein was able to obtain for himself millions of dollars in ill-gotten gains at the expense of public investors.

3. In 2002, Stein's wife, relief defendant Tracey Hampton-Stein ("Hampton-Stein"), became the largest shareholder of Heart Tronics, owning approximately 85% of the Company's common stock.

She owned this stock through a holding company, relief defendant ARC Finance Group, LLC ("ARC Finance"). From at least December 2005 through September 2008, while Stein was orchestrating a campaign of misinformation designed to inflate the price of Heart Tronics stock, Stein and Hampton-Stein (collectively, "the Steins") directed the sale of more than $5.8 million worth of Heart Tronics stock without disclosing it to the public as required by law. To conceal their purchases, the Steins used accounts in the name of purportedly blind trusts and other nominee entities, identified above as relief defendants. The Steins used the proceeds of the sales to fund their lavish lifestyle, which included multiple homes, exotic cars, and private jets.

4. To accomplish this, Stein enlisted defendant Mark Nevdahl ("Nevdahl"), a registered representative of a broker-dealer registered with the Commission (stock broker) to act as the trustee on the blind trust accounts. This created the façade that the Steins' Heart Tronics stock was held by separate legal entities under the control of an independent trustee, when, in fact, the trusts were "blind" in name only. Nevdahl met the Steins' regular demands for cash by continually selling Heart Tronics stock through the trusts. The blind trusts were further designed as part of a scheme to avoid the required regular public disclosures under the federal securities laws of ARC Finance's sales.

5. Stein was also aided in his fraudulent schemes by, among others, defendant Martin Carter ("Carter"). For example, Stein and Carter fabricated documents designed to make it appear to Company

officers that Heart Tronics had entered into viable sales orders for millions of dollars worth of Heart Tronics products when, in fact, it did not.

6. At the same time, Stein drafted false and misleading press releases and other public statements for the Company to announce sales orders, or directed other Company officers to draft public statements based on false and misleading information he provided.

7. For his role in the scheme, Carter received, among other things, approximately $600,000 in cash and approximately $1.4 million in improperly registered Heart Tronics stock pursuant to a sham consulting agreement between Carter and Heart Tronics. At Stein's direction, Carter sold the Heart Tronics stock in the market and kicked-back substantially all the cash and proceeds of the stock sales to Stein.

8. During the relevant period, although nominally the senior-most officers of Heart Tronics, Gault and Perkins rarely questioned Stein's direction and abdicated their fiduciary responsibilities to Heart Tronics shareholders. Among other things, Gault and Perkins signed, or unlawfully authorized to be signed, public Commission filings containing false statements about the Company's purported sales.

9. In late 2008, Stein and Gault also defrauded an individual investor into making a substantial investment in Heart Tronics based on, among other things, materially false representations that the proceeds of the investment would be used for the Company's operational expenses. Instead, Stein and Gault diverted the investor's proceeds for their

personal use, including the purchase of Heart Tronics stock on the open market to create the appearance of active trading volume and to inflate Heart Tronics' stock price.

10. In an additional effort to artificially inflate Heart Tronics' stock price, Stein caused Heart Tronics to hire promoters to tout Heart Tronics' stock to investors. One such promoter, defendant Ryan Rauch ("Rauch"), solicited numerous investment advisers, institutional and retail brokers, and other investors to buy Heart Tronics stock. Rauch purported to give objective recommendations, but failed to disclose that he was being compensated by the Company in exchange for his promotion.

11. By the third quarter of 2008, Heart Tronics had incurred cumulative net losses of more than $60 million, and it has been delinquent in its public filings with the Commission since it failed to file its Form 10-K for fiscal year 2008. Stein and the other defendants, however, reaped ill-gotten gains from their violations of the federal securities laws of approximately $8 million.

12. By engaging in the practices and transactions alleged in this Complaint, defendants violated numerous provisions of the federal securities laws.

JURISDICTION AND VENUE

13. This Court has jurisdiction over this action pursuant to Sections 20(b), 20(d)(I), and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b), 77t(d)(1) & 77v(a)], and Sections 21(d), 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), and 78aa].

14. Venue in this District is proper pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 27 of the Exchange Act [15 U.S.C. § 78aa] because acts or transactions constituting federal securities law violations occurred within the Central District of California and several of the defendants reside in this district.

15. Defendants, directly or indirectly, made use of the mails and of the means and instrumentalities of interstate commerce in furtherance of the acts, practices and courses of business described in this Complaint.

DEFENDANTS

16. Heart Tronics is a Delaware corporation headquartered during the relevant period in Studio City, California and, earlier, in Greenville, South Carolina. During various time periods relevant to this Complaint, Heart Tronics was known by its prior corporate names, including primarily "Signalife, Inc." from November 2, 2005 through November 20, 2008; accordingly, all references herein to "Heart Tronics" refer to Company under its prior names as well as under the name Heart Tronics, Inc. Heart Tronics became a public company in 2002 via a reverse merger with a public shell company. Heart Tronics purports to sell a proprietary electrocardiogram (heart monitoring device) called the Fidelity 100. At all relevant times, the Company's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act. At all relevant times, Heart Tronics filed reports with the Commission pursuant to Section 13 of the Exchange Act. The common stock of Heart Tronics was listed on the American Stock

Exchange ("AMEX") from approximately June 8, 2005 until September 15, 2008. Heart Tronics' stock is now quoted on the OTC Link (formerly "Pink Sheets") under the symbol "HRTT.PK."

17. Mitchell Jay Stein ("Stein") is a California attorney who has purportedly acted as outside counsel to Heart Tronics from approximately 2002 to the present. From at least December 2005 through December 2008, Stein effectively controlled Heart Tronics and its officers, but nominally was not an officer, director or shareholder of the Company. Stein is married to relief defendant Tracey Hampton-Stein. Stein is a United States citizen living in Hidden Hills, California.

18. Willie James Gault ("Gault") is a former professional football player. From approximately October 15, 2008, through June 23, 2011, Gault was Heart Tronics' President and "co-CEO of Administration." Gault also served on Heart Tronics' Board of Directors from approximately July 28, 2008, through June 23, 2011. Gault is a United States citizen living in Encino, California.

19. J. Rowland Perkins II ("Perkins") is the current Chief Executive Officer of Heart Tronics. Perkins served as Heart Tronics' interim CEO beginning on or about May 1, 2008. He became CEO on or about June 1, 2008, but later shared responsibility with Gault as "co-CEO for Operations." Perkins has served on Heart Tronics' Board of Directors since approximately August 23, 2005, in roles including Chairman and member of the Audit Committee. Previously, Perkins was a founder of the Creative Artists Agency talent agency. Perkins is a

United States citizen living in Beverly Hills, California.

20. Martin Bert Carter ("Carter") was purportedly a consultant to Heart Tronics from approximately January 20, 2008, through November 5, 2008. Carter is an unlicensed electrician who provided handyman, chauffer and other personal services for Stein. Carter is a United States citizen living in Boca Raton, Florida.

21. Mark Crosby Nevdahl ("Nevdahl") is a registered representative presently associated with a broker-dealer firm registered with the Commission. At all relevant times, Nevdahl served as the stock broker and trustee for the purportedly blind trusts beneficially owned by the Steins. Nevdahl is a United States citizen living in Spokane, Washington.

22. Ryan Allan Rauch ("Rauch") is a former securities research analyst who was an "investor relations" consultant to Heart Tronics from approximately January 30, 2008 through late April 2008. Rauch is believed to be unemployed. Rauch is a United States citizen living in San Clemente, California.

RELIEF DEFENDANTS

23. Tracey Hampton-Stein ("Hampton-Stein"), the wife of Stein, is the sole managing member of ARC Finance Group LLC, Heart Tronics' largest shareholder. Hampton-Stein is believed to be unemployed. Hampton-Stein is a United States citizen living in Hidden Hills, California. Hampton-Stein was unjustly enriched by receiving the proceeds of the unlawful sale of Heart Tronics stock.

24. ARC Finance Group LLC ("ARC Finance") is a single-member Delaware limited liability company formed in 2002 by Hampton-Stein. ARC Finance is a shell company that has no business operations, and its address is a private mailbox in Boca Raton, Florida shared by Stein and Hampton-Stein. ARC Finance has held a majority position of Heart Tronics' securities (originally approximately 85%) since 2002. ARC Finance was unjustly enriched by receiving the proceeds of the unlawful sale of Heart Tronics stock.

25. ARC Blind Trust is a purportedly blind trust established on or about December 19, 2005 under the laws of the State of Nevada. ARC Finance was both the settlor and the beneficiary of the trust. Nevdahl served as both the trustee and the broker of the trust's brokerage account. ARC Blind Trust was unjustly enriched by receiving the proceeds of the unlawful sale of Heart Tronics stock.

26. THS Blind Trust is a purportedly blind trust established on or about August 1, 2005 under the laws of the State of Nevada. ARC Finance was the settlor of the trust and Mitchell Stein was the beneficiary. Nevdahl served as both the trustee and the broker of the trust's brokerage account. THS Blind Trust was unjustly enriched by receiving the proceeds of the unlawful sale of Heart Tronics stock.

