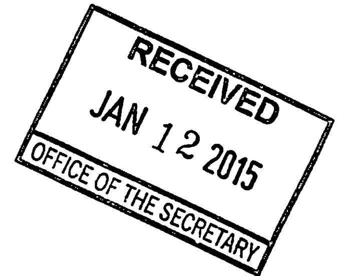
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16037



In the Matter of

EDGAR R. PAGE and
PAGEONE FINANCIAL INC.,

Respondents.

THE DIVISION OF ENFORCEMENT'S MOTION AND MEMORANDUM OF LAW IN SUPPORT OF ITS MOTION IN LIMINE NO. 2 TO PRECLUDE THE REPORT OR TESTIMONY OF PROFESSOR STEVE THEL

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The Division of Enforcement ("Division") respectfully moves the Court, and submits this memorandum of law in support of that motion, to strike Professor Steve Thel's Expert Report, Jan. 5, 2015 ("Thel Report"), and to preclude Professor Thel's testimony.

PRELIMINARY STATEMENT

This case is about whether investment advisers—Edgar R. Page ("Page") and PageOne Financial, Inc. ("PageOne")—satisfied their fiduciary duties to fully and openly disclose all real and potential conflicts of interest presented by the United Group of Companies, Inc.'s ("UGOC") acquisition of PageOne stock (and the terms of that acquisition), as required by the Sections 206(1) and (2) of the Investment Advisers Act of 1940 ("Advisers Act").[1] Specifically, Respondents needed to inform their clients—especially the clients that they were recommending invest in funds managed by UGOC ("Funds")—of the acquisition and its terms. Respondents admit that they did not.[2] Instead, they argue that they "over-disclosed" by describing conflicts that did not actually exist in order to avoid disclosing those that did. In support of their position, Respondents seek to introduce the Thel Report and testimony from Professor Thel.[3]

However, Professor Thel's report is replete with opinions that—because they are foreclosed by Supreme Court and Commission precedent—are wholly irrelevant and

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1 See Division Pre-hearing Brief at 1; Amended Order Instituting Proceedings ("OIP"), ¶¶ 2, 4, 23, 31.

2 See, e.g., Div. Ex. 94 at 5 (Respondents Wells Submission noting that Respondents disclosed "referral fees" and that Page was paid as "consultant," not because these were true, but to "put[] investors on notice of a financial relationship between Mr. Page and United without prematurely revealing nascent merger negotiations); Div. Ex. 97 at 3 (Respondents' Supplemental Wells Submission acknowledging that the conflicts PageOne disclosed to its clients were "technically different from the one that may have been created by the negotiations with United") (emphasis in original); see also Answer to OIP, ¶ 33 (admitting that Page did not tell his clients about the promissory notes).

3 A copy of the Thel Report is attached hereto as Exhibit A.

unreliable. First, Professor Thel opines that (1) "[i]t is appropriate" for parties to merger negotiations to keep those negotiations secret. (Thel Report at 1.) This opinion might be true in the non-fiduciary context of a listed company making disclosures to the public. However, it is manifestly untrue where, as here, the merger negotiations involved an investment adviser and created a real (or even potential) "conflict[] of interest which might incline a[n] investment adviser—consciously or unconsciously—to render advice which was not disinterested" to his clients. SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-92 (1963). Indeed, under Capital Gains and its progeny an investment adviser has to disclose every single conflict or potential conflict regardless of whether they might arise in the context of merger negotiations or not. The Commission recently unambiguously confirmed this point, holding that, "Capital Gains repeatedly emphasized an adviser's fiduciary duty to disclose 'all conflicts of interest'." In the Matter of Montford and Co., Inc., IA Rel. No. 3829, 2014 WL 1744140, at *15 (May 2, 2014) (Commission Op.) (emphasis added), quoting Capital Gains, 375 U.S. at 191-92. Plainly such a conflict existed here because Respondents insisted on continuing to recommend the UGOC Funds, while taking money for the acquisition from UGOC. Of course, had Respondents simply refrained from recommending the Funds during the pendency of the acquisition, the issues before this Court would different; but they did not.

Second, Professor Thel argues that Respondents' disclosures where not "[m]aterially [m]isleading." (Thel Report at 4.) Again, this opinion is foreclosed by Capital Gains. That case and its progeny—including Commission precedent—hold that conflicts of interest between an investment adviser and his client are per se material and all of them (even potential conflicts) must be disclosed.

Professor Thel's Report simply ignores these realities. The Report does not address the type of conflicts investment advisers are required to disclose to their clients (and potential clients) or the materiality of those conflicts under the Advisers Act, the only statute at issue in this case. Instead, the Thel Report conflates (without making it clear that it is doing so) the duty of disclosure owed by an investment adviser, on the one hand, and the duty owed by a public company (and materiality standards for that disclosure) to its investors under the Securities Act of 1933 and the Securities Exchange Act of 1934, on the other. From that flawed analysis, the Thel Report concludes that the acquisition of an investment adviser only presents a material conflict if the acquisition was probable to conclude and would present a conflict if it did conclude. The Thel Report's future looking analysis entirely misses the point. The Advisers Act looks to whether a conflict or potential conflict existed at the time of the investment recommendation. If it did, the adviser must disclose it. Professor Thel's Report compares apples to oranges and, in this respect, his methodology is entirely unreliable.

LEGAL STANDARD

The Court "shall exclude all evidence that is irrelevant [or] immaterial. . . ." Rule of Practice 320. "The Supreme Court has made clear that judges have broad discretion in determining whether to admit or exclude evidence, and this is particularly true in the case of expert testimony." In the Matter of Scott G. Monson, IC Rel. No. 28323, 2008 SEC LEXIS 1503, at *22 (June 30, 2008) (Commission Op.) (citations and quotation marks omitted). Moreover, in determining whether evidence is irrelevant or immaterial, Administrative Law Judges look to federal law and reference the Federal Rules of Evidence. See In the Matter of Miguel A. Ferrer, AP Rel. No. 730, 2012 WL 8751437, at *

5 n.1 (Nov. 2, 2012) (Murray, CALJ) ("The Commission's case law is that the Federal Rules of Evidence do not govern Commission proceedings, however, they are often used a reference point").

