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Why The SEC Sued Me – And Why You Should Care

By **Porter Stansberry**

The reason you might have heard about my Securities and Exchange Commission (SEC) lawsuit is because I didn't settle the case.

When most people are sued by the SEC, they do their best to put the matter behind them – as quickly and quietly as possible.

This normally involves paying a large fine and essentially promising "not to do it again." If you pay the fine, the chances are good most people will ignore the matter. You're not required to admit any guilt. Thus, the damage to your reputation is largely mitigated and you can go on with your life. That's why most people settle with the SEC when it comes to civil (noncriminal) lawsuits.

But I didn't settle when they sued me.

Even when a settlement was offered to me for as little as $1 million, I refused it. Instead, I've faced a lengthy court battle that's brought with it tremendous risks to my reputation and legal bills amounting to almost $3 million.

Why on Earth would I try to fight the "city hall" of the securities industry?

Because I'm eager for the facts of my case to come to the public's attention. I know when the facts of my case are *accurately* known by the public, my subscribers will support my decision to fight the SEC. That's why I've never tried to hide this matter from anyone.

Unfortunately, so far, almost none of the critical issues at stake in my fight have been accurately reported. Worse, people who have no idea what they're talking about continue to assume my case is another example of a financial publisher acting scurrilously – front-running his subscribers or ripping people off by promoting penny stocks that he's been paid to endorse.

And so... at the risk of upsetting the judges who have to date refused to believe a word I've said about the matter... I would like the opportunity to tell you, my subscribers, exactly why I've refused to settle my case. I'd also like the opportunity to direct you to several reliable sources of information about the matter. Most of the things written about the case elsewhere are patently false and misleading.

For example, most people don't know my battle with the SEC is a lot more complex than your run-of-the-mill securities case. Normally, the laws the SEC enforces in civil matters, like mine, pertain to things like insider trading, selling unregistered securities, or manipulating markets for personal financial gain.

The truth is, there isn't any allegation that I ever owned the stock in question – and there never has been.

I didn't "front run" my recommendation. I wasn't being paid by promoters to recommend a stock. These things have all been said about the case – even by a few fellow journalists. But in fact, I wasn't even accused of doing them by the SEC.

So what is this case about, if it's not about trading in securities?

Testimonials

"...I've known Porter Stansberry personally for over a decade. I've found him to be, without exception, a man of unimpeachable integrity. Further, his advice is consistently sound and well thought out. Upon looking at the facts in this matter, I find it shameful that the SEC is pursuing this case. I urge the SEC, in the interest of simple justice, to drop this action..."

Doug Casey

See all testimonials »

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All Judges Are Not Created Equal

My lawsuit with the SEC started as a fight over the First Amendment rights of a publisher – me. It continued because I refused to settle or buckle under to the government. I maintain my writing was honest, materially correct, and is certainly protected by the First Amendment of the U.S. Constitution.

As a legal matter, two federal judges of the U.S. Court of Appeals for the Fourth Circuit found that the First Amendment was not at play in my case; however, on *identical* facts, seven judges of the highest court of the state of Maryland unanimously found that the publications in question triggered First Amendment protections.[1]

See, this case is really about the First Amendment. Do you really want the SEC suing publishers of independent, disinterested financial analysis? Per an article published in the *Wall Street Journal* on November 7th, 2008, supporting my case:

> …the SEC has no more business penalizing a writer who simply covers the markets than the Food and Drug Administration has in regulating a cookbook publisher because an official questions the nutritional content in a meatloaf recipe.[2]

At issue in my case: a promotional e-mail marketing piece for a Special Report I wrote in 2002. In my report, I claim a former unit of the Department of Energy – a unit that was sold to investors in 1996 and is now known as USEC – was withholding material information from the public.

Because USEC was trading at a very distressed price (half of book value) and was paying such a high dividend (yielding more than 8%), I believed the stock would soar once this long-pending agreement was made public. In my report, I explained why the agreement would turn USEC into a profitable company by lowering the company's raw material costs dramatically. I predicted the stock would double on the news.

And that's *almost* exactly what happened.

Based on what I'd learned from a company insider (the director of investor relations), I wrote the agreement would be announced at a major nuclear summit featuring presidents Bush and Putin on May 22, 2002. The insider explained the details of the summit to me in advance, long before they appeared in the newspaper and told me to "watch the stock on May 22." And in fact, the long-awaited announcement came about a month later, on June 19, 2002. Keep in mind, this agreement had been pending for more than two years. And yet, somehow, I was able to pinpoint almost to the day when it would be announced to the public.