27. JAYMI Blind Trust is a purportedly blind trust established on or about March 2, 2007 under the laws of the State of Nevada. ARC Finance was both the settlor and the beneficiary of the trust. Nevdahl served as both the trustee of the trust and broker of the trust's brokerage account. JAYMI Blind

Trust was unjustly enriched by receiving shares of Heart Tronics stock from ARC Finance and the proceeds of the unlawful sale of Heart Tronics stock.

28. Oak Tree Investments Blind Trust is a purportedly blind trust established on or about March 30, 2008, under the laws of the State of Nevada. ARC Finance was both the settlor and the beneficiary of the trust. Nevdahl served as the co-trustee and the broker of the trust's brokerage account. The Steins' former housekeeper served as the other co-trustee. Oak Tree Investments Blind Trust was unjustly enriched by receiving shares of Heart Tronics stock from ARC Finance.

29. WBT Investments Blind Trust is a purportedly blind trust established on or about September 21, 2007 under the laws of the State of Nevada. ARC Finance was both the settlor and the beneficiary of the trust. Nevdahl served as both the trustee of the trust and broker of the trust's brokerage account. WBT Investments Blind Trust was unjustly enriched by receiving shares of Heart Tronics stock from ARC Finance.

30. Catch 83 General Partnership is a general partnership formed on or about April 5, 2005 between Gault and his daughter. Gault conducted his personal securities trading through brokerage accounts in the name of Catch 83 General Partnership, and Nevdahl served as the broker. Catch 83 General Partnership was unjustly enriched by receiving investor capital diverted from Heart Tronics and the proceeds of the unlawful sale of Heart Tronics stock.

31. Five Investments Partnership is a general partnership formed on or about December 11, 2006 under the laws of the State of Nevada between Stein and Carter. Nevdahl was the broker on Five Investments' brokerage account. Five Investments Partnership was unjustly enriched by receiving shares of stock issued by Heart Tronics from transactions unlawfully registered with the Commission on Form S-8, or the proceeds from the unlawful sale of such stock.

OTHER RELEVANT PERSON

32. Dr. Lowell T. Harmison, Ph. D., deceased, served as President and Chief Operating Officer of Heart Tronics beginning on July 2, 2007. He served as President and CEO from August 17, 2007, through June 2, 2008. Harmison also served as a member of Heart Tronics' Board of Directors from June 6, 2003, to June 8, 2008.

FACTUAL ALLEGATIONS

I. Schemes to Inflate the Price of Heart Tronics Stock

33. From at least December 2005 through December 2008, Stein, together at times with certain of his co-defendants, engaged in fraudulent schemes to inflate the price of Heart Tronics stock. They did so primarily through a campaign of misinformation centered around falsely reporting fictitious sales orders of Heart Tronics' flagship product, the Fidelity 100, in an effort to make Heart Tronics appear more successful than it was.

A. Fraudulent Disclosure of Sales Revenue in 2006

34. In approximately September 2006, after previously having arranged a failed joint sales marketing arrangement with another company, Stein arranged a transaction to create the false impression that Heart Tronics had made, and profited from, its first sale of its Fidelity 100 product.

35. More specifically, Stein arranged for a company that specialized in leasing cars and equipment (the "Leasing Company") to finance a lease of Fidelity 100 units from Heart Tronics to a doctor in Los Angeles (the "Doctor"). The Leasing Company, which had previously leased luxury cars to Stein, agreed to finance the transaction based on Stein's representations that the Doctor was a *bona fide* customer, that Stein would personally guarantee the loan, and that the product would be used by the Doctor for medical purposes. The Doctor was a personal friend of Stein's, whom Stein brought into the transaction after another physician declined to participate further. In fact, as discussed further below, the Doctor had no legitimate interest in the units and was simply a straw purchaser arranged by Stein.

36. In approximately September 2006, the Leasing Company agreed to purchase 11 units of Heart Tronics' Fidelity 100 product and lease them to the Doctor. On or about September 30, 2006, the Leasing Company issued a check for the full purchase price payable to Heart Tronics. Under the arrangement, Heart Tronics would deliver the Fidelity 100 to the Doctor pursuant to a separate purchase or lease agreement.

37. On or about September 20, 2006, in connection with this purported sale to the Doctor, Heart Tronics issued a materially false and misleading press release announcing that the Fidelity 100 "has been sold and shipped to everyone from surgeons to cardiologists to internists, to, as well, a multi-billion-dollar corporation." The press release was drafted by Stein or by others based solely on information provided by Stein.

38. In fact, as noted above, the Doctor was not a *bonafide* purchaser. Indeed, the Doctor's initial deposit payment to the Leasing Company failed to clear for insufficient funds, and the Leasing Company did not receive any further payments from the Doctor. The Leasing Company then sought and obtained partial repayment from Stein based on his guarantee of the transaction. While described by the Company as a legitimate sale, Stein effectively self-funded the Doctor's purported lease from September 2006 to September 2008 by paying over $100,000 to the Leasing Company. Stein concealed this fact from Heart Tronics' Chief Financial Officer ("CFO"), its auditor, its outside securities disclosure counsel (the "Disclosure Lawyer"), and its other officers. In 2008, Stein ceased making payments to the Leasing Company, and the Leasing Company re-possessed at least 8 of the 11 units in their original, unopened shipping boxes.

39. Notwithstanding these facts, beginning with its Form 10-Q for the third quarter 2006, which the Company filed with the Commission on November 13, 2006, Heart Tronics stated that it had "recently commenced commercial marketing of our ... Fidelity

100 Monitor System, and recorded our first revenues from product sales in October 2006." In substantially the same words, Heart Tronics repeated these disclosures in each subsequent quarterly and annual report filed with the Commission through April 3, 2008. In addition, Heart Tronics' financial statements included in the Forms 10-K filed with the Commission on April 2, 2007 and April 3, 2008 reported revenue from product sales of $190,170 in 2006, driven primarily by this purported sale. This was the only sales revenue recorded by Heart Tronics in its corporate history; the Company never completed any further sales to any customer. The repeated reporting of this sales revenue from the purported sale to the Doctor, without disclosing the true facts surrounding the purported sale or its financing (including the fact that it was a related-party transaction), was materially false and misleading.

B. Fraudulent Disclosure of Two Additional Fictitious Sales in September 2007

1. Fraudulent Sale to "Cardiac Hospital Management"

40. On approximately September 14, 2007, Heart Tronics contracted to sell approximately $2 million worth of its Fidelity 100 product to an individual located in Portland, Oregon (the "Customer"), who had a prior relationship with Lowell Harmison, then the CEO of Heart Tronics. More specifically, the Customer signed an order to purchase 180 units of the Fidelity 100 for $1,980,000. Stein negotiated and drafted the purchase order with the Customer, and it was signed on behalf of Heart

Tronics by Harmison. The Customer sent Heart Tronics a personal check for $50,000 as a deposit for the units.

41. Heart Tronics disclosed the sales order in a press release dated September 20, 2007 and in the following periodic reports filed with the Commission: (a) Form 10-Q filed November 14, 2007; (b) Form 10-K filed April 3, 2008; (c) Form 10-Q filed May 15, 2008; and (d) Form 10-Q filed August 15, 2008. These disclosures were drafted by Stein, or by others based solely on information provided by Stein. As discussed further below, each of these disclosures was materially false and misleading.

42. Although the Customer contracted to purchase the units in his personal capacity for use in the medical supply business he owned, the purchase order that was counter-signed by Harmison and returned to the Customer identified the Customer as "Cardiac Hospital Management" ("CHM"). CHM is a fictitious entity that was not known to the Customer.

43. At the time of the signing of the purchase order, Stein and Harmison falsely told the Customer that the Fidelity 100 units were fully manufactured and ready to be shipped. Over the subsequent months, however, Heart Tronics failed to ship any product to the Customer, blaming the delay on manufacturing problems beyond its control. Accordingly, the Customer terminated the purchase order and had no further contact with Heart Tronics or its officers. Heart Tronics did not return the Customer's deposit.

44. When it became clear that Heart Tronics could not deliver the product and the Customer was canceling his order, Stein orchestrated an elaborate

scheme to mislead Heart Tronics' officers, its auditors, and the public about the sale's continued viability. The ruse began with a letter dated December 31, 2007, purportedly sent from "CHM," the nominal purchaser inserted on the Customer's September 14,2007 sales order, indicating that CHM intended for the sale to move forward. The letter provided a "new address" in Tokyo, Japan, and was signed in the name of "Toni Nonoy," the purported purchasing agent of CHM.

45. In fact, this letter was one of many bogus documents created by Stein and Carter to create the illusion that Heart Tronics had a viable sales order. Stein provided the fraudulent letter to Heart Tronics' officers, and the false document was retained in the Company's books and records as support for the continued disclosure of the pending sale.

