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UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3273 / September 7, 2011

ADMINISTRATIVE PROCEEDING
File No. 3-14536

In the Matter of

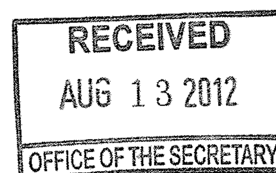
MONTFORD AND COMPANY, INC. d/b/a MONTFORD ASSOCIATES,

and

ERNEST V. MONTFORD, SR.,

Respondents.

RESPONDENTS' REPLY BRIEF



RESPONDENTS' REPLY BRIEF

Division in its Response all but concedes that the ALJ made at least three clear errors of law in the Initial Decision – each on dispositive issues. The ALJ's analysis of the threshold Dodd-Frank issue was so badly reasoned that it did not even draw a defense from Division in its Response Brief. With respect to monetary penalties, the ALJ ignored the statutory requirements for the imposition of Tier Three penalties, as Division implicitly concedes. As Division explicitly acknowledges, the ALJ also applied the wrong standards for determining public interest. The ALJ then imposed sanctions of unprecedented severity, many times more harsh than what Division had requested. This Initial Decision reflects an adjudicative process badly off the rails. The Initial Decision must be reversed.

After recounting basic facts, Montford will provide a brief reply on each of the issues raised.

I. Background Facts

The general facts of this case are not in dispute. Montford is a 65 year old investment advisor with no record of any prior violations of law. In this case, Montford was charged with violations relating to the failure to disclose payment that Montford received from a fund manager for work Montford did for the fund manager unrelated to any investment advice. The fund manager – Stanley J. Kowalewksi ("SJK") -- turned out to be a fraud, and, because of SJK's fraud, Montford's clients lost money. There was no evidence or even contention by Division that Montford had any role in, or knowledge of, SJK's fraud. Indeed, Montford himself was a victim of the fraud, having invested his own retirement funds with SJK.

There was no evidence that the payments Montford received from SJK were related to, or contingent upon, advice that Montford gave to his clients. Still, Montford testified that accepting and not disclosing the money was a mistake that he regretted and for which he had paid dearly. Montford's clients' testified that they wished Montford had disclosed the payments, but otherwise always had found Montford's advice to be professional and competent. Montford reached an amicable settlement with the only client that sued it, and cooperated fully with the S.E.C. and the Justice Department in the separate investigation of SJK's massive fraud.

II. Argument

A. Missing the Dodd-Frank Deadline Requires Dismissal

In its Opening Brief on the Merits, Montford explained that Commission staff violated Dodd-Frank by failing to file the OIP within 180 days of the issuance of the

Wells notice and failing to obtain a proper extension. Dodd-Frank allows the Director of Enforcement to grant an extension, but only after finding that the complexity of the investigation requires an extension. In this case, the Director of Enforcement did not make the determination required by Dodd-Frank. In the Initial Decision, the ALJ held that the Director's failure to make the Dodd-Frank determination was retroactively excused by the Commission's selection in the OIP of a 300-day schedule under Rule 360. In the Opening Brief, Montford explained that the ALJ's analysis is totally and fundamentally flawed for a number of reasons, including the fact that it confuses two entirely separate deadlines and that it allows the Commission to make a determination that Congress (sensibly) delegated to the Director of Enforcement.

In its Response, Division, to its credit, makes no attempt to support the ALJ's deeply flawed and bizarre analysis. Instead, Division advances alternative arguments to reach the same result. First, Division contends that Commission staff did comply with Dodd-Frank. As explained in Section 1, below, this argument finds no support in the evidentiary record. Second, Division contends that missing the Dodd-Frank deadline has no consequence. As explained in Section 2, Congress would never have enacted the deadline if it intended it to have no effect, and the consequence of missing the deadline is dismissal. Further, as explained in section 3, for the Commission to adopt Division's arguments would send the wrong signal to Commission staff, the federal courts, and to Congress about the Commission's intent to follow the letter and spirit of the law. Congress in Dodd-Frank clearly wanted Commission staff to either file an action within the deadline or dismiss the action – a clear congressional intent that should be honored in this case with the reversal and vacatur of the Initial Decision.

