UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

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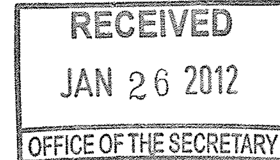
ADMINISTRATIVE PROCEEDING
File No. 3-14536

In the Matter of :
MONTFORD AND COMPANY, INC.
d/b/a MONTFORD ASSOCIATES, :

and :

ERNEST V. MONTFORD, SR., :
Respondents.
: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DIVISION OF ENFORCEMENT'S POST-HEARING REPLY BRIEF

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Pursuant to Rule of Practice 340, the Division of Enforcement of the United States Securities and Exchange Commission ("Division") respectfully submits this Post-Hearing Reply Brief in connection with the hearing held on November 7, 2011.[1]

I. INTRODUCTION

Respondent Ernest V. Montford, Sr., ("Montford") and Respondent Montford and Company, Inc. d/b/a Montford Associates ("Montford Associates") (collectively, "Respondents") filed their Post-Hearing Brief on January 13, 2012. Essentially conceding they have no substantive defense to the Division's claims, Respondents' lead argument – consuming over 6 pages of a brief that totals only 16 – is a renewal of their motion to dismiss based on Section 929U of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), 15 U.S.C. § 78d-5(a)(2). Not surprisingly, Respondents offer no new argument and make no additional showing in support of their motion.

Respondents also challenge the Division's claims under Sections 206 and 207 of the Investment Advisers Act of 1940 ("Advisers Act"), but do not challenge, however, the Section 204/Rule 204-1(a)(2) claims. In Respondents' Section 206 argument, they boldly claim they were not subject to any conflict of interest despite the hefty payments received from Stanley J. Kowalewski ("Kowalewski") and SJK Investment Management, LLC ("SJK"). The facts belie the argument that the payments from SJK were solely to compensate Respondents for administrative work. Also, their argument is based on a selective quotation of SEC v. Capital Gains Bureau, Inc., 375 U.S. 180, 188 (1963) cropped so finely that it ignores language *from the same paragraph* making clear that the subconscious motivation, for example, to maximize a

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[1] Exhibits from the trial will be identified by their exhibit number ("[Ex. __.]"). The transcript of the trial will be identified as "[T. __.]"

payment of unknown amount coming later in the year from an investment manager, presents a conflict of interest.

Regarding Section 207, Respondents argue that the $210,000 from SJK/Kowalewski was not given "in connection with giving advice to clients" and that the statement in Respondents' 2010 Form ADV that they did not accept "any fees" from investment managers really meant only "a finder's fee or a commission." Respondents' Post-Hearing Brief, p. 11. Respondents' argument – which contains no supporting authority – ignores the fact that, even under Montford's version of the facts, the administrative services he allegedly provided in exchange for the money were necessary to effectuate the advice he gave to his clients, and thus the fee from SJK plainly was given in connection with giving advice to clients. And of course, the language in Respondents' Form ADV speaks for itself. The phrase "any fees" is unlimited in scope, and that is what was represented to investors.

Finally, Respondents make several arguments contesting the relief requested by the Division, all of which, as set forth below, lack merit.

The Division has demonstrated that Respondent Montford Associates violated Sections 206(1), 206(2), 204 and 207 of the Advisers Act, as well as Rule 204-1(a)(2) thereunder, and that Respondent Montford violated Sections 206(1), 206(2) and 207 of the Advisers Act, and aided and abetted and caused Respondent Montford Associates' violations of Section 204 of the Advisers Act and Rule 204-1(a)(2) thereunder. The Court should issue an Initial Decision finding Respondents liable for those violations and imposing remedies as set forth in the Division's Post-Hearing Brief.

II. FACTS

The Division relies on its previously filed Proposed Findings of Fact and Conclusions of Law. In response to Respondents' Findings of Fact and Conclusions of Law, the Division objects to each of the enumerated paragraphs to the extent they differ from those offered by the Division. The Division further objects as follows:

- Paragraph 3 – As demonstrated in Exhibit 2 and set forth below, Montford does not have an unblemished record of compliance with the securities laws.

- Paragraph 21 – There is no evidence that the $210,000 Respondents received from SJK was the reasonable value of their services. The transaction reeks of an illicit agreement – even by Montford's account, the "work" was undertaken by him and his firm with no knowledge of how much the payment would be, the amount was not negotiated, no time records were kept, and Respondents did not even provide SJK an estimate of how much time was spent.

