BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Mitchell H. Fillet Riverside, CT, Respondent.	DECISION Complaint No. 2008011762801r Dated: March 7, 2016

On remand from the Securities and Exchange Commission for reconsideration of sanctions. Held, sanctions modified.

Appearances

For the Complainant: David F. Newman, Esq., and Leo F. Orenstein, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Pro Se

Decision

I. Background

This matter is before us on remand from the Securities and Exchange Commission. In a National Adjudicatory Council ("NAC") decision dated October 2, 2013, we found that Mitchell H. Fillet ("Fillet") engaged in securities fraud by misrepresenting and failing to disclose certain material facts in offering documents to one investor. We also found that Fillet falsified documents related to seven customers' variable annuity transactions that caused his firm's books and records to be inaccurate and provided these falsified documents to a FINRA examiner. The NAC suspended Fillet for two years and fined him $10,000 for the falsification of records and consecutively suspended Fillet for 18 months and fined him an additional $10,000 for the fraud.

Fillet appealed the NAC's decision to the Commission. On appeal, the Commission affirmed FINRA's findings that Fillet, in violation of NASD Rules 3110 and 2110, falsified his firm's records by backdating his approval of customer documents related to variable annuity transactions and then provided these records to FINRA. The Commission sustained the NAC's two-year suspension of Fillet and $10,000 fine for this misconduct. In addition, the Commission sustained the NAC's order that Fillet pay $2,584.65 in hearing costs.

With respect to Fillet's violations of the antifraud provisions, the Commission sustained the NAC's findings of violation with one exception, the violation of Securities Exchange Act of 1934 ("Exchange Act") Rule 10b-5(b). The Commission found that Fillet, in a private placement of securities offering document, misrepresented material facts and failed to disclose the criminal history of the person integral to the success of the offering, in violation of NASD Rules 2120 and 2110 and NASD IM-2310-2. The Commission further found that Fillet's omission of the criminal history information violated Exchange Act Section 10(b) and Exchange Act Rules 10b-5(a) and (c). The Commission, however, set aside FINRA's findings that the misrepresentations in the offering document violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5(b).[1] Because the Commission set aside a portion of the fraud findings, the Commission remanded the case to FINRA to re-determine the sanctions for Fillet's fraud in light of this dismissal.

On remand, we find it appropriate to suspend Fillet for 12 months and fine him $10,000 for his fraud.

II. Facts

The following facts are pertinent to the Commission findings that Fillet violated the antifraud provisions. We review these facts in connection with the consideration of appropriate sanctions for Fillet's fraud.

A. The Securities Offering

Fillet, on behalf of his firm, The Riderwood Group ("Riderwood" or the "Firm"), entered into an engagement agreement with Catering Acquisition Corp. ("CAC"), and its President and

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[1] Fillet argues on remand that because the Commission dismissed the Exchange Act Rule 10b-5(b) findings, FINRA failed to prove that he engaged in *any* fraud. Fillet is incorrect as set forth by the Commission's decision. *See Mitchell H. Fillet*, Exchange Act Release No. 75054, 2015 SEC LEXIS 2142, at *19-43 (May 27, 2015) (discussing findings that Fillet violated NASD Rules 2120 and 2110, NASD IM-2310-2, and Exchange Act Section 10(b) and Exchange Act Rules 10b-5(a) and (c)). The Commission's findings of fraud against Fillet are its final order and not before us on remand. *See id.* at *65-66. Equally unavailing is Fillet's contention on remand that FINRA impermissibly "pushed the burden of proof of defense against these allegations onto [Fillet]." Fillet bore the burden of producing evidence to support his claimed defenses to the charges in the complaint, and he failed to do so as evidenced by the Commission's findings against him. *See Kirlin Sec., Inc.*, Exchange Act Release No. 61135, 2009 SEC LEXIS 4168, at *64 n.87 (Dec. 10, 2009).

CEO, Allan Sloan ("Sloan"), in June 2007.[2] CAC was a shell company created for the purpose of acquiring food service companies. CAC had no assets or business operations. Pursuant to the engagement agreement, Riderwood agreed to provide CAC "advisory, investment banking, and placement services" in connection with "the design and execution of the acquisition of a series of food-related enterprises" in New York City and "the creation of a food and food service brand" that was intended to be expanded nationally. Riderwood agreed to conduct due diligence, help structure a financing plan, draft transactional documents, identify prospective investors, and act as a placement agent in connection with CAC's private offering of its securities. Sloan paid Riderwood between $20,000 and $30,000 for its services.