1. Division Did Not Comply with the Dodd-Frank Act

Division contends that Commission staff complied with Dodd-Frank because the Director of Enforcement granted an extension. Even if there were any admissible evidence of an extension (and there is none), Division misses the point entirely. Dodd-Frank limits the circumstances in which the Director of Enforcement is authorized to grant an extension, requiring the Director of Enforcement to determine that the complexity of the investigation requires the extension. In this case, the Director *did not make this determination*. There is no evidence that the Director did so and the Division does not contend that the Director did so. Division, having no evidence that the Director did so, assumes that the Director made this determination because he (supposedly) granted the extension, but that assumes away the entire issue. Again, even if the self-serving triple hearsay affidavit of Division's counsel is deemed admissible evidence – an absurd proposition – the most Division can say is that the Director granted an extension, not that the Director followed the law in doing so.

Make no mistake, this is no oversight. Montford has taunted Division on this point in the briefs, repeatedly stating the truth – that there is no evidence or even contention that the Director actually made the complexity determination – and Division has not once asserted to the contrary. The Division's brief on this point is carefully written, but it does not say (because it cannot say) that the Director complied with the law in granting the extension.

Instead of affirmatively representing that the Director made the determination required by law, Division makes a clever, but ultimately disturbing, argument. Division states on the bottom of page 24 and the top of page 25:

> Respondents also contend that the Division has not produced sufficient 'evidence' that the Division Director made the complexity determination required by Section 929U when extending the Dodd-Frank deadline. Respondents, however, offer no authority for the proposition that they are entitled to such transparency with respect to that process. Moreover, even if the Commission or the court were inclined to allow it, Section 929U does not provide sufficient standards for review.

There are at least three fundamental problems with this argument. First, the issue is not whether there is "sufficient" evidence that the Director made the complexity determination, but whether there is *any* evidence that the Director did so – and there is no such evidence. As a result, there is no evidence of compliance with the law.

Second, in our advocacy system, the normal response to an argument that there is "no evidence" to support a position is to counter: "yes, there is evidence, and here it is in the record." Instead of pointing to evidence in the record to rebut Montford's showing, however, Division puts the word "evidence" in quotes, mocking Montford for making such a naïve argument about evidence and proof, as if those concepts are beneath the grand purposes of securities law enforcement. Montford does not believe that it is naïve to insist that the Government prove its case.

Third, Division's argument that Montford offers "no authority for the proposition that they are entitled to such transparency with respect to that process" may be the most arrogant statement of a government official since *Animal Farm*. This is a very basic and fundament point: for the Government to prevail, it has to introduce evidence to prove by a preponderance of the evidence every element of its case, including evidence that it has jurisdiction to prosecute the case and that it has complied with the statutory preconditions for bringing the action. To the extent that requiring the Government to come forward with actual evidence in support of the elements of its case is requiring

"transparency," then yes, everything about our advocacy system, our rules of evidence, our system of Government, the due process clause, the Bill of Rights, and the Administrative Procedure Act requires transparency.

It is critically important, however, to return to the actual issue presented. Division's "transparency" argument is a smoke-screen. The issue in this case is not whether the Director's decision that the investigation was too complex is supported by substantial evidence or whether Montford is entitled to look behind that determination to litigate whether it is correct or not. To the contrary: since there is no evidence that the Director made the complexity determination, we do not even reach the issue of whether Director made that decision correctly or what deference would be afforded such a decision.

Since there is no evidence, or contention, that the Director made the complexity determination required by the law, the ALJ erred in not dismissed the action.