- Paragraph 22 – The Division demonstrated at the hearing that Montford previously testified that part of what he was paid for included meeting with his clients on behalf of SJK to recommend investing with SJK, and Montford's denial of that at the hearing was not credible. The purported soundness of investing with SJK is irrelevant under the Supreme Court's ruling in Capital Gains, 375 U.S. at 287. And the Division presented substantial evidence of a conflict of interest.

- Paragraph 24 and the unnumbered paragraphs following it on pages 11-13 – The Division objects to the relevancy of the assertions contained therein. The Court denied Respondents' attempts to introduce testimony from the staff regarding the SJK investigation and to introduce Kowalewski's investigative testimony transcript. These references are totally improper and should not be considered.

- Paragraph 27 – The record demonstrates that Montford did not "gather all relevant documents" in response to the December 9, 2010 staff subpoena.

- Paragraph 28 – There is absolutely no evidence that the Division was aware that Montford's document production was incomplete. Respondents' implicit assertion that the Division "knew" that Respondents had failed to comply with the subpoena simply because no electronic documents were produced is asinine.

- Paragraph 29 – Respondents objected when the Division offered Montford's December 17, 2010 testimony transcript into evidence, yet they now make assertions about the substance of the examination. Since Respondents have raised the issue, the Court should

review that transcript [Ex. 61.] in order to judge for itself. In addition, Montford did not produce the $80,000 invoice until Feb. 14, 2011, nearly two months after his initial testimony. [Ex. 14.]

- Paragraph 31 – As set forth below, the Division presented sufficient evidence to warrant equitable relief against Respondents.

- Paragraph 32 – The timing of the Wells Notice is not relevant to the resolution of the substantive issues in this case.

- Paragraphs 33 and 34 – The facts surrounding the Dodd-Frank extension that was granted in this case are also irrelevant for purposes of the Initial Decision. And, as the Commission noted in its Order Denying Suggestion for Interlocutory Review, this Court already found that the Division Director made the required complexity determination as required by the statute.

III. RESPONSE TO RESPONDENTS' ARGUMENT

A. Respondents' Offer No New or Compelling Basis for Reversing the Court's Correct Rejection of their Dodd-Frank Argument

As their first argument in their Post-Hearing Brief, Respondents renew their motion to dismiss based on Section 929U of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), 15 U.S.C. § 78d-5(a)(2).

To be clear, this same argument – virtually verbatim – was considered and rejected in the Court's October 5, 2011 Order. There is no reason to revisit the merits. Equally important, Respondents to date have not offered any compelling argument countering the Division's contention, supported by the strong parallels between Dodd-Frank and the statute at issue in the Supreme Court's decision in Brock v. Pierce County, 476 U.S. 253 (1986), that the compliance issues Respondents desire to endlessly rehash are, in fact, academic. Because it does not specify a consequence for non-compliance, a failure to comply with the 180-day deadline in Dodd-Frank does not divest the Commission of its authority to enforce the federal securities laws.

In the October 5, 2011 Order, however, the Court found that the Division complied with Dodd-Frank. Undeterred, Respondents now repeat their assertion that the Division failed to sufficiently demonstrate that the Division Director actually made the complexity determination required by the statute. Respondents, however, ignore the statement made by the Commission in its November 9, 2011 Order Denying Suggestion for Interlocutory Review that "the law judge implicitly found that the Division Director had made the required complexity determination, noting that the Division had asserted that 'the Division Director is not required to articulate or memorialize the reason for deciding that an investigation is sufficiently complex.'" Order Denying Suggestion for Interlocutory Review at 4. In addition, Respondents have yet – despite extensive briefing on the subject – to address the similarly-decided opinion in In the Matter of Gualario & Co., LLC, Admin. Proc. Rel. No. 680 (Aug. 11, 2011), which supports the Division's position that Respondents simply are not entitled to the level of transparency they purport to want. Moreover, in their haste to point out that the record is now closed, Respondents forget that, during the October 3, 2011 teleconference during which their motion was originally argued, the Court offered them the opportunity to have documents produced to the Court verifying the representations made by the Division, and Respondents declined the offer. As a result, Respondents can hardly be heard to complain about the state of the evidence.[2]

Respondents may disagree with the Court's denial of their motion, but they offer no new reason or argument warranting reconsideration of that decision. Accordingly, Respondents' renewed motion to dismiss should be denied.

