UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-19145

In the Matter of **Matthew R. Rossi and** **SJL Capital, LLC**	**Administrative Law Judge** **James A. Grimes**

BRIEF OF THE DIVISION OF ENFORCMENT IN OPPOSITION TO PETITION FOR REVIEW

Dated: April 8, 2020

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The Division of Enforcement ("Division") submits this brief in opposition to the Review Brief filed by Respondents Matthew R. Rossi ("Rossi") and his investment adviser firm, SJL Capital, LLC ("SJL," together with Rossi "Respondents").

The Division respectfully requests that the Securities and Exchange Commission ("Commission") affirm the Initial Decision and order Respondents to pay a civil money penalty in the amount of $520,311, disgorgement in the amount of $28,935, and prejudgment interest.

I. INTRODUCTION

Rossi repeatedly lied to his investors and advisory clients regarding Respondents' investment strategy and the performance of the investments. He defrauded SJL's clients ("SMA Clients"), including a church, and at least one investor in SJL's MarketDNA Hedge Fund LP ("Fund"). To keep his fraud afloat, he even created bogus tax documents and account statements and sent them to investors. He even concocted a phony story about a "rogue trader" to deflect blame for huge losses caused by his reckless unhedged options trading. Because of Rossi's fraud, Respondents' investors and clients lost over $1.6 million in nine months (between July 2016 and March 2017).

The Administrative Law Judge's ("ALJ") Initial Decision should be affirmed in all respects. Respondents do not challenge the ALJ's calculations of disgorgement, prejudgment interest, or civil penalties. Rather, they argue only that the ALJ erred in finding they did not carry their burden of proving their financial inability to pay. They are wrong. The ALJ correctly determined that Rossi earns substantial income and much of the "proof" he presented for his supposed debts and liabilities was inaccurate, incomplete, and unsubstantiated. Moreover, the ALJ also correctly held that, given the outrageousness of Respondents' misconduct, they were not

entitled to a reduction of the financial remedies imposed *even if* they had proven their inability to pay them.

II. PROCEDURAL BACKGROUND

Pursuant to Respondents' agreement, the Commission instituted this case as a partially settled (or bifurcated) administrative proceeding. (OIP [J.Ex.[1] 1] 1-2, 9.) The Commission's OIP found that Respondents violated the antifraud provisions of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934, subsections (1), (2), and (4) of Section 206 of the Investment Advisers Act of 1940, Exchange Act Rule 10b-5, and Advisers Act Rule 206(4)-8. (*Id*. ¶¶ 40-44.) The proceedings before the ALJ were limited to ***one issue***: "what, if any, disgorgement, prejudgment interest, and civil penalties are appropriate and in the public interest under the Securities Act, Exchange Act, and Advisers Act." (*Id*. 9.)

The parties filed cross motions for summary disposition. On July 23, 2019, the ALJ entered an order granting in part and denying in part the Division's motion. (Summ. Disp. Op. 5, 7, 9.) The ALJ granted the Division's request for disgorgement and prejudgment interest. (*Id*. 5.) Although the ALJ found the Division had established that the "threshold requirements for third tier penalties—fraud, deceit, or manipulation plus substantial losses—are met" (*id*. 7), he denied the Division's request for summary disposition on the issue of civil penalties. (*Id*. 7.)

The ALJ denied Respondents' motion, which argued only that financial remedies should not be imposed because of Rossi's alleged inability to pay them.[2] (*Id*. 1, 9.)

On August 21, 2019, the ALJ held a merits hearing, at which Rossi testified regarding his alleged inability to pay the monetary remedies requested by the Division. (Initial Decision ["I.D."]

[1] "J.Ex." refers to the parties' Joint Exhibits admitted by the ALJ during the merits hearing.
[2] Respondents presented no evidence concerning SJL's financial ability to pay before the ALJ (I.D. 16 n.106), or with their Review Brief.

2.) Following the hearing, the ALJ issued his Initial Decision on December 23, 2019. The ALJ found that the public interest weighs in favor of imposing third tier monetary penalties "[b]ecause Respondents lied to induce investments and fund Rossi's undisclosed, risky trading and then worked to cover up their lies." (I.D. 14.) Further, the ALJ refused to credit Respondents' assertions that Rossi is unable pay such penalties, both because they failed to meet their burden of proof and because of the "egregiousness" of their conduct. (*Id*. 18, 19.) The ALJ ordered Respondents, jointly and severally, to pay a civil money penalty of $520,311, in addition to the previously-ordered disgorgement and prejudgment interest. (*Id*. 20.)

Respondents' Petition for Review was granted by the Commission on February 6, 2020. On or about March 9, 2020, Respondents filed a "Review and Scheduling Brief" ("Review Brief" or "Respondents' Brief"). Respondents do not challenge the ALJ's findings that the legal requirements for the award of third tier civil penalties, disgorgement, and prejudgment interest have been met or that the imposition of civil penalties generally is in the public interest. Respondents argue only that the ALJ erred in finding they failed to prove their inability to pay the financial remedies he imposed.