2. Compliance with Dodd-Frank is a Precondition to Maintaining an Action

Division argues in the alternative that any failure of the Commission staff or the Director to follow the law should not result in a dismissal of the action. The parties agree that this issue concerns the application of the Supreme Court's decision in *Brock v. Pierce County,* 476 U.S. 253 (1986), which address the circumstances in which the government may take action even after a statutory deadline has passed. Division correctly notes that *Brock* addressed a number of different factors, but analysis of each of these factors support Montford's argument.

The first consideration is whether the statute specifies the consequences of missing the deadline. In *Brock,* the statute was silent. In this case, however, the Commission is given two, and only two, options: file the OIP on time or dismiss the

action. Division argues that Dodd-Frank does not "say anything about dismissing an action." (Brief at 27). This is an extraordinarily bureaucratic and crabbed reading of the statute. Here is what the statute says:

> Not later than 180 days after the date on which Commission staff provide a written Wells notification to any person, the Commission staff shall either file an action against such a person or provide notice to the Director of Enforcement of its intent not to do so.

Division argues that the statute "provides no consequence if the staff fails to do either." But no statute that is framed as an "either/or" proposition provides a consequence if neither option is taken; the intent is that the two options are exclusive – if you do not do the one, you must do the other. This is common sense.

Division would apparently require Congress to specify a third option by saying: "and, if Commission staff totally disobeys this clear command by failing to do either, the Commission staff shall notify the Director of Enforcement of its intent to not pursue an action, and this time we mean it." But even this third option, under Division's logic, would be insufficient because Congress did not specify what would happen if Commission staff failed to do any of the three options.

By giving Commission staff two and only two options, Dodd-Frank clearly specifies the consequence of non-compliance and is materially distinguishable from the statute in *Brock*.

The second *Brock* consideration is whether deeming the deadline a deadline would work a hardship upon the agency. Division does not even suggest that there would be any hardship. Commission staff has total control over the timing of the investigation and the filing of the OIP because the 180 days runs from the date Commission staff issues the Wells notice. Obviously, what Congress intended was this:

before Commission staff issues a Wells notice, it must be ready to prosecute the case, and if it is not ready to prosecute the case, it should wait to issue the Wells notice until it is ready to do so.

The third *Brock* consideration is whether public interests are at stake. Here Division simply assumes, without any analysis, that the "public interest" is the same as the "government's interest," and the "government's interest" is the same as the interest of Commission staff. Montford concedes that it would be in Commission staff's best interest for its failure to follow the law to be excused in this case. But that is not in the public interest. The public interest has been articulated by Congress, which has made it very clear that these cases, if they are going to be prosecuted, need to be initiated within 180 days of the issuance of the Wells notice.

This is a question of statutory intent. It is abundantly clear that Congress wanted Commission staff, if it were going to file an action, to do so within 180 days. Commission staff did not do so in this case and, out of respect for Congress's clear intent, this action should be dismissed.

3. Adopting the Division's Argument Would Send a Very Bad Signal

Even if the law did not compel the Commission to dismiss this action, the Commission would still have the authority to do so given its supervisory role over investigations and prosecutions and general regulatory power. Montford respectfully submits that the Commission should exercise this responsibility and authority to hold that the failure of Commission staff to comply with Dodd-Frank will not be tolerated. It is not difficult to comply with the law, and the least this law enforcement agency can do is insist that its staff follow the law before prosecuting a citizen for not following the law. Such a holding would give notice to Commission staff, the federal courts, and to

Congress that the Commission is serious about staff complying with the letter and spirit of the law and that it will insist upon disciplined and professional prosecution of cases such as this. Adopting Division's argument, on the other hand, will signal just the opposite.

For all these reasons, the judgment should be reversed and the case dismissed because the action was not commenced within the time period specified by Congress in Dodd-Frank.