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[2] Respondents again argue that "unintended consequences" necessarily follow from this Court's statement in its October 5, 2011 Order that "the complex nature of the proceeding is demonstrated by the fact that the Commission directed that an Initial Decision be issued within 300 days, the time allowed for deciding the most complex proceedings." Respondents' arguments defy common sense and do not warrant further analysis.

B. <u>Montford and Montford Associates Violated Section 206 of the Advisers Act</u>

Respondents fare no better in their opposition to the Division's claim that Respondents violated Sections 206(1) and 206(2) of the Advisers Act. Respondents assert that there is no Section 206 violation because they were not subject to a conflict of interest. Respondents' argument is riddled with error and fails on multiple levels.

As an initial matter, there is no doubt that Respondents were subject to a conflict of interest. Throughout Respondents' Posthearing Brief, they conveniently ignore the reasonable inference that Montford knew that he would be paid more for continuing to bring additional investor dollars to SJK, something that he undeniably accomplished between the first and second payments in 2010. But even setting that likelihood aside, by his own account, Montford knew that SJK had paid him $130,000 in January 2010 and promised to pay him an undisclosed amount later that year. Thus, even if the Court were to accept Respondents' assertion that there was no explicit agreement to that effect, Montford's incentive during 2010 to maximize whatever amount Kowalewski would ultimately pay him later that year – by bringing as much investor money to SJK as possible – obviously existed. That is a textbook conflict of interest, and, as Respondents concede, "*if* there is a conflict of interest, . . . *then* the S.E.C. does not need to prove that [Respondents] actually yielded to that conflict" and "those conflicts are material and should be disclosed to investors." Respondents' Post Hearing Brief, p. 9.

Respondents brashly (and incorrectly) assert that the Division misstates the law under Section 206. Respondents claim that the key issue under the Supreme Court's decision in <u>SEC v. Capital Gains Research Bureau, Inc.</u>, 375 U.S. 180, 187 (1963), "is whether 'advice to a client might result in financial benefit to the advisor – other than the fee for his advice.'" Respondents'

Post-Hearing Brief, p. 7, quoting Capital Gains, 375 U.S. at 187. Respondents twist that language, ignore contrary verbiage in the same paragraph, and conclude that in order to create a conflict of interest for an investment advisor, a financial benefit must be conferred directly in exchange for the advice in question. In other words, they ignore the word "might" and argue that there must be an explicit "quid pro quo" arrangement of money for advice. Respondents further argue that the Division is required to show direct evidence of that arrangement. Of course, Respondents selectively quote Capital Gains to reach that conclusion, and a more fulsome review of that opinion demonstrates precisely why Respondents are wrong: (1) the Supreme Court's view of how advice to a client might result in financial benefit to the advisor is much broader than Respondents' assertion; and (2) the Supreme Court indicated that requiring the SEC to directly show an improper agreement so easily hidden would defeat the purpose of the statute.

On the first point, the Supreme Court's opinion in Capital Gains repeatedly emphasizes that a financial conflict could be subconscious, and that in fact, the subconscious motivation to favor one's own financial interest (such as maximizing bogus payments or growing a relationship that includes thinly-veiled arrangements for kickbacks) was as much a concern behind the Advisers Act as "deliberate intent:"

> This concern was not limited to deliberate or conscious impediments to objectivity. Both the advisers and the Commission were well aware that whenever advice to a client might result in financial benefit to the adviser-other than the fee for his advice-'that **advice to a client might in some way be tinged with that pecuniary interest (whether consciously or) subconsciously motivated** * * *.' The report quoted one leading investment adviser who said that he 'would **put the emphasis * * * on subconscious' motivation in such situations. It quoted a member of the Commission staff who suggested that a significant part of the problem was not the existence of a 'deliberate intent' to obtain a financial advantage, but rather the existence 'subconsciously (of) a prejudice' in favor of one's own financial interests.**