"[A]lthough testimony concerning the ordinary practices in the securities industry may be received . . . to evaluate a defendant's conduct against the standards of accepted practice," SEC v. Tourre, 950 F. Supp. 2d 666, 675 (S.D.N.Y. 2013), an expert's opinion is admissible only if it is relevant and reliable. See SEC v. Shanahan, 07 Civ. 270 (JCH), 2010 WL 415267, at ** 3-4 (E.D. Mo. Jan. 26, 2010), discussing Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579 (1993) and citing Lauzon v. Senco Products, Inc., 270 F.3d 681, 686 (8th Cir. 2001).[4] As the Lauzon Court noted:

> First, evidence based on scientific, technical, or other specialized knowledge must be useful to the finder of fact in deciding the ultimate issue of fact. This is the basic rule of relevancy . . . Third, the proposed evidence must be reliable or trustworthy in an evidentiary sense, so that, if the finder of fact accepts it as true, it provides the assistance the finder of fact requires.

Lauzon, 270 F.3d at 686 (emphasis added and citations and quotation marks omitted). Where the expert's opinion "is so fundamentally unreliable that it can offer no assistance," it should be precluded. Shanahan, 2010 WL 415267, at *5. In addition, experts may not provide testimony "encompassing an ultimate legal conclusion." Tourre, 950 F. Supp. 2d at 675, quoting United States v. Bilzerian, 926 F.2d 1285, 1295 (2d Cir. 1991). The party seeking to introduce the proffered expert testimony bears the burden of establishing, by a

[4] Daubert focused "on the admissibility of scientific expert testimony." SEC v. Mannion, 10 Civ. 3374 (WSD), 2013 WL 1291621, at *7 (N.D. Ga. Mar. 25, 2013). However, the Supreme Court later extended its analysis there "to experts who are not scientists." Id., citing Kumho Tire Co. v. Carmichael, 526 U.S. 137 (1999).

preponderance of the evidence, that all requirements have been met. United States v. Williams, 506 F.3d 151, 160 (2d Cir. 2007) (citations omitted).

ARGUMENT

1. *Sections A & C of the Thel Report: Professor Thel's Opinions Concerning the Secrecy of Merger Negotiations and Materiality are Foreclosed by Binding Legal Precedent*

In SEC v. Capital Gains Research Bureau, Inc., the Supreme Court pronounced the rule, now blackletter law, that an investment adviser must inform its clients of all potential and actual conflicts of interest. As the Court noted:

> [t]he Investment Advisers Act of 1940 thus reflects a congressional recognition of the delicate fiduciary nature of an investment advisory relationship, as well as a congressional intent to eliminate, or at least to expose, all conflicts of interest which might incline a[n] investment adviser—consciously or unconsciously—to render advice which was not disinterested.

375 U.S. 180, 192 (emphasis added and quotation marks omitted).[5] Moreover, investment advisers are not allowed to hide any facet of a conflict (or potential conflict) from their advisory clients: "[W]hat is required is 'a picture not simply of the sho[p] window, but of the entire store . . . not simply truth in the statements volunteered, but disclosure." Id. at 201.

Thus, Capital Gains and its progeny have consistently stood for the proposition that every conflict (or even potential conflict) of interest is material as a matter of law both before the federal courts and the Commission. See Vernazza v. SEC, 327 F.3d 851, 859 (9th Cir. 2003) ("It is indisputable that potential conflicts of interest are 'material' facts

[5] Such a conflict arises, at least, when, "advice to a client might result in financial benefit to the adviser—other than the fee for his advice—'that advice to a client might in some way be tinged with that pecuniary interest (whether consciously or) subconsciously motivated . . . .". Id. at 188.

with respect to clients and the Commission"); SEC v. Slocum, Gordon, & Co., 334 F. Supp. 2d 144, 182 (D.R.I. 2004) ("Potential conflicts of interest are always material") (emphasis added); In re Stein, IA Rel. No. 2114, 2003 WL 1125746, at *7 (Mar. 14, 2003) (Commission Op.) ("for a fiduciary . . . the disclosure of potential conflicts of interest is fundamental to preserving the integrity of the relationship with the client"). As the Commission has held:

> An adviser has a duty to render disinterested advice to his client and to disclose information that would expose any conflicts of interest. Indeed, disclosure is required even where there is only a potential conflict.

In the Matter of Kingsley, Jennison, McNulty & Morse, Inc., IA Rel. No. 1396, 1993 WL 538935, at *3 (Dec. 23, 1993) (Commission Op.) (emphasis added). Recently the Commission made the point even more explicitly:

> Contrary to Respondents' claim, the Court in Capital Gains repeatedly emphasized an adviser's fiduciary duty to disclose 'all conflicts of interest,' not just those created by an illicit quid pro quo agreement.

In the Matter of Montford and Co., Inc., IA Rel. No. 3829, 2014 WL 1744140, at *15 (May 2, 2014) (Commission Op.) (emphasis added), quoting Capital Gains, 375 U.S. at 191-92.

Thus, the only questions that are relevant in this Advisers Act case are: (1) did the adviser's relationships present a potential for conflict with the interest of his clients; (2) did the adviser fail to fully and openly describe those conflicts; and (3) did the adviser do so knowingly, recklessly, or merely negligently.[6] Plainly, the relationship between Page and

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[6] Indeed, because an adviser has a fiduciary duty to disclose all conflicts, courts have held that the mere failure to disclose without more constitutes a violation of Advisers Act Section 206(2). See SEC v. Slocum, Gordon, & Co., 334 F. Supp. 2d at 183-4 (holding that even though defendants acted without scienter they were liable for violating Section 206(2) merely because their fiduciary duty "compelled disclosure" even of potential conflicts that "could have occurred to the detriment of clients").