B. The ALJ Erred in Imposing Tier Three Damages

The ALJ's imposition of monetary damages against Ernie Montford that were six times what Division sought in the case, and against his company that were twenty times what Division sought in this case, was clear and reversible error: the ALJ applied the incorrect legal standard in determining the applicable of Tier Three penalties and applied the incorrect legal standard in making the "public interest" determination.

1. The ALJ Does Not Apply the Correct Standard for Tier Three Penalties

As the Commission is well aware, the statute governing the imposition of monetary penalties lists the three "tiers" of monetary penalties and outlines, for each, the required showing. In its Opening Brief, Montford showed that the ALJ did not apply any of the elements required for a Third Tier penalty. In its response, Division does not answer this charge, contending instead that *had* the ALJ applied the correct legal standard, the ALJ might have reached the same result. This kind of analysis cannot save a flawed Initial Decision, for once it is clear that the ALJ applied the wrong legal standard, the decision must be reversed.

In the Initial Decision, the ALJ cited the correct statute, 15 U.S.C. § 80b-3(i),[1] but then proceeded to ignore the statute entirely. The ALJ did not make *any* factual findings necessary for the imposition of Tier Three penalties. Instead, the ALJ concluded that severe penalties "are warranted given Respondents' brazen conduct toward their non-profit clients and should serve to deter other fiduciaries from similar self-serving conduct." (Initial Decision, p. 23). Even if the ALJ's conclusions were factually correct (and they are not), those conclusions have nothing to do with the statute, which requires a finding that the respondent's conduct "created a substantial risk of substantial losses" or resulted in "substantial pecuniary gain." The statute does not allow enhanced penalties based on the corporate status of the investor (non-profit or for profit), says nothing about deterrence, and does not list "brazen conduct" as a consideration. Some of these considerations might be worthy objectives for other penal regimes, but none of them are factors selected by Congress for the violations asserted in this case.

Montford was entitled to a hearing and an adjudication in which the correct legal standards were applied to the facts. That did not happen in this case, as Division all but concedes, and for this reason the Initial Decision must be reversed. *McBride v. Eastman Kodak Co.,* 844 F.2d 797 (D.C. Cir. 1988) (application of incorrect legal standard by ALJ requires reversal and remand); *Butler v. Barnhart,* 353 F.3d 992 (D.C. Cir. 2004) (failure of the ALJ to apply the correct legal standard required reversal and

[1] The statute sets maximum penalties for three tiers, each requiring additional findings. Third tier sanctions require a finding that "the act or omission described in paragraph (1) involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; and such act or omission directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons or resulted in substantial pecuniary gain to the person who committed the act or omission."

remand). *See also S.E.C. v. Chenery Corp.,* 318 U.S. 80, 94-95 (1943); *PPG Industries, Inc. v. United States,* 52 F.3d 363 (D.C.Cir. 1995).

2. The ALJ Applied the Incorrect Law on the "Public Interest"

As Montford explained in its Opening Brief, 15 U.S.C. § 80b-3(i)(3)[2] lists "public interest" considerations to be taken into account in the imposition of monetary sanctions. Rather than citing and applying this statute, however, the ALJ applied the so-called *Steadman* factors, from an old Fifth Circuit case. In its Response, Division does not explain this departure, other than to state that the statute is "nearly coextensive with the *Steadman* factors," as if close were good enough. (Division Response Brief at 30). But the ALJ did not come close to applying the correct statutory factors. Among other omissions, the ALJ failed to consider "the extent to which any person was unjustly enriched, taking into account any restitution made to persons injured by such behavior."