375 U.S. at 188 (emphasis added; footnotes omitted); see also Id. at 195-97. This passage highlights why Respondents' theory that a quid pro quo arrangement is necessary fails – the notion that only a deliberate exchange of money for tainted advice qualifies as a conflict is utterly inconsistent with the Court's emphasis on the risk posed by "subconscious" motivations. Instead, Capital Gains clarifies that subconscious prejudice in favor of one's own financial interests – such as that posed by a coming payment of an unknown amount from a favored investment manager – also creates a conflict of interest that falls within the purview of the Advisers Act.[3] Respondents here, of course, claim that the amount was already fixed by Kowalewski and based solely on "work" performed in the fall of 2009. However, Montford's own testimony was that Kowalewski did not communicate the amount until the fall of 2010, and that Montford had no understanding of how the payments from Kowalewski were calculated. Therefore, Montford's claim that his clients' investments with SJK during 2010 had no bearing on the amount, and that he did not (consciously or subconsciously) suspect that it might turn out to be greater if his clients invested more money with SJK, has no basis whatsoever.

On the second point from Capital Gains, the Supreme Court discussed in some detail both the reasoning behind the prohibition against conflicts of interest for fiduciaries, and the attendant impact those grounding tenets have on what must be shown to establish such a conflict. Id. at 196, n.50. The Supreme Court stated that, due to human nature, in the realm of fiduciaries, even the temptation to violate the trust relationship is a problem, and that when shown to be present, such a temptation is enough because improper conduct is typically hidden:

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[3] Importantly, the opinion also makes plain that those advising the Commission on best practices opined that investment advisers should not engage in outside employment activities (like those Respondents here claim were the "real" services behind the payment) because they might "directly or indirectly bias their investment judgment," and that in order to avoid conflicts like this, an advisor's compensation should be limited to advisory fees Id. At 190.

> This Court, in discussing conflicts of interest, has said: 'The reason of the rule inhibiting a party who occupies confidential and fiduciary relations toward another from assuming antagonistic positions to his principal in matters involving the subject matter of the trust is sometimes said to rest in a sound public policy, but it also is justified in a recognition of the authoritative declaration that no man can serve two masters; and **considering that human nature must be dealt with, the rule does not stop with actual violations of such trust relations, but includes within its purpose the removal of any temptation to violate them.** * * *' * * * In Hazelton v. Sheckells, 202 U.S. 71, 79, 26 S.Ct. 567, 568, 50 L.Ed. 939, we said: **'The objection [to conflicts of interest] * * * rests in their tendency, not in what was done in the particular case. * * * The court will not inquire what was done. If that should be improper it probably would be hidden, and would not appear."** United States v. Mississippi Valley Generating Co., 364 U.S. 520, 550, 81 S.Ct. 294, 309, 5 L.Ed.2d 268, n. 14.

Id. The Court went on to apply this principle in that case, stating that **"[t]o impose upon the Securities and Exchange Commission the burden of showing deliberate dishonesty** as a condition precedent to protecting investors . . . **would effectively nullify the protective purposes of the statute**. Reading the Act in light of its background we find no such requirement commanded." 375 U.S. at 200. Accordingly, Respondents' argument that the Division "needed to prove the connection between the advice and the payment" is plainly contrary to the Supreme Court's teachings in Capital Gains and fails. Under Capital Gains, direct evidence of an improper quid pro quo arrangement is not necessary because, as observed by the Supreme Court, improper conduct is typically hidden, and it is contrary to the purpose of the Advisers Act to require such evidence.

The ruling in Capital Gains notwithstanding, however, the Division in fact presented evidence that Montford's advice to his clients resulted in a financial benefit to Montford apart from his advisory fees. First, as stated above, at the hearing, Montford conceded that he had an expectation of additional payment in the fall of 2010. His incentive to influence Kowalewski to maximize that payment by continuing to bring new investment funds to SJK is, as noted by the

Supreme Court, simply human nature. Moreover, the Division effectively showed that Montford testified – in December 2010, virtually in real time – that part of the "work" he performed for SJK in exchange for the money was meeting with his clients on behalf of SJK to recommend investing with SJK. [T. 61-66.] The Court witnessed his nonsensical attempt to recant that testimony, which the Division submits is totally implausible. [T. 62.] Respondents clearly regret Montford's investigative testimony and consistently complained when the Division appropriately used it to show his lack of candor at the hearing. However, the Court should not allow Respondents to simply change their story and then claim no direct evidence was adduced.[4] The Court should reject Montford's incredible recantation in favor of the much more likely inference that the deal with SJK involved Respondents meeting with clients on behalf of SJK to recommend investing with SJK.