1. The Offering Documents that Fillet Drafted

Pursuant to the engagement agreement, Fillet drafted several documents for a private placement of securities to be issued by CAC and FAO Sweet Shoppes, Inc. ("Sweet Shoppes"), another shell company run by Sloan. Sloan formed Sweet Shoppes to operate a retail store that combined toys, food, and party facilities and was fashioned after FAO Schwarz's ("FAO") former Fifth Avenue store in New York. Fillet drafted a "Confidential Term Sheet" ("Term Sheet"), promissory notes, and a subscription agreement (together, "offering documents") for the offering. The Term Sheet prominently identified Riderwood as the "sole" and "exclusive" "marketing agent" for the $3,000,000 offering of 20 units, and Fillet as the contact person for the offering. Each $150,000 unit consisted of an $80,000 CAC "Series A 10% Corporate Note" due December 1, 2009, a $70,000 Sweet Shoppes "Series A 10% Corporate Note" due December 1, 2009, and detachable warrants to purchase shares of CAC and Sweet Shoppes. The Term Sheet identified Sloan as the President and CEO of both CAC and Sweet Shoppes.

The Term Sheet, dated January 14, 2008, that Fillet drafted made numerous representations about CAC and Sweet Shoppes that were inaccurate. For example, the Term Sheet represented that CAC "was founded in 2007 to create a vertically-integrated, brand name food service company that started in New York City but became national in scope." With respect to Sweet Shoppes, the Term Sheet stated that Sweet Shoppes operated "under a global license from FAO Schwarz and the FAO Family Trust." "Though not part of the corporate entity that owns and manages FAO," the Term Sheet added that "Sweet Shoppes is closely aligned with FAO, itself."

In reality, CAC was not an operating company nor was it national in scope. CAC was a shell company with no assets or operations. Sweet Shoppes was merely a concept and had not secured a global license from FAO or the FAO Family Trust. Fillet conceded in his hearing testimony that as of the date of the Term Sheet, CAC was neither an operating company with any

[2] In addition to a traditional brokerage business, Riderwood conducted an investment banking business, including private placements, mergers, and acquisitions. Fillet held an ownership interest in Riderwood and was the Firm's CEO, President, and senior investment banker. Riderwood withdrew from FINRA membership in February 2009 and is no longer in business.

assets nor "national in scope," and Sweet Shoppes had not secured "a global license from FAO and FAO Family Trust."

2. PM's Investment in the Offering

In December 2007, Edward Schmults ("Schmults"), the then CEO of FAO, told his friend PM about the Sweet Shoppes venture. Schmults told PM that he planned for the first Sweet Shoppe to be located in Greenwich, Connecticut. Schmults asked PM, who is a lawyer and a specialist in real estate investment and management, to speak with Sloan regarding the location. Schmults told PM that Sloan was an experienced food services operator and that FAO was relying on Sloan to run the business. After several phone calls between PM and Sloan regarding the Greenwich location, Sloan invited PM to meet with him and his investment banker, Fillet, who was putting together the Sweet Shoppes private placement.

The only meeting between Fillet and PM took place at PM's office on January 16, 2008. PM could not recall with certainty whether Sloan was also present at the meeting, but testified that he believed he was there to introduce Fillet, which Fillet's testimony corroborated. Fillet testified that the purpose of the meeting was to determine whether PM would be interested in investing in the CAC/Sweet Shoppes offering. PM had the impression that Fillet "was an investment banker who had done a lot of offerings," that Fillet was "participating to add credibility" to Sloan and the investment, and was "involved in raising the money." During the meeting, PM and Fillet discussed Sloan's business plan, the businesses of CAC and Sweet Shoppes, the terms of the offering, PM's qualifications as an accredited investor, and PM's potential investment of $150,000. Through PM's conversations with Fillet and Sloan, PM understood that CAC was on the verge of acquiring Glorious Food, which PM knew to be a prominent catering company in New York. PM also understood that CAC was already operating a food preparation business that would provide the food for the Sweet Shoppes.