Did the stock soar? No, not exactly. It moved from around $6.85 on May 13th to around $8.39 on June 19th. That's roughly a 22% move in a few weeks. That's not bad. More importantly though, following the new agreement with the Russian uranium supplier, the stock traded all the way up to nearly $18 over the following three years. In fact, by the time my case reached its first federal judge, investors who followed my advice would have made more than 150% on the investment, thanks to capital gains and big dividends. (The stock eventually went to $25.65 during the uranium bubble of 2007.)

Yes... that's right. The SEC came after me for a matter that involves a stock that went from under $8 to $25.[3] That's more than a 200% gain. You've got to be kidding, right? Nope.

But why would the SEC risk a constitutional battle with a bona fide journalist over a report even *The New York Times* says was basically correct?[4] Why would the SEC want to shut down a business like Stansberry & Associates Investment Research – which has offered refunds to unsatisfied customers and whose analysts never trade in the securities they recommend?

I Did *All* of the Things Any Reputable Writer Would Do

Instead of pursuing the possibility USEC's managers and bankers were withholding this material information, the SEC decided to attack me. Keep this in mind: I didn't use this information for my own personal gain. I didn't buy the stock. Or even just tell my friends to buy the stock. No, instead I did my job. I published a report about what I'd learned and offered to sell my report to any (and all) interested investors.

I also sent a copy of my report (and the accompanying sales letter) to my source at USEC. ***He never asked me to change a single word of my report.*** He had my cell phone number. He had my office number. He had my e-mail address. If there was any legitimate problem with my report, all he had to do was ask for a correction. He never did. Not even to this day.

I checked my source's facts. Sure enough, a presidential summit was approaching. Sure enough, there was a large pending contract. Sure enough, the new deal would change the economics of the company in a dramatically positive way. I sent a copy of my report to my source. And I offered it for sale to the public. If anyone wasn't satisfied with the report, for any reason, I gave him his money back.

Incredibly, the SEC sued me for securities fraud, saying I had lied about what my source told me and that selling my report about USEC was tantamount to brokering the stock. Specifically, the SEC claimed my source didn't tell me to "watch the stock on May 22," which was the only part of our conversation that I quoted

Overlooking the 'Smoking Gun'…

Even today, looking back at the matter through the lens of time and experience, I still think my USEC report was one of the great stories of my career and I'm proud of the report I wrote. Are there things I would have done differently? Yes. I would have made sure to have a recording of my interview.

In the discovery process of our lawsuit, we uncovered an April 18th, 2002 correspondence from USEC's investment bank, Bank of America, in which, analysts *clearly indicated* that the Russian contract agreement could be approved "near or during the next President Bush / President Putin summit in May 2002."[5] On another Bank of America document pertaining to the pending Russian contract, handwritten notes observe: "Maybe May @ undersecretary levels."[6] **USEC privately expressed to their bankers a link between the upcoming presidential summit and the Russian contract agreement... and court records show this as undisputed evidence.**

But the court still didn't believe that my source at USEC told me the date…

Since I can't prove what my source said, you might assume I must be lying. *But if he didn't explain the timing of the deal to me, how could I have known – within a month – exactly when the deal would close?* The fact is, until our discussion, I didn't know anything about the upcoming presidential summit. It wasn't reported in *The Wall Street Journal* until about a week after our discussion.

But... just for the sake of the argument... what if you assume I knew about the summit from another source and I merely attributed it to the company in order to claim I really had "inside" information? Why then, even after I wrote the report and sent my source a copy, did he not demand a retraction?

And if the company knew my report was false, why didn't it put out a press release denying it? The NYSE rules require companies to put out press releases anytime there's a material misstatement in the press

The fact of the matter is, my report was overwhelmingly correct.

And my source couldn't deny my report because he didn't know whether or not I had a recording of our conversation (which took place over the phone).

When the SEC first came calling in 2002, I expected it would be going after the company for selective disclosure – a violation of SEC regulation FD.[7] The SEC asked for all of my personal financial records (and even my fiancé's financial records) to make sure I wasn't front-running the stock. I complied.

But then, instead of shifting its investigation to the company, the SEC demanded to have the entire subscription list of not just my publishing company, but also of our parent company, Agora, Inc.

It wasn't going after USEC for withholding material information; it was going after us by intimidating our subscribers. And it didn't ask for just the USEC report subscribers – **it demanded every single name and address on our entire database, including my parent company's database**.