III. STATEMENT OF UNDISPUTED FACTS

Respondents' outrageous conduct is set forth in the OIP.[3]

[3] Respondents spend much of their brief quibbling over irrelevant issues. (*See*, *e.g.,* Resps.' Br. 5: "Tthe [sic] Initial Decision fails to show Mr. Rossi as an Investor in the Fund.") Or they improperly dispute factual recitations in the Initial Decision that are based on the Commission's *uncontestable* findings in the OIP. Further, even if Respondents were allowed to dispute the OIP's findings, their brief improperly includes arguments for which they cite no evidentiary support in the record. (*See* SEC Rule of Practice 450(b): "Exceptions shall be supported by citation to the relevant portions of the record… .")

A. Respondents

Rossi was the founder, managing partner, and 80% majority owner of SJL. (OIP ¶ 7.) SJL was an investment adviser registered with the states of California or Connecticut. SJL managed the Fund and several SMAs. It terminated its registrations in Connecticut and California on July 21 and August 20, 2017. (*Id*. ¶ 8.)

Rossi launched the Fund in January 2016. SJL was the general partner of the Fund, Rossi was the managing partner of SJL, and Rossi was solely responsible for both the Fund's and SJL's investment decisions. (*Id.* ¶ 9.)

B. Respondents' MarketDNA Strategy

The Fund's private placement memorandum ("PPM"), which Rossi approved, stated that the Fund's investment objective was to maximize capital appreciation. The PPM further represented that the Fund would "seek consistent positive absolute returns primarily through a combination of long-term and short-term investments in order to achieve capital appreciation, while also attempting to preserve capital and mitigate risk through the diversification of investments." The PPM stated that the Fund "invests in a diversified portfolio consisting primarily of equity securities that are traded publicly in the U.S. markets." The Fund purportedly used Rossi's "proprietary algorithm known as MarketDNA which takes advantage of inefficiencies in dissemination of information within the derivatives market to determine equity directional movement." According to the PPM, SJL would use the MarketDNA algorithm to identify investment opportunities, analyze the underlying fundamentals of the companies identified, and then use "technical analysis to determine when to purchase or sell a given stock." (*Id.* ¶ 10.)

The Fund's initial investors were associates of Rossi. As of May 2016, the Fund's brokerage account had assets of $417,675.80, which Rossi allocated among himself and his

associates, as follows: Fund Investor A ($265,675.80), Fund Investor B ($50,000), Fund Investor C ($10,000) and Rossi ($92,000).[4] (*Id.* ¶ 11.)

C. Rossi Lied to New Investors.

In May 2016, Rossi met Fund Investor D[5] at a finance industry conference in Las Vegas. At the conference, Rossi told Fund Investor D that the Fund's MarketDNA strategy had been through many years of testing and that the strategy included "safety valves" that would cause the Fund to liquidate a position if losses exceeded 5%. (*Id.* ¶ 12.)

Rossi met SMA Client 1[6] at an asset management conference in New York City. Rossi told him that the MarketDNA strategy could analyze options market activity to predict stock price movement, that Rossi would trade only if his experience and other "confirming signals" indicated a good investment opportunity, and that stop losses were in place to limit downside risk. (*Id.* ¶ 13.)

In fact, Respondents engaged in unhedged options trading in the Fund, which did not comport with the purported MarketDNA strategy and did not include any safety valves or stop loss limits. Rossi had generated significant losses through such trading in the years preceding the launch of the Fund. (*Id.* ¶ 14.)

D. Rossi's Unhedged Options Trading Posted Early Gains in the Fund.

In June 2016, Rossi used Fund assets to make a series of unhedged trades in short-dated Priceline options. Rossi initially bought Priceline put options, which he held for one day before

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[4] During the merits hearing, Rossi identified these Fund investors. Investor A is Susan Ennis (also known as Susan Kmec), who is Rossi's friend. Investor B is Patrick Walters, one of Rossi's business associates. Investor C is Elizabeth Stiegler, who was Rossi's girlfriend. (*See* I.D. 3; *see also* 8/21/19 Hrg. Tr. ["Tr."] 69: "Q. Susan Ennis is also Susan Kmec? A. Correct.".)

[5] Fund Investor D was not formally identified at the merits hearing. (I.D. 3.) Respondents, however, identify him in their Review Brief as "Larry Bobba [sic]." (Resps.' Br. 5.) (In fact, their investor's actual name is Larry "Bober"—although the Division does not believe his actual name appears in the record.)