Soon after the January 2008 meeting, PM received the Term Sheet, subscription agreement, and accompanying promissory notes.[3] After PM's attorneys reviewed these documents, PM completed and signed the subscription agreement that he dated February 21, 2008. PM also issued a check payable to "Catering Acquisition Corp." for $150,000. The memo portion of the check noted "re notes and warrants." Sloan picked up the completed documents and check from PM.

After several conversations with Sloan in the following months, PM became "uncomfortable" with his investment in CAC and Sweet Shoppes. Sometime thereafter, Schmults told PM that FAO's "arrangement" with Sloan had been terminated. Schmults said

[3] The record is unclear as to the exact date when PM received the offering documents or the identity of the person who provided the Term Sheet to PM. Fillet stated that he provided the documents to Sloan's attorney and later became aware that the Term Sheet was provided to PM. PM stated that the documents were delivered to his office, but PM could not recall who sent them.

that a confidentiality agreement precluded him from explaining further, but instructed PM to "Google" Sloan. After having one of his employees run Internet searches on Sloan, PM discovered that Sloan had a criminal history and had been disbarred.

PM subsequently requested reimbursement of his investment from Fillet and Sloan. Fillet disclaimed any responsibility to return the money, noting that the money had been paid to Sloan, and insisting that he was merely Sloan's agent. Sloan agreed to repay PM. On three different occasions thereafter, Sloan gave PM a check for $150,000. Each of the checks bounced. PM never recovered any of his investment.

B. Fillet Knew that Sloan Had a Criminal History

In late 2007, while conducting due diligence pursuant to the terms of the engagement agreement, Fillet learned that Sloan had been convicted of possession of stolen property (a rental car) in 2003, for which he was sentenced to three to six years in prison. Sloan subsequently provided Fillet with a letter from Sloan's criminal defense attorney in which the attorney described the stolen property prosecution as "absurd," despite Sloan's conviction. Fillet and Riderwood's only due diligence on Sloan consisted of running a misspelled Pacer search of "Alan Sloan" and searching the Commission's website for "TriBakery Capital," which Fillet described as CAC's predecessor.[4] Fillet undertook no further research of Sloan's background. Had he done so, he would have learned that Sloan had been disbarred from practicing law as a result of a 1987 felony conviction for offering a false affidavit to a New York court. Fillet testified that he learned in early 2008 that Sloan was disbarred. Prior to being disbarred, Sloan was disciplined for violating various New York attorney disciplinary rules related to converting client funds. Sloan also had hundreds of thousands of dollars in civil judgments and liens against him and had filed for personal bankruptcy in 2003.

At the time of Fillet's meeting with PM and PM's subsequent investment, Fillet knew of Sloan's stolen property conviction, but he did not disclose it to PM. Instead, Fillet told Sloan to disclose it to PM and FAO. Fillet also did not include any of Sloan's legal history in the CAC and Sweet Shoppes offering documents.

III. Discussion

We have considered the complete record in this case and the parties' briefs filed on remand. Given the Commission's dismissal of a segment of the fraud findings, we conclude that it is appropriate to modify our prior determination to suspend Fillet for 18 months for his violations of the antifraud provisions. As discussed below, we instead impose a 12-month suspension for Fillet's fraud. We also determine that the $10,000 fine that the NAC ordered prior to the remand remains appropriate under the FINRA Sanction Guidelines ("Guidelines") and impose it here.

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[4] Public records show that Sloan was known as "Allen Sloan," "Alan Sloan," and "Allan Gerald Slotnick."

The Guidelines for intentional or reckless misrepresentations and omissions of material facts recommend a fine of $10,000 to $100,000, and a suspension of 10 business days to two years.[5] In an egregious case, the Guidelines recommend a bar.[6] Prior to the remand, we determined that Fillet's misconduct was serious, but not egregious.