Rather than give in to this subpoena, we filed for a protective order in federal court to protect our subscribers' privacy. We did the same in the state of Maryland against a parallel state action on the same facts, and won.[8] We proudly established a legal precedent that protects a publisher's subscriber lists. (What you decide to read is none of the government's business.) So, we were victorious in the state court… and the government of the state of Maryland left us alone.

The federal court, however, dismissed our protective action, since the SEC (with impeccable timing, mind you) counter sued us for fraud. And, from that point forward, like the proverbial ostrich, the federal court *refused to even acknowledge* the prior opinion of the Maryland court.

That's part of the story I'm sure you've never heard before: We sued the SEC first. And we did so to protect our subscribers, the overwhelming majority of whom never bought the USEC report in the first place. In fact, of the 1,217 readers who purchased my USEC report, only 18% asked for a refund… and 90% of those customers purchased a subsequent publication from either Stansberry & Associates, or our parent company, Agora, Inc. [9]

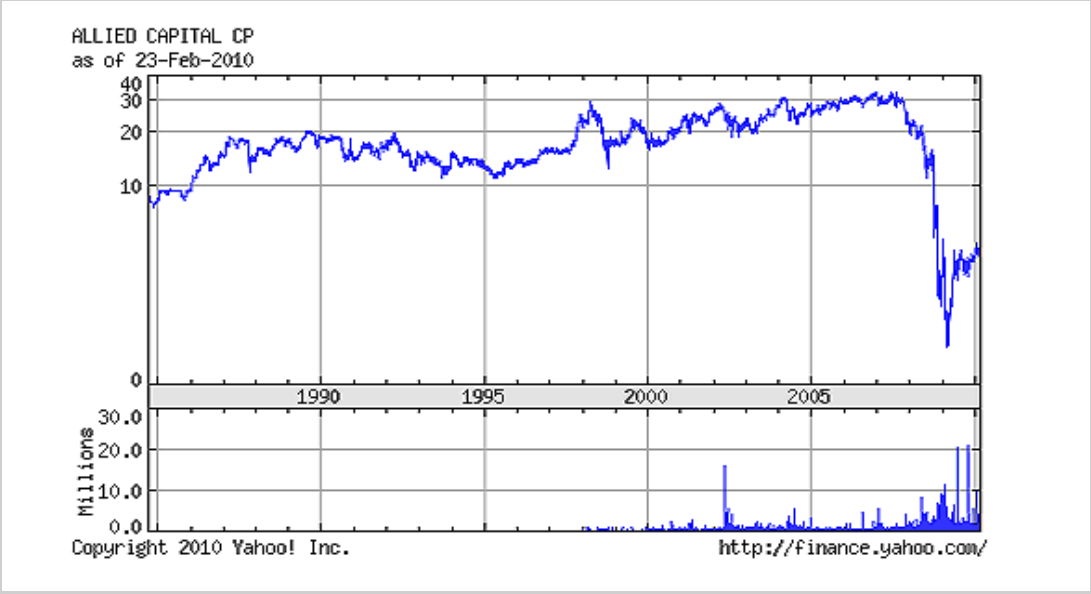
I understand that you might reasonably wonder... How could any of this be true? I mean, wouldn't you expect that as soon as the SEC knew I'd sent my source a copy of the report, the matter would be closed? Or don't you think as soon as it knew I wasn't trading the stock or front-running it, the SEC would have simply left me alone?

I understand my story might be hard to believe – at first. The public generally has confidence in our government.

My story isn't entirely unique…

At the same time the SEC was expanding the scope of its power, subjecting me to interrogations, subpoenas, and crushing legal bills – all in violation of the First Amendment – it was also going after many other legitimate market participants – including David Einhorn, the well-regarded hedge-fund manager (Greenlight Capital) for merely speaking about securities.

As with my case, the SEC came after Einhorn for speaking openly about abuses taking place at a Washington-based business (Allied Capital), a company that – like USEC – was heavily staffed with former government officials, including Joan Sweeney, the company's chief operating officer, who was a former senior member of the SEC's Division of Enforcement. Our stories are eerily similar...



THIS IS WHAT EINHORN WAS WARNING INVESTORS ABOUT, AS EARLY AS 2002. THE SEC RESPONDED BY INVESTINGATING EINHORN.

