

**BEFORE THE
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C.**

In the Matter of the Application of

LOUIS OTTIMO

For Review of Disciplinary Action Taken By

Financial Industry Regulatory Authority

Administrative Proceeding File No. 3-17930

**BRIEF OF APPLICANT LOUIS OTTIMO IN SUPPORT OF
APPLICATION FOR REVIEW**

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I. INTRODUCTION

This case is about alleged material omissions in the biographical section of a private placement memorandum (“PPM”). The PPM was drafted by a prominent Wall Street law firm for a private offering by a special purpose vehicle that was formed for the limited purpose of purchasing pre-IPO Facebook, Inc. (“Facebook”) stock. The PPM included biographical summaries for the two principals of the fund manager, including Applicant Louis Ottimo (“Ottimo”). FINRA contends that Ottimo’s biography fraudulently omitted material information about two companies referenced therein. This is the sole basis for the fraud findings by FINRA.

This application is to request review of the March 15, 2017 decision issued by the National Adjudicatory Council (“NAC”).¹ The NAC found that Ottimo “consciously chose” not to include alleged material negative information about Jet One Jets (“JOJ”), a private jet

¹ Under Sections 19(d) and (e) of the Securities Exchange Act of 1934, the Commission reviews the final disciplinary actions of FINRA, which in this case is the NAC’s March 15, 2017 decision.

brokerage company, and Wheatley Capital, Inc. (“Wheatley”), a pass-through entity, and only included positive information about these companies. RP 6359 (pg. 7).² The NAC claims that this information ran the risk of misleading investors. RP 6359 (pg. 8).

On the contrary, the omitted information did not the run the risk of misleading investors given the limited purpose of the offering. Investors were interested in buying shares of Facebook, a household name. Investors did not care whether the person buying the Facebook stock was Ottimo or another registered representative. In other words, Ottimo’s successes or failure regarding JOJ and Wheatley, two unknown entities, was inconsequential to investors. In fact, the only task to be performed by Ottimo *and* his co-manager, Nancy Lotvin (who was also the Chief Compliance Officer of the placement agent), was to purchase Facebook stock on the Dutch auction market and perform related administrative tasks. This is what, in fact, occurred and no investors were harmed.

Additionally, the PPM was drafted by a team of experienced securities attorneys from a premier Wall Street law firm. These attorneys, which included two partners of this well-known firm, carefully considered Ottimo’s entire background before deciding what to include or omit from his PPM biography. Ottimo reasonably relied on this expert legal advice and provided the attorneys everything they requested. Finally, with regard to certain findings concerning Ottimo’s role as a principal of the fund manager, an SEC exempt private fund adviser, FINRA lacks jurisdiction.

In sum, for the reasons detailed herein, all of the fraud findings should be dismissed and the bar imposed against Ottimo should be eliminated as it is based solely on the fraud charges.

² "RP" refers to the record page number in the certified record filed in this case by FINRA.

RP 6359 (pg. 17). Alternatively, if the Commission finds that there were violations, the sanctions should be substantially reduced in view of the mitigating circumstances.

II. QUESTIONS PRESENTED

1. Whether the omitted information underlying the fraud charges was material.
2. Whether Ottimo acted with scienter.
3. Whether Ottimo reasonably relied on counsel.
4. Whether FINRA has jurisdiction to make findings with regard to Ottimo's role as principal of an SEC private fund adviser.

III. FACTUAL BACKGROUND

A. The Origins of the Offering and the Law Firm's Crucial Role in the Offering

Customers of EKN Financial Services, Inc. ("EKN"), a FINRA member firm, expressed a desire to purchase Facebook stock ahead of its initial public offering. RP 5606. EKN decided to accommodate its clients' wishes, but wanted to make sure the transaction was fully compliant with all applicable regulations. Accordingly, the services of a highly regarded Wall Street law firm, Carter, Ledyard & Milburn, LLP (hereinafter, "the Law Firm"), were retained to advise on how to structure such a transaction and to draft the PPM, among other things. RP 5867-5870 (Retainer Agreement); RP 5711-5768 (Law Firm invoices); RP 2713 – 3065, 2741 (Tr. pg. 1024).

The Law Firm formed a special purpose vehicle to conduct the private offering, drafted the PPM, formed a private fund adviser to act as the fund manager, and performed numerous other tasks to ensure that the transaction under contemplation was fully compliant. RP 5711-5768 (Law Firm Invoices); RP 4639 – 4742 (PPM). The special purpose vehicle that was formed was a limited liability company by the name of First Secondary Market Fund, LLC (hereinafter, "SPV" or "the fund"). *Id.*

The plan was for SPV to purchase Facebook in a private market operated by SecondMarket, Inc. RP 5605 – 5612; RP 2343 – 2712, 2349 – 2351, 2391 (Tr. pgs. 632 – 634, 674); RP 2713 – 3065, 2740 (Tr. pg. 1023). This private market hosted a series of Dutch auctions, requiring bids of at least \$1 million to buy the required minimum of 25,000 shares of Facebook. *Id.* In a Dutch auction, the seller establishes an asking price which is gradually lowered until it meets a matching bid. *Id.* The bidders place orders for the number of shares they want, specifying the prices they are willing to pay. The final price is the one at which there are enough bidders willing to buy all of the shares in the offering. In such an auction, the bidders (such as SPV) have little or no say in the determination of the price. All bidders were vetted and approved by an attorney for SecondMarket, Inc. and Facebook before SPV could purchase the Facebook stock. *Id.* It is undisputed that SPV did, in fact, accomplish its limited purpose of purchasing Facebook stock in three weekly Dutch auctions and that no investors were harmed.

