UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Admin. Proc. File No. 3-17930

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In the Matter of the Application of :

LOUIS OTTIMO :

For Review of Disciplinary Action Taken :
By FINRA

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APPLICANT'S OPENING BRIEF

INTRODUCTION

On June 28, 2018, the Commission partially reversed fraud findings that had been erroneously made by FINRA in a disciplinary proceeding brought against Louis Ottimo ("Ottimo"). The Commission remanded the matter to FINRA for reconsideration of the permanent bar sanction that FINRA had imposed on Ottimo based, at least in part, upon the erroneous fraud finding.

Nearly two years later, on March 27, 2020, FINRA re-imposed the permanent bar sanction despite the fact that half of its fraud claims had been reversed by the Commission. In its most recent decision, FINRA erroneously concluded that Ottimo's conduct was "egregious". Worse, FINRA determined that Ottimo's efforts to defend himself against the fraud charges constituted proof of a "propensity for future wrongdoing."

The Commission must reverse the permanent bar sanction against Ottimo because any fair and balanced review of the evidence demonstrates conclusively that there is no principled basis for imposing a permanent bar as a remedial sanction. If the Commission upheld the permanent bar in this case as "remedial", then the Commission would, in substance, authorize FINRA to impose a permanent bar in every disciplinary proceeding in which an associated person has been found liable on any "fraud" charge, regardless of the character and severity of the underlying conduct. Such a blanket sanction cannot be considered "remedial" and is completely contrary to FINRA's own Sanctions Guidelines and applicable Commission precedent. Therefore, the Commission must vacate the permanent bar sanction in this case because it is clearly punitive and not justified by a reasoned application of FINRA's Sanctions Guidelines.

FACTS

A. The PPM

The permanent bar sanction imposed against Ottimo arose from two sentences that appear in a twenty-nine page private placement memorandum ("PPM") for First Secondary Market Fund LLC (the "Fund"). The business purpose of the Fund was to pool investor monies to purchase pre-IPO common stock issued by Facebook Inc. (and possibly other companies such as Twitter.) The PPM was drafted by attorneys at Carter, Ledyard & Milburn LLP ("CLM"), hired for the express purpose, by Ottimo and the co-manager of the Fund, of preventing any possible improper solicitation of investors through the PPM. The relevant two sentences contained the following information about Jet One Jets, Inc. ("Jet One"), a private, unrelated business for which Ottimo had served as a senior executive for a period of time:

> Previously, Mr. Ottimo co-founded Jet One Jets in April 2006 and successfully negotiated an exclusive reseller agreement with American Express to handle the Jet One Jets prepaid card. Jet One Jets grew to $18 million in revenues inside approximately 18 months.

The fraud finding against Ottimo is based on the claim that those two positive sentences triggered an obligation by the Fund and Ottimo to include specific pieces of negative information about Jet One Jets in the PPM and the failure to include the negative information made the entire PPM materially misleading.

During the course of their work for the Fund, CLM requested that Ottimo and the co-manager of the Fund provide biographies to CLM for inclusion in the PPM. Ottimo drafted a short biography largely based on a biography that had been published by a company for which he served on the board of directors and biography included the two sentences about Jet One Jets. In addition to submitting that document to CLM for review, CLM also received a FINRA

BrokerCheck report concerning Ottimo, which described Ottimo's history in the securities industry and included disclosure of substantial negative personal financial information, including Federal tax liens and unsatisfied private civil judgments.

B. The Prior Commission Decision

When FINRA first brought its fraud charges against Ottimo, those charges were based on alleged material omissions from Ottimo's biography that appeared in the PPM concerning both Jet One Jets and Wheatley Capital ("Wheatley"), another private company for which Ottimo served as a senior executive. Both the Initial Decision issued by a FINRA Disciplinary Panel in July 2015 and a decision issued by the FINRA National Adjudicatory Council in March 2017 found that FINRA's Department of Enforcement had proven the fraud charges concerning omitted information regarding both Jet One Jets and Wheatley.