Rather than investigating Einhorn's claim that Allied Capital was cooking its books by using fraudulent accounting, the SEC instead began investigating him, alleging securities fraud because of *what he'd said about Allied Capital during a presentation at an investment conference that's held to benefit charities.*

After several years of threats and abuses (like having his phone records stolen), Einhorn was vindicated. The shares of Allied Capital collapsed as the company was revealed as fraudulent. But even today, Joan Sweeney is still with Allied Capital. The SEC has never been forced to fire any of the agents who abused their power during the investigation of David Einhorn.

To draw attention to the abuse he'd suffered, Einhorn decided to donate all of the money he made from shorting Allied Capital to charity, and he wrote an entire book about the situation called, Fooling Some of the People All of the Time.

Says Einhorm about his experience:

> *Allied isn't the biggest, most egregious, or most audacious fraud I have seen. In a sense it is a garden-variety fraud – dishonest business dealings by dishonest management. So why all the fuss? The story I am telling is one that has been surprising and unexpected – even to me. I think it is important and needs to be told. This book reveals some serious problems in the regulatory landscape that I am in a unique place to discuss.*
>
> *I care that the SEC and other regulators seem to have stopped enforcing laws against corporate malfeasance. I care that company officials can lie with impunity on public conference calls. And I have been appalled that the government officials overseeing the lending programs that Allied has defrauded are so indifferent and unwilling to act even when presented with clear evidence of abuse. The overall lack of law enforcement is startling...*
>
> *If we are going to permit the retribution against the whistleblowers shown in this story – defamation, investigation, invasion of privacy and so forth – then we surrender public free speech. If we allow the people in this story to operate outside the law, then we nourish a corrupt business culture. Rather than turn a blind eye to the fraud I witnessed, I made a decision to stand up and speak out despite the consequences. I hope my story inspires regulators and government agencies to do the right thing.* [10]

Most people don't fight the SEC because they don't want their names in the paper, they don't want the stigma of being investigated by the government, etc.

Believe me, I can understand why. When the news of the SEC's investigation of me leaked out, publishers around the world refused to do business with me. Potential employees refused to come to work with me. Companies refused to be interviewed by me. The lawsuit has made it vastly more difficult for me to simply stay in business. Even today, every time a potential subscriber stumbles across information about the lawsuit on the Internet (and much of it is completely untrue) he's likely to cancel his subscription or simply decide not to renew.

And... maybe you still trust the SEC. And if you do and you want to believe Porter Stansberry is out to harm investors by publishing independent reports on public companies – many that come with a money-back guarantee – there's probably very little I can do to change your mind.

On the other hand, if you ask any securities industry professional who reads our newsletters, I have no doubt he will tell you our work is among the best you can buy anywhere and is far superior to nearly all of the research put out by the brokerage firms. I know this is true because thousands of professionals are subscribers and I have hundreds, if not thousands, of testimonials from these readers

Don't you wonder why the SEC would target my business – which doesn't manage money or broker stocks – while ignoring enormous ponzi schemes going on in the businesses it supposedly regulates?

I can't prove it... but I don't think the government likes it very much when I tell investors the truth about things like Fannie, Freddie, and General Motors. (In 2008, even *Barron's* called me a "savvy pro," my research firm "highly regarded," and my analysis of Freddie Mac and Fannie Mae "remarkably prescient.")[11] I don't think the SEC wants the American people to know the truth about our financial markets – or the state of our government's finances. And I think the government is afraid of what will happen when you find out the truth.

In the spring of 2010, I saw an outpouring of support from fellow journalists and members of the press… More than 20 of the most prominent companies and associations from the broadcasting and publishing communities petitioned the Supreme Court to review my case, urging them to specifically address the First Amendment concerns that previous courts simply overlooked. Those who stood behind me: The Reporters Committee for Freedom of the Press[12], The American Society of News Editors, The Associated Press, The Association of American Publishers, Inc., The Radio Television Digital News Association, The Thomas Jefferson Center for the Protection of Free Expression, The Society of Professional Journalists[13], Investorplace Media, LLC, Alm Media, LLC, CNBC, Inc., The E.W. Scripps Company, Eagle Publishing, Inc., The Financial Publishers Association, Forbes LLC, Gannett Company, Inc., The Hearst Corporation, Landmark Media Enterprises, LLC, Lee Enterprises, Inc., The Mcclatchy Company, Media General, Inc., The New York Times Company, The Newspaper Association of America, and the Washington Post Company, LLC.[14]

A *Wall Street Journal* article profiling my case presented a striking argument in my favor, highlighting the importance of First Amendment protections for publishers:

> In leaving publishers outside the scope of securities regulation, we live with the risk of some downside -- they will make mistakes - in order to benefit from the possible upside -- they may spot the next Fannie Mae or Lehman Brothers before it's too late. Now that's a hedge worth taking.[15]

Ironically, "The Right to Be Wrong"

On June 28, 2010, the Supreme Court refused to review the decision. On July 4th, The *New York Times* ran a piece profiling my case titled "The Media's Right to Be Wrong," which

ironically, contained a few factual errors (Agora, Inc. was dismissed from the suit, and as I've just explained, USEC's stock did in fact soar… just not in the short window I had expected).[16]

However, the heart of the article was spot-on. They clearly outlined what my case could mean for **all** financial journalists:

> The implications of the SEC's action are potentially profound: newspapers or Web sites promising their paying readers stock information that later turns out to be untrue suddenly leave themselves open to fraud charges. *Any financial commentator who passes on bad information in good faith could be sued.*

Additionally, the *New York Times* warned:

"…if the SEC does not begin to stick to actual securities fraud and stop whittling at the First Amendment, financial journalism could become more cautious and less robust."

And it's not just the media being sympathetic to the plight of a fellow journalist... even the prominent legal community has taken a critical approach to the court's decision in my case…

Several well respected legal journals have discussed the court's baffling interpretation of Section 10(b) of the Securities Exchange Act of 1934, which prohibits false statements "in connection with the purchase or sale of any security."[17] On appeal, the federal court came up with an entirely new theory (one that even the SEC had not submitted) to satisfy the "in connection with" requirement: In short, the re-issuance of the marketing piece selling the Special Report with updated USEC prices enhanced the credibility of the report and motivated subscribers to purchase the Special Report.[18] This would leave one to reason that the *initial* marketing piece offering my Special Report was out of the SEC's scope… and that *simply pointing out the fact that people are reading my publications* is what gave the SEC an "in." It's absurd.

Unfortunately in my case, the court read "existing precedent as broadly as possible."[19] An article in the *New York Law Journal* noted that the court "disregarded virtually all the requirements previously understood to anchor the…'in connection with' standard."[20] Further, the authors cautioned that if other courts adopt this same analysis, "there could be no limit to the boundaries to §10(b)."

At this point, we plan to lobby Congress to amend the Securities Exchange Act of 1934 to expressly include an exemption for *all* impersonal, disinterested financial media.

I hope you'll know I did, and have always done, my best to tell you the truth.

After all, unlike the government, the truth is my only weapon.

Regards,
Porter Stansberry
September 2010

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1. http://mdcourts.gov/opinions/coa/2005/128a03.pdf,
   Lubin v. Agora, Inc., 882 A.2d 833 (Md. 2005),
   [Note: Seven judges of the highest court of the state of Maryland unanimously ruled in favor of Stansberry and against the state government.]
2. http://online.wsj.com/article/SB122603145921008063.html,
   David B. Rivkin Jr. and Bruce D. Brown, The SEC Should Leave Journalists Alone, Wall Street Journal, Nov. 7, 2008.
3. USEC Inc (USU) chart
4. Adam Liptak, *E-mail Stock Tip Tests Limits of Securities Laws*, N.Y. TIMES, Aug. 3, 2003.
   "Mr. Stansberry's report was more premature than inaccurate. The predicted deal did materialize, on June 19, 2002, but the stock price did not move significantly in reaction to it. The day before, after the deal cleared a hurdle with the Energy Department, the stock did rise 12 percent."

5. Bank of America Memo on Meeting with USEC's Treasurer **(Evidence)** (April 18th 2002)
Filed as undisputed evidence in the case, a memo from USEC's investment bank, Bank of America, clearly indicating that the Russian contract agreement could be approved "near or during the next President Bush/President Putin summit in May 2002."

6. Bank of America Document **(Evidence)**
Filed as undisputed evidence in the case, handwritten notes on a Bank of America document pertaining to the Russian contract agreement, observing: "Maybe May @ undersecretary levels."