46. By March 2008, Heart Tronics still had not shipped any product to CHM which, as discussed above, did not exist. However, Stein sought to ensure that the pending purchase order was still included in the Company's public filings with the Commission because reporting sales orders would inflate the price of Heart Tronics' stock and potentially attract new investors or customers.

47. Given the materiality of the $1.98 million dollar sales order to the Company's financial disclosures, in connection with preparing the Company's disclosures in the Form 10-K to be filed in April 2008, Heart Tronics' CFO and Disclosure Lawyer sought to obtain confirmation from CHM of its intention to complete the purchase. Stein provided them with a toll-free fax number, purportedly for CHM, to which they could send such a request for

confirmation. On March 21, 2008, the Disclosure Lawyer and CFO faxed a confirmation letter to CHM at the number that had been provided by Stein. Unbeknownst to the Disclosure Lawyer or CFO, the toll-free number had, in fact, been registered by Carter at Stein's request as part of the scheme to continue the facade that there was a legitimate purchaser on the other end of the CHM sales order.

48. On March 25, 2008, a confirmation letter, purportedly signed by CHM's "Tony Nony" (a different spelling of the name of the purported CHM purchasing agent) was returned to the Disclosure Lawyer and CFO by facsimile. In fact, Carter, pretending to be "Tony Nony," fraudulently signed and transmitted the false confirmation letter to the Disclosure Lawyer and CFO at Stein's direction. Indeed, the fax number from which the facsimile was sent was registered to Carter's residence in Boca Raton, Florida.

49. Over the ensuing months, Carter and Stein prepared other false documents to give the impression to Heart Tronics' officers, as well as the public, that the CHM sale was still viable. For example, in June 2008, Stein gave Carter an envelope addressed to Heart Tronics and instructed him to travel to Tokyo, Japan to mail the letter back to Heart Tronics to create the appearance that it originated from Japan. Carter made a one-day round trip to Japan in approximately July 2008 to carry out Stein's instructions.

50. Harmison, the CFO, the Disclosure Lawyer, and Heart Tronics' auditors relied on the false documents prepared by Stein and Carter in preparing and filing the Company's 2007 Form 10-K and Form

10-Qs for the fiscal quarters ended September 30,2007, March 31, 2008, and June 30, 2008 (filed on April 3, 2008, November 14, 2007, May 15, 2008, and August 15, 2008, respectively). In each of those filings, Heart Tronics fraudulently reported that it had a significant pending purchase order with a hospital/medical group purchasing organization (CHM) with expected gross proceeds of $1,980,000. Because the Company did not otherwise have sales revenue, the repeated false and misleading disclosure of these pending sales orders was plainly material.

2. Fraudulent Sale to "IT Healthcare"

51. Meanwhile, at the same time he was orchestrating the scheme with respect to CHM, Stein orchestrated a similar scheme with respect to a second fictional sales order.

52. On approximately September 24, 2007, Heart Tronics purportedly entered into an order to sell 300 units of the Fidelity 100 to an Israeli entity called "IT Healthcare" for $3.3 million. On October 4, 2007, the Company purportedly entered into a follow-on sales order with IT Healthcare for an additional 47 units for $564,000.

53. The sales were disclosed to the public by the Company in press releases drafted by Stein, or by others based solely on information provided by Stein, dated September 25, 2007, and October 10, 2007. The Company also disclosed the pending sales in the following periodic reports filed with the Commission: (a) Form 10-Q filed November 14, 2007; (b) Form 10-K filed April 3, 2008; (c) Form 10-Q filed May 15, 2008; and (d) Form 10-Q filed August 15, 2008.

54. However, IT Healthcare was a fictional company and not a *bona fide* purchaser of Heart Tronics' products.

55. Prior to this supposed sales order by IT Healthcare, Heart Tronics had only recognized nominal revenue from product sales related to the purported sale involving the Doctor and the Leasing Company in 2006. Even the supposed sales order by CHM was valued at only approximately half the value of the IT Healthcare order. Therefore, the press releases and Commission filings disclosing the pending sale to IT Healthcare were material.

56. Stein and Carter fabricated and executed documents related to this transaction, including the sales orders, confirmations, and shipping instructions, in the name of fictitious people supposedly affiliated with IT Healthcare, just as they did for the CHM sale. As with the fake CHM documents, several documents supposedly written by an officer of IT Healthcare contained disparate spellings of that person's name.

57. As with the disclosure of the CHM sale, in early 2008, Heart Tronics' Disclosure Lawyer and CFO sought confirmation that the purported sales orders from IT Healthcare were still viable prior to disclosing them in the Company's public filings with the Commission, because the large sales orders would be material to investors. Accordingly, they sent a letter to IT Healthcare, via a facsimile number provided by Stein, requesting the customer confirm its intention to complete the sales. In reply, the Disclosure Lawyer and CFO received a facsimile containing a signed confirmation and other correspondence purportedly from IT Healthcare.

58. In reality, just like the earlier confirmation from CHM, this facsimile was a false confirmation sent by Carter at Stein's instruction from the telephone line registered at Carter's home in Boca Raton, Florida.

59. To enhance the illusion of legitimacy regarding the pending sales orders to IT Healthcare, on approximately March 28, 2008 and April 4, 2008, the Company made two shipments of Fidelity 100 units to the fictitious IT Healthcare. On May 15, 2008, Heart Tronics filed its Form 10-Q for the quarter ended March 30, 2008, in which it publicly disclosed that it had begun shipping product to customers. Heart Tronics also issued a press release dated March 25, 2008 announcing that the Company "has been and continues to ship orders," although the press release pre-dated by several days actual tender of boxes to the carrier for shipment. Regardless, for the reasons stated below, these disclosures were materially false and misleading.

60. While the Company did actually ship approximately 15 Fidelity 100 units to the attention of "IT HealthCare-Agency Division" at an address in Loveland, Ohio, this address was not associated with any bona fide purchaser. Instead, this address was the residence of Carter's high school friend, who ran a landscaping business from his home. Stein and Carter had arranged for Carter's friend to store the shipment of boxes as a personal favor. To further conceal the scheme, the telephone number for IT Healthcare that appeared on the shipping instructions was another toll-free telephone number registered by Carter at Stein's direction.

61. In approximately July or August 2008, acting at Stein's direction, Carter collected the boxes from his friend, tampered with the product to create the appearance that they were defective, and returned the units to the contract manufacturer as if they were coming from IT Healthcare. Then, on August 15, 2008, Heart Tronics filed its Form 10-Q for the quarter ended June 30, 2008, in which it stated that it had "commenced shipments on the September 24, 2007 order, however, they were returned by the lessee on the basis that too much time had passed since the purchase order was given."

62. In fact, this disclosure was materially false and misleading, as it implicitly represents that the products were shipped to a *bona fide* purchaser, .and this was not the reason that the Fidelity 100 units had been returned. Rather, Stein caused the units to be returned to delay further discovery of his fraudulent scheme. Indeed, once shipped, Heart Tronics' officers, auditors and investing public would expect to see revenue recognized in the Company's financial statements from the sale; but because Stein knew that the customer was non-existent and the sales order was fictitious from the start, he concocted the scheme to have Carter return the product to the manufacturer as untimely and apparently defective.

C. Fraudulent Disclosure of Further Sales Orders and Projected Revenue in 2008

63. In Spring 2008, at the same time that he was providing false information to Heart Tronics officers and the public about the purported sales orders to CHM and IT Healthcare, Stein caused the

Company to make false and misleading statements about additional fraudulent sales orders designed to inflate the price of Heart Tronics stock.

64. On approximately March 17, 2008, Heart Tronics issued a press release announcing that it "has received several formal purchase and financial commitments.... These commitments have come internationally, including in Japan, other parts of Asia and Europe, as well as domestically." On March 25, 2008, the Company issued a press release announcing that it "has received an additional $7.5 million in Fidelity 100 device delivery orders in the month of March, 2008, which the company intends to fill during the next two quarters. The Company said it may fill these orders sooner." Both press releases were drafted by Stein, or by others based solely on information provided by Stein. Both were materially false and misleading.

65. In fact, Heart Tronics had not entered into formal purchase or financial commitments. Rather, Stein—acting for the Company—had obtained only (1) a preliminary agreement with a Korean company regarding that company becoming a distributor of Heart Tronics' products in Asia, and (2) a one-page "purchase commitment" letter from a company identified as A.R. Pacific Group ("ARPG") that claimed to be based in Japan and was purportedly signed by someone with the name as a person affiliated with CHM. In addition, Stein reported to Harmison and others that he had reached an agreement with an unnamed Chinese company to purchase approximately $180 million worth of Heart Tronics' products. In all three cases, no formal orders

for Fidelity 100 units were placed, no monies were received, and no products were shipped. These unsubstantiated, preliminary, and ultimately illusory sales orders were the basis for the Company's several false or misleading public announcements.