[6] SMA Client 1 is Mr. Oldenkamp. (I.D. 3; Tr. 50.)

selling them at a loss; but, he recovered and made money through subsequent short-term Priceline put trades. The Fund ended the month with a return of approximately 101%. The Fund achieved additional gains of 15% from unhedged options trading in July 2016. The Fund reached its peak valuation of over $1.3 million at the end of July 2016.[7] (*Id.* ¶ 15.)

Rossi told Fund Investor D about the Fund's June 2016 performance. Based on Rossi's representations, Fund Investor D invested $100,000 in the Fund on July 8, 2016. (*Id.* ¶ 16.)

E. The Fund Collapsed and Rossi Covered It Up.

The Fund lost approximately 88% of its balance in August 2016, as a result of Rossi's unhedged options trading. The largest losses came on August 19th, when Rossi sold short-dated Amazon call options at a loss of over $600,000. Minutes after closing that position, he purchased more Amazon call options as well as Priceline call options. Rossi lost over $68,000 when he sold the Amazon options on August 22nd. He sold the Priceline options on August 26th—hours before they expired—for a $360,000 loss. (*Id.* ¶ 17.)

Rossi deceived Fund Investor D about the Fund's trading activity and performance in August 2016. On August 18th, Fund Investor D emailed Rossi asking for an update on the Fund. The next morning, shortly before he locked-in the losses on the Amazon call options, Rossi responded to Fund Investor D that "[t]he trading is doing well" despite some recent trades that "went opposite on us." Rossi reassured Fund Investor D that the Fund had "a couple of positions

[7] In their Response Brief, Respondents claim the ALJ got it wrong when he said it was unclear whether Rossi's supposed algorithm was "highly successful," which is what Rossi told his investors. (Resps.' Br. 5, *citing* I.D. 4.) According to Respondents, "it was stated and clear in the OIP … that a return of over 100% in the total value of the fund occurred in June 2016 due to the algorithm." (*Id*.) Respondents—not the ALJ—are wrong. The OIP states that the profits in June were generated from Rossi's unhedged ***options*** trading—not from the algorithm. (OIP ¶ 15.) Rossi's purported algorithm was supposed to help Rossi purchase ***stocks***, which he admittedly "didn't do." (*Id*. ¶¶ 2, 10; Tr. 102: "I continued to run the algorithm. But what I didn't do, I didn't follow it in terms of just making sure I traded equities.")

that should pay off … over the next couple days." When Fund Investor D asked how bad the August returns were looking, Rossi falsely replied "we were down 4% then bk [sic] to even. No. It's not bad." After he learned the truth about the August trading losses, Fund Investor D withdrew from the Fund and received approximately $11,000, the remainder of his $100,000 investment. (*Id.* ¶ 18.)

The Fund continued to lose money in September and October 2016 due to Rossi's unhedged options trading. (*Id.* ¶ 19.) By November 2016, the Fund's assets had decreased to approximately $22,000. Rossi transferred those assets to SJL's brokerage account in two transactions on November 7 and 17, 2016, leaving the Fund with $0. The Fund's $0 balance remained unchanged through the end of the year. (*Id.* ¶ 20.)

To cover up the full extent of the Fund's losses, Rossi created and sent false account statements to Fund Investor B and false tax documents to Fund Investors A and B. For example, Rossi sent Fund Investor B false account statements for his investment in the Fund that showed slight losses for September and October and a year-end balance of $26,790.28, when in fact the entire Fund was worth only $21,618.50 at the end of October and ended the year with no assets. Rossi also sent Fund Investor B a false K-1 statement reporting a $26,790.28 year-end balance for 2016. (*Id.* ¶ 21.)

F. Rossi Signed Up the SMA Clients.

1. SMA Client 1 and SMA Client 2[8]

Rossi continued soliciting SMA Client 1 following their June meeting in New York. SMA Client 1 told Rossi that he and his wife were interested in making an investment that would follow Rossi's MarketDNA strategy, and were especially comforted by the existence of stop losses to

[8] SMA Client 2 is Mrs. Oldenkamp. (I.D. 3; Tr. 50.)

reduce risk; but, they did not want to invest in the Fund directly. Shortly after their initial meeting, Rossi provided SMA Client 1 with temporary online access to "read-only" returns for an account that Rossi represented was trading according to the same MarketDNA strategy used by the Fund. SMA Client 1 thereafter observed the gains posted in the account for June and July 2016. (*Id.* ¶ 23.)

Beginning in or about early July 2016, Rossi and SMA Client 1 began speaking with each other by phone on approximately a weekly basis to discuss the Fund, the MarketDNA strategy, and a potential investment by SMA Client 1 or his wife ("SMA Client 2"). Rossi told SMA Client 1 about the Fund's performance and provided SMA Client 1 with tearsheets representing the Fund's performance through June 2016. (*Id.* ¶ 24.)