UGOC presented such conflicts: Page was advising his clients to invest in UGOC-managed funds, while at the same time receiving acquisition payments from the Funds' manager.[7] Thus, Respondents were obligated to tell their clients the full truth about the acquisition.[8]

Professor Thel's opinion that it is "appropriate" to keep the acquisition secret turns these precedents—requiring full disclosure—on their head. Surprisingly, Professor Thel's report does not even address disclosure obligations in the contexts of the Advisers Act or the investment advisory industry. Instead, he cites exclusively to precedent holding that under Section 10(b) of the Securities Exchange Act of 1934, public companies are not necessarily required to disclose merger talks as long as what they do say they say truthfully.[9] (Thel Report at 1-3.) However, those authorities merely stand for the well-worn proposition that, under Section 10(b), "[s]ilence, absent a duty to disclose, is not misleading." Basic v. Levinson, 485 U.S. 224, 239 n.17 (1988).

But, Capital Gains and its progeny—precisely because they impose just such a duty to disclose—require far more of communications between investment advisers and their clients. Nonetheless, throughout his report, Professor Thel repeatedly confuses the duties

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7 To say nothing of other facts, which exacerbated Page's conflicts: (1) that he committed to raise $20 million for the Funds; (2) that he was obligated to repay all the acquisition payments if he and UGOC could not complete the acquisition, and (3) that Page knew that UGOC was illiquid and, thus, unlikely to be able to continue the acquisition payments without investments from his clients. (See OIP, ¶¶ 2, 10, 14, 15, 36.)

8 See Capital Gains, 375 U.S. at 201.

9 See Thel Report at 2 (citing Flamm v. Eberstad, 814 F.2d 1169, 1176 (7th Cir. 1987) (discussing materiality of merger negotiations under Section 10(b)), abrogated by Basic, Inc. v. Levenson, 485 U.S. 224 (1988)); Securities Act Rel. No. 6835 (May 18, 1989) (discussing public companies' obligation to disclose preliminary merger negotiations)).

that a public company owes to its investors with those an investment adviser owes to its clients. For example, Professor Thel cites to four cases for the proposition that, in the merger context, "[d]isclosure may in fact be more misleading than secrecy so far as investment decisions are concerned."[10] Each of those cases however, addressed whether, under Section 10(b), a public company must inform its investors of nascent merger talks, not, whether an investment adviser must inform its clients that it is in the process of being acquired by the manager of the very funds he is recommending they invest in. Page was an investment adviser—not a public company with stock trading on the public markets—and, thus, was required to be fully open about his conflict.[11]

That the law requires such a degree of openness of investment advisers reflects the delicate fiduciary relationship between an investment adviser and his clients. In short, it allows the clients to decide for themselves what is important. Again, the Commission has recently confirmed this point: "[D]isclosing such conflicts . . . allows clients to evaluate overlapping motivations . . . in deciding whether an adviser is serving two masters or only one," the client. Montford, 2014 WL 1744140, at *15, quoting Capital Gains, at 196 (quotation marks omitted). The Commission went on: "As we have held it is the client, not the adviser, who is entitled to make the determination whether to waive the adviser's conflict." Montford, 2014 WL 1744140, at *16. Professor Thel's opinions, and the

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10 See Thel Report at 3 n.6, citing Reiss v. Pan American World Airways, Inc., 711 F.2d 11, 14 (2d Cir. 1983); Greenfield v. Heublein, Inc., 742 F.2d 751, 756 (3d Cir. 1984), abrogated by Basic, Inc. v. Levenson, 485 U.S. 224 (1988); Staffin v. Greenberg, 672 F.2d 1196, 1206 (3d Cir. 1982), abrogated by Basic, Inc. v. Levenson, 485 U.S. 224 (1988).

11 Of course, had he wanted, Page could have removed the conflict and chosen to remain silent about the planned acquisition simply by not recommending that his clients invest in the Funds. Page chose not to do that and, thus, at a minimum was obliged to disclose the true terms of his relationship with UGOC.

authorities he cites, are not contrary to the Division's position; rather they are simply irrelevant under the Advisers Act.[12]

Professor Thel's opinion that Respondents' conflict of interest disclosures were not materially misleading (Thel Report at 4.) is likewise foreclosed by Capital Gains. As discussed above, all conflicts of interest are material under Capital Gains and its progeny.[13] Professor Thel, however, argues that—rather than being required to disclose all actual conflicts—it is sufficient to disclose a "substantial conflict of interest." (Thel Report at 6). In other words, Professor Thel argues that investment advisers' failure to disclose the actual conflicts they face is immaterial as long as advisers put clients on notice about some type of conflict. Again, this conclusion is contrary to the law, which states clearly that an adviser must disclose all conflicts and that all such conflicts (whether actual or merely potential) are material. It would be a strange result, indeed, if investment advisers were allowed, contrary to Capital Gains, to pick and choose which conflicts to disclose. It would be stranger still if—as Respondents urge now—investment advisers could "disclose" conflicts that do not actually exist, instead of ones that do.

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[12] Professor Thel also notes that parties to an acquisition "almost always agree to keep such negotiations confidential" and that "[p]rovisions like these are ordinary and appropriate." (Thel Report at 2.) While that may be true in arms-length transactions, his opinion is irrelevant to the question of whether Respondents needed to disclose their arrangement to their clients under the Advisers Act. Indeed, it is axiomatic that parties cannot exempt themselves from the federal securities laws by contract. See, Advisers Act Section 215(a) [15 U.S.C. § 80b-15(a)] ("Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or with any rule, regulation, or order thereunder shall be void").

[13] See Vernazza v. SEC, 327 F.3d 851 (9th Cir. 2003); In re Stein, IA Rel. No. 2114, 79 SEC Docket 2390, 2003 WL 1125746 (Mar. 14, 2003); and In the Matter of Kingsley, Jennison, McNulty & Morse, Inc., Advisers Act Rel. No. 1396, 55 SEC Docket 2064, 1993 WL 538935 (Dec. 23, 1993).