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[2] The statutes provides:

> (1) Determination of public interest
> In considering under this section whether a penalty is in the public interest, the Commission may consider—
>
> (A) whether the act or omission for which such penalty is assessed involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement;
>
> (B) the harm to other persons resulting either directly or indirectly from such act or omission;
>
> (C) the extent to which any person was unjustly enriched, taking into account any restitution made to persons injured by such behavior;
>
> (D) whether such person previously has been found by the Commission, another appropriate regulatory agency, or a self-regulatory organization to have violated the Federal securities laws, State securities laws, or the rules of a self-regulatory organization, has been enjoined by a court of competent jurisdiction from violations of such laws or rules, or has been convicted by a court of competent jurisdiction of violations of such laws or of any felony or misdemeanor described in subsection (e)(2) of this section;
>
> (E) the need to deter such person and other persons from committing such acts or omissions; and
>
> (F) such other matters as justice may require.

Id. In considering monetary sanctions, the ALJ should have taken into account, among other things, that the ALJ was separately ordering full restitution in the form of the disgorgement remedy. The ALJ also did not take into consideration that Montford had never "been found by the Commission [or any other regulatory agency] to have violated the Federal securities laws." *Id.* The ALJ's failure to apply the correct statutory considerations of the public interest is clear reversible error. *McBride, supra* (ALJ's application of incorrect legal standard requires reversal); *Barnhart, supra* (same).

3. Wildly Excessive Penalties

Since the ALJ applied at least two the wrong legal standards in her consideration of monetary penalties, her decision must be reversed without consideration of the actual penalty assessed. A review of that penalty, however, further demonstrates that the Initial Decision cannot, on any basis, be sustained.

In its Response, Division does not cite a single case in which penalties of this magnitude were assessed for comparative conduct. *Compare Sheer Asset Management*, 1995 CCH ¶ 85,609 ($10,000 civil penalty, and no disgorgement, for failure to disclose payments over a three year period from broker to investment advisor of $150,000). Division does not cite a single case in which the ALJ imposed sanctions higher than those sought by the Government, much less six and twenty times higher than the sanctions sought by the Government. Division makes no attempt to explain why these particular numbers are justifiable given the facts of this case, or what the ALJ knew, that Division did not, in assessing the appropriate level of punishment.

The one point that Division does make, over and over again, is that Montford deserves harsh treatment because Montford never accepted responsibility or acknowledged wronging. (Division Brief at 30, 35, 36). This is incorrect, a plain

misstatement of the record. The wronging was the failure of Montford to disclose to his clients the payments that he received from SJK. Montford plainly and candidly acknowledged this wrongdoing at the hearing. (Tr. at 176). It is also true that Montford has vigorously defended this case, and insisted that he never labored under an actual conflict of interest, but those positions have no bearing on his acceptance of responsibility for failing to disclose the payments that he received from SJK. In any event, given that the ALJ clearly applied two incorrect legal standards, and given that there is no authority of the imposition of such extreme sanctions, the Initial Decision must be reversed.

C. Disgorgement Inappropriate on the Facts of this Case

Division does not address most of Montford's arguments on disgorgement, dismissing them in a footnote, and relies instead upon a single argument: that disgorgement was appropriate because Montford's receipt of the $210,000 from SJK was itself wrongful and, because the receipt of the money itself was wrongful, "disgorging" that money was an appropriate remedy.

This is entirely incorrect. SJK paid Montford for the work Montford did for SJK. Montford did nothing wrong accepting that money. In fact, even if the payment was a complete gratuity there would have been nothing wrong in accepting the payment. Division cites no state or federal law that was broken by the payment or receipt of this money. With alarm, Division notes that Montford did not keep time slips recording how much time his staff spent on the SJK work, as if the failure to do so was a federal crime. Further, Division neglects to mention that SJK told the SEC of these payments in April of 2010. If these payments were so alarming, wrong, and deserving of disgorgement, why did the payment cause the SEC no alarm in 2010 and why did the S.E.C. not

immediately seek punishment of SJK and Montford? The reason? There was obviously nothing wrong with the payments.