66. As he did with respect to the purported purchase orders involving CHM and IT Healthcare, the Disclosure Lawyer requested supporting documentation from Stein related to the purported sales to ARPG for the Company's forthcoming annual report on Form 10-K for the year ended December 31, 2007. Stein did not provide any additional information, and the Disclosure Lawyer refused to include any statements about the purported sale in the Company's annual report.

67. On April 14, 2008, however, Harmison held a public "webcast" over the Internet in which he provided investors with guidance on Heart Tronics' projected revenue for the rest of the Company's fiscal year. The script for the webcast was drafted by Stein and Harmison. Harmison announced more than $40 million of expected revenue for Heart Tronics over the next five fiscal quarters. Harmison claimed this figure was related to the supposed transactions with the Korean, Japanese and Chinese companies described above. Neither Stein nor Harmison had any basis for these projections, which were materially false and misleading.

68. Following the webcast, Heart Tronics directors, including Perkins, exchanged emails revealing skepticism of the revenue projections Harmison had made. They professed concern about

Harmison and Stein's ongoing involvement with the Company.

69. In late April 2008, Harmison resigned as CEO. Perkins became the interim and, subsequently, the permanent CEO. In addition, the Company hired an outsider as the Company's new President.

70. In May 2008, the new President began to investigate the 2007 and 2008 sales orders described above (which were still described in the Company's public filings with the Commission as "pending purchase orders," but for which the Company still had not recognized any revenue). In doing so, he discovered that the product supposedly shipped to IT Healthcare had, in fact, been shipped to a residential address in Ohio. He further questioned why the owner of the property, whom he discovered ran a lawn maintenance business, would have any reason to purchase approximately $3.8 million worth of medical equipment. He brought this information to Perkins' and Stein's attention, but he was told to stop investigating and was accused by Stein of trying to damage the Company. Shortly thereafter, the new President resigned from the Company.

71. By no later than May 2008, when he took over for Harmison as interim CEO of the Company, Perkins knew or was reckless in not knowing that Heart Tronics disclosures regarding pending sales of Fidelity 100 units were false and misleading.

72. Despite being aware of these significant red flags and his admitted "skeptical" view of the sales, Perkins authorized the IT Healthcare and CHM sales orders to be disclosed in the Form 10-Qs for the first and second fiscal quarters of 2008, which he

signed and which were filed with the Commission on May 15, 2008, and August 15, 2008, respectively. Perkins took no steps to determine the validity of the purportedly pending sales orders or the projections announced by Harmison on behalf of the Company in April 2008. Nor did Perkins take any steps to implement or improve upon the Company's internal controls over financial reporting.

73. When questioned by the Commission staff about the decision by Perkins and other board members not to take any steps to verify the purportedly pending sales orders or Harmison's claims in the webcast, Perkins testified: "We didn't do anything to—I mean, we didn't know what to do, what could you do. I mean, we didn't want to put fuel on the fire. I mean, if you—what are you going to do, come out and say it's wrong? We didn't know what to do. We figured doing nothing was the best way to handle it."

D. Hiring of Stock Promoters to Tout Heart Tronics Stock

74. At the same time that he was leading a campaign of misinformation about the success of Heart Tronics, Stein enlisted the assistance of several stock promoters to tout Heart Tronics' stock on the Internet.

75. On approximately January 30, 2008, at Stein's direction, Heart Tronics entered into a consulting agreement with a former securities research analyst, defendant Ryan Rauch, purportedly for investor relations and corporate strategy consulting.

76. In reality, Rauch was a stock promoter. Rauch solicited investment advisers, retail and

institutional brokers, and other potential investors to buy Heart Tronics stock for themselves or for their clients' accounts.

77. Stein falsely told Rauch that Heart Tronics would imminently announce up to $100 million in sales and that the Company's stock price was artificially depressed by naked short sellers. From approximately January through April 2008, Rauch repeated this information to numerous potential investors, or their brokers or investment advisers, to encourage them to buy Heart Tronics stock. In particular, Rauch encouraged investors to enter orders to buy Heart Tronics stock at or near the time of the market close to attempt to increase the closing price of Heart Tronics' stock.

78. Heart Tronics paid Rauch $75,000 over three months, with a promise of a $250,000 bonus if he could keep the Company's stock price above $1 per share for a period of 30 days, which was one criterion for Heart Tronics to retain its listing on the AMEX. Rauch generally did not disclose to potential investors that he was being compensated by the Company for promoting Heart Tronics stock.

II. Schemes to Profit from Sales of Heart Tronics Stock

79. While he was seeking to inflate the price of Heart Tronics stock through the assorted deceptive tactics, materially false and misleading statements, fraudulent schemes, and other means described above, Stein devised numerous ways to profit illicitly from the sale of Heart Tronics securities.

A. Fraudulent Scheme to Secretly Sell Heart Tronics Stock

80. Stein's primary method of profiting from his scheme was to direct the sale of Heart Tronics stock held by relief defendant ARC Finance, a single-member limited liability company solely owned by his wife, Hampton-Stein.

81. ARC Finance had been the majority shareholder of Heart Tronics since September 2002, when it sold to the Company's predecessor the rights to proprietary technology, valued at $78,023, in exchange for 23.4 million shares of common stock (approximately 85% of the Company's outstanding equity).

82. Although Stein did not file any required forms with the SEC disclosing a beneficial ownership position in Heart Tronics, Stein controlled the voting of ARC Finance's shares and controlled the investment decisions of ARC Finance's assets.

83. On June 29,2005, Heart Tronics registered the resale of 3.5 million of the shares held by ARC Finance with the Commission on Form SB-2. From July 2005 to October 2005, ARC Finance directly sold 344,200 registered shares of Heart Tronics stock for a profit of approximately $1.2 million.

84. Beginning in approximately December 2005, however, Stein devised a scheme to sell ARC Finance's shares without publicly reporting the sales, as required under the federal securities laws. The scheme allowed Stein to create the appearance that ARC Finance was not selling the previously-registered shares but, rather, holding them as a long-term investment.

85. Beginning in approximately December 2005, ARC Finance transferred a portion of its holdings to two purportedly blind trust accounts, relief defendants ARC Blind Trust and the THS Blind Trust, established for the benefit of ARC Finance and Stein, respectively. Defendant Mark Nevdahl was appointed trustee for each trust, and also served as the securities broker for each trust. This created the appearance that the stock was held by independent legal entities controlled by Nevdahl and that neither ARC Finance nor Stein had control over the disposition of the trusts' assets.

86. Nevdahl frequently discussed the accounts he managed for the Steins, including the ARC Blind Trust and the THS Blind Trust, with Stein via telephone, e-mail and correspondence sent via the mails. On at least two occasions, Nevdahl met with the Steins regarding the management of their investment accounts at their home in Hidden Hills, California.

87. Notwithstanding the fact that the trusts were purportedly blind, ARC Finance, through Stein and his wife, retained control over the shares that were transferred to these trusts. At Stein's direction, Nevdahl did not re-title the securities in the name of the trusts. In addition, although the trusts were purportedly "blind," Nevdahl took explicit instructions from Stein over the trusts' corpus. Among other things, Stein (1) told Nevdahl to generate enough cash (necessitating the sale of stock) each month to meet the Steins' lifestyle demands; (2) told Nevdahl how to vote shares on proxy ballots; and (3) negotiated "private placements" to sell shares held by one of the trusts in off-the-market transactions. Stein also

directed Nevdahl to wire the proceeds generated by Nevdahl's share sales to bank accounts in the name of Stein and ARC Finance. Thus, Nevdahl knew that the purportedly blind trusts were not, in fact, blind.

88. Although the trust indentures placed the obligation on Nevdahl (as trustee) to file reports of any transactions in the trusts required by the federal securities laws, Stein informed Nevdahl that the sales within the trusts were exempt from the reporting requirements under Section 16 of the Exchange Act because the trusts were blind and held less than 10% of Heart Tronics' equity. In light of his knowledge that the trusts were not, in fact, blind, Nevdahl knew, or was reckless in not knowing, that the transactions were not exempt and that the he was participating in a fraudulent effort to use the trusts to evade the reporting requirements under the federal securities laws.

89. Nevdahl performed no independent analysis of this and other issues pertaining to propriety of the trusts' stock sales, nor did he seek approval from his firm's legal or compliance departments.

90. Between approximately December 2005 and September 2008, the Steins, through transactions executed by Nevdahl, covertly sold more than 3.7 million shares of Heart Tronics stock through the ARC Blind Trust and the THS Blind Trust, for more than $5.8 million. Because the shares had a cost basis of approximately $0.005 per share, nearly all the proceeds were profit.

91. Neither Stein, ARC Finance, ARC Blind Trust nor THS Blind Trust filed any reports with the Commission on Forms 3, 4 or 5 during this period.

92. Nevdahl was paid brokerage commissions of approximately $78,000, in addition to trustee fees, for his work as trustee and broker for the purportedly blind trusts.