In June 2018, the Commission reversed the fraud findings concerning Wheatley (the "2018 Commission Order"). The Commission held that Ottimo had not been required to disclose negative financial information about Wheatley because there is no general affirmative duty to disclose information about unrelated business activities when privately selling securities issued by a new special purpose investment vehicle. 2018 Commission Decision, pp. 18-19. However, the Commission upheld the portion of the fraud charges based upon omitted information concerning Jet One because, *inter alia*, the two sentences in the PPM concerning Jet One "misleadingly implied that [Jet One] was a profitable business." 2018 Commission Decision, p. 18. The Commission further found that the negative information concerning Jet One Jets omitted from the PPM was material because investors would need to rely on Ottimo's management

abilities concerning the business of the Fund. 2018 Commission Decision, pp. 13-14.[1] The Commission made these findings concerning the materiality of the omitted information even though the hearing record did not include expert testimony or testimony from Fund investors that the omitted information would have been important to a reasonable investor considering an investment in the Fund.

Based on its reversal of the fraud charges relating to Wheatley, the Commission remanded the proceeding to FINRA so that FINRA could "determine what sanctions are appropriate for the portion of the fraud violation" that involved the Jet One Jets information. 2018 Commission Decision, pp. 19-20.

C. FINRA's Decision On Remand

On March 27, 2020, the FINRA National Adjudicatory Council issued a decision that reaffirmed the permanent bar sanction (the "2020 FINRA Decision"). According to FINRA, the hearing record demonstrated that Ottimo "committed an egregious offense in connection with the sales of securities to the investing public that warrants robust sanctions." 2020 FINRA Decision, p. 6. This decision identified the following to be aggravating factors supporting the imposition of a permanent bar: (a) Ottimo had acted with scienter; (b) the "fraudulent omissions significantly impacted the entire Fund offering period, which lasted several weeks"; (c) the amount of money raised and number of investors were "substantial"; and (d) Ottimo defended himself against the fraud charges and refused to "accept responsibility for his conduct." 2020 FINRA Decision, p. 7.

[1] The 2018 Commission Decision erroneously stated that Ottimo must have been affiliated with Jet One Jets at the time of its bankruptcy filing because Ottimo "personally signed its bankruptcy petition". 2018 Commission Decision, p. 13. The record in this matter shows that Ottimo's brother, Richard Ottimo, signed that bankruptcy petition.

On remand, FINRA also rejected all of Ottimo's arguments that the existence of mitigating factors did not justify the imposition of a permanent bar. 2020 FINRA Decision, pp. 7-9.

The 2020 FINRA Decision, in substance, holds that any person associated with a member firm who is charged with fraud, defends himself against those charges, and loses before a FINRA disciplinary panel must be permanently barred from association with a member firm. FINRA's characterization of Ottimo's conduct in this case as "egregious" erroneously lumps together omissions from a PPM that was drafted and reviewed by outside legal counsel with raw Ponzi schemes. Moreover, many of the "aggravating" factors relied upon by FINRA to justify the permanent bar sanction would be present in every disciplinary proceeding brought by FINRA's Department of Enforcement that included fraud charges and were not settled by the associated person prior to a hearing. If FINRA believes that all persons found liable for fraud by a FINRA disciplinary panel should be permanently barred from association with a member firm, then FINRA should propose such a rule to the Commission. Until that time, FINRA should consistently apply the factors described in its Sanctions Guidelines which, in this case, cannot justify the imposition of a permanent bar as a purely remedial sanction.

ARGUMENT

THERE IS NO PRINCIPLED, RATIONAL BASIS FOR IMPOSING THE PERMANENT BAR AS A REMEDIAL SANCTION BASED UPON THE ACTUAL EVIDENCE IN THIS PROCEEDING AND THE FINRA SANCTIONS GUIDELINES

Section 19(e)(2) of the Securities Exchange Act of 1934 provides that the Commission, "having due regard for the public interest and the protection of investors", may cancel any FINRA sanction that is "excessive or oppressive." In determining whether a sanction is "excessive or oppressive", the Commission must consider any aggravating or mitigating factors and whether the sanction imposed by FINRA is remedial, rather than punitive. *See Saad v. SEC*,

718 F.3d 904, 906 (D.C. Cir. 2013); *PAZ Sec., Inc. v. SEC*, 494 F.3d 1059, 1064-65 (D.C. Cir. 2007). While the Commission is not bound by the Sanction Guidelines published by FINRA, the Commission has referenced those guidelines when reviewing a FINRA-imposed sanction. *Gregory Evan Goldstein*, Exchange Act Release No. 71970, 2014 WL 1494527, at *10 (Apr. 17, 2014).