2. *Section C(2) of the Thel Report: Professor Thel's Methodology is Unreliable*

In addition to his opinions being irrelevant to this case, Professor Thel's methodology in determining whether the conflicts were "material" is unreliable. In his report, he states:

> While negotiations over the sale of part of PageOne were ongoing, the materiality of any potential conflict depended upon the balance of the probability that the transaction would be completed and the magnitude of the conflict that would exist if the acquisition did occur.

(Thel Report at 5 (emphasis added).) In other words, Professor Thel looks to the future—the probability the acquisition would be finalized and the magnitude that future conflict would present—to determine whether a conflict was material in the present. Under the Advisers Act, this is simply the wrong metric.[14] Again, Capital Gains and its progeny require investment advisers to determine if they face any conflicts (or potential conflicts) at the moment they are advising clients and, if yes, to disclose them, irrespective of their potential future "magnitude."

The question for this Court is not whether the acquisition would occur, but whether Page had a secret motive—or the appearance of such motive—when he was advising his clients to invest in the Funds. Indeed, whether or not the acquisition was ultimately consummated is irrelevant for those purposes. At the time he was recommending the Funds to his clients, Page knew that UGOC was paying him to buy his firm, that he had committed to raise money for UGOC as part of that acquisition, and that he was on the

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[14] For this proposition, Professor Thel cites to Basic v. Levinson, 485 U.S. 224 (1988). (Thel Report at 5 n.12.) This citation might be apt in the context of when a public company needs to disclose a merger to the public market, but is entirely irrelevant to the questions presented here.

hook to repay the promissory notes if he and UGOC could not close the deal. Those facts saddled him with a conflict because they motivated him—or simply presented the possibility of inclining him to be motivated—to recommend the investment to his clients from which he might benefit. Page needed to disclose these conflicts. That Page may no longer need to tell his clients of a conflict (here the ongoing acquisition) at some point in the future if it fell apart, did nothing to lessen his obligation to tell clients before it fell apart.[15]

3. Section B of the Thel Report: The Thel Report Also Contains an Impermissible Opinion of What Page Meant During his Own Testimony

Professor Thel also opines that Page—when he testified that he did not want to reveal the acquisition because "[i]t's too dangerous. It would cause thousands of clients to get extremely nervous if I was selling my firm" (Div. Ex. 166 at 118:12-19)—was not expressing that "he thought the negotiations were important," and that, in any event, his fear of such disclosure was "typical and legitimate." (Thel Report at 3.) However, Professor Thel is not qualified to opine on what was in Page's mind when he testified or even as to what he was thinking when he made certain statements. In that regard, this case is surprisingly similar to SEC v. Badian, 822 F. Supp. 2d 352 (S.D.N.Y. 2011). There, Professor Thel attempted to testify as to what a defendant meant when he uttered certain phrases. The Court precluded Professor Thel's testimony, stating that "Thel is not qualified to testify as to what was in the defendant's mind when he used these words or phrases." 822 F. Supp. 2d at 358; see also Highland Capital Management, L.P. v. Schneider, 379 F.

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[15] See also Thel Report at 5 ("I do not believe that the acquisition, if consummated, would have materially increased the Respondents' conflict of interest in recommending investment in the Private Funds to their clients") (emphasis added). Again, the metric is not whether there would be a greater conflict in the future than existed in the present. The only question is whether there was a conflict in the present.

Supp. 2d 461, 469 (S.D.N.Y. 2005) (precluding expert from offering his "speculation regarding the state of mind and motivations of certain parties . . . ."). The same rule should apply here.

4. Professor Thel Attempts to Offer Inadmissible Testimony About Evidence Law

Professor Thel further argues that

> the importance of the acquisition negotiations cannot be demonstrated by asking clients of the Respondents whether they wish they had known of the negotiations, or whether they would have acted differently had they known.

(Thel Report at 4.) However, what evidence the Division proffers to prove materiality is far beyond Professor Thel's expertise. That is solely the province of the Court. Moreover, Professor Thel is simply wrong. Courts routinely permit investors to establish materiality by testifying to the information that was, or would have been, important to them at the time they decided to invest. In fact, even in criminal cases, investors are routinely permitted to answer hypothetical questions about the importance of undisclosed information to their investment decision.[16]

5. Section D of the Thel Report Offers an Impermissible Legal Conclusion Concerning the Definition of the Word "Affiliate" Under the Advisers Act

Finally, the Thel Report seeks to provide the Court with the legal definition of the work "Affiliate" under the Advisers Act and the conclusion that "[i]t is absolutely clear that

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[16] See, e.g., United States v. Platten, 448 F. App'x 873, 876 (11th Cir. 2011) (affirming trial court's decision to allow investor to testify to the impact on his investment decision of information that he did not know); United States v. Laurienti, 611 F.3d 530, 549-50 (9th Cir. 2010) (rejecting defendant's challenge to prosecution's examination of investors with questions about how disclosure of undisclosed facts would have affected investment decision); United States v. Dukes, 242 F. App'x 37, 45-46 (4th Cir. 2007) (affirming use of hypothetical questioning with investor about effect of undisclosed information).

the Respondents and the Funds were unaffiliated within the meaning of the securities laws." (Thel Report at 9-10.) However—as the Second Circuit recognized in a very similar case—such testimony constitutes an impermissible legal conclusion. In United States v. Bilzerian, the District Court precluded defendant's expert from testifying as to what the phrase "personal funds," meant in the context of Form 13D, "because it related directly to the issue of whether Bilzerian's actual 13D disclosures complied with the legal requirements." 926 F.2d at 1295. The Second Circuit upheld the District Court's ruling. So it is here, where Professor Thel—abandoning all pretense of discussing industry custom—provides the legal conclusion that the Respondents use of the term was "absolutely correct." (Thel Report at 9.) This opinion is foreclosed by Bilzerian and should be precluded here.