Respondents' argument on Section 206 also fails because they flatly ignore the Division's misrespresentation claims. Even if everything Respondents asserted in their papers were true (and the truth in nearly every instance is just the opposite), Respondents would still be liable under Sections 206(1) and 206(2) because they knowingly made material misrepresentations about a material fact in their 2009 and 2010 Forms ADV: "We do not accepts any fees from investment managers . . . ." False and misleading statements and omissions are actionable under Section 206 (1) and (2). SEC v. Blavin, 760 F.2d 706, 711 (6th Cir. 1985); SEC v. Bolla, 401 F. Supp.2d 43, 70 (D.D.C. 2005). Respondents weakly assert that "the payments Montford

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4 The Division notes that Respondents still have not addressed the difficult facts that despite claiming the $210,000 payment was for time spent on administrative matters related to transferring clients' accounts to SJK, none of Respondents' employees kept track of their time and Respondents never even provided an estimate of time spent to SJK. In addition, Respondents have not explained why they charged for that service in this instance (or how it could possibly be worth so much) when Montford conceded he had performed it twice before for free. [T. 44.]

received from SJK were not 'fees,'" but that is contrary to Montford's testimony and the documents in evidence. Montford testified that he considered the money from SJK to be a "fee," and the invoices submitted by Montford indicated on their face that they were for "Marketing and Syndication Fee for the SJK Investment Management LLC Launch." [T. 90; Ex. 4, p. CC-6; Ex. 17.] The statement in Respondents' 2010 Form ADV claiming they accepted no fees from investment managers was false when made, and Respondents have no defense.[5]

Accordingly, the Division did not misstate the law on conflicts of interest, but rather has sufficiently proven that Respondents violated Section 206(1) and 206(2) of the Advisers Act.

C. Montford and Montford Associates Violated Section 207 of the Advisers Act

Respondents spend a paragraph arguing that that they did not violate Section 207 of the Advisers Act. Respondents' Prehearing Brief, p. 11. Respondents claim that the Division has failed to show, under Item 13.A. of the firm's 2010 Form ADV Part II, that the economic benefit received from SJK was conferred "in connection with" giving advice to clients. Respondents also assert that the Division cannot base its Section 207 claim on the representation contained in Schedule F of that same form that the firm did "not accept any fees from investment managers . . ." because Montford subjectively intended "any fees" to mean a finder's fee or commission. Respondents are incorrect.

As set forth in the Division's Post-Hearing Brief, Section 207 of the Advisers Act makes it unlawful for any person willfully to make any untrue statement of a material fact or omit to state any material fact required to be stated in an application or report filed with the Commission.

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[5] Even if Montford intended the language "[w]e do not accept any fees from investment managers" contained in his Form ADV to have the limited "finder's fee or a commission" meaning Respondents advance on page 11 of their brief, the use of the modifier "any" makes the language false and misleading and thus a sufficient basis for finding a violation.

Montford Associates' 2010 Form ADV Part II was prepared by Montford and deemed filed with the Commission on March 29, 2010. [Ex. 29.] Item 13.A of Form ADV Part II stated that Montford and Montford Associates received no economic benefit from a non-client in connection with giving advice to clients. That response was materially false and misleading – even accepting, *arguendo*, Montford's version of events as true, he concedes that the administrative services he allegedly provided in exchange for the money were necessary to effectuate the advice he gave to his clients to invest with SJK. Thus, SJK, a non-client, provided an economic benefit in connection with that advice. This position is supported by Montford's (admittedly convoluted) testimony that the services he provided in exchange for the money were done on behalf of his clients, but paid for by SJK – it is precisely that sort of ethically precarious arrangement that Item 13.A. is designed to expose. [T. 71-72.]