The Law Firm formed First Secondary Managers, LLC (the “Manager”) to be the manager of SPV pursuant to Rule 203(m)-1 under the Investment Advisers Act of 1940, sometimes referred to as the “private fund adviser exemption.” RP 004650; RP 5606 – 5607. Ottimo and Nancy Lotvin (“Lotvin”) co-managed the Manager and had equal voting control over the Manager. RP 2343 – 2712, 2356 (Tr., 639); RP 2713 – 3065, 2747 - 2748 (Tr. pgs. 1030-1031). Lotvin was also a general securities principal at EKN and held the positions of chief operating officer and financial and operations principal. RP 3107 – 3124 (CX-2); RP 2713 – 3065, 2722 - 2728 (Tr., pgs. 1005 - 1011). Prior to joining EKN, she had held multiple key compliance positions with various FINRA member firms. *Id.*

Given the limited purpose of SPV, Ottimo’s and Lotvin’s only substantive roles as principals of the Manager were to decide the bid price that SPV would place for the Facebook

shares on the Dutch auction market. RP 2343 – 2712, 2391 - 2395 (Tr. 674 – 678); RP 004650 (CX-105, p 12).

EKN was the sole placement agent for the SPV offering. The EKN principal who signed the Placement Agent Agreement was Thomas Giugliano, a Managing Director and the President of EKN. RP 4743 - 4756 (CX-106).

EKN's compliance with FINRA and SEC rules as regards the SPV offering did not rest with Ottimo, who was *not* a General Securities Principal (Series 24) of EKN. RP 3067 - 3105 (CX-1). Ottimo was a registered representative (Series 7) of EKN. *Id.* He has never been licensed as a principal. *Id.*

EKN's chief compliance officer ("CCO") during the relevant period (i.e., the SPV offering) was Richard Borgner ("Borgner"). RP 2343 – 2712, 2601 - 2602 (Tr. 884-885; CX-3). Borgner was responsible for sending out the PPMs to investors and processing the paperwork. RP 2343 – 2712, 2622, 2646 - 2647 (Tr. 905, 929-930). Borgner conceded that he "perused" the PPM and would not have allowed the PPM to go out if there was something misleading in it. *Id.* Indeed, as EKN's Chief Compliance Officer, he and/or another EKN principal would have been required to conduct a reasonable investigation of SPV as part of its due diligence before acting as placement agent, as well as reviewing the PPM to ensure that it was not materially misleading.³

B. The PPM is Prepared By a Premier Wall Street Law Firm

The Law Firm, a top-notch securities firm, devoted substantial resources to drafting the PPM. No less than five (5) lawyers, including two partners, worked directly on the PPM and an additional three attorneys worked on a related Form ADV filing which also required disclosures

³ FINRA members are under a duty to conduct a reasonable investigation of an issuer's securities and the representations made about it and to respond to red flags. See e.g., FINRA Regulatory Notice 10-22.

concerning Ottimo's background. RP 5715 – 5718; RP 5867 - 5870. Prior to commencing the first draft of the PPM and before obtaining a biography from Ottimo, the Law Firm had already pulled his FINRA BrokerCheck Report and were scrutinizing it. RP 5714 – 5715; RP 5893 – 5895. The BrokerCheck Report included, among other things, the following: 1) Ottimo's affiliations with Wheatley, JOJ and two other companies (i.e., Ottimo's outside business activities); 2) all of Ottimo's registrations with prior broker-dealers; 3) all of Ottimo's securities licenses; and 4) "Disclosures of Customer Disputes, Disciplinary, and Regulatory Events," which included eleven events.⁴ Id. In an internal email, the Law Firm discussed the fact that Ottimo had what they referred to as a "colorful past" based on the BrokerCheck Report, but did not ask Ottimo about the BrokerCheck Report as they did not believe it was relevant given that the only purpose of the offering was to buy Facebook stock.⁵ RP 2713 – 3065, 2971 - 2972 (Tr. 1254 – 1255).

Ottimo provided a biography to the Law Firm, as requested. The Law Firm did not give Ottimo any guidance on what to include in his biography and did not give him a background

⁴ The disclosure events consisted of the following: 1) eight liens, including one involving *Wheatley*; 2) two customer disputes (one resulted in an award and the other was closed without action); and 3) a 25-year old misdemeanor plea (without admitting guilt) that was *not* related to securities or any type of malfeasance. RP 5882 – 5891.

⁵ In a February 15, 2012 email string, with the subject line, "EKN placement," attorney Bruce Rich emailed four attorneys relaying a conversation with Ottimo's brother which included the question of whether Ottimo's brother should be a principal of the Manager given his disciplinary history. RP 5893 – 5895. One of the attorneys (Mary Joan Hoene) replied that the regulatory past of Ottimo's brother would have to be reported on the Exempt Reporting Adviser filing with the SEC under Item 10, Control Person, which covers executive officers and key investment advisory personnel. Id. Attorney Faith Colish replied, in turn, "... I believe his brother, Louis [Ottimo], also has a colorful past. We are supposed to receive Louis's bio today." Then Ethan Silver responds, "Each of their colorful BrokerCheck reports are attached. The disciplinary history is towards the back..." Id. The Wells Submission prepared by the Law Firm explains that this information, along with JOJ and Wheatley, was not relevant. RP 5605 – 5612.

questionnaire. RP 2713 – 3065, 2991 – 2992 (Tr. 1274 – 1275).⁶ The only biography Ottimo had at the time was a biography that he had prepared for another company, which biography was far more bare bones than the biography he provided to the Law Firm. RP 2343 – 2712, 2360 (Tr. 643). Additionally, Ottimo had never prepared a PPM nor had he ever been involved in this type of offering. RP 2343 – 2712, 2431 (Tr. 714). It is in this context that Ottimo provided the Law Firm with the following biography:

Louis Ottimo

██████████ ██████████
Oyster Bay Cove, New York ██████████

Louis graduated from the University of Maryland in 1987 with a Bachelor of Science degree in Financial Studies. After several years in a family transportation business, Louis passed his Series 7 and Series 63 security licenses in 1995.

He founded North Pacific Capital in 1996, which owned an Office of Supervisory broker dealer. Under his control the branch office grew to over \$25 million in annual sales with up to 100 Registered Representatives.

Louis founded Wheatley Capital in 2001, which maintained an operating agreement with EKN Financial Services through 2008.

Louis co-founded Jet One Jets in 2006 with his brother Anthony Ottimo and successfully negotiated an exclusive reseller Agreement with American Express to handle the Jet One pre-paid card. Jet One grew to \$18 million in revenues inside approximately 18 months.