CONCLUSION

For the foregoing reasons, the Division respectfully requests that the Court strike Professor Thel's Report Sections A, B, C, and D and to preclude Professor Thel from giving any testimony on these topics.

Dated: January 12, 2015
New York, New York

DIVISION OF ENFORCEMENT

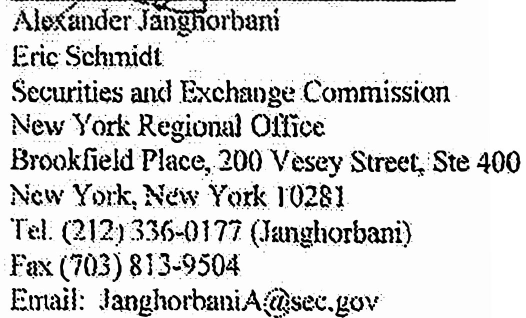

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EXHIBIT A

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16037

In the Matter of

EDGAR R. PAGE and PAGEONE FINANCIAL INC.,

Respondents.

EXPERT REPORT OF STEVE THEL

I have been retained by counsel for the Respondents in the above-captioned proceeding to provide expert testimony as to the matters discussed herein. I am being compensated at my ordinary hourly rate, and my compensation it not dependent on my opinions or the outcome of this matter.

I am the I. Maurice Wormser Professor of Law at Fordham University in New York City, where I teach courses in contracts, corporate law and securities regulation. I have also taught securities regulation at the Columbia, Cornell, Mississippi and NYU law schools. My resume, which documents my qualifications and includes a list of my publications, is appended to this report as Exhibit 1.

I have testified as an expert and submitted expert reports, declarations and affidavits on contract law, securities regulation, investment management, corporate and securities industry practice in various judicial proceedings and arbitrations. I have been retained by the United States government to testify as an expert in numerous criminal securities fraud cases and by the SEC to testify as an expert in numerous civil and administrative cases.[1] A list of the matters in which I have testified as an expert at trial or by deposition recently, including within the preceding four years, is appended to this report as Exhibit 2.

In preparing this report, I reviewed documents that I received from counsel, and which are listed in Exhibit 3 to this report, and I have assumed their authenticity. I have also done such research as I have considered appropriate. The opinions set forth below are based on my review of these documents, my research and my experience.

A. It is the appropriate custom and practice of parties negotiating corporate acquisitions to agree to keep their negotiations secret.

1. Parties engaged in takeover negotiations have important, legitimate and well-known interests in keeping those negotiations confidential. Indeed, negotiating parties typically promise each other to keep the negotiations confidential, and insist that those promises be kept.

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[1] I have also been retained by the SEC to testify in a number of cases in which my testimony eventually proved not necessary, including *SEC v. Calmes* (S.D. Fla.); *SEC v. Ogle* (N.D. Ill.); and *SEC v. Teo* (D.N.J.).

2. A potential acquirer does not want its interest to attract other bidders, and wants to avoid becoming involved in a bidding war. Potential acquirers almost always insist that the target not disclose the bid, and often demand that the target not seek other bids. A target, in turn, wants to assure the bidder that it will not misuse the bid to attract competing bidders, for the failure to make such assurances is likely to lead the potential acquirer to reduce its bid or even walk away. Moreover, the potential acquirer will want to review the target's books and records, and the target will naturally want the acquirer to keep those books and records confidential. Acquirers typically demand confidentiality of their bids as part of the price for their promises to keep the target's records confidential.

3. Accordingly, parties almost always agree to keep such negotiations confidential. I understand that it is undisputed that the Respondents and the potential acquirers of PageOne agreed to keep their negotiations confidential. Provisions like these are ordinary and appropriate. Indeed, it would have been remarkable if the parties had not agreed to such provisions.

4. Courts and regulators alike have recognized that parties negotiating corporate acquisitions have legitimate and compelling interests in keeping their negotiations secret. I offer the following authorities not as statements of governing law, but as examples of judicial and administrative recognition of the importance and legitimacy of keeping negotiations secret.

5. Courts have regularly found that negotiating parties' interest in maintaining confidentiality is entitled to respect. For example, a number of the federal circuits held that the parties legitimately keep preliminary merger negotiations confidential because revelation of negotiations might kill deals.[2]

6. The SEC itself has explained that, notwithstanding the requirement of Item 303 of Regulation S-K that management discuss trends likely to have a material effect on an issuer's financial condition, registrants need not disclose merger negotiations:

> While Item 303 could be read to impose a duty to disclose otherwise nondisclosed preliminary merger negotiations, as known events or uncertainties reasonably likely to have material effects on future financial condition or results of operations, the Commission did not intend to apply, and has not applied, Item 303 in this manner. As reflected in the various disclosure requirements under the Securities Act and Exchange Act that specifically address merger transactions, the Commission historically has balanced the informational need of investors against the risk that premature disclosure of negotiations may jeopardize completion of the transaction. In general, the Commission's recognition that registrants have an interest in preserving the confidentiality of such negotiations is clearest in the context of a registrant's continuous reporting obligations under the Exchange Act,

[2] *See, e.g.*, *Flamm v. Eberstadt*, 814 F.2d 1169, 1176 (7th Cir. 1987).

where disclosure on Form 8-K of acquisitions or dispositions of assets not in the ordinary course of business is triggered by completion of the transaction.[3]

The self-regulatory organizations have also recognized that the importance of keeping negotiations over corporate acquisitions confidential justify exceptions from otherwise applicable disclosure obligations.[4]

B. Mr. Page's fear that PageOne's clients would overreact to disclosure of the negotiations was a common and legitimate concern and does not show that the negotiations were material or that he thought they were.