93. Stein used the purportedly "blind" nature of the trusts to intentionally mislead investors regarding ARC Finance's share position in Heart Tronics' periodic reports filed with the Commission. For example, the Company disclosed in its annual report on Form 10-K for 2007, filed on April 3, 2008, that "[a]s of this date neither ARC Finance Group nor [Heart Tronics] knows if the independent trustees have sold any of such shares or, in the alternative, increased their position. ARC Finance Group ... to our knowledge [] has not, to date, sold those shares." Stein reviewed the Company's Commission filings during 2006 and 2007 and knew that the filings were materially false and misleading. Stein knew or was reckless in not knowing that, contrary to the disclosures in Heart Tronics' periodic filings, shares of Heart Tronics stock under the control of ARC Finance were being continuously sold into the market through the ARC Blind Trust and THS Blind Trust and that Nevdahl was wiring the proceeds of the sales to the Steins' bank accounts.

94. Between approximately March 2008 and May 2008, ARC Finance also transferred more than 10 million shares of Heart Tronics stock to three additional trusts: relief defendants JAYMI Blind Trust, Oak Tree Investments Blind Trust, and the

WBT Investments Blind Trust. Nevdahl was the broker and trustee for the JAYMI Blind Trust, Oak Tree Investments Blind Trust and WBT Investments Blind Trust as well. On April 14, 2008, the same day as the webcast in which Harmison announced revenue projections of $40 million, Nevdahl sold 25,000 shares of Heart Tronics stock on behalf of the JAYMI Blind Trust.

B. Schemes to Sell Improperly Registered S-8 Stock

95. In addition to profiting from the sale of Heart Tronics shares held by ARC Finance through the scheme described above using the trusts, Stein devised a scheme to profit from stock Heart Tronics issued to Carter from transactions registered with the Commission on Form S-8.

96. Starting in 2006, Heart Tronics had registered millions of shares of Heart Tronics stock on Form S-8 registration statements filed with the Commission on June 12, 2006, October 11, 2006, November 20, 2006, May 19, 2008, and November 5, 2008. These shares were purportedly to be issued pursuant to the Company's Omnibus Equity Compensation Plan.

97. Form S-8 is available to register the offer and sale of a company's stock to employees or consultants under certain circumstances. The eligible employees or consultants must perform permissible, bona fide services that are not in connection with a capital raising transaction and do not indirectly promote or maintain a market for the stock.

98. FormS-8 is not available to register offers and sales of securities to consultants where, by prearrangement or otherwise, the issuer or a promoter controls or directs the resale of the securities in the public market, or the issuer or its affiliates directly or indirectly receive a percentage of the proceeds from such resales. In addition, consultants who provide investor relations or shareholder communications services may not receive S-8 stock because of the promotional nature of their services.

99. An improper use of S-8 shares—i.e., under the prohibited circumstances described below - is not an effective registration of the S-8 shares, or their subsequent sale, under Section 5 of the Securities Act.

100. In approximately January 2008, Stein drafted and caused Heart Tronics to enter into a consulting agreement by which Heart Tronics hired Carter to consult on product engineering and design with the intention that Carter would be compensated primarily with S-8 stock. In fact, Carter lacked the education, skills and resources to provide the services described in the contract, and he provided no services to Heart Tronics under the contract.

101. Notwithstanding the fact that Carter provided no meaningful services to Heart Tronics, between approximately November 2007 and September 2008, Heart Tronics paid Carter approximately $2 million under the consulting contract in the form of cash (approximately $600,000) and 6.035 million shares of Heart Tronics stock from transactions registered on Form S-8 (valued at approximately $1.4 7 million based on the stock price

on the date of each issuance). Stein caused the Company to instruct its transfer agent to issue the shares to Carter.

102. Between approximately January 2008 and September 2008, Carter sold substantially all the S-8 stock issued to him under his purported consulting contract in personal brokerage accounts or in accounts accessible to both him and Stein, including accounts in the name of relief defendant Five Investments Partnership. Carter then transferred substantially all of the stock, or the proceeds from the sales of the stock, to bank or brokerage accounts controlled by Stein. Accordingly, both because of these transfers and because Carter performed no bona fide services to Heart Tronics, the issuance of S-8 stock to Carter was a violation of the registration requirements of Section 5 of the Securities Act.

103. On approximately February 6, 2008, Heart Tronics also issued approximately 500,000 shares of common stock from transactions registered on Form S-8 as compensation to at least three other individuals who were hired by Stein to promote Heart Tronics stock on the Internet. Stein signed the contracts with the promoters, created false documents that identified the promoters as "subcontractors" working on engineering matters under Carter's consulting contract, and caused Heart Tronics to issue the shares to the promoters. Because these individuals were not providing permissible consulting services in exchange for the issuance of S-8 stock, these issuances were also in violation of Section 5 of the Securities Act.

III. Stein and Gault Defrauded an Individual Investor

104. In addition to the above schemes, as described in more detail below, beginning in late 2008, in connection with the purchase and sale of securities, Stein and the Company's then co-CEO, defendant Willie Gault, defrauded an individual investor in Heart Tronics out of more than $150,000 for their personal gain.

105. More specifically, between approximately November and December 2008, an individual investor (the "Investor") made private investments of more than $150,000 in Heart Tronics in exchange for a series of convertible interest-bearing note securities from the Company. In making his investment decision, the Investor relied on false statements by Stein and Gault that Heart Tronics was close to generating revenue through product sales to customers in Mexico, South America and Canada. Stein also told the Investor that Heart Tronics, which was nearly bankrupt at the time, needed an infusion of capital to fund operations while marketing the product and pursuing imminent sales leads.

106. On approximately November 4, 2008, the Investor wire transferred $100,000 to a joint bank account he established with Gault in exchange for a note security issued by the Company. Stein and Gault had represented that the funds deposited would be used to pay the Company's operating expenses while it tried to generate sales revenue to repay the note. This investment was disclosed by Heart Tronics in its Form 10-Q for the period ended September 30, 2008,

filed with the Commission on November 19, 2008, at Gault's authorization during his tenure as co-CEO.

107. In approximately December 2008, in exchange for another note, the Investor again deposited $50,000 in the joint bank account with Gault, based on Stein and Gault's representations that the funds would be used to pay Heart Tronics' operating expenses.

108. However, even though they had told the Investor that Heart Tronics would use the invested capital for corporate expenses, Stein and Gault fraudulently diverted the invested capital for their own personal use.

109. For example, on the same day as the Investor's initial transfer to the joint bank account, $20,000 was transferred to a brokerage account owned by Gault in the name of relief defendant Catch 83 General Partnership.

110. Over the next approximately two months, Gault, with Stein's knowledge and participation, transferred all or substantially all of the joint bank account's balance, without the Investor's knowledge or authorization, to his Catch 83 General Partnership brokerage account. Gault, with Stein's knowledge and participation, used the money to trade Heart Tronics' stock in his personal brokerage account.

111. None of the capital invested by the Investor was used to pay Company expenses, despite Stein and Gault's representations. The Investor suffered a complete loss of his investment.

112. Despite numerous requests from the Company's CFO, Gault refused to provide the CFO access to the joint bank account or provide an accounting of the assets in the account or a description of the use of the cash.

IV. False Statements in Commission Filings, Sarbanes-Oxley Certifications, and the Company's Accounting Books and Records

113. As described above, from late 2006 through 2008, Heart Tronics issued numerous false and misleading press releases and filed numerous false and misleading reports with the Commission, referencing the fictitious sales orders of the Fidelity 100.

114. In addition to the false and misleading public filings and announcements, Heart Tronics' books and records reflected various purchase orders, invoices, and other documents relating to fictitious sales orders described above that had purportedly been placed by customers that did not exist.

115. That is because, in part, Heart Tronics did not have reasonable accounting controls to ensure that the purported product sales in 2006 through 2008 were to bona fide customers. The Company had no written accounting policies or procedures, and the Company's most senior officers, including Gault and Perkins, exercised no independent judgment but relied solely on Stein.

116. Through Stein's control of Heart Tronics and acts of deception, Stein and Carter were able to circumvent the entire system of accounting controls, to the extent any existed, and substantially further

the Company's recording and disclosure of fraudulent sales orders. Even as the Company's officers and directors became skeptical of the pending purchase orders, Perkins knowingly failed to implement a reasonable system of internal accounting controls. Likewise, Gault knowingly circumvented the Company's internal controls to effect the fraud he committed against the Investor with Stein.

117. While most of the false press releases and reports described above were issued during Harmison's tenure as CEO, the false and misleading Commission filings continued under the leadership of Gault and Perkins after Harmison resigned in late April 2008.

118. As Heart Tronics' CEO or co-CEO from late April 2008 to the present, Perkins reviewed and signed at least three of the Company's quarterly reports filed with the Commission, which he knew or was reckless in not knowing contained materially false and misleading information concerning, among other things, its sales orders and potential customers.