Additionally, Respondents' 2010 Schedule F stated that Montford Associates would "disclose to clients ... all matters that reasonably could be expected to impair [the firm's] ability to make unbiased and objective recommendations." [Ex. 29.] Tellingly, Respondents offer no argument against this allegation, which clearly calls for disclosure of the fee arrangement with SJK. Also in Schedule F, the Forms ADV expressly represented that the firm did "not accept any fees from investment managers . . . ." Montford now claims that when he included the phrase "any fees," in his mind, he intended to limit the meaning to "a finder's fee or a commission." Respondents' Post-Hearing Brief, p. 11. Respondents' argument here is preposterous, as the representation in the disclosure document speaks for itself. In addition, the Division notes that even if Montford subjectively intended the meaning Respondents now

advance, the use of the modifier "any" makes the language false and misleading and thus a sufficient basis for finding a violation.

All of the identified statements materially misstated the facts at the time and, as such, the 2010 Form ADV was false when filed in violation of Section 207.

IV. RELIEF REQUESTED

A. Montford Has Been the Subject of Securities Fraud Claims Before and Acted with Scienter in this Case

Respondents assert that Montford has "a long and spotless record" that should be considered for purposes of relief. Respondents' Post-Hearing Brief, p. 11. Although the Division did not intend to raise the issue, because Respondents have affirmatively (and knowingly) made an incorrect overstatement to the Court, the Division is compelled to complete the record. As reflected in Exhibit 2, in 1978, Montford, who at the time was employed as a registered representative with Merrill Lynch, was sued by a customer for violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The complaint alleged unsuitable options trading and failure to register in the relevant state (Florida), and sought damages of over $1 million. [Ex. 2.] According to Exhibit 2, the claims were later settled out of court for $30,000.

Respondents also allege that Montford's state of mind entitles him to mitigating consideration because he claims to have not known about SJK's fraud. As Respondents are well aware, however, this case is not about SJK's fraud, but instead is about Respondents' fraudulent misrepresentations and failure to disclose their conflict of interest, and as set forth in the Division's Post-Hearing Brief, Montford acted with a high degree of scienter in several instances (including, but not limited to, Montford's failure to disclose the conflict to his clients in 2010, when he knew he had been paid $130,000 and another payment of unknown amount was

forthcoming, and lying to the Savannah Country Day School Endowment Committee in response to a direct question about fees from managers).

B. A Cease-and-Desist Order is Appropriate

Respondents argue that a cease-and-desist order is unnecessary in this case because the Division has not sufficiently shown a risk of future violations. Respondents' Post-Hearing Brief, p. 12. Respondents also argue, at some length, that "[a] cease and desist order that simply commands Montford to obey the law is unlawful in this Circuit," citing SEC v. Smyth, 420 F.3d 1225 (11th Cir. 2005) and a handful of other inapposite cases. Id., pp. 13-14. Respondents' argument with respect to the risk of future violations fails because Respondents have already violated the securities laws and their assurances against future violations are not sincere. In addition, Respondents' argument regarding Smyth (which grossly misstates Eleventh Circuit law on the issue) likewise fails because the Eleventh Circuit has recognized that Congress specifically authorized such injunctions and cease-and-desist orders in the context of the federal securities laws, and they also fall within an exception to the common law rule against "obey the law" injunctions.

As the Commission has stated, "[t]hough 'some' risk [of future violations] is necessary, it need not be very great to warrant issuing a cease-and-desist order. Absent evidence to the contrary, a finding of violation raises a sufficient risk of future violation. To put it another way, evidence showing that a respondent violated the law once probably also shows a risk of repetition that merits our ordering him to cease and desist." In re KPMG Peat Marwick, LLP, 74 S.E.C. 357, 2001 WL 47245 at *24 (Jan. 19, 2001). That level of risk (and, as set forth below, frankly a much greater risk) is certainly present in this case.

Moreover, when determining whether to impose a cease-and-desist order, the Court also should consider a range of traditional factors, including "the sincerity of the defendant's assurances against future violations." Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981); see also In the Matter of Richard C. Spangler, Inc., 46 S.E.C. 238, 254 n.67 (1976). On that issue, Respondents' argument regarding the Section 206 violations reveals in full their lack of contrition and the insincerity of their assurances against future violations. In their Prehearing Brief, Respondents stated "Montford has recognized . . . that it should never have accepted any payment from SJK . . . . At the time, Montford did not believe it posed a conflict of interest . . . . Regardless of the outcome of this proceeding, Montford regrets the mistake." Respondents' Prehearing Brief, p. 2. At the hearing, Montford testified that, in the future, he would never "take money for any services from a manager . . . without disclosing the fact of that compensation, whatever form it might take, to [his] clients." [T. 176.] Yet now, pushed to the wall and facing the stark reality of the Division having proved that they knowingly defrauded their clients, Respondents adopt a pious countenance and profess that *they did nothing wrong*: "Since Montford was not (potentially or actually) going to [be] paid more to steer clients to SJK, there was no potential or actual conflict of interest and no duty to make any additional disclosures." Respondents' Post-Hearing Brief, p. 9. Thus, according to Montford, he should face no liability now and can do the same thing with impunity in the future.[6]