On August 12, 2016, SMA Client 2 signed an Investment Advisor Contract with SJL, appointing SJL as the investment adviser for her SMA and authorizing SJL to supervise and direct the investments of her brokerage account. SMA Client 2 allowed Rossi, through SJL, to begin trading the $150,000 that was in her account at the time. (*Id.* ¶ 25.)

Respondents never disclosed the Fund's massive August 19 and 22 losses to SMA Clients 1 or 2. Earlier that month, SMA Client 1's temporary access to the "read-only" statements expired. He and SMA Client 2, therefore, were no longer able to follow the returns and had no knowledge of the Fund's steep decline. (*Id.* ¶ 26.)

Contrary to Rossi's representations to SMA Client 1, Respondents engaged in unhedged options trading in the SMA Clients' accounts which did not comport with the purported MarketDNA strategy and did not include any stop loss limits. (*Id.* ¶ 27.)

Unlike the Fund, SMA Client 2's account generated modest gains during August and September 2016 of 1.54% and 1.35%, respectively, but then suffered an 11% loss in October 2016. On November 2, 2016, Rossi emailed SMA Client 1, reporting that SMA Client 2's account was up 9% from her $150,000 starting investment.[9] (*Id.* ¶ 28.)

One week later, SMA Client 2 deposited another $50,000 into her account. On November 14, SMA Client 1 deposited $200,000 into another brokerage account that he gave Rossi and SJL authority to manage. Their accounts enjoyed modest gains through the end of December 2016. (*Id*.)

2. SMA Client 3 (The Church)

In early September 2016, Rossi gave SMA Client 1 marketing materials and background information to provide to the leaders of his church. The marketing materials included a tearsheet falsely representing that Rossi, in his capacity as a portfolio manager, had generated "live" returns of 135.6% for the months of May through August. The tearsheet failed to disclose or take into account the Fund's substantial losses in August. (*Id.* ¶ 29.)

Based on Rossi's representations and the apparent success of Rossi's MarketDNA strategy, SMA Client 1 recommended that his church ("SMA Client 3," together with SMA Client 1 and SMA Client 2, the "SMA Clients") invest with Rossi and SJL. SMA Client 3 deposited a total of $300,000 in three equal installments between December 21, 2016 and February 1, 2017, into its SMA account to be managed by Rossi and SJL. (*Id.* ¶ 30.)

On January 3rd, Rossi sent SMA Client 1 an email attaching a December 2016 tearsheet that falsely represented that the MarketDNA strategy had a net return for the calendar year of

[9] Respondents contend (Resps.' Br. 6) that it was "false" for the ALJ to state in the Initial Decision that Rossi told "the Oldenkamps that Mrs. Oldenkamp's account was up 9%" from August through October 2016, when in fact it was down 8%. The ALJ's statement, however, accurately summarizes paragraph 28 of the OIP, which Respondents cannot dispute.

186.44%. Later in January, Rossi sent SMA Client 1 hedge fund rankings that showed the Fund was "#1 for Returns %" for "2016 YTD." Rossi knew that these returns and rankings were false and that he had lost all of the Fund's assets. (*Id.* ¶ 31.)

On January 27, 2017, SMA Client 2 deposited an additional $600,000 into her SMA. On February 1, 2017, SMA Client 3 deposited an additional $100,000 into its SMA. On February 3, 2017, SMA Client 1 deposited an additional $499,000 into his SMA. (*Id.* ¶ 32.)

G. Rossi Lied to the SMA Clients About Losses in February 2017.

SMA Client 1 noticed large losses in his and SMA Client 2's accounts in mid-February 2017. When he asked for an explanation, Rossi blamed most of the losses on a rogue trader whom he had allegedly allowed to access the accounts on February 16 and 17, while Rossi purportedly underwent knee surgery. Rossi told SMA Client 1 he gave this trader "access to login to our advisory account to monitor the portfolio. Unfortunately the person executed trades, not associated with the algorithm that incurred losses of nearly 58% to the portfolio of [sic] which my personal account is linked to as well as your two accounts and the churches [sic] account." (*Id.* ¶ 33.)

Rossi assured SMA Client 1 that SJL had taken steps to make sure this mistake would not recur. Rossi told SMA Client 1 that SJL had revised its "vetting process" for future traders and asked SMA Client 1 to "stick with us," adding "I truly believe we will recover a significant amount in March and the following months." The three SMA accounts for SMA Clients 1, 2, and 3 lost over 70% of their value in February 2017. (*Id.* ¶ 34.)

SMA Client 1 continued investigating Rossi's explanations for the losses into March 2017. On March 20, 2017, after Respondents lost an additional 56% of the SMA Clients' remaining investment funds, SMA Clients 1, 2, and 3 revoked Rossi's access to their accounts. The SMA Clients suffered combined losses in excess of $1.5 million. (*Id.* ¶ 35.)