7. http://www.sec.gov/rules/final/33-7881.htm, *Regulation FD (Fair Disclosure) is a new issuer disclosure rule that addresses selective disclosure. The regulation provides that when an issuer, or person acting on its behalf, discloses material nonpublic information to certain enumerated persons (in general, securities market professionals and holders of the issuer's securities who may well trade on the basis of the information), it must make public disclosure of that information. The timing of the required public disclosure depends on whether the selective disclosure was intentional or non-intentional; for an intentional selective disclosure, the issuer must make public disclosure simultaneously; for a non-intentional disclosure, the issuer must make public disclosure promptly. Under the regulation, the required public disclosure may be made by filing or furnishing a Form 8-K, or by another method or combination of methods that is reasonably designed to effect broad, non-exclusionary distribution of the information to the public.*

8. http://mdcourts.gov/opinions/coa/2005/128a03.pdf, *"Pursuant to an investigation into potential violations of Maryland securities laws, appellant, the Maryland Securities Commissioner, served two subpoenas duces tecum on appellee, Agora, Inc., a company whose business includes publishing investment newsletters. Following Agora's refusal to produce its subscriber lists, marketing lists, and other documents containing information identifying any of its subscribers, the Commissioner filed a motion to compel enforcement. The trial court denied the motion, concluding that the Commissioner had failed to demonstrate a compelling need for the subscriber lists as required by the First Amendment and that the demand for subscriber lists was overbroad. We must decide whether the First Amendment to the United States Constitution prevents the Commissioner from compelling discovery of the identities of Agora's subscribers. We shall hold that it does."*

9. Pirate Investor LLC v. SEC – Petition for Certiorari.pdf

10. http://www.foolingsomepeople.com/main/the-allied-story.html

11. Alan Abelson, Au Revoir or Goodbye?, BARRON'S, July 14, 2008

12. Brief Amici Curiae of the Reporters Committee for Freedom of the Press and Media Organizations in Support of Petitioners

13. Brief of Society of Professional Journalists as Amicus Curiae in Support of Petitioners

14. BRIEF OF INVESTORPLACE MEDIA, LLC; ALM MEDIA, LLC; CNBC, INC.; THE E.W. SCRIPPS COMPANY; EAGLE PUBLISHING, INC.; THE FINANCIAL PUBLISHERS ASSOCIATION; FORBES LLC; GANNETT COMPANY, INC.; THE HEARST CORPORATION; LANDMARK MEDIA ENTERPRISES, LLC; LEE ENTERPRISES, INC.; THE MCCLATCHY COMPANY; MEDIA GENERAL, INC.; THE NEW YORK TIMES COMPANY; THE NEWSPAPER ASSOCIATION OF AMERICA; AND THE WASHINGTON POST COMPANY LLC AS AMICI CURIAE IN SUPPORT OF PETITIONERS

15. David B. Rivkin Jr. and Bruce D. Brown, The SEC Should Leave Journalists Alone, WALL STREET JOURNAL, Nov. 7, 2008.

16. The Media's Right to Be Wrong, N.Y. TIMES, July 3, 2010.

17. http://www.sec.gov/about/laws/sea34.pdf, *Section 10(b) of the Securities Exchange Act of1934 provides in relevant part: "It shall be unlawful for any person, directly or indirectly … (b) To use or employ, in connection with the purchase or sale of any security … any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78j(b).*

18. SEC v. Pirate Investor, LLC, 580 F.3d 233, (4th Cir. 2009), *"Thus, the rising stock was important to the success of the scheme because it served to motivate later purchasers to part with their requisite $1,000 payment. The fraud was not complete when investors paid $1,000 to learn the identity of the company in question; Appellants also needed those investors to purchase the stock thereby increasing the stock price so as to boost the credibility of the solicitation e-mail to obtain more $1,000 payments."*

19. SEC v. Pirate Investor LLC: Expansion of the "In Connection With" Requirement Under Exchange Act Section 10(b), DECHERT, May 2010.*"The Fourth Circuit's decision in Pirate Investor readers existing precedent as broadly as possible in interpreting Section 10(b)'s "in connection with" requirement. The Court embraces subjective standards, such as a speaker's understanding of whether investors may rely on his or her statements in making investment decisions. As such, the decision has implications beyond the financial newsletter industry."*

20. Sarah S. Gold and Richard L. Spinogatti, Section 10(b)'s 'In Connection With' Requirement Untethered, N.Y. LAW JOURNAL, Oct. 16, 2009. *"Pirate pushed the boundaries of §10(b)'s requirement that fraud be sufficiently connected to securities transactions for liability to attach. The Fourth Circuit disregarded virtually all the requirements previously understood to anchor the otherwise amorphous "in connection with" standard. Purveyors of financial analysis and disinterested financial advice will be interested in, if not discomforted by, this decision. But, were other courts to adopt the Fourth Circuit's untethered analysis, there could be no limit to the boundaries of §10(b)."*