119. Perkins also signed materially false and misleading certifications required by the Sarbanes-Oxley Act of 2002 ("SOX"). In SOX certifications filed with the Company's Form 10-Qs for the periods ended March 31, 2008, July 31, 2008, and September 30, 2008 (filed with the Commission on May 15, 2008, August 15, 2008, and November 19, 2008, respectively), Perkins falsely represented that based on his knowledge, each filing did not "contain any untrue statement of a material fact or [omission]." Perkins did not have a basis for these representations because the filings included disclosures of the

Company's pending sales orders, and Perkins was aware of numerous red flags concerning those disclosures—including specific information about potential fraud associated with the IT Healthcare shipments to a residential address in Ohio.

120. Further, as part of each of these filings, Perkins certified that he designed and evaluated the effectiveness of Heart Tronics' disclosure controls and procedures and internal controls over financial reporting. This certification was materially false and misleading because the Company had no reasonable system of internal controls, and Perkins undertook no effort to design, supervise or evaluate the purported controls. Perkins also falsely certified that he had disclosed to Heart Tronics' auditor and Audit Committee of the Board of Directors "any fraud, whether material or not, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting," but he failed to do so, even after the President informed him of suspected fraud in the IT Healthcare transaction and Perkins took no action.

121. Gault was designated Heart Tronics' "co-CEO for Operations" in October 2008, but he was little more than a celebrity figurehead who provided no meaningful oversight to the Company.

122. On or about November 19, 2008, Gault authorized the filing of both a Form 10-Q for the third fiscal quarter of 2008 and a SOX certification filed with the Commission on November 19, 2008, in his capacity as one of Heart Tronics' principal executive officers. In fact, Gault never manually signed any version of either document, in violation of the federal

securities laws. These documents were electronically filed with the Commission at Gault's direction under Gault's signature.

123. Gault's practice was to not review or read the periodic reports that Heart Tronics filed with the Commission, even though he was the Company's co-CEO for Operations and the reports were filed at his authorization under his signature.

124. Thus, Gault's SOX certifications were materially false and misleading. For example, contrary to his SOX certifications, Gault never actually "reviewed this quarterly report on form 10-Q," and had no basis to state "based on [his] knowledge, this report does not contain any untrue statement of a material fact or [omission]" or that "based on [his] knowledge, the financial statements... fairly present in all material respects the financial condition" of Heart Tronics. Similarly, Gault had no basis for certifying the he was responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting. Finally, Gault falsely represented that he had disclosed to the Company's auditor and Audit Committee "[a]ny fraud, whether or not material, that involves management or other employees who have a significant role in [Heart Tronics'] internal controls over financial reporting," when he did not do so, even though Gault himself defrauded an individual investor into investing money in Heart Tronics during this period.

FIRST CLAIM FOR RELIEF

Violations of Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5

(Heart Tronics, Stein, Carter, Perkins, Gault, and Nevdahl)

125. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

Employing Devices, Schemes, and Artifices to Defraud, and Engaging in Acts, Practices and Courses of Business Operating As a Fraud or Deceit in Violation of Section 10(b) and Rule 10b-5(a) and (c)

126. By reason of the conduct described above, defendants Heart Tronics, Stein, Carter, Gault, and Nevdahl, in connection with the purchase or sale of securities, by the use of the means or instrumentalities of interstate commerce or of the mails, or of any facility of any national securities exchange, directly or indirectly, knowingly or recklessly (l) employed devices, schemes, or artifices to defraud or (2) engaged in acts, practices, or course of business which operates or would operate as a fraud or deceit upon any persons, including purchasers or sellers of the securities, in violation of Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and subsections (a) and (c) of Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5(a) and (c)]. Unless enjoined, these defendants will continue to violate Exchange Act Section 10(b) and subsections (a) and (c) of Exchange Act Rule 10b-5.

Making Misrepresentations and Misleading Omissions of Material Fact in Violation of Section 10(b) and Rule 10b-5(b)

127. By further reason of the conduct described above, defendants Heart Tronics, Stein, Gault, and Perkins in connection with the purchase or sale of securities, directly or indirectly, by the use of the means or instrumentalities of interstate commerce, or of the mails, or of any facility of any national securities exchange, knowingly or recklessly, made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, in violation of Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and subsection (b) of Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5(b)].

128. More specifically, these defendants violated and, unless enjoined, will continue to violate, Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and subsection (b) of Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5(b)] by the following:

(a) Heart Tronics, through the actions of its officers, directors, employees, attorneys, agents, and controlling person, including but not limited to the issuance of materially false and misleading press releases, Commission filings, and other public broadcasts described above.

(b) Stein's actions including but not necessarily limited to making false and misleading statements about Heart Tronics to an Investor in late 2008.

(c) Gault's actions including, but not necessarily limited to (1) making false and misleading statements about Heart Tronics

to an Investor in late 2008; and (2) authorizing the issuance a false and misleading periodic report filed with the Commission on Form 10-Q for Heart Tronics' fiscal quarter ended September 30, 2008, including the SOX certifications included therewith, under his signature.

(d) Perkins actions, including but not necessarily limited to signing false and misleading periodic report filed with the Commission on Form 10-Q for Heart Tronics' fiscal quarter ended March 31, 2008, June 30, 2008, and September 30, 2008, including the SOX certifications included therewith.

SECOND CLAIM FOR RELIEF

Violations of Section 17(a) of the Securities Act

(Heart Tronics, Stein, Gault, Carter, and Nevdahl)

129. Paragraphs 1 through 124 are realleged and are incorporated herein by reference.

130. Defendants Heart Tronics, Stein, Gault, Carter, and Nevdahl have, directly or indirectly, by use of means of instrumentalities of transportation or communication in interstate commerce or by use of the mails, in the offer or sale of securities: (a) knowingly or recklessly employed devices, scheme or artifices to defraud; (b) knowingly, recklessly, or negligently obtained money or property by means of any untrue statements of material fact, or have omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c)

knowingly, recklessly or negligently engaged in transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon the purchasers of securities; in violation of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

131. More specifically, defendants Heart Tronics, Stein, Gault, Carter, and Nevdahl violated and, unless enjoined, will continue to violate, Sections 17(a)(1) and 17(a)(3) of the Securities Act [15 U.S.C. § 77q(a)] by employing the fraudulent schemes and other activities described above.

132. Furthermore, defendants Heart Tronics, Stein, and Gault violated and, unless enjoined, will continue to violate, Section 17(a)(2) of the Securities Act [15 U.S.C. § 77q(a)] by obtaining money and property by means of the various materially false and misleading press releases, Commission filings, and other public broadcasts described above, as well as the false and materially misleading statements in late 2008 to an Investor.

THIRD CLAIM FOR RELIEF

Aiding and Abetting Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder

(Stein, Carter, Gault, and Nevdahl)

133. Paragraphs 1 through 124 and paragraphs 126 through 128 above are realleged and incorporated by reference.

Primary Violations by Heart Tronics and Stein

134. By reason of the conduct described above, and particularly as set forth in the First Claim for Relief above, Heart Tronics and Stein violated Section

10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

Defendants Knowingly Provided Substantial Assistance to the Primary Violations

135. Defendant Stein, acting knowingly, provided substantial assistance to Heart Tronics' violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], by his actions described above.

136. Defendant Carter, acting knowingly, provided substantial assistance to Heart Tronics' and Stein's violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], by his actions described above.

137. Defendant Gault, acting knowingly, provided substantial assistance to Heart Tronics' and Stein's violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], by his actions described above.

138. Defendant Nevdahl, acting knowingly, provided substantial assistance to Stein's violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], by his actions described above.

139. Accordingly, Stein, Carter, Gault, and Nevdahl aided and abetted the primary violations described above and, pursuant to Section 20(e) of the Exchange Act [15 US.C. § 78t(e)], Stein, Carter, Gault, and Nevdahl are liable for such violations.

140. Unless restrained and enjoined, Stein, Carter, Gault and Nevdahl will continue to aid and abet, or will in the future aid and abet, violations of

Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

FOURTH CLAIM FOR RELIEF

Controlling Person Liability for Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder

(Stein)

141. Paragraphs 1 through 124 and paragraphs 126 through 128 above are realleged and incorporated by reference.

142. Stein (a) directly or indirectly controlled Heart Tronics; (b) possessed the power and ability to control Heart Tronics as to its violation of Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5; (c) was in a meaningful sense a culpable participant in Heart Tronics' violations of Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5, including by knowingly authorizing and causing Heart Tronics to issue false and misleading statements in press releases, Commission filings and other public broadcasts.

143. Stein is jointly and severally liable with and to the same extent as Heart Tronics for Heart Tronics' violations of Exchange Act Section 10(b) and Exchange Act Rule 10b-5, as stated above in the First Claim for Relief.

144. By engaging in the conduct described above, Stein is liable as a controlling person pursuant to Section 20(a) of the Exchange Act [15 U.S.C. § 78t(a)] by controlling, and possessing the power and ability to control, Heart Tronics in its violation of Exchange Act Section 10(b) and Rule 10b-5.