In 2009, Louis became a Registered Representative with EKN Financial Services, Inc. where he maintains retail clients.

Louis currently resides in Oyster Bay Cove with his wife and three children.

⁶ Lotvin, the co-manager of the Manager, was similarly asked to provide a biography and, likewise, was not given any guidance or a questionnaire. RP 2713 – 3065, 2768 - 2770 (Tr. 1051-1053). Lotvin also confirmed that when she prepared her biographical summary she was not thinking, “is this fair and balanced” as she wrote it. Id. The Law Firm also had access to her FINRA BrokerCheck Report. The PPM biography for Lotvin is similar to Ottimo’s in terms of its omission of negative information with regard to the companies with which she was associated. Lotvin testified that she read Ottimo’s biography though didn’t have a specific recollection of doing so. Id.

RP 5897 (RX-17).

The NAC decision erroneously found that Ottimo provided the above biography to the Law Firm “to be included in the PPM.” RP 6359 (NAC decision, p. 5). To the contrary, Ottimo merely did as he was told and provided a biography to the best of his ability, with no knowledge or experience as to what a PPM biography ought to include. The NAC decision also erroneously found that the Law Firm “made minor technical edits to Ottimo’s biography and that Ottimo approved the final version of his biography that was provided in the PPM.” *Id.* First, as detailed below, the Law Firm made more than technical edits to the biography and even assuming *arguendo* the edits were “technical,” Ottimo reasonably relied upon the Law Firm to determine what parts of the biography to use or discard. Further, while Ottimo approved the PPM, he did not do so with a legal understanding of what should or should not be included in a PPM biography, just as his approval of the PPM did not signify that he understood the level of detail that needed to be included in his co-manager’s biography (which is similar in brevity) or the sections in the PPM regarding the operating agreement or tax considerations.

Before deciding what biographical information to include in the PPM and the related Form ADV, the Law Firm considered the background of Ottimo and others, and made deliberate determinations regarding what to include and omit. This is reflected in internal emails among the lawyers at the Law Firm, several of which are noted above, as well as others.⁷ Ottimo received these and other internal emails from the Law Firm, along with the entire file, on the eve

⁷ In another Law Firm email, dated February 27, 2012, from Ethan Silver to Gideon Even-Or, Ottimo’s BrokerCheck Report is circulated a second time and Ethan Silver states, “Attached is Louis’s BrokerCheck report. Use the employment dates in it for his relevant employment listed in the management section.”

of the hearing.⁸ RP 2343 – 2712, 2345 - 2347 (Tr. 628-630). The Law Firm represented Ottimo during FINRA’s investigation of this matter, but not at the hearing. Alarming, the Law Firm did not raise the reliance on counsel defense during the investigation nor when they submitted the Wells Submission on Ottimo’s behalf. RP 5605 – 5612. The conflict of interest is obvious and Ottimo was severely disadvantaged at the hearing as a result. To add insult to injury, Ottimo was effectively pro se at the hearing as his attorney was frequently absent during the hearing and Ottimo was left to defend himself. The foregoing facts raise troubling fairness issues with regard to the conduct of the underlying investigatory and disciplinary proceeding.

Notwithstanding the foregoing, the Law Firm’s internal emails provide compelling evidence that the firm, not Ottimo, was responsible for any defects in the PPM. Additionally, the Law Firm’s contemporaneous time entries on their invoices demonstrate that the Law Firm was carefully considering the background disclosures that had to be included in the PPM and related Form ADV. There are a series of February 15, 2012 time entries which coincide with the Law Firm’s internal emails of the same date which reference Ottimo’s “colorful past” on his BrokerCheck Report.⁹ Additionally, there are time entries on February 27, 2012 which coincide

⁸ Ottimo provided the Law Firm file to FINRA’s Department of Enforcement forthwith so they too could use it at the hearing. RP 2343 – 2712, 2345 - 2347 (Tr. 628-630).

⁹ February 15, 2012 time entries by attorneys (Ethan Silver and Bruce Rich) working on the “*Private Fund*” matter state:

Confer w/G. Even-Or re formation of the entities & other questions on drafting of PPM;
exchange email re same

Questions re background, structure & regulatory matters

... prepare first draft of PPM.

RP 5714, 5718.

February 15, 2012 time entries by attorneys working on the “*Investment Adviser*” matter state:

[Footnote continued on next page]

with the Law Firm's emails of the same date which reflect a continuing focus on the PPM and Ottimo's background.¹⁰

There were two teams of lawyers at the Law Firm who were working on the PPM and evaluating Ottimo's background, the team working on the "Private Fund matter" and the team working on the "Investment adviser matter." Id. The word "PPM" appears in the February 2012 time entries approximately 30 times. RP 5713 – 5718.¹¹ For all of the work performed on the SPV transaction, the Law Firm was paid approximately \$150,000, an amount that Ottimo was willing to approve to ensure full compliance with all applicable regulations. RP 2713 – 3065, 2745 (Tr. 1028). Clearly, Ottimo had good reason to believe that the Law Firm had prepared a PPM that complied with all applicable regulations, including the section relating to his biography.

[cont'd]

Telephone call E. Silver re private fund advisor exemption and reporting and fund structure.

Confer with F. Colish re private fund advisor exemption and reporting and fund structure.

Development analysis and discussion w/E. Silver & B. Rich; email re reporting of disciplinary history in Form ADV Part I for Exempt Reporting Advisers; internal correspondence re FINRA filings.

RP 5722, 5724.

¹⁰ February 27, 2012 time entries state in pertinent part:

Exchange email w/N. Lotvin re EIN #s & SAA form & provide her evidence of EINs; review F. Colish email re revisions to PPM requested by the client & other comments & respond to same; confer w/N. Lotvin & L. Ottimo re Conflicts of Interest section of draft PPM; confer with w/G. Even-Or re revising same. [Ethan Silver.]

Revise draft of PPM to reflect to [sic] comments from N. Lotvin and L. Ottimo; incorporate comments from E. Silver and B. Rich; confer with F. Colish re PPM. [Gideon Even-Or.]

Review draft PPM & discuss w/G. Even-Or questions re. principal background and offering. [Bruce Rich.]