7. The Commission's Staff asserts that Mr. Page's admitted desire to keep secret the negotiations to sell all or part of PageOne was somehow suspect.[5] However, the fear of investor overreaction (like the fear that premature disclosure of negotiations will lead to their collapse) is itself an important reason to keep negotiations secret. The fact that Mr. Page held this fear is typical and legitimate and does not mean either that he thought the negotiations were important information for investors or that the negotiations were important to the Respondents' clients.

8. The possibility of investor overreaction to disclosures has long been recognized as a real and important phenomenon. The problem has been recognized as particularly pronounced when the question comes to acquisition discussions. I note cases have held that premature disclosure of merger negotiations can confuse and harm investors by leading them to erroneously believe that a deal is certain. (And, again, I cite these cases not for propositions of law but as examples of judicial recognition of the problem.) Some of these courts quite consciously so held in part for fear that investors told of negotiations would overestimate the likelihood that negotiations would lead to actual mergers. "Such negotiations are inherently fluid and the eventual outcome is shrouded in uncertainty. Disclosure may in fact be more misleading than secrecy so far as investment decisions are concerned."[6]

9. Mr. Page's legitimate fear was amplified in this case, where disclosure of the preliminary acquisition negotiations in Form ADV would have revealed these negotiations to thousands of PageOne's investment clients and its business partners, compared to the very small number of PageOne's clients who were suitable Private Fund investors. Thus, Form ADV was not an appropriate disclosure mechanism for the Respondents' acquisition negotiations given the enormous discrepancy between the limitless universe of who would have been given access to

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[3] SEC, *Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures*, Securities Act Release No. 6835 (May 18, 1989).
[4] *See Flamm*, 814 F.2d at 1176 ("Both the New York and the American Stock Exchanges therefore suggest that listed firms postpone announcements [of mergers] until definitive agreements have been reached.").
[5] *See* Amended Order Instituting Proceedings ¶ 17.
[6] *See Reiss v. Pan American World Airways, Inc.*, 711 F.2d 11, 14 (2d Cir. 1983); *see also Greenfield v. Heublein, Inc.*, 742 F.2d 751, 756 (3d Cir. 1984); *Staffin v. Greenberg*, 672 F.2d 1196, 1206 (3d Cir. 1982).

this confidential information and the very limited universe of clients who might consider investing in the Private Funds.

C. *The Respondents' Conflict of Interest Disclosures Relating to Recommending of the Private Funds Were Not Materially Misleading.*

1. *Some Background Observations on Materiality*

10. Materiality is a mixed question of law and fact[7] about which courts routinely rely upon experts for guidance.[8] My opinions on the questions of materiality in this case are not presented as an opinion on the law, but rather are presented to elucidate industry practices and custom that provide an important context in which to evaluate the determination of materiality.

11. In this regard, I also note that the standard applicable to determine whether the acquisition negotiations were material is whether a reasonable person would consider them material, not whether a client of PageOne actually believed that the negotiations would have been important to his or her decision of whether to invest in the Private Funds.[9] Thus, the importance of the acquisition negotiations cannot be demonstrated by asking clients of the Respondents whether they wish they had known of the negotiations, or whether they would have acted differently had they known.

12. In addition, the materiality of the acquisition negotiations cannot be judged based upon "hindsight bias" — i.e., by judging disclosures that were made in the past based upon information that is now known.[10] Thus, it would be improper to say that the unimportance of the negotiations is demonstrated by the fact that the acquisition never occurred. The importance of the negotiations has to be judged at the time at which they occur, not in hindsight.

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[7] *TSC Industries, Inc. v. Northway*, 426 U.S. 438 (1976) ("The issue of materiality may be characterized as a mixed question of law and fact, involving as it does the application of a legal standard to a particular set of facts.").

[8] *SEC v. Cuban*, 2013 U.S. Dist. LEXIS 37167 (N.D. Tex. July 23, 2013).

[9] *TSC Industries, supra*; *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1318 (2011) ("In *Basic* [*v. Levinson*, 485 U.S. 224 (1988)], we held that this materiality requirement is satisfied when there is 'a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available.' [485 U.S.] at 231-232 . . . (*quoting* [*TSC Industries*, 426 U.S. at 449]. We were 'careful not to set too low a standard of materiality,' for fear that management would 'bury the shareholders in an avalanche of trivial information.' 485 U.S. at 231 . . . (*quoting TSC Industries*, 426 U.S. at 448-449.").

[10] *City of Pontiac Policemen's and Firemen's Retirement System v. UBS AG, et al.*, 752 F.3d 173 (2d Cir. 2014) ("We do not recognize allegations of fraud by hindsight"); *Special Situations Fund III QP, LP v. Deloitte Touche Tohmatsu CPA, Ltd.*, 2014 U.S. Dist. LEXIS 99861 (S.D.N.Y. July 21, 2014) ("To the extent that Plaintiffs argue that new management quickly unearthed the fraud, and thus it was easily discoverable, this argument suffers from hindsight bias"); *In re PUDA Coal Securities Inc. Litig.*, 2014 U.S. Dist. LEXIS 83138 (S.D.N.Y. June 25, 2014) ("Facts merely supporting an inference that an audit could have been done better constitute 'fraud by hindsight' and do not support the requisite scienter").

2. The Probability-Magnitude Standard of Materiality Applicable in This Case

13. I do not understand the Commission Staff to allege that an investment adviser must inform its clients whenever it is negotiating a sale of all or part of its investment management business.[11] Instead, I understand the Commission Staff to allege that the negotiations created serious conflicts of interest between the Respondents and their clients, such that the Respondents were obligated to disclose those conflicts to any clients to whom they recommended the Private Funds.