145. Unless enjoined, Stein will again engage in conduct that would render him liable, under Section 20(a) of the Exchange Act, for violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

FIFTH CLAIM FOR RELIEF

Violations Section 5(a) and 5(c) of the Securities Act

(Heart Tronics, Stein and Carter)

146. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

147. Defendants Heart Tronics, Stein and Carter directly or indirectly, singly or in concert with others: (1) without a registration statement in effect as to the securities transaction, (a) made use of the means or instrumentalities of transportation or communication or the mails in interstate commerce to sell securities through the use or medium of a prospectus or otherwise, or (b) carried or caused to be carried such securities for the purpose of sale or for delivery after sale; and (2) made use of the means or instrumentalities of transportation or communication or the mails in interstate commerce to sell or offer to buy through the use or medium of a prospectus or otherwise securities as to which a registration statement had not been filed as to such securities.

148. By engaging in the conduct described above regarding the unlawful issuance and sale of shares of Heart Tronics stock from transactions registered on Form S-8 pursuant to sham consulting agreements, defendants Heart Tronics, Stein and Carter violated and, unless enjoined will continue to

violate, Sections 5(a) and (c) of the Securities Act [15 U.S.C. § 77e(a) & (c)].

SIXTH CLAIM FOR RELIEF

Violations of Section 13(a), 13(b)(2)(A), 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 12b-ll, 12b-20, 13a-l, 13a-ll, and 13a-13

(Heart Tronics)

149. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

150. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.13a-1, 240.13a-11, and 240.13a-13] require issuers of securities registered pursuant to Section 12 of the Exchange Act to file with the Commission accurate periodic reports. Exchange Act Rule 12b-20 [17 C.F.R. § 240.12b-20] requires that periodic reports contain any additional material information necessary to make the required statements made in the reports not materially misleading. Exchange Act Rule 12b-11 [17 C.F .R. § 240.12b-11] requires any document required to be filed with or furnished to the Commission "shall be manually signed," or the "signatory to the filing shall manually sign a signature page or other document authenticating, acknowledging or otherwise adopting his or her signature that appears in the filing."

151. As set forth above, defendant Heart Tronics filed reports with the Commission that contained materially false and misleading statements and information, and failed to include additional material necessary to make the statements and information, in light of the circumstances in which

they were made, not misleading, in violation of Section 13(a) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13.

152. In addition, as set forth above, from at least December 2005 through December 2008, defendant Heart Tronics failed to (a) maintain and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflected the transactions and dispositions of its assets, and (b) devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that: (i) transactions were executed in accordance with management's general or specific authorization; (ii) transactions were recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and to maintain accountability for assets; (iii) access to assets was permitted only in accordance with management's general or specific authorization; and (iv) the recorded accountability for assets was compared with the existing assets at reasonable intervals and appropriate action was taken with respect to any differences. As a result, Heart Tronics violated Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

153. Furthermore, set forth above, Heart Tronics failed to obtain and retain manual signatures on its documents filed with or furnished to the Commission, or obtain and retain a signature page or other document authenticating, acknowledging or otherwise adopting each signatory's signature that appears in the filing. Heart Tronics failed to furnish to

the Commission staff, upon its request, a copy of any or all documents retained pursuant to Exchange Act Rule 12b-11. As a result, it violated Exchange Act Rule 12b-11.

154. By reason of the foregoing, Heart Tronics violated and, unless enjoined, will continue to violate Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Exchange Act Rules 12b-11, 12b-20, 13a-1, 13a-11, and 13a-13.

SEVENTH CLAIM FOR RELIEF

Aiding and Abetting Heart Tronics' Violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 13a-1, 13a-11, 13a-13, and 12b-20

(Stein, Perkins, and Carter)

155. Paragraphs 1 through 124 and paragraphs 150 through 154 are realleged and incorporated herein by reference.

156. As set forth in the Sixth Claim for Relief above, defendant Heart Tronics violated Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)] and Exchange Act Rules 13a-1, 13a-11, 13a-13, and 12b-20 [17 C.F.R. §§ 240.13a-1, 240. 13a-11, 240. 13a-13, and 240.12b-20].

157. Based on the facts set forth above, defendants Stein, Perkins and Carter knowingly provided substantial assistance to defendant Heart Tronics in the commission of certain of these violations. More specifically:

a) Stein, acting knowingly, substantially assisted Heart Tronics' violations of Sections 13(a),

13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 13a-1, 13a-11, 13a-13, and 12b-20. Accordingly, Stein is liable for such violations pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)]. Unless restrained and enjoined, Stein will continue to aid and abet, or will in the future aid and abet, these violations.

b) Carter, acting knowingly, substantially assisted Heart Tronics' violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Exchange Act Rules 13a-1, 13a-11, 13a-13, and 12b-20. Accordingly, Carter is liable for such violations pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)]. Unless restrained and enjoined, Carter will continue to aid and abet, or will in the future aid and abet, these violations.

c) Perkins, acting knowingly, substantially assisted Heart Tronics' violations of Section 13(b)(2)(B) of the Exchange Act. Accordingly, Perkins is liable for such violation pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)]. Unless restrained and enjoined, Perkins will continue to aid and abet, or will in the future aid and abet, this violation.

EIGHTH CLAIM FOR RELIEF

Violations of Exchange Act Rule 13b2-1

(Stein and Carter)

158. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

159. Defendants Stein and Carter directly or indirectly falsified or caused to be falsified books, records or accounts of Heart Tronics that were subject

to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

160. By engaging in the conduct described above, defendants Stein and Carter violated and, unless enjoined, will continue to violate Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

NINTH CLAIM FOR RELIEF

Violations of Section 13(b)(5) of the Exchange Act

(Stein, Gault, Perkins, and Carter)

161. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

162. Defendants Stein, Gault, Perkins and Carter knowingly circumvented or knowingly failed to implement a system of internal accounting controls or knowingly falsified, directly or indirectly, or caused to be falsified books, records or accounts of Heart Tronics maintained pursuant to Section 13(b)(2) of the Exchange Act.

163. By engaging in the conduct described above, defendants Stein, Gault, Perkins and Carter violated and, unless enjoined, will continue to violate Section 13(b)(5) [15 U.S.C. § 78m(b)(5)] of the Exchange Act.

TENTH CLAIM FOR RELIEF

Violations of Exchange Act Rule 13a-14

(Gault and Perkins)

164. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

165. Gault violated Rule 13a-14 of the Exchange Act [17 C.F.R. § 240.13a-14] by providing a

certification required by that rule to be signed on his behalf, pursuant to a power of attorney or other form of confirming authority, and by failing to manually sign the required certification included in Heart Tronics' quarterly report on Form 10-Q for the third fiscal quarter of 2008 filed with the Commission on November 19, 2008.

166. In addition, Gault violated Rule 13a-14 by falsely certifying, among other things, (1) that the forms fully complied with the requirements of the Exchange Act and fairly presented, in all material respects, the financial condition and results of operations of the company when, in fact, the reports contained untrue statements of material fact and omitted material information necessary to make the reports not misleading; and (2) that he and other officer(s) of Heart Tronics had designed disclosure controls and procedures and internal controls over financial reporting, had evaluated such controls and procedures, and had identified no deficiencies when, in fact, Gault had done no such thing.

167. Perkins violated Rule 13a-14 by signing Heart Tronics' quarterly reports on Form 10-Q for the first, second, and third fiscal quarters of 2008 (filed with the Commission on May 15, 2008, August 15, 2008, and November 19, 2008, respectively) certifying, among other things, (1) that the forms fully complied with the requirements of the Exchange Act and fairly presented, in all material respects, the financial condition and results of operations of the company when, in fact, the reports contained untrue statements of material fact and omitted material information necessary to make the reports not misleading; and (2)

that he and other officer(s) of Heart Tronics had designed disclosure controls and procedures and internal controls over financial reporting, had evaluated such controls and procedures, and had identified no deficiencies when, in fact, Perkins had done no such thing.

168. By engaging in the conduct described above, defendants Gault and Perkins violated Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14]. Unless enjoined, defendants Gault and Perkins will continue to violate Rule 13a-14 [17 C.F.R. § 240.13a-14].

ELEVENTH CLAIM FOR RELIEF

Violation of Section 302(b) of Regulation S-T

(Heart Tronics)

169. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

170. Defendant Heart Tronics violated Section 302(b) of Regulation S-T by failing to ensure that all signatories of the certifications for its quarterly report on Form 10-Q for the third fiscal quarter of 2008 (filed with the Commission on November 19, 2008) had signed the certifications before or at the time they were electronically filed, and by failing to retain the original executed documents for five years, or to provide the Commission staff with copies of the documents upon request.

171. Unless restrained and enjoined, Heart Tronics will continue to violate Section 302(b) of Regulation S-T [17 C.F.R. § 232.302(b)].