RP 5717.

¹¹ The PPM was finalized on February 29, 2012. RP 5718.

It is in this context that the Law Firm prepared Ottimo's biography for "The Manager" section of the PPM (hereinafter, "the PPM Biography"), which reads as follows:

Mr. Louis Ottimo is the Chief Executive Officer of the Manager. In such capacity, Mr. Ottimo is authorized to manage the Manager to effect the objectives and purposes of the Company. Mr. Ottimo has been a registered representative of EKN, where he maintains retail clients, since 2009. Mr. Ottimo currently serves on the board of directors of Bsafe Electrix, Inc. 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 pre-paid card. Jet One Jets grew to \$18 million in revenues inside approximately 18 months. In April 2001, Mr. Ottimo founded Wheatley Capital, Inc. and was its president until 2011. He also founded North Pacific Capital, LLC in 1996, which was an Office of Supervisory Jurisdiction of Tasin & Company, Inc., a registered broker-dealer. Under his ownership the branch office grew to over \$25 million in annual sales with up to 100 Registered Representatives.

Mr. Ottimo graduated from the University of Maryland in 1987 with a Bachelor of Science degree in Financial Studies. He has passed the FINRA Series 7 and Series 63 exams.

RP 4650.

A comparison of the PPM Biography with the biography that Ottimo provided to the Law Firm reveals that the firm made more than "minor technical edits." Specifically: 1) the Law Firm added the fact that Ottimo was on the board of directors of Bsafe Electrix; 2) the Law Firm revised the reference to Wheatley by deleting the information about Wheatley maintaining an operating agreement with EKN through 2008, and by referencing the fact that Ottimo was the president until 2011; 3) the Law Firm revised the reference to North Pacific Capital to state that it was an Office of Supervisory Jurisdiction of Tasin & Company, Inc., a registered broker-dealer; and 4) the Law Firm deleted Ottimo's personal information.

Additionally, the Law Firm decided to omit the eleven disclosure events that were in Ottimo's BrokerCheck Report, which legal determinations FINRA did apparently agree with as these "omissions" are not part of the fraud allegations in the Complaint and they were directly

addressed in the Wells Submission prepared by the Law Firm on behalf of Ottimo. RP 4650; RP 23 – 27; RP 5609; RP 5888 – 5891. The Law Firm also made the decision not to include additional details regarding JOJ and Wheatley, such as whether they were profitable or whether they were the subject of liens.

C. The SPV Offering Successfully Closes and Facebook Stock is Purchased

The offering was conducted in conformity with Regulation D, including Rule 506. In order to participate in the offering, EKN customers were required to be both “accredited investors” as defined in Rule 501(a) of Regulation D and “qualified clients” as defined in Rule 205-3 under the Investment Advisers Act of 1940. RP 5606 – 5607.

It is undisputed that during the period March 6, 2012 to April 10, 2012, twenty (20) EKN customers invested a total of approximately \$3.76 million. RP 1 – 68 (Complaint, ¶141). EKN was the sole placement agent. *Id.* All customers were both accredited and qualified, and the Facebook stock was purchased on the Dutch auction market. No investors were harmed.

IV. ARGUMENT

A. The Legal Standard of Proof

FINRA has the burden of proving by a preponderance of the evidence each allegation in the Complaint. “A ‘preponderance of the evidence’ means the greater weight of the evidence; it is that evidence which, when weighed with that opposed to it, has more convincing force and is more probably true and accurate. If, upon any issue in the case, the evidence appears to be equally balanced, or if it cannot be said upon which side it weighs heavier, then the plaintiff has not met his burden of proof.” *Kiser v. Dearing*, 2010 U.S. Dist. LEXIS 56582 (E.D. Tex. June 9, 2010); *see also, DOE v. Respondent*, OHO Hearing Panel Remand Decision No. E9B2003033701 (Aug. 11, 2010). In this case, FINRA has not met its burden of proof with regard to the fraud findings.

B. The Fraud Charge Were Not Proven By a Preponderance of the Evidence and Relevant Evidence was not Given Due Considerations

A violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder requires a showing that: (1) the misrepresentations or omissions were made in connection with the purchase or sale of securities; (2) the misrepresentations or omissions were material; and (3) the misrepresentations or omissions were made with the requisite intent, *i.e.* scienter. *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1467 (2d Cir. 1996). FINRA Rule 2120 contains similar requirements.¹² Here, the record does not establish that the omissions in question were material or that Ottimo acted with scienter. Additionally, with regard to Ottimo's role as co-manager of the private fund adviser, FINRA lacks jurisdiction.

C. The Information Omitted from Ottimo's Biography Was Not Material

A fact is not considered material unless "there is a substantial likelihood that a reasonable shareholder would consider it important" in making an investment decision.¹³ An omitted fact is not material unless 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."¹⁴ The test is not just *more probable than not* that the reasonable investor would consider the fact important, nor even substantially likely that the investor *might* consider it important.¹⁵

¹² Conduct Rule 2120 states, "No member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance."

¹³ *Basic Inc. v. Levinson*, 485 U.S. 224, 231 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

¹⁴ *Basic*, 485 U.S. at 231–32 (quoting *TSC*, 426 U.S. at 449).

¹⁵ These distinctions are important because one significant aspect of *TSC*, 426 U.S. at 446–47, was its correction of a "misplaced" reliance on statements in two earlier decisions of the Court

The NAC decision found that the PPM Biography contained only positive information regarding his business experiences with JOJ and Wheatley and omitted material, unfavorable information related to their financial condition. RP 6359 (pp. 4, 7). With regard to Wheatley, the PPM Biography benignly states:

In April 2001, Mr. Ottimo founded Wheatley Capital, Inc. and was its president until 2011.

There is no indication as to whether Wheatley was a success or failure. Thus, the NAC's finding that the PPM Biography contains "only positive informative" about Wheatley is incorrect. RP 6359 (pp. 4). Significantly, this brief description of Wheatley is precisely what is found in Ottimo's BrokerCheck report, which is clearly not misleading. Indeed, a brief description of corporate affiliations is all that is required on the Form U-4/BrokerCheck.