The Guidelines for misrepresentations and omissions of material facts advise that adjudicators consider the "Principal Considerations in Determining Sanctions."[7] Several of these considerations apply and serve to aggravate Fillet's misconduct. Fillet recklessly misrepresented and omitted important information in an offering document that was to be used to persuade potential investors to purchase units in the CAC and Sweet Shoppes offering.[8] As the Commission noted when finding that Fillet acted "at least recklessly," Fillet "was Riderwood's senior investment banker and had almost forty years' experience, [yet] he took no steps to prevent a potential investor from being misled if the document were to be released." *Fillet*, 2015 SEC LEXIS 2142, at *28. Once Fillet became aware that PM had received the Term Sheet, Fillet made no attempt to clarify for PM that the statements contained in the Term Sheet were subject to contingencies. *See id*. As a result, PM could not make an informed investment decision and accurately assess whether an investment in CAC and Sweet Shoppes was in his best interest. Indeed, PM testified that he would not have invested in the offering had he known the true status of CAC and Sweet Shoppes and Sloan's criminal past. The fact that FAO terminated its business relationship with Sloan once it discovered Sloan's criminal past further underscores the importance of this information that Fillet withheld from PM. Fillet, as a broker associating himself with this offering, failed to meet the high standards that FINRA expects of its members, including the obligation that he deal fairly with PM. *See FINRA Regulatory Notice 10-22*, 2010 FINRA LEXIS 43 (Apr. 2010); *see also Fillet*, 2015 SEC LEXIS 2142, at *28; NASD Rule 2110; NASD IM-2310-2. PM's testimony further illustrates the significance that a broker brings to an offering such as this. PM believed Fillet was participating in the offering to "add credibility" to Sloan, and through Fillet's involvement, PM understood that the statements made about the issuers rested on solid ground.

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5 *FINRA Sanction Guidelines* 88 (2011) [hereinafter *Guidelines*]. In 2015, FINRA revised its Guidelines, including those applicable to fraud violations. *See FINRA Regulatory Notice 15-15*, 2015 FINRA LEXIS 19 (May 2015). In the usual case, we apply the revised version of the Guidelines. *See FINRA Sanction Guidelines* 8 (2015) (explaining that the 2015 version supersedes prior editions of the Guidelines). Because the NAC applied the 2011 version of the Guidelines when rendering its initial decision in October 2013, we again apply the 2011 Guidelines on remand in re-determining sanctions for Fillet's fraud.

6 *Guidelines*, at 88.

7 *Id.* at 6-7 (Principal Considerations in Determining Sanctions), 88.

8 *See id.* at 7 (Principal Considerations in Determining Sanctions, No. 13).

We also find aggravating that Fillet's misconduct was a factor in PM's losses.[9] Fillet's failure to provide information about Sloan's criminal history—information Fillet undeniably knew—deprived PM of the opportunity to assess fully his investment in the CAC and Sweet Shoppes offering. Furthermore, Fillet has not accepted responsibility for or otherwise acknowledged his misconduct related to the CAC and Sweet Shoppes offering.[10] Throughout the course of these proceedings, Fillet repeatedly has attempted to shift the blame for his own actions to Sloan and PM.[11] *See N. Woodward Fin. Corp.*, Exchange Act Release No. 74913, 2015 SEC LEXIS 1867, at *44 (May 8, 2015) (explaining that respondent is "entitled to present a vigorous defense" but the denial that conduct was wrongful demonstrated either a misunderstanding or a lack of recognition of his duties as a professional and of his regulatory obligations). Indeed, on remand and irrespective of the Commission's findings of violations to the contrary, Fillet argues that he should receive no sanctions because FINRA failed to prove that he engaged in *any* fraud. Fillet misunderstands the Commission's findings and the consequence of those findings. His failure to appreciate the requirements of the securities business and the gravity of his misconduct and the harm it caused warrants robust sanctions. *See, e.g.*, *Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *75 (Jan. 30, 2009) ("We agree with FINRA that Epstein's demonstrated insouciance and indifference towards his responsibilities under NASD rules poses a serious risk to the investing public." (Internal quotation marks omitted)), *aff'd*, 416 F. App'x 142 (3d Cir. 2010); *Geoffrey Ortiz*, Exchange Act Release No. 58416, 2008 SEC LEXIS 2401, at *28 (Aug. 22, 2008) (finding the fact that respondent never accepted responsibility for his misconduct and blamed others for what occurred were factors that supported a significant sanction).

In favor of mitigation, Fillet previously argued before the NAC that PM had access to information about the offering because PM was an attorney and a broker, and PM had an established relationship with FAO's then-current CEO, Schmults. We acknowledge that PM had direct contact with Schmults, and Schmults was the person who first made PM aware of the new venture. The fact that PM may have been a knowledgeable investor who had access to Schmults, however, does not provide Fillet with a "license to" defraud or otherwise mislead PM. *See Lester Kuznetz*, 48 S.E.C. 551, 554 (1986), *aff'd*, 828 F.2d 844 (D.C. Cir. 1987).