FINRA has repeatedly emphasized in its Sanctions Guidelines that disciplinary sanctions should be imposed: (a) "when necessary and appropriate to protect investors"; and (b) "consistently and fairly". In addition, disciplinary sanctions should "reflect the seriousness of the conduct at issue" and be "remedial", not punitive. *See, e.g.*, 2019 FINRA Sanctions Guidelines, https://www.finra.org/sites/default/files/Sanctions_Guidelines.pdf, pp. 2-3.

A bar from association with a member firm is the most severe sanction available in a FINRA disciplinary proceeding. By imposing a bar, FINRA makes a public determination that the person against whom the bar is imposed cannot be deterred from future violations by the lesser sanctions of a suspension and fine. If a lesser sanction is sufficient, the imposition of a permanent bar is necessarily punitive and, therefore, improper.

To assess the "seriousness of the conduct at issue", the Sanctions Guidelines identifies a list of factors – the Principal Considerations in Determining Sanctions – that "should be considered in conjunction with the imposition of sanctions with respect to all violations." FINRA Sanctions Guidelines, p. 7. The Sanctions Guidelines further state that "the relevancy and characterization of a factor depends on the facts and circumstances of the case and the type of violation." *Id.*

Here, the only "aggravating" factors that apply are Principal Considerations Nos. 13 (the misconduct was the result of an intentional act or recklessness) and 16 (the misconduct resulted

in the potential for monetary or other gain). Balanced against those two factors are the following mitigating considerations:

1. Ottimo and the co-manager of the Fund hired CLM for the express purpose of making sure that the PPM complied with all securities laws and regulations. Ottimo provided all information requested by CLM and understood that CLM evaluated whether additional negative information concerning Ottimo needed to be included in the PPM. Clients hire attorneys to provide legal advice and to ask questions of the clients as needed. Ottimo reasonably relied on CLM to guide the Fund concerning the disclosures to be made in the PPM. [Principal Consideration No. 7.]

2. The sole basis for the fraud charge is the failure to include negative information regarding Jet One Jets in the PPM, which was used by the Fund to raise monies from twenty-one investors over a period of several weeks. There was no evidence that Ottimo engaged in a pattern of misconduct regarding private placement memoranda or that the incomplete information concerning Jet One Jets included in the PPM involved "numerous acts." [Principal Consideration No. 8.]

3. The time period that the PPM was used to raise funds from investors was less than two months. No evidence of fraudulent conduct was presented at the hearing concerning any other time period. [Principal Consideration No. 9].

4. None of the investors in the Fund suffered any injury. [Principal Consideration No. 11.]

5. The number and size of the transactions at issue was extremely small – one offering for a limited time period that involved twenty-one investors and less than $4 million in monies raised by the Fund. [Principal Consideration No. 17.]

6. The affected customers were all sophisticated, accredited investors. [Principal Consideration No. 18.]

More generally, the basis of the fraud charge -- the omission of negative information regarding Jet One Jets, a business completely unrelated to the Fund – is simply not an example of "egregious" fraud. No affirmative misrepresentations were made by Ottimo concerning the Fund, his personal background or any other subject discussed in the PPM. No monies were misappropriated from the Fund by Ottimo or anyone else. No investor suffered any financial

losses in connection with their investment in the Fund. The investors received exactly what the PPM represented concerning the Fund.