However, the NAC erroneously found that the PPM should have disclosed that Wheatley had no operating revenues from 2008 – 2010, and filed for bankruptcy in 2010. Wheatley was merely a pass-through entity and so the absence of revenues was irrelevant. Further, this business experience was immaterial as to whether Ottimo was qualified to discharge his responsibilities as co-principal of the Manager, which merely required that he purchase the Facebook stock. Similarly, the bankruptcy filing was immaterial, particularly given the facts surrounding it. In April 2010, while involved in a lawsuit with its then landlord, Wheatley filed for Chapter 11 bankruptcy in order to have a stay issued that prevented the company from being evicted. This was a tactical procedural decision made on advice of counsel and did not result in the discharge or reduction of any debts, nor did it compromise the rights of investors or creditors.

[cont'd]

that were interpreted by some to establish the test for materiality to be those facts that "might" rather than "would" influence an investor.

RP 5608 – 5609. The Chapter 11 filing was dismissed less than four months after it was filed.
Id.

Likewise, Ottimo's experience with regard to JOJ, a private jet broker, was irrelevant to his ability to buy Facebook stock. As regards JOJ, the PPM Biography states the following:

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 pre-paid card. Jet One Jets grew to \$18 million in revenues inside approximately 18 months.

At the outset, it should be noted that the above statements are true and evidence was submitted on this point. RP 5609 – 5610; RP 2343 – 2712, 2659 - 2694 (Tr. 942 – 976). But even these facts have no relevance to Ottimo's ability to purchase Facebook in the private market at the best available price and this was all that investors were interested in. However, the NAC erroneously found that the PPM should have disclosed that JOJ never made a profit, had no taxable income for 2007 and 2008, and filed for bankruptcy in August 2010 (which was *after* Ottimo left the company), and that certain JOJ investors lost their principal investment when JOJ ceased operations in 2008.

With regard to the absence of information regarding JOJ's profits or losses, any reasonable accredited/qualified investor would clearly understand that this biographical summary did not purport to give a full financial picture of JOJ, Wheatley or any of the other companies referenced in the biography. Moreover, the Facebook investors in this offering clearly knew that "revenues" did not equate to profits or losses, however, they did not care as they just wanted their Facebook stock. With regard to JOJ's 2010 bankruptcy, it occurred two years after Ottimo's departure from JOJ in 2008. RP 2312 – 2313. However, whether JOJ investors lost money was simply not material to the limited purpose of the fund.

Similarly, with regard to the NAC's finding that the PPM should have disclosed that the Department of Transportation ("DOT") issued a consent order against JOJ in March 2008, alleging unfair and deceptive practices, this was also immaterial. This action ultimately resulted in a \$1,500 - \$2,500 fine and was not related in any way to securities or malfeasance, despite some of the hyperbolic language. RP 2362 – 63. Indeed, the small amount of the actual fine paid reveals the technical nature of the alleged infraction, which related to required DOT verbiage that needed to be included on JOJ's website, hardly an event that needed to be included in the biography. *Id.*

It should also be noted that the NAC decision relies on cases that are not applicable to the facts of this case. Specifically, in support of its materiality findings, the NAC cites to *LeadDog Capital Markets, LLC*, 2012 SEC LEXIS 2918 ("*LeadDog*") and *SEC v. Carriba Air*, 681 F.2d 1318 (11th Cir. 1982) ("*Carriba*"). *LeadDog* involved a traditional hedge fund (not a special purpose vehicle) where the defendant disclosed some of his broker-dealer employers but excluded the "disgraced firms" that had been expelled by FINRA. Moreover, the defendant had not relied upon independent counsel, as is the case herein. In *Carriba*, the issuer was an airline carrier and the prospectus failed to disclose the close connection of its principals with another bankrupt airline carrier and other failed business ventures. Obviously, an officer's prior failure in running an airline business (or other business) is relevant if the business of the issuer is running an airline. But that is not the case here.

Materiality is both a question of fact and law.¹⁶ Whether a particular fact is material often

¹⁶ See *TSC*, 426 U.S. at 450 ("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. . . . Only if the established omissions are 'so obviously important to an investor, that reasonable minds cannot differ on the question of materiality' is the ultimate issue of materiality

[Footnote continued on next page]

requires fact-intensive analyses and consideration of the context of the situation.¹⁷

In this case, investors were buying Facebook stock indirectly through SPV. Investors were *not* “buying” into Ottimo’s ability to manage a portfolio or run a company. Investors were not induced to invest in SPV based on the proven track record or any unique attributes of Ottimo or his co-manager, Nancy Lotvin. Ottimo and Lotvin were not required to choose investments or build a portfolio. Additionally, they were not required to make any portfolio allocation decisions as is the case with hedge fund managers. Thus, the personal investment skills of Ottimo or his co-manager, were not material to an investor’s decision to invest in the fund. Even less material to investors was Ottimo’s success or failures in running a pass-through company (Wheatley) or a private jet brokerage company (Jet One Jets).

The NAC decision attempts to inflate the importance of Ottimo’s role by citing passages in the PPM which state that the Manager has sole discretion and control over all decisions relating to the fund and that “the selection of Portfolio Securities ... will be made by and in the sole discretion of the Manager.” RP 6359 (pg. 3). This and other boilerplate language included in the PPM by the Law Firm cannot take away from the fact that SPV was formed to buy Facebook stock, period. If the Manager had purchased anything other than the Facebook stock, the investors would have revolted and fraud charges would have been lodged by the investors, in addition to the regulators.

[cont’d]

appropriately resolved ‘as a matter of law’ by summary judgment.” (quoting *Johns Hopkins Univ. v. Hutton*, 422 F.2d 1124, 1129(4th Cir. 1970))).

¹⁷ See *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1321 (2011) (the court’s analysis of whether adverse event reports were material to investors indicates just how fact intensive materiality determinations can be wherein the court required consideration of the source, content, and context of the reports).