TWELFTH CLAIM FOR RELIEF

Violations of Exchange Acts Section 13(d) and 16(a) and Rules 13d-1 and 16a-3 thereunder

(Stein)

172. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

173. By means of his indirect control over the blind trusts that he created to sell Heart Tronics stock held beneficially by his wife, Stein was the beneficial owner of more than 10% of Heart Tronics stock. Pursuant to Section 13(d) of the Exchange Act [15 U.S.C. § 78m(d)] and Rule 13d-1 thereunder [17 C.F.R. § 240.13d-1] Stein was required to disclose his status as a beneficial owner of more than 5% of Heart Tronics' equity by filing the required forms with the Commission within 10 days of his becoming such a beneficial owner. Stein never did so. As a result, Stein violated and, unless enjoined, will continue to violate Section 13(d) of the Exchange Act and Rule 13d-1 thereunder.

174. Moreover, not only did Stein beneficially own more than 10% of Heart Tronics' common stock, as set forth above, Stein was a de facto officer of Heart Tronics, in that he performed policy-making functions for Heart Tronics akin to an officer. Accordingly, pursuant to Section 16(a) of the Exchange Act [15 U.S.C. § 78p(a)] and Rule 16a-3 [17 C.F.R. § 240. 16a-3] thereunder, Stein was required to file with the Commission an initial statement on Form 3 disclosing his beneficial ownership position, as well as subsequent statements of changes on Forms 4 and 5. Stein never did so. As a result, Stein violated and,

unless enjoined, will continue to violate Section 16(a) of the Exchange Act and Rule 16a-3 thereunder.

THIRTEENTH CLAIM FOR RELIEF

Violation of Securities Act Section 17(b)

(Rauch)

175. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

176. As described in paragraphs 74 through 78 above, defendant Rauch, by use of means or instrumentalities of interstate commerce or of the mails, gave publicity to a security for consideration received, directly or indirectly, from an issuer, without fully disclosing the receipt of such consideration and the amount thereof.

177. By reason of the activities described herein, Rauch violated and, unless enjoined, will continue to violate Section 17(b) of the Securities Act [15 U.S.C. § 77q(b)].

FOURTEENTH CLAIM FOR RELIEF

Unjust Enrichment of Tracey Hampton-Stein; ARC Finance Group, LLC; ARC Blind Trust; THS Blind Trust; JA YMI Blind Trust; Oak Tree Investments Blind Trust; and WBT Investments Blind Trust

178. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

179. As set forth above, defendant Stein profited from his illicit schemes by, among other things, inflating and secretly selling stock in Heart Tronics that had initially been held beneficially by his wife, relief defendant Tracey Hampton-Stein, through

relief defendant ARC Finance Group, LLC. In an effort to avoid reporting obligations and further deceive the marketplace about whether or not Heart Tronics' majority shareholder was selling Heart Tronics stock, Stein effected these sales, with the assistance of Hampton-Stein, through the purportedly blind trusts, relief defendants ARC Blind Trust, THS Blind Trust, JA YMI Blind Trust, Oak Tree Investments Blind Trust, and WBT Investments Blind Trust.

180. As further set forth above, from at least December 2005 through September 2008, while the share price of Heart Tronics' common stock was artificially inflated as a result of Stein's illicit activities, Hampton-Stein, ARC Finance, ARC Blind Trust, THS Blind Trust, JAYMI Blind Trust, Oak Tree Investments Blind Trust, and WBT Investments Blind Trust sold more than $5.8 million worth of Heart Tronics stock.

181. Relief defendants Tracey Hampton-Stein, ARC Finance Group, LLC, ARC Blind Trust, THS Blind Trust, JA YMI Blind Trust, Oak Tree Investments Blind Trust, and WBT Investments Blind Trust therefore have no legitimate claim to those funds, and have thus been unjustly enriched under circumstances in which it is not just, equitable, or conscionable for them to retain such profits.

FIFTEENTH CLAIM FOR RELIEF

Unjust Enrichment of Catch 83 General Partnership

182. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

183. Defendant Gault transferred the ill-gotten gains from his fraud on the Investor to relief defendant Catch 83 General Partnership and used the ill-gotten gains to purchase and sell shares of Heart Tronics stock. Catch 83 General Partnership therefore has no legitimate claim to those funds, and has thus been unjustly enriched under circumstances in which it is not just, equitable, or conscionable for it to retain such profits.

SIXTEENTH CLAIM FOR RELIEF

Unjust Enrichment of Five Investments Partnership

184. Paragraphs 1 through 124 are realleged and incorporated herein by reference.

185. As described above, defendants Stein and Carter engaged in an illicit scheme to have Heart Tronics issue stock from transactions registered on Form S-8 to Carter pursuant to a sham consulting contract. They then proceeded to transfer such stock, or to sell that stock and deliver proceeds from such sales, to relief defendant Five Investments Partnership, a partnership they had established for the very purpose of furthering their schemes. Five Investments Partnership therefore has no legitimate claim to those funds, and has thus been unjustly enriched under circumstances in which it is not just, equitable, or conscionable for it to retain such profits.

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court enter a final judgment:

A. preliminarily and permanently enjoining defendant Heart Tronics from violating Sections 5(a)

and (c), and Section 17(a) of the Securities Act; Securities Act Regulation S-T, Rule 302(b); Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 10b-5, 12b-11, 12b-20, 13a-1, 13a-11, and 13a-13.

B. preliminarily and permanently enjoining defendant Stein from violating Sections 5(a) and (c), and Section 17(a) of the Securities Act; Sections 10(b), 13(b)(5), 13(d), and 16(a) of the Exchange Act; and Exchange Act Rules 10b-5, 13b2-1, 13d-1, and 16a-3; and from aiding and abetting violations of Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13.

C. preliminarily and permanently enjoining defendant Gault from violating Section 17(a) of the Securities Act; Sections 10(b) and 13(b)(5) of the Exchange Act; and Exchange Act Rules 10b-5 and 13a-14; and from aiding and abetting violations of Sections 10(b) of the Exchange Act and Exchange Act Rule 10b-5.

D. preliminarily and permanently enjoining defendant Perkins from violating Sections 10(b) and 13(b)(5) of the Exchange Act and Exchange Act Rules 10b-5(b) and l3a-14; and from aiding and abetting violations of Section l3(b)(2)(B) of the Exchange Act.

E. preliminarily and permanently enjoining defendant Carter from violating Sections 5(a) and (c), and Sections 17(a)(1) and (3) of the Securities Act; Sections 10(b) and 13(b)(5) of the Exchange Act; and Exchange Act Rules 10b-5(a) and (c), and 13b2-1; and from aiding and abetting violations of Sections 10(b),

13(a), 13(b)(2)(A) of the Exchange Act and Exchange Act Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13.

F. preliminarily and permanently enjoining defendant Nevdahl from violating Sections 17(a)(1) and (3) of the Securities Act; Section 10(b) of the Exchange Act; and Exchange Act Rules 10b-5(a) and (c); and from aiding and abetting violations of Sections 10(b) of the Exchange Act and Exchange Act Rule 10b-5.

G. preliminarily and permanently enjoining defendant Rauch from violating Section 17(b) of the Securities Act.

H. ordering defendants Heart Tronics, Stein, Gault, Perkins, Carter, Nevdahl, and Rauch to disgorge, jointly and severally, all ill-gotten gains, plus prejudgment interest thereon, wrongfully obtained as a result of their illegal conduct, and provide an accounting of monies and shares of Heart Tronics stock that they received and the disposition of such monies and stock;

I. ordering defendants Heart Tronics, Stein, Gault, Perkins, Carter, Nevdahl, and Rauch to pay civil penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)] and Section 21(d) [15 U.S.C. § 78u(d)] of the Exchange Act; and

J. permanently barring defendants Stein, Gault, Perkins and Carter, pursuant to Section 20(e) of the Securities Act [15 U.S.C. §77t(e)] and Section 21(d)(2) of the Exchange Act [15 U.S.C. §78u(d)(2)], from serving as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. §781] or that is

required to file reports pursuant to Section 13 of the Exchange Act [15 U.S.C. §78m];

K. prohibiting defendants Stein, Gault, Perkins, Carter and Rauch from engaging in any offering of penny stock pursuant to Section 20(g) of the Securities Act [15 U.S.C. §77t(g)] and Section 21(d)(6) of the Exchange Act [15 U.S.C. § 78u(d)(6)];

L. ordering relief defendants Tracey Hampton-Stein, ARC Finance Group, LLC, ARC Blind Trust, THS Blind Trust, WBT Investments Blind Trust, JAYMI Blind Trust, Five Investments Partnership, and Catch 83 General Partnership to disgorge, jointly and severally, all monies, plus prejudgment interest thereon, obtained as a result of the defendants' illegal conduct alleged in this Complaint, and provide an accounting of monies and shares of Heart Tronics stock that they received and the disposition of such monies and stock;

M. granting the Commission such other relief as is just and appropriate.

Dated: December 20, 2011 Respectfully submitted,

[handwritten: signature]
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Appendix H

CONSTITUTIONAL PROVISION INVOLVED
U.S. Const. amend. VII

In suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise reexamined in any court of the United States, than according to the rules of the common law.