The February losses were caused by Rossi's unhedged options trading; his representations regarding the cause of the losses were false. First, most of the February 2017 losses resulted from Rossi's purchase of Amazon options before the date that he claimed to have turned over the account to the rogue trader. Second, the "rogue trader" did not exist. In fact, if Respondents had hired a trader, it would have been a violation of the Investment Advisory Agreements entered into with the SMA Clients, which required written authorization from the clients before any new traders were allowed access to the accounts. (*Id.* ¶ 36.)

H. Respondents Took Approximately $29,000 in Fees.

Rossi's false representations and failure to disclose the actual performance of his trading strategy to SMA Client 1 enabled Rossi to obtain advisory contracts and fees to which he was not entitled and would not otherwise have obtained. In November 2016 and January 2017, Rossi requested prepayment of certain performance-based fees from SMA Client 1 based on the gains in his and SMA Client 2's accounts. Although SMA Client 1 knew that Rossi was not yet entitled to these fee payments, he agreed to make four transfers into SJL's account, totaling nearly $29,000 as a "gesture of good faith." (*Id.* ¶ 38.)

IV. ARGUMENT

Respondents' fraud in this case was egregious and pervasive. Their fraud caused substantial financial harm to their victims, including a church. The Commission should affirm the Initial Decision and the sanctions imposed against Respondents in all respects.

Respondents raise no arguments that would justify overturning the Initial Decision. They merely object to the ALJ's characterization of the evidence and reassert specious arguments about Rossi's financial situation that were rightly rejected as unsupported in the record. Respondents

have not demonstrated that the financial remedies imposed should be reduced or waived due to an alleged inability to pay.

A. Disgorgement of $28,935 in Performance Fees Received as a Result of Rossi's Misrepresentation, Plus Interest, is Appropriate.

The ALJ correctly ordered Respondents to disgorge $28,935, the total received in performance fees from two of their SMA Clients. (Summ. Disp. Op. at 4-5.) Disgorgement is not "punitive"; it is meant to "ensure [Respondents'] illegal actions do not yield unwarranted enrichment." *Jay T. Comeaux*, SEC Rel. No. 3902, 2014 WL 4160054 at *4-5, nn. 32 & 36 (Aug. 21, 2014) (quotations and citations omitted). $28,935 is the "reasonable approximation of profits causally connected to the violation." *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1475 (2d Cir. 1996) (internal quotation marks omitted). Respondents have admitted and do not contest that Rossi received this amount in the form of pre-paid performance fees. (OIP ¶ 38.)

The ALJ also properly ordered Respondents to pay prejudgment interest because it, like disgorgement, "serves the important purpose of deterrence, which is central to securities law." *SEC v. Shehyn*, 04 Civ. 2003 (LAP), 2010 WL 3290977, at *7 (S.D.N.Y. Aug. 9, 2010).

B. Third-Tier Penalties Are In the Public Interest.

Nor do Respondents argue that the statutory requirements for the imposition of third-tier civil penalties were not met, or that the method the ALJ used to arrive at $520,311 in civil penalties—calculated by imposing a separate third-tier penalty for each of three anti-fraud statutes Respondents violated—was improper. (*See* I.D. 15.)

Section 8A of the Securities Act, Section 21B of the Exchange Act, and Section 203(i) of the Advisers Act authorize the Commission to impose civil money penalties for willful violations of those Acts. *Dennis J. Malouf*, SEC Rel. No. 766, 2015 WL 1534396, at *41-42 (I.D. Apr. 7,

2015) (respondents who willfully violate the federal securities laws should be ordered to pay civil penalties "in any cease-and-desist proceeding . . . after notice and opportunity for hearing where penalties are in the public interest and the person has violated or caused the violation of any provision").

A third-tier penalty—the highest penalty range—is appropriate where, *inter alia*, a respondent's violation (1) involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement, and (2) resulted in substantial losses or created a significant risk of substantial losses, or resulted in substantial pecuniary gain to Respondents. *See* 15 U.S.C. §§ 77h-1(g), 78u-2(b), 80b-3(i)(2). Third-tier penalties are appropriate "for each" violative "act or omission." *See* Adjustments to Civil Monetary Penalty Amounts, Rel. No. 3557, 2013 WL 1154360, at *5 (Feb. 27, 2013) (amounts in effect in 2016); 15 U.S.C. § 80b-3(i)(2)(C).

The Commission imposes civil penalties when they serve the public interest, according to the factors identified in *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979). The *Steadman* factors include: the egregiousness of Respondents' actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of Respondents' assurances against future violations, Respondents' recognition of the wrongful nature of their conduct, and the likelihood that Respondents' occupation will present opportunities for future violations. Other factors relevant to a civil penalty include the degree of harm to others resulting from the violation, unjust enrichment, and the extent to which the sanction will have a deterrent effect. *See* 15 U.S.C. §§ 78u-2(c), 80b-3(i)(3).