Ottimo and co-manager Nancy Lotvin (who was FINRA's witness) both testified that the fund was formed for the limited purpose of buying Facebook stock for EKN customers. RP 2354 – 2355, 2740 (Tr. 637, 1023). Additionally, the Law Firm's invoices are replete with contemporaneous billing entries unequivocally showing that the goal of SPV was to purchase Facebook stock.¹⁸ Further, the fund got its name ("First Secondary Market Fund, LLC") from the private market ("SecondMarket, Inc.) at which the Facebook stock was purchased and the origins of the offering stem from EKN customers' desire to buy Facebook stock. Perhaps the definitive evidence of the narrow goal of the fund is the undisputed fact that Facebook stock was, in fact, purchased with investor proceeds shortly after the successful closing of the offering. No other securities were purchased.

In sum, the biographical information about Ottimo should be viewed from the same perspective as the required disclosures on his BrokerCheck Report. That is because Ottimo's sales of SPV securities to EKN customers was no different from his sales of other securities to EKN customers.

The irrelevancy of the omitted information is further underscored by letters that SPV investors signed (hereinafter, "the Investor Letters") stating the following:

I hereby acknowledge that the additional information provided by Mr. Ottimo relating to his personal financial issues would have had no impact on my decision

¹⁸ "Confer ... re his plan to form fund to invest in Facebook restricted stock ... discuss form of entity to be used, manner of offering ..." [Entry dated 2/10/12].

"Confer ... re forming a fund to buy Facebook; research secondary market for trading private securities ..." [Entry dated 2/10/12].

"Confer w/[attorney GE] re question from client re whether Fund can purchase Facebook stock w/o using a broker ..." [Entry dated 2/13/12].

RP 005713, 5714, 5743; see also RP 5605-5611.

to invest in the First Secondary Market Fund LLC had they been disclosed as part of his biography in the PPM.

RP 4851 – 4928.

The Investor Letters also refer to the Wheatley bankruptcy, the current status of Wheatley, the liens and judgments against Ottimo, and the fact that the PPM says nothing about the profitability of JOJ. The Investor Letters inform each investor that Ottimo believes that his successes and failures in other businesses, including JOJ, have no relevance to the limited purpose of SPV, echoing the position of the Law Firm, who drafted the Investor Letters in an attempt to allay FINRA's concern during the investigative stage of this matter. RP 2422 - 2423 (Tr. pg 705-706).¹⁹

In sum, the record does not support the NAC's findings that the omissions in question were material.

D. Ottimo Did Not Act With Scienter

Scienter is defined as a “mental state embracing intent to deceive, manipulate, or defraud” and includes “recklessness.” *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976); *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1569-70 (9th Cir. 1990). Reckless conduct may be defined as a highly unreasonable misrepresentation or omission, “involving not

¹⁹ During the hearing, Ottimo was cross-examined by FINRA staff, who took the dubious position that the Investor Letters themselves included material omissions. FINRA essentially claimed the following: 1) the purpose of SPV went beyond the purchase of Facebook stock; 2) Wheatley was not an ongoing concern; and 3) the letters do not reference specific losses allegedly incurred by JOJ. The first point has already been addressed – the purpose of SPV offering was, in fact, to purchase Facebook. With regard to the second point, Wheatley was in fact an ongoing concern, though this point is a “red herring” as the PPM does not state that Wheatley was an ongoing concern. RP 2410 - 2414 (Tr 693 – 697). Finally, the fact that the purported existence of specific losses for JOJ is not referenced in the letters is superfluous as each investor confirmed that they do not view as relevant the personal successes or failures of Ottimo.

merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.” *Hollinger*, 914 F.2d at 1569. A long-accepted definition of reckless conduct in the context of omitted information is the following:

A highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.²⁰

1. Reliance on Counsel

Reliance on counsel is recognized as rebuttal to proof of scienter.²¹ The reliance on counsel defense applies where the defendant (1) made a complete disclosure to counsel; (2) requested counsel’s advice as to the legality of the contemplated action; (3) received advice that it was legal; and (4) relied in good faith on that advice.²² In this case, the Law Firm agreed to advise on all aspects of the SPV transaction, which included the PPM. RP 5867 – 5870 (Retainer Agreement). Additionally, the Law Firm’s contemporaneous billing entries, detailed above, demonstrate that it did, in fact, advise on all aspects of the PPM, including Ottimo’s biography and background.

The Law Firm was well aware of Ottimo’ background and even referred to him as having a “colorful past.” Additionally, Ottimo provided the Law Firm everything it asked for. The Law

²⁰ *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977) (quoting *Franke v. Midwestern Okla. Dev. Auth.*, 428 F. Supp. 719, 725 (W.D. Okla. 1976), *vacated on other grounds*, 619 F.2d 856 (10th Cir. 1980)).

²¹ *SEC v. Savoy Indus., Inc.*, 665 F.2d 1310, 1315 n.28 (D.C. Cir. 1981).

²² *Id.*

Firm asked Ottimo for a biography but gave him no guidance as to what level of detail they wanted. Ottimo provided what he reasonably believed to be an acceptable biography. If the Law Firm wanted more detail, Ottimo would have gladly provided it. If the Law Firm had asked Ottimo to complete a detailed background questionnaire, he would have gladly done so. The Law Firm did not want any additional information about Ottimo's business experience because they did not think it was relevant for an offering where the only purpose was to buy Facebook stock.

The Wells Submission that the Law Firm submitted on Ottimo's behalf is revealing with regard to the lawyers' state of mind concerning why they decided to include or omit information relating to Wheatley, JOJ and the other companies in Ottimo's and Lotvin's biographies. RP 5605 - 5611. In fact, the Wells Submission was prepared and signed by one of the lawyers who actually drafted the PPM and evaluated Ottimo's background prior to finalizing the PPM (i.e., Ethan Silver). RP 5611; RP 5713 - 5718. Among other things, the Law Firm did not think such detail was relevant or material because the SPV had such a narrow scope and Ottimo's role was no different than his registered representative role at EKN.²³

Taking the foregoing into consideration, it is clear that the Law Firm attached minimal importance to the references to JOJ and Wheatley. But it should be emphasized that these were choices made by the Law Firm, not Ottimo. The PPM Biography is the work product of the Law Firm, following careful consideration of relevant rules and regulations. This is borne out by the

²³ Unfortunately, the attorneys at the Law Firm would not testify at the hearing in this matter absent a subpoena and FINRA does not have subpoena power of them. However, this should not prevent consideration of the Law Firm's written statement and invoices for the same reason that FINRA is permitted to offer customer statements where the customer cannot or will not testify voluntarily. *See e.g., In re Henry James Faragalli, Jr.*, 52 S.E.C. 1132, 1145 n.40 (1996) (applicant had no right to confront authors of complaint letters in NYSE disciplinary proceeding because constitutional right to confront adverse witnesses does not attach to SRO proceeding).

many differences between the PPM Biography and the biography Ottimo sent them, described above. Moreover, the Law Firm pulled Ottimo's detailed BrokerCheck Report and acknowledged reviewing the eleven disclosure events contained therein. The Law Firm consciously chose not to include those events in Ottimo's PPM biography or even ask Ottimo about them because, again, it did not seem material to them.