Nor should Ottimo's conduct be judged fairly to be "egregious" when he specifically hired expert legal counsel to provide advice concerning the PPM and he followed the advice provided. Even if Ottimo's communications with CLM failed to meet the standard of proof required for a formal "advice of counsel" defense to the fraud charge, the fact remains that CLM was hired in good faith and paid substantial fees so that the Fund's PPM fully complied with the Federal securities laws. The Commission has repeatedly recognized that determining when additional disclosure is required can be a complex task where even legal experts can disagree on the judgment calls involved in that determination. For example, in April 2014, Keith F. Higgins (then-Director of the Division of Corporate Finance) made the following comments to the Federal Regulation of Securities Committee of the American Bar Association:

> We also understand that materiality is not an easily applied litmus test. If there any gray areas — and as disclosure lawyers I would suspect that you more frequently see shades of gray, rather than black and white — the company is likely to include the disclosure in its filing. And why wouldn't you? Why would you take the risk of omitting disclosure that might be material? But are too many items in the obviously immaterial category being included?
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> Disclosure overload for one person, however, may be not enough disclosure for another. While an individual investor may feel overloaded — and a bit overwhelmed — with information in a periodic report, other investors have said there is not a "part of the disclosure pie that goes uneaten." Investors in different securities also might have different needs. Are the informational needs of fixed income and equity securities the same? The question "who is the disclosure written for?" does not lend itself to an easy answer.

https://www.sec.gov/news/speech/2014-spch041114kfh (footnote omitted).

In the 2020 FINRA Decision, FINRA blithely pretends that these disclosure judgment calls do not exist and further claims that, "[a]s an experienced securities professional", Ottimo

"should have known to include fair and balanced disclosure and to not make his PPM biography misleading." 2020 FINRA Decision, p. 7. Based on his past professional experience, Ottimo sensibly hired CLM to provide legal advice concerning what needed to be disclosed in the PPM. If CLM had believed that the two sentences regarding Jet One Jets in Ottimo's biography could possibly be materially misleading given all the other disclosures in the PPM, CLM would have made further inquiries to Ottimo regarding the business operations of Jet One Jets before signing off on the PPM. While FINRA and the Commission are within their power to determine that CLM and Ottimo got it wrong, for FINRA to describe Ottimo's conduct as "egregious" fraud is utter nonsense.[2]

FINRA's discussion of the so-called "aggravating" factors also reflects the same surreal, upside-down quality as its characterization of Ottimo's conduct as "egregious". Even though the offering period for the Fund "lasted several weeks", FINRA concluded that such a time period constitutes an "extended period of time" and, therefore, an "aggravating" factor. 2020 FINRA Decision, pp, 7, 8 (*citing* Principal Considerations in Determining Sanctions, No. 9). Similarly, even though the number of investors was less than twenty-five and the amount raised was less than $4 million, FINRA concluded that the number and size of the transactions was so "substantial" that the number and size of the transactions constituted an "aggravating" factor. *Id.*

The improperly punitive nature of the permanent bar sanction imposed by FINRA is best demonstrated by FINRA's finding that Ottimo had refused "to accept accountability for his conduct", which "strongly indicates a propensity for future wrongdoing." 2020 FINRA Decision,

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[2] *See* L. Carroll, *Through The Looking Glass* (1871), Chapter 6: "When I use a word," Humpty Dumpty said in rather a scornful tone, "it means just what I choose it to mean — neither more nor less." "The question is," said Alice, "whether you CAN make words mean so many different things." "The question is," said Humpty Dumpty, "which is to be master – – that's all."

p. 7. FINRA further claimed that Ottimo "blamed others for his own gross failure to disclose material adverse information regarding Jet One Jets." *Id.* Neither of these findings are based upon the facts or Ottimo's testimony, which accurately described the work performed by CLM in connection with the PPM. Maybe Ottimo's testimony did not establish a full advice of counsel defense to the fraud charge concerning Jet One Jets. But that is a far cry from "blaming others" and "refusing to accept accountability for his conduct." The Commission has long encouraged securities market participants to seek out legal advice from competent counsel; the Commission has never held that by describing legal counsel's role in a transaction, a defendant had demonstrated "a propensity for future wrongdoing."

CONCLUSION

For the reasons set forth above and based on the actual evidence presented at the hearing in this proceeding, the Commission should reverse FINRA's erroneous, unjustified, clearly punitive permanent bar sanction.

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