Here, the ALJ weighed the *Steadman* factors and concluded third-tier penalties against Respondents are appropriate and in the public interest. Rossi's conduct involved repeated, scienter-

based fraud; his acts cost his investors over $1.6 million; Rossi pocketed almost $29,000 in fees; and, especially because Rossi was serving as a fiduciary to his clients, the need to deter similar conduct by other fiduciaries is high. (I.D. 12-13.) Assessing a single third-tier penalty for each of the three securities acts Respondents admittedly violated (as requested by the Division), the ALJ calculated an appropriate civil penalty amount to be $520,311, even though a much higher penalty could have been imposed. (I.D. 14-15: "Because seven investors were defrauded, the resulting penalty could be as much as $1,325,989 for Rossi and $6,629,910 for SJL.")

Respondents do not challenge any of these findings.[10]

C. The ALJ Properly Refused to Reduce Liability Based on Inability To Pay.

The only argument raised by Respondents is that the ALJ should have found Respondents had proven Rossi's financial inability to pay monetary remedies. The ALJ, however, was right to discredit Respondents' claims, to find they did not carry their burden, and to rule that, even if they had, no discount was warranted given the egregiousness of their fraudulent conduct.

The Commission may, in its discretion, consider evidence of a Respondent's financial condition in deciding whether the public interest supports imposing a penalty. *See* 15 U.S.C. §§ 77h-1(g)(3), 78u-2(d), 80b-3(i)(4). But such inability is not dispositive, it is only one factor that informs the appropriate sanction. *Thomas C. Bridge*, SEC Rel. No. 9068, 2009 WL 3100582, at *25 (Sept. 29, 2009), *pet. denied*, *Robles v. SEC*, 411 F. App'x 337 (D.C. Cir. 2010); *see SEC v.*

[10] The Commission has wide discretion to determine what constitutes "each" violative act on Respondents' part, and then order them to pay a total civil penalty that is a multiple of the third-tier amount. *John A. Carley*, SEC Rel. No. 292, 2005 WL 1750288, at *68 (I.D. July 18, 2005); *SEC v. Pentagon Capital Management PLC*, 725 F.3d 279, 288 n.7 (2d Cir. 2013) (affirming district court's imposition of third-tier penalties by counting each late trade as a separate violation); *SEC v. Kenton Capital, Ltd.*, 69 F. Supp. 2d 1, 17 n.15 (D.D.C. 1998) ("multiplying the maximum third tier penalty . . . by the number of investors who actually sent money to [defendant]"); *Shehyn*, 2010 WL 3290977, at *2, *8 (court found defendant "committed 5 [statutory] violations" and awarded "$120,000 for each violation: Section 10(b), Rule 10b–5, Section 17(a), Section 20(a) and Section 15(a)").

Warren, 534 F.3d 1368, 1370 (11th Cir. 2008) ("At most, ability to pay is one factor to be considered in imposing a penalty."). Here, Respondents neither met their burden of proving Rossi's inability to pay, nor demonstrated that the egregiousness of their conduct should be set aside in order to credit such alleged inability.

1. Respondents Have Not Met Their Burden of Proving Inability to Pay.

"It is well settled that an applicant bears the burden of demonstrating inability to pay." *Steven E. Muth*, SEC Rel. No. 8622, 2005 WL 2428336, at *19 (Oct. 3, 2005). "[V]ague and unsubstantiated" disclosures are "neither adequate nor credible as a basis for reducing … penalty amounts." *David Henry Disraeli*, SEC Rel. No. 8880, 2007 WL 4481515, at *19 (Dec. 21, 2007). Incredible, thinly-supported assertions cannot establish Respondents' inability to pay. *Id*.

Rossi claims a net worth in the negative six figures and an income that barely covers expenses. Under questioning however, Rossi admitted that his financial distress is overblown. His claimed liabilities are unproven and some of his expenses—notably gambling, leisure travel, and college costs for his children—are, respectively, wasteful, unnecessary, and temporary.

The largest components of Rossi's claimed liabilities are alleged personal loans from his father and two close friends. Based on these undocumented, unsecured, interest-free purported loans, Respondents argue they should be excused from paying their victims. (Resps.' Br. 7.) But Rossi was unable to produce any supporting evidence demonstrating that the money—received from his father, a long-time friend, and a former girlfriend—were loan proceeds and not gifts. (J.Ex. 9 Form D-A] p. 94; J.Ex. 10 [Deposits-Expenses] rows 4-6; Tr. 45-46, 48-50, 52, 70-72.) The purported loans are undocumented. (Tr. 48, 52 ("There's no loan documentation. That's correct.").) In lieu of any actual loan documents, Rossi created a chart for the merits hearing that listed his purported creditors, a few terms, and a payment schedule. (J.Ex. 10 rows 4-6; J.Ex 16; Tr.