14. While negotiations over the sale of part of PageOne were ongoing, the materiality of any potential conflict depended upon the balance of the probability that the transaction would be completed and the magnitude of the conflict that would exist if the acquisition did occur.[12]

a. Probability

15. In the end, the transaction was not completed, and in the end the negotiations were abandoned. I understand that throughout the negotiations there was substantial doubt that the acquisition would be made, and the Commission Staff itself emphasizes this fact. These facts suggest that the probability of the acquisition occurring was far less than 100 percent during the period 2009 through 2011.

b. Magnitude

16. Assuming the acquisition was guaranteed to occur — i.e., a 100 percent probability of occurrence — the question then becomes whether the magnitude of the event — the acquisition — would have changed the total mix of information made available to the Respondents' clients when they evaluated the recommendations by the Respondents to invest in the Private Funds. This analysis depends upon whether the conflict of interest disclosures made by the Respondents materially misled the Respondents' clients into believing that the Respondents were materially less conflicted than was the case. In analyzing this question, the relevant investment decision to which materiality is relevant is a simple one: how the Respondents' clients would have evaluated the recommendations of the Respondents to invest in the Private Funds if they had known the additional facts. In my opinion, and based upon industry custom and practice, I do not believe that the acquisition, if consummated, would have materially increased the Respondents' conflict of interest in recommending investment in the Private Funds to their clients.

17. In analyzing this question, I note several facts which I understand to be undisputed. First, the decision to invest in the Private Funds was made by each individual client; the Respondents did not make these investment decisions for the clients by using a power of attorney. Second, all of the clients who invested in the Private Funds were accredited investors. Third, I understand that all of the Respondents' clients who invested in the Private Funds

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[11] An investment adviser is not obligated to make such a disclosure, and it is not customary for advisers to do so.

[12] *Basic Inc. v. Levinson*, 485 U.S. 224 (1988).

received a private placement memorandum for each Fund and there is no allegation that these memoranda were false or misleading.

18. I also understand that it is undisputed that the Respondents made conflict of interest disclosures in connection with recommendations of the Private Funds. In fact, PageOne disclosed facts that would alert potential investors to a direct conflict of interest faced by PageOne in advising clients to invest in the Private Funds in Part 2 of its Form ADV. Form ADV, and particularly Part 2, is the primary mechanism for communicating with clients about conflicts. The Forms are publicly available at a number of places and I understand PageOne always made its current Form ADV Part 2 publicly available on its website, in a place that was never password-protected.

19. PageOne's Forms ADV Part 2, dated July 31, 2009, April 15, 2010, and June 10, 2010, stated, with respect to the Private Funds, that:

> *Fee Schedule:* PageOne Financial does not directly charge the client a fee for this service. PageOne Financial is compensated by a referral fee paid by the Manager of the Private Fund(s) in which its clients invest. The management and other fees the client pays to the Private Funds are not increased as a result of Registrant's referral of clients to the Private Funds. PageOne Financial will typically receive, on an annual basis, a referral fee of between 7.0% and 0.75% of the amount invested by the client in the applicable Private Fund(s).

These documents also stated that "PageOne Financial will act as a solicitor for certain private investment funds, and for doing so will receive a referral fee."

20. PageOne amended its Form ADV again on September 14, 2010 to delete the longer statement set out above (but continued to include the shorter statement), and added that:

> Edgar R. Page, Chairman and Chief Financial Officer of PageOne Financial, is also employed as a consultant to The United Group of Companies, Inc. ("UGOC"). UGOC is a real estate investment and development firm. Mr. Page is compensated for the consulting services he provides to UGOC. As disclosed above, PageOne Financial recommends private funds that are managed by the UGOC to PageOne's advisory clients for which PageOne Financial receives an advisory fee. Advisory clients are under no obligation to participate in such investments.

21. These statements revealed a substantial conflict of interest attendant to the Respondents' recommendations of the Private Funds. The first set of Form ADV amendments told potential investors that PageOne would receive referral fees of up to 7% *per year* from the Fund Manager, if they invested in the Private Funds. The second set also stated that PageOne would receive referral fees, although without stating the amount, but added that Mr. Page was employed and compensated by the Fund Manager. These statements revealed a significant conflict of interest. Based on my experience with conflict of interest disclosures by investment advisers and my understanding of industry practices and customs, I conclude that disclosure of the negotiations would not have changed the total mix of information available to PageOne clients.

22. The difference between the conflict of interest that PageOne disclosed to its clients and the potential conflict of interest that would have been disclosed if the acquisition negotiations were revealed was not, based upon my experience, material.[13] The investors were informed that PageOne had substantial conflicts of interest in recommending the Funds. Further disclosure of the negotiations would not have led reasonable investors to conclude that the conflict was greater than the conflict that the Respondents revealed. There is no substantial likelihood that a reasonable client who invested in the Private Funds in the face of the statements the Respondents made would not have invested if the Respondents had disclosed the negotiations.[14]

23. I understand that there is a dispute about the status of the negotiations. Broadly speaking, I understand that the Commission Staff alleges that there was an agreement and that the final portion of the purchase price would not be paid until Mr. Page raised approximately $20 million for the Private Funds.[15] I also understand that the Respondents again speaking broadly, insist that there was no such agreement to sell part of PageOne only if $20 million was raised by Respondents for the Private Funds, and that the payments the Fund Manager made to Mr. Page were earnest money deposits. I also understand there is an allegation that the Respondents knew that the Fund Manager was paying for the acquisition from the proceeds from investments in the Private Funds by the Respondents' clients, although this allegation is also disputed.