Ottimo, for his part, reasonably believed that the Law Firm was working hard to produce a compliant PPM as he received their invoices reflecting numerous entries relating to work on the PPM. As mentioned above, the word "PPM" appears approximately 30 times in the February 2012 time entries, five attorneys were working on the PPM and additional attorneys were working on a related Form ADV, which also required scrutiny of Ottimo's background.

Clearly, Ottimo relied in good faith that the biography the Law Firm prepared for him was compliant with all applicable rules and regulations. The Law Firm is a prestigious firm that specialized in this type work. Moreover, Ottimo spared no expense in approving the generous compensation that was paid to the Law Firm for this work (i.e., a total of \$150,000 for all of the legal work performed on the transaction).²⁴

The NAC decision did not consider the reliance on counsel defense in evaluating scienter and only included a discussion of it in the "facts" and "sanctions" sections. The NAC decision found that Ottimo, "provided no evidence that he sought or received legal advice from [the Law Firm] about whether he could omit these facts from his biography." RP 6359 (NAC decision, p.

²⁴ Ottimo's concern for compliance is also demonstrated by his reaction to learning about an SEC action against Felix Investments, which involved Facebook. RP 2746, 2771 - 2775. Ottimo wanted to make sure that everything was being in full compliance with the regulation and the Law Firm was again directed to make sure this was the case. This issue arose before the Facebook stock had been purchased and Ottimo stood ready to rescind the offering if the Law Firm had found any regulatory issues. *Id.* Lotvin confirmed this during her testimony, as well. *Id.*

15-16). To the contrary, Ottimo engaged the most prestigious and experienced Wall Street firm that he could find to draft the PPM and paid handsomely to ensure that they drafted a PPM that was compliant with all applicable rules and regulations. This is evidenced by the Law Firm's engagement letter, invoices and internal emails, as detailed above. As part of that engagement, it was incumbent upon the Law Firm to take all necessary steps to ensure that they had all of the information they needed to draft a biographical section that included all required disclosures. Ottimo, for his part, did not know what disclosures should be included in a PPM biography, or the other sections of the PPM for that matter, and that is why the Law Firm was hired.²⁵ The NAC findings effectively conclude that Ottimo should have researched the securities laws and figured out what a PPM biography ought to include and then put that in the biography that he sent to the firm. Such a conclusion is absurd and defeats the whole purpose of why he hired an experienced securities firm to draft the PPM.

In this case, the Law Firm provided Ottimo no guidance with regard to what he should include in the biography that they requested from him. Ottimo, for his part, did what he was told and stood ready to provide whatever additional information the Law Firm required. The Law Firm did not ask for anything else and wrote the PPM biography. The Law Firm did not view the Wheatley and JOJ information as material, a fact which they admit in the Wells Submission they wrote on Ottimo's behalf.

In sum, because the NAC decision contains the foregoing erroneous findings and because Ottimo's reliance on counsel negates scienter, the fraud charges should be dismissed.

²⁵ Ottimo's co-manager, Nancy Lotvin, also testified that they completely relied on the Law Firm to draft a proper PPM. RP 2743 (Tr. 1026). Nancy Lotvin, like Ottimo, also testified that the Law Firm knew that they had no experience with PPMs. RP 2768 (Tr. 1051).

2. Other Factors Negating Scienter

Assuming for the sake of argument that any of the omitted information is determined to be material (though applicant strongly argues that it is not), consideration should be given to the borderline nature of its materiality and Ottimo's actual belief that it was not material, as factors that negate scienter.

If a team of experienced securities attorneys got it wrong, then how can Ottimo be expected to get it right? Indeed, EKN's chief compliance officer, Borgner, also concluded that there was nothing misleading in the PPM and he was well aware of Ottimo's background. Borgner was specifically aware of the Wheatley bankruptcy as he notarized the bankruptcy petition. Additionally, Wheatley and JOJ were disclosed on Ottimo's BrokerCheck Report, as noted above. Further, Borgner could see when he reviewed the PPM that Ottimo's biography included only revenues for JOJ and included no financial information for Wheatley. Additionally, Borgner testified that he distributed the PPM and would not have done so if he had thought it was misleading.

Further, Ottimo's co-manager, Lotvin, also reviewed Ottimo's PPM Biography and apparently had no issue with it. Moreover, the PPM biography for Lotvin includes only summary references to the companies she worked for and those companies undoubtedly had negative information associated with them. Thus, from Ottimo's perspective, upon reviewing Lotvin's PPM biography, all indications were that a summary biography was all that was needed for the PPM of a special purpose vehicle.

Further, Ottimo testified that he did not actually know that his biography was misleading (again, assuming arguendo, that it was misleading). When asked by one of the hearing panelists what Ottimo thought investors would want to know about him given his role as co-manager of the fund, Ottimo candidly replied that they would want assurances that he wasn't going to steal

their money, that he was regulated, and that he would stick to the objectives of the fund and would not stray from them. RP 3019 (Tr. 1302). Investors in fact received all material disclosures on these key issues. The fund manager was a private fund adviser that had reported to the SEC, EKN (the placement agent) was a FINRA member firm, Ottimo was a registered representative and Ottimo's co-manager (Lotvin) was a longtime securities professional with a strong compliance background, having held multiple key compliance positions. To the extent it is found that the securities laws also required disclosure of additional financial information on JOJ and Wheatley, this was not apparent to Ottimo.