70.) In addition to there being no loan documentation, the "loans" are interest free and unsecured. (J.Ex. 10 rows 4-6; Tr. 48-49 [agreeing that purported loans from his father are unsecured].)

Moreover, neither Rossi nor his alleged "lenders" treated these "loans" as binding legal obligations before the Division advised Rossi it intended to charge him. He first began making "nominal" payments to his longtime friend (Susan Ennis/Kmec) in February 2019—just a few weeks before entering into the bifurcated settlement with the Division and more than two years after he first received money from her. (J.Ex. 16; Tr. 52, 70-71.) He only pays his ex-girlfriend Lisa Stiegler (also known as Lisa Alverado) "if I have extra cash" (Tr. 49-50), although he previously gave her $6,000 after persuading the Oldenkamps to pre-pay him some advisory fees. (OIP ¶ 39.) And he currently is not making any payments to his father. (Tr. 47-49.)

It's quite possible Rossi ***now*** prefers to pay his friends and family instead of paying money to the Oldenkamps and the church, who lost over $1.5 million because of Respondents' fraud. But Rossi has not proven that these undocumented, unsecured, interest free "loans" are binding legal obligations, and they should not serve as a basis for avoiding the consequences of his fraud.

Moreover, cross-examination revealed a number of additional problems with Rossi's financial disclosures. For example, he listed as liabilities a loan against a life insurance policy and an auto loan, but failed to list the insurance policy or the car as assets. (I.D. 18, *citing* Tr. 35-39.) Although he did not produce the life insurance policy, he admitted that it was a "$250,000" policy and that the loan he took out did not need to be paid back. (Tr. 37-39.) Rossi also admitted that his claimed expenses included thousands of dollars in recent online gambling costs. (Tr. 63 ["In order for me to try to make more income because I couldn't survive, I decided that I would try to play

poker online."].)[11] Rossi's gambling is not a legitimate expense and should not help him avoid paying of disgorgement and penalties. (I.D. 18.) He also conceded that his claimed expenses include "eat[ing] out a lot" and he typically eats out for lunch "in one of the most expensive parts of [New York] City." (*Id*., *citing* Tr. 60-61.)

For these and other reasons in the record, the ALJ correctly concluded that Rossi's financial disclosure "is not completely reliable." (*Id*.) *See also Disraeli*, 2007 WL 4481515, at *19 ("[V]ague and unsubstantiated" disclosures are "neither adequate nor credible as a basis for reducing … penalty amounts.").

Other expenses Rossi claimed were non-recurring or temporary. For example, Rossi listed [redacted] in SEC-related legal fees and [redacted] to purchase a car. (J.Ex. 9 p. 96; J.Ex. 10 row 1422; Tr. 54.) However, Rossi is representing himself in this proceeding, and he should have no need to purchase another car. Rossi reported $[redacted] in college expenses and support for his two college-age children and a high school junior. (J.Ex. 9 p. 96; Tr. 20-22.) These costs are not perpetual; Rossi's oldest child is in her final year of college. (Tr. 22 ("One more year of tuition? Mr. Rossi: Yes, one more year. Thank goodness.").) Therefore, support for his children is not a long-term expense that will meaningfully undermine Rossi's ability to pay monetary remedies once they have graduated.

[11] *See also* Tr. 63-64, 66-68, 82-86. Before being cross-examined, Rossi told the ALJ that he didn't spend money on anything "extra," except for a [redacted] monthly YMCA membership. (Tr. 16-17: "I don't spend my money on anything extra. The only extra thing I spend on, Your Honor, is [redacted] a month for a YMCA membership. … That's the only other extra that I afford myself in terms of the income that I have coming in, versus the expenses that I have going out.") Even after he was confronted with his gambling expenses, he testified that his gambling was not an "extra" because he only "tried it for two months" and then "immediately stopped." (Tr. 64.) That too was false. (*See* I.D. 8 n. 64 [noting that the records showed Rossi's gambling December 2018 through May 2019], *citing* record.)

Respondents also claim that Rossi's annual income is barely sufficient to support his lifestyle. (Resps.' Br. 3-4, 10.) Even if that were true, it is only because Rossi chooses to live well beyond his means. He has substantial income and is only 51 years old. He makes over [redacted] a week as a financial controller at JJJ International ("JJJ"). (Tr. 17; J.Ex. 10 rows 45-64.) Annualized, that amounts to a 52-week income of over [redacted] (not including the [redacted] bonus he received from JJJ). (J.Ex. 9 p. 95, line 3.) Monetary sanctions, including third-tier penalties, are appropriate "despite a defendant's inability to pay, [when] the defendant may subsequently acquire the means to satisfy the judgment." *SEC v. Robinson & Cellular Video Car Alarms, Inc.*, 2002 WL 1552049, at *8-13 (S.D.N.Y. July 16, 2002) (rejecting defendant's inability to pay argument and ordering defendant to pay disgorgement, prejudgment interest and third-tier civil penalties). Rossi has significant employment income which he can use in the years to come to pay for his misconduct.