24. In particular, the Order Instituting Proceedings alleges the following:

> Specifically, from early 2009 through approximately September 2011, Respondents knowingly or recklessly failed to tell their clients that:
>
> a. One of the Private Funds' managers (the "Fund Manager") was in the process of acquiring at least 49% of PageOne for approximately $2.7 million;
>
> b. As part of that acquisition, E. Page had agreed to raise millions of dollars for the Private Funds from his advisory clients; and
>
> c. The Fund Manager was paying for the acquisition by making a series of installment payments over time, the timing and amounts of which were, at least partially, tied to Respondents' ability to direct client money into the Private Funds[16]

25. Even if the Commission Staff is correct on the facts, the question remains whether the disclosure of the Staff's version of the facts would have changed the total mix of information available to the investors. As noted above, the Respondents told potential investors that they faced substantial conflicts in recommending the Funds. Those conflicts, which were stated to

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[13] The General Instructions for Form ADV instruct registrants to amend their brochure supplements (Part 2 of Form ADV) "if any information in them becomes materially inaccurate."
[14] *See TSC Industries*, 426 U.S. at 446.
[15] *See* Amended Order Instituting Proceedings ¶ 20.
[16] *See* Amended Order Instituting Proceedings ¶ 2.

arise from the receipt of referral fees when clients invested in the Private Funds, were, as disclosed, dependent upon the Respondents' clients investing in the Private Funds. This disclosed conflict of interest is not materially different from the alleged undisclosed conflict that would arise if $20 million were invested in the Private Funds, thereby providing the funding for the 49% investment in the Respondents' advisory business.[17] The disclosed conflict put the Respondents' clients on notice that the Respondents' recommendations of the Private Funds were materially conflicted and this conflict arose because the Respondents stood to profit if their clients invested in the Private Funds. This is not a materially different conflict of interest than the one the Commission's Staff alleges existed.

26. The Commission Staff alleges that the Respondents and the Fund Manager had agreed that the acquisition would not close, and the final payment of the purchase price would not be made, until the Respondents raised approximately $20 million for the Private Funds.[18] The Staff also alleges that Mr. Page was obligated to return the earnest money deposits if the acquisition was not completed.[19] I understand that the Respondents position is that no acquisition agreement was ever completed, and that the Respondents were entitled to keep part of the earnest-money deposits regardless of whether an acquisition ever occurred.[20]

27. If the Staff is right, then the conflict that the Respondents disclosed—a 7% per year referral fee—was greater than the conflict that actually existed. The Respondents stated that they would receive a large fee from every investment in the Private Funds. On the Staff's version, however, the Respondents were not entitled to anything until $20 million was invested in the Private Funds, and even then the Respondents would have to surrender 49% of PageOne. The Respondents' Forms ADV stated that they were certain to receive substantial payments if their clients invested in the Private Funds, while, according to the Staff, the right to payment was quite uncertain and contingent.[21] Thus the Respondents disclosed a conflict much more severe than the one the Staff claims existed. Accordingly, if the Staff's version of the facts is correct, the Respondents' Forms ADV actually overstated the conflict that actually existed.

28. I also understand that the parties disagree about whether the earnest money deposits (or what the Staff calls "installment payments") were tied to the amount of money the Respondents' clients invested in the Private Funds. Even if they were, however, the Forms ADV overdisclosed whatever conflict this would have created, inasmuch as they indicated that the Respondents would receive up to 7% *per year* in referral fees.

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[17] *See* Amended Order Instituting Proceedings ¶ 22.
[18] *See* Amended Order Instituting Proceedings ¶¶ 10, 36.
[19] *See* Amended Order Instituting Proceedings ¶¶ 22, 39.
[20] *See also* Resp. Ex. 15 (April 14, 2010 Proposal) ¶ 2.
[21] An investor who intended to stay in the Funds for a little over two years expected that the Respondents would get the same benefit under either version of the facts, with payment under the Staff's version conditioned as discussed in the text.

D. Neither the Fund Manager nor the Private Funds were Affiliates of the Respondents.

29. Finally, I note that I strongly disagree with the Commission Staff's repeated contention that the Forms ADV were misleading when they stated that the Private Funds and the Fund Manager were "unaffiliated" with the Respondents.[22]

30. The word "affiliate" is extremely important in securities regulation and has very precise definitions, which turn on control.[23] It is absolutely clear that the Respondents and the Funds were unaffiliated within the meaning of the securities laws. The Respondents used the word "unaffiliated" in Forms ADV filed with the Commission, in a manner entirely consistent with the definition of the term "affiliate" in the Commission's own glossary of terms for Form ADV.[24] The Commission Staff's contention that the Respondents' absolutely correct use of the term was misleading is untenable.

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[22] *See* Amended Order Instituting Proceedings ¶¶ 20, 29.

[23] Thus SEC rule 405 provides that, "An affiliate of, or person affiliated with, a specified person, is a person that directly, or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with, the person." "Control," in turn, means "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." The Investment Advisers Act and the Investment Company Act define the term "affiliated person" in even more detail.

[24] The Glossary states, in pertinent part,

"**Advisory Affiliate:** Your advisory affiliates are (1) all of your officers, partners, or directors (or any ***person*** performing similar functions); (2) all ***persons*** directly or indirectly ***controlling*** or ***controlled*** by you; and (3) all of your current ***employees*** (other than ***employees*** performing only clerical, administrative, support or similar functions). "

"**Control:** The power, directly or indirectly, to direct the management or policies of a ***person***, whether through ownership of securities, by contract, or otherwise.

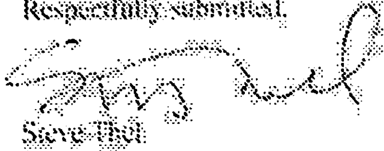
Each of your firm's officers, partners, or directors exercising executive responsibility (or ***persons*** having similar status or functions) is presumed to control your firm.

A ***person*** is presumed to control a corporation if the ***person***: (i) directly or indirectly has the right to vote 25 percent or more of a class of the corporation's voting securities; or (ii) has the power to sell or direct the sale of 25 percent or more of a class of the corporation's voting securities.

A ***person*** is presumed to control a partnership if the ***person*** has the right to receive upon dissolution, or has contributed, 25 percent or more of the capital of the partnership.

A ***person*** is presumed to control a limited liability company ("LLC") if the ***person***: (i) directly or indirectly has the right to vote 25 percent or more of a class of the interests of the LLC; (ii) has the right to receive upon dissolution, or has contributed, 25 percent or more of the capital of the LLC; or (iii) is an elected manager of the LLC.

Respectfully submitted,



Steve Thiel

January 5, 2015

A *person* is presumed to control a trust if the *person* is a trustee or ***managing agent*** of the trust."