Regarding the Smyth case and "obey the law" injunctions, Respondents seriously misstate the law in the Eleventh Circuit. In SEC v. Carriba Air, Inc., 681 F.2d 1318, 1321 (11th

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[6] Respondents cannot have it both ways. Previously, Respondents appeared to concede they were subject to a conflict, but negligently failed to recognize it. Now, Respondents would have the Court believe that the substantial financial benefit Respondents received from SJK presented no conflict of interest whatsoever to Respondents. Respondents' argument, much like their assurances against future violations, strains credulity.

Cir.1982), the Eleventh Circuit affirmed such an injunction, recognizing that an exception to the common law rule that "equity will not enjoin a crime" exists in cases of public nuisances that were also crimes.[7] Importantly, in Carriba Air, the Eleventh Circuit also noted that under 15 U.S.C. § 77t, Congress "specifically authorized [district courts to issue] an injunction . . . to prohibit the violation of the securities laws," and that such injunctions comport with the common law exception against "obey the law" injunctions.[8] Id. The Eleventh Circuit has moreover found that the failure to issue an injunction against future violations of securities laws and regulations where all legal requirements were met was clear error. SEC v. Ginsburg, 362 F.3d 1292, 1305 (11th Cir. 2004).

By contrast, in Smyth, the defendant settled with the Commission under terms that included waiving his right to appeal the entry of an injunction, and thus, on appeal, he did not challenge the injunctive provisions contained in the consent decree. SEC v. Smyth, 420 F. 3d 1225, 1233 n. 14 (11th Cir. 2005). The court, however, *sua sponte* stated – in dicta lodged in a footnote – that "obey the law" injunctions have been held invalid and suggested that the injunction at issue was likely unenforceable on those grounds. Id. The Eleventh Circuit has never considered that question as an issue properly before the court, however, and thus, Smyth is far from controlling precedent. In the context of SEC actions, district courts within the Eleventh Circuit have routinely followed the decision in Carriba Air and dismissed Smyth as dicta. See SEC v. Rivers, 272 F.R.D. 607, 609 (M.D.Fla. 2011) ("This Court joins those decisions that have

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[7] The cases cited by Respondents apart from Smyth do not fall within this exception and are therefore inapplicable.

[8] The Division notes that while injunctions issued pursuant to 15 U.S.C. § 77t such as the ones at issue in Carriba Air are reserved for civil actions brought in district court, this Court is expressly authorized to enter a cease-and-desist order pursuant to 15 U.S.C. § 80b-3(k) in this case.

found the dicta in Smyth less compelling than the holdings in Carriba Air and Ginsburg"); SEC v. Huff, 758 F.Supp.2d 1288, 1354-55 (S.D.Fla. 2010) (citing Carriba Air, "Numerous courts, including the Eleventh Circuit, have construed these statutory sections to authorize injunctions to prevent future securities laws violations"); SEC v. U.S. Pension Trust Corp., Civ. Action No. 07-22570-CIV, 2010 WL 3894082 (S.D.Fla. Sept. 30, 2010) ("Dicta in SEC v. Smyth . . . stating that such injunctions are unenforceable 'obey the law' injunctions is not, therefore, controlling"); SEC v. Barriermed, Inc., Civ. Action No. 6:09-CV-102-Orl-28KRS, 2010 WL 4056021 (M.D.Fla. Sept. 24, 2010) ("Congress specifically authorized the issuance of an injunction to prohibit the violation of securities laws . . . the Eleventh Circuit has determined that this statutory authority overrides the usual prohibition against enjoining a party to obey the law"); SEC v. Solow, 554 F.Supp.2d 1356, 1361–62 (S.D.Fla. 2008) ("Thus . . . footnote 14 of Smyth is dicta, and Eleventh Circuit case law appears to permit the type of injunction the SEC seeks here"); SEC v. Converge Global, Inc., Civ. Action No. 04-80841CV, 2006 WL 907567 (S.D.Fla. March 10, 2006) ("The Eleventh Circuit's recent dicta in SEC v. Smyth . . . does not compel a different conclusion"). Thus, Smyth is not law in the Eleventh Circuit, and under Carriba Air, injunctions prohibiting future violations of the securities laws are perfectly permissible.