It makes no sense that Ottimo was supposed to know that the omitted information should have been included in the PPM when the Law Firm, EKN's chief compliance officer (Borgner) and his co-manager (Lotvin) did not. Clearly, Ottimo did not know that there was a danger of misleading investors nor was the danger so obvious that he must have been aware of it. Thus, reckless or intentional misconduct is not present in this case.²⁶ On this basis alone, scienter is negated.²⁷

In view of the foregoing, NAC's findings of scienter must be overturned. The NAC found that Ottimo acted with scienter because allegedly he knew about the negative information

²⁶ See, *Kalnit v. Eichler*, 264 F.3d 131, 142 (2d Cir. 2001) (applying test of strong circumstantial evidence of conscious misbehavior or recklessness); *ECA & Local 134 IBEW Joint Pension Trust v. JP Morgan Chase Co.*, 553 F.3d 187, 202-03 (2d Cir. 2009) (same). These cases essentially hold that whether scienter has been pleaded may include consideration of the defendant's consciousness of the materiality of the alleged deception in the context of whether there is strong circumstantial evidence of conscious misbehavior or recklessness. In this case, Ottimo was not conscious of the materiality of the omitted information for all of the reasons detailed herein.

²⁷ See, *Wilson v. Bernstock*, 195 F. Supp. 2d 619, 639 (D.N.J. 2002) (“[K]nowledge or reckless disregard of the potential materiality of the information misstated or omitted is an element of scienter [that is] based on allegations of intentional or reckless misconduct,” citing Sundstrand).

and “consciously chose” not to include this information “when he drafted his biography to be included in the Fund’s PPM.” RP 6359 (pp. 7 – 8). Ottimo did not choose to omit anything from the biography that he sent to the Law Firm. The Law Firm did not give Ottimo any guidance with regard to what they wanted the biography to include, nor was Ottimo given a background questionnaire to include. With no guidance from the Law Firm and no experience with drafting PPMs, Ottimo did the best he knew how. There was nothing nefarious about the biography that Ottimo sent to the Law Firm and there is no evidence in the record to support this speculative conclusion. Ottimo had no idea what might be considered material under the securities laws. Had Ottimo been provided with a background questionnaire, he would have gladly completed it. Had Ottimo been given specific instructions for the biography, he would have followed them.

By reason of the foregoing, Ottimo did not act with scienter. Given that the NAC decision does not support a finding of materiality or scienter, the fraud findings should be dismissed.

E. FINRA Lacks Jurisdiction with Regard to Ottimo’s Role as a Principal of the Manager

Ottimo had two roles with regard to the allegations in the Complaint: 1) as a principal of the Manager of SPV (jointly with Lotvin); and 2) as a registered representative of EKN who sold SPV shares to two EKN customers. RP 1 – 65 (¶¶ 132 – 146). With regard to Ottimo’s individual liability, the Complaint states the following:

[SPV] sold shares to EKN customers using means of interstate commerce, including email, United States mail, electronic transfers and checks drawn on United States banks.

Ottimo made material misrepresentation and omitted material facts concerning his prior business experience in the [SPV] PPM.

Ottimo knew, or was reckless in not knowing, that the [SPV] PPM contained these material misrepresentations and omissions.

RP 1 – 65 (¶¶ 176 – 178).²⁸

With regard to Ottimo's role as principal of an SEC private fund adviser, i.e., SPV's sales of shares to EKN customers, FINRA lacks jurisdiction to bring an enforcement action based on these activities. It is undisputed that regulation of investment advisers rests with the Commission, not FINRA. See Study on Investment Advisers and Broker-Dealers, <https://www.sec.gov/news/studies/2011/913studyfinal.pdf>. Accordingly, with regard to these activities, the fraud charges should be dismissed in their entirety.

This means that the only activities at issue with regard to the fraud allegations are Ottimo's two sales to EKN customers as a registered representative, which dramatically reduces the scope of the fraud claims. Given this fact, if the fraud charges are not dismissed or if Ottimo is determined to have been merely negligent, then the sanctions should be dramatically reduced, as further discussed below.

F. Sanctions

If the Commission upholds any of the fraud findings or determines that Ottimo was merely negligent, Applicant respectfully requests that the sanctions be overturned as they are excessive and oppressive in view of the mitigating circumstances detailed above. FINRA's Sanction Guidelines provide that certain principal considerations be factored into any sanctions determination. The principal considerations include, among other things, whether the respondent reasonably relied upon counsel, whether the respondent acted negligently versus intentionally or

²⁸ The controversial nature of the fraud allegations against Ottimo is suggested in the Complaint, which pleads the fraud allegations in the *second* cause of action, after the Form U4 reporting cause of action, and also includes an *alternative cause of action* for non-scienter based misrepresentations.

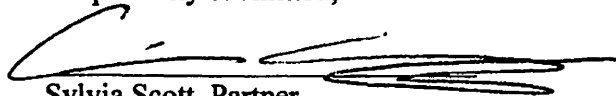
recklessly, and the level of sophistication of the affected customers. As detailed above, Ottimo reasonably relied upon counsel and was, at best, negligent. Moreover, the customers were all accredited and qualified, and had specifically expressed a desire to purchase Facebook stock.

Clearly, this is not a case that warrants the most severe sanction in FINRA's arsenal, particularly given that Ottimo was involved in sales to only two customers (factoring in the jurisdictional issue, discussed above). Given this and all of the mitigating circumstances, a letter of caution is more than sufficient in this case. Thus, if the fraud charges are not dismissed, then it is requested that this case be remanded back to the NAC with instructions that substantial mitigating circumstances warrant a significantly reduced sanction.

V. CONCLUSION

By reason of the foregoing, Ottimo respectfully requests that the Commission grant his application for review and dismiss all of the fraud charges. If the fraud charges are not dismissed, then Ottimo respectfully requests that this case be remanded back to the NAC with instructions that substantial mitigating circumstances warrant a significantly reduced sanction.

Respectfully submitted,



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