Fillet also previously argued that neither he nor Riderwood received compensation from PM's "loan to Mr. Sloan." Fillet's hearing testimony undercuts this claim. Fillet stated that Riderwood received fees of $20,000 to $30,000 from Sloan pursuant to the engagement agreement. Fillet, through Riderwood, had the potential for additional monetary gain under the engagement agreement, including 5% of the outstanding and voting common shares of CAC within 10 days of the closing of the transaction and a percentage of the gross proceeds raised in the offering. And, as the Commission found, Fillet stood to gain financially and "had a financial

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9 *See Guidelines*, at 6 (Principal Considerations in Determining Sanctions, No. 11).

10 *See id.* (Principal Considerations in Determining Sanctions, No. 6).

11 For example, Fillet faults PM for not investigating Sloan's background himself.

incentive to withhold the information." *Fillet*, 2015 SEC LEXIS 2142, at *34. Moreover, even if Fillet's claim was accurate, "[t]he absence of monetary gain . . . is not mitigating, as our public interest analysis focus[es] . . . on the welfare of investors generally." *Howard Braff*, Exchange Act Release No. 66467, 2012 SEC LEXIS 620, at *26 & n.25 (Feb. 24, 2012) (internal quotations omitted). As the Commission explained, "[w]ithholding damaging information about the issuers' CEO increased the likelihood that PM and others would invest in the offering and thereby Fillet's total compensation." *Fillet*, 2015 SEC LEXIS 2142, at *35. We determine that Fillet's potential for pecuniary gain further aggravates his misconduct.[12]

The Department of Enforcement argues on remand that Fillet's sanctions for fraud should remain the same (an 18-month suspension and $10,000 fine) irrespective of the Commission vacating a portion of the fraud findings. We agree that several factors serve to aggravate Fillet's misconduct in this case as discussed above and therefore warrant a meaningful suspension and fine. The Commission's determination, under the Supreme Court's *Janus Capital Group v. First Derivative Traders* opinion, to vacate our findings that Fillet violated Exchange Act Rule 10(b)-5(b) causes us however to reassess sanctions in a remedial way. We have determined on remand that a 12-month suspension, a suspension around the midpoint of the Guidelines for serious but not egregious misconduct, is an appropriate balance between the aggravating factors present and the dismissal of a portion of the findings of violations. We also find that a $10,000 fine remains appropriate as a fine amount at the low end of the Guidelines' range, given the aggravating circumstances present in this case.[13] Accordingly, we suspend Fillet for 12 months and fine him $10,000 for his fraud.[14]

IV. Conclusion

Accordingly, for the fraudulent misrepresentations and omissions, we suspend Fillet for 12 months and fine him $10,000. We order that Fillet serve the suspension for fraud consecutively with the two-year suspension for falsifying his Firm's records, a suspension that the Commission sustained in its opinion. *See Fillet*, 2015 SEC LEXIS 2142, at *63; *see, e.g.*, *Siegel v. SEC*, 592 F.3d 147, 157-58 (D.C. Cir. 2010) (affirming imposition of consecutive suspensions for violations involving different kinds of misconduct).[15]

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[12] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 17).

[13] *See Guidelines*, at 88.

[14] The Hearing Panel declined to order restitution to PM because it was not clear that Fillet was the proximate cause of PM's losses. *See id*. at 4 ("Adjudicators may order restitution when an identifiable person, member firm or other party has suffered a quantifiable loss proximately caused by a respondent's misconduct."). Proximate causation "is normally understood to require a direct relation between conduct alleged and injury asserted." *Siegel*, 592 F.3d at 159. We agree that the record in this case does not support ordering restitution.

[15] We also have considered and reject without discussion all other arguments of the parties.

[Footnote continued on next page]

On Behalf of the National Adjudicatory Council,

Marcia E. Asquith
Senior Vice President and Corporate Secretary

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Pursuant to FINRA Rule 8320, any member that fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs or other monetary sanction, after seven days' notice in writing, will summarily be revoked for non-payment.