Accordingly, based upon the evidence presented at the hearing in this matter, the Court should order Respondents Montford and Montford Associates to cease and desist from committing or causing violations of and any future violations of Sections 206(1), 206(2), 204 and 207 of the Advisers Act and Rule 204-1(a)(2) thereunder.

C. An Order Requiring Disgorgement Plus Prejudgment Interest is Appropriate

Respondents challenge the Division's position regarding disgorgement, but their efforts are unpersuasive. Respondents continue to confuse the SJK fraud with their own, which, while not as egregious as Kowalewski's, is still the fraud at issue. Respondents ignore the Division's on-point precedent on this issue in favor of a series of incoherent bullet-points citing irrelevant law. As stated in the Division's Post-Hearing Brief, disgorgement in this case should be equal to the amount paid under the agreement, which is "the fruit of their fraud." In the Matter of IMS/CPAS & Associates, et al., Admin. Rel. No. 119, 1998 WL 7448 at *14 (Jan. 12, 1998); see also SEC v. Washington Co. Utility Dist., et al., 676 F.2d 218, 227 (1981) (reversing district court decision denying disgorgement; "[b]ecause we hold [Defendant] liable for the failure to disclose those payments, we conclude that the district court should order [Defendant] to disgorge a sum of money equal to the total value of all the payments he received . . . .") Respondents' arguments about disgorgement applying only to profits and/or unjust enrichment miss the mark because they do not comport with the facts in this case.

Respondents' contention that the $210,000 is actually "the fruit of Montford's labor" only serves to again underscore the sketchy nature of the transaction. The lack of any timekeeping records (or even an estimate of time spent), the absence of an agreement as to payment amount before beginning work, the unknown basis for the calculation, and the disproportionately large size of the payments relative to the revenue from Respondents' advisory services all belie Respondents' explanation and suggest improper conduct. Respondents' receipt of the monies is the fraud and, as such, should be disgorged. IMS/CPAS, 1998 WL 7448 at *14; Washington Co. Utility Dist., et al., 676 F.2d at 227.

D. <u>Respondents' Civil Settlement with a Single Victim Has No Bearing on Civil Penalties</u>

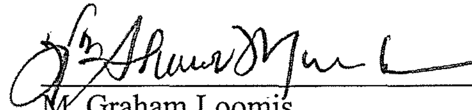
Respondents assert that because they paid $40,000 to settle a private fraud action brought by a client victimized by their fraud, that payment should somehow satisfy their liability for civil penalties. Respondents cite no authority supporting this novel theory – <u>In the Matter of Sheer Asset Management, Inc., et al.</u>, Advisers Act Rel. No. 1459, 1995 WL 6234 (Jan. 3, 1995), the only case mentioned, is a settled action involving no fraud charges and no third-party settlement such as Respondents attempt to rely on here.

In this case, Respondents conduct involved deceit, manipulation, and/or deliberate or reckless disregard of a regulatory requirement. Montford's conduct involved affirmative deceptions and misrepresentations demonstrating scienter, and Montford's entire business model was based on his purported independence, which was a sham. Montford's settlement with St. Joseph's/Candler Hospital, which the Court will recall invested, on Respondents' recommendation, over $7 million in September 2010 – barely a month before Respondents received the second payment from SJK for $80,000 and nine months after Respondents received the original $130,000 payment – has no bearing on whether the Court should find a civil penalty to be in the public interest. Civil penalties as set forth in the Division's Post-Hearing Brief should be granted.

V. CONCLUSION

For the foregoing reasons, and based on the evidence presented by the Division at the hearing, the Court should find that Respondents violated the Advisers Act provisions set forth in the OIP and grant relief as requested in the Division's Post-Hearing Brief.

This 25th day of January, 2012



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