Respondents' citations to two prior decisions are misplaced. (Resps.' Br. 11-12.) The ALJ's decision to deny civil penalties and limit disgorgement in the *Scott M. Stephan* matter turned on his finding that "Stephan has established that he is unable to pay a substantial civil penalty," a showing which Rossi has not made, and the Division in *Stephan* did "not attempt to rebut." *Scott M. Stephan*, SEC Rel. No. 888, 2015 WL 5637557 at *5, *7 (I.D. Sept. 25, 2015). The ALJ in *Stephan* also based his finding of inability to pay on evidence that the respondent had no college degree, a "low-paying" job, and he and his wife had filed for Chapter 7 Bankruptcy. (*Id.* at *4.) Rossi cannot make a similar showing. In fact, the exact opposite is true. Rossi has two degrees; he earns a substantial income and bonuses from his employer; and he has not submitted evidence of a bankruptcy claim.

Similarly, the ALJ limited the second-tier penalties in the matter of *Edgar Lee Giovannetti* in part because "there [was] no evidence of economic harm" caused by the respondent's misconduct, nor was he unjustly enriched. *Edgar Lee Giovannetti*, SEC Rel. No. 914, 2015 WL 6777088 at *25 (I.D. Nov. 6, 2015). Neither are true in this case, where Respondents caused $1.6 million in investor losses and Rossi pocketed almost $29,000 in unearned fees. Therefore, *Stephan* and *Giovannetti* are inapplicable to this case.

As the party bearing the burden of proof on this issue, it was incumbent upon Rossi to demonstrate—through credible supporting documentation—his supposed inability to pay. His case is woefully inadequate and should be disregarded as incredible, unsupported, and insufficient.

2. Even if Respondents Could Establish Their Inability to Pay, Civil Penalties Are in the Public Interest.

The egregious nature of Respondents' fraud, discussed *supra*, demands a penalty. "[W]here, as here, the conduct is egregious, [Respondents' ability to pay] may be disregarded." *Johnny Clifton*, SEC Rel. No. 9417, 2013 WL 3487076, at *16, n. 116 (July 12, 2013). Moreover, the sanction imposed by the ALJ pales in comparison to the financial losses suffered by Rossi's investors—over $1.6 million.

Rule of Practice 630(a) states, in relevant part: "The Commission ***may***, in its discretion … consider evidence concerning ability to pay in determining whether … a penalty is in the public interest." 17 C.F.R. § 201.630(a) (emphasis added). In other words, ability to pay may be considered, but "it is only one factor" and "[c]onsidering it is also discretionary." *Johnny Clifton*, 2013 WL 3487076, at *16, n. 116. "Even when a respondent demonstrates an inability to pay, we have discretion not to waive the penalty…, particularly when the misconduct is sufficiently egregious." *Gregory O. Trautman*, SEC Rel. No. 9088A, 2009 WL 6761741, at *24, n.115 (Dec.

15, 2009) (internal quotes and cite omitted) (refusing to order discretionary waiver of disgorgement, prejudgment interest, and/or penalties because of the egregiousness of respondent's market timing and late trading scheme); *Edgar R. Page*, SEC Rel. No. 822, 2015 WL 3898161, at *12 (I.D. June 25, 2015) (citations omitted), aff'd in part, modified in part, vacated in part, Rel. No. 4400, 2016 WL 3030845 (May 27, 2016).

Here, Respondents' conduct was particularly egregious. Respondents—acting through Rossi—lied throughout their entire relationship with their investors and clients. To lure in the investors and clients, Rossi lied about his investment strategy and the existence of supposed safety valves that would limit their downside risk. He lied about his Fund's trading and hid his massive trading losses. He created phony account statements and tax documents. He defrauded a church, including by creating fake marketing materials touting the Fund's supposed returns. He made up a bogus story about a rogue trader in order to hide his ongoing fraud. When all was said and done, Respondents' fraud caused his investors and clients to suffer over $1.6 million in losses.

Policy arguments favor discounting evidence of inability to pay. This is especially true here, where Rossi was serving as a fiduciary, engaged in deplorable conduct, has substantial income, and a significant portion of his documented expenses are non-recurring, discretionary, or temporary.

V. CONCLUSION

For these reasons, the Division respectfully requests that the Commission affirm the Initial Decision and order Respondents to pay a civil money penalty in the amount of $520,311, disgorgement in the amount of $28,935, and prejudgment interest.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

The attached **Brief of Division of Enforcement in Opposition to Petition for Review** has been sent to the following parties, on April 8, 2020, via email and UPS overnight mail:

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