The fact that the failure to disclose the payments was wrongful does not convert the funds into ill-gotten gains. For the funds to be "disgorgeable," they would need to be returned to the party who paid the money in the first place – disgorgement reverses an ill-gotten gain. But these funds were paid by SJK, who masterminded the fraud in the first place and stole millions of dollars from Montford and Montford's clients. Division has never suggested that the payments should be reversed so that master fraud SJK may recoup monies he paid Montford, yet this is the exact purpose of disgorgement as an equitable remedy.

As Montford explained in its Opening Brief, just because disgorgement is equitable does not mean that it has no definition and can be applied in any circumstance, as Division suggests. To the contrary, there are a number of well-recognized rules which define and limit the disgorgement remedy. In response, Division states in footnote 13 on page 33:

> Respondents set forth several additional argument attempting to show that disgorgement is inappropriate in this case. Those additional arguments are based on rigid readings of boilerplate statements of law that do not acknowledge the flexible nature of an equitable remedy such as disgorgement and therefore fail.

The cases Montford cited may be rigid but they constitute a well-developed body of law that should not be so lightly regarded. Indeed, as Division's failure to offer any response to these arguments suggests, they require reversal in this case. The rules of law include the following:

1. Disgorgement is appropriate to reverse a payment from the victim to the

perpetrator; here, the payment came from SJK, the perpetrator, and was made to Montford, one of the SJK's victims. *See S.E.C. v. Collello,* 139 F.3d 674 (9th Cir. 1998) (disgorgement applies to funds defrauding party took from victims).

2. Division contended that disgorgement applies to the "fruit of the fraud." But the payments from SJK were not the "fruit of the fraud" but the fruit of Montford's labor. The ALJ did not find that Montford committed fraud by working for and receiving money from SJK. That was not a fraud, and the fruits of that labor are not subject to disgorgement.

3. Disgorgement is an appropriate remedy when the amount of the money disgorged is equal (or at least related) to the damages caused by the receipt of the money. The ALJ made no finding of any relationship between the amount of money SJK paid to Montford and any damage caused by Montford's failure to disclose the payment to his clients.

4. The purpose of the disgorgement remedy is to protect the public. *S.E.C. v. Cavanaugh,* 445 F.3d 105, 117 & n. 25. The ALJ did not find that disgorgement will protect the public.

5. Disgorgement only applies to profits that Montford derived. Here, the ALJ disgorged the gross amount of payments Montford received. *See S.E.C. v. Haligiannis,* 470 F. Supp.2d 373 n. 10 (rejecting the SEC's position that it could recover gross payments); *S.E.C. v. Blatt,* 583 F.2d 1325, 1335; *S.E.C. v. Amerifirst Funding, Inc.*, 2008 WL 1959843. At the hearing, Montford introduced substantial documentary evidence establishing the efforts undertaken to earn the $210,000. Montford would have introduced additional testimony, but the ALJ stated that she did not believe any of the additional evidence was necessary because the difficulty of Montford's work for SJK

was not in dispute. The ALJ stated: "But I don't think the Division of Enforcement is questioning that the was all messy. . . . I imagine they would agree that this was a very messy business." (Tr. at 155). It is abundantly clear, however, that Montford's efforts on SJK's behalf were substantial, that the $210,000 was earned, and that it is contrary to equity to require Montford to "return" the money to SJK or to give it to anyone else.

6. Disgorgement is to "prevent unjust enrichment." *S.E.C. v. Banner Fund Int'l*, 211 F.3d 602, 617 (D.C.Cir. 2000). The ALJ did not find that that SJK's payments to Montford unjustly enriched Montford.

For these reasons, the Initial Decision's disgorgement remedy constituted a clear error of law and must be reversed.

D. Industry Bar, Cease and Desist, Unnecessary

As Montford explained in the Opening Brief, the ALJ erred by imposing an industry bar and issuing a cease and desist order because there was no showing of a risk of future violations. Division's response on each issue is to argue that if a violation is shown, the risk of a future violation is presumed, and consequently no additional evidence is necessary. This, plainly, is not the law. *Monetta Financial Serv., Inc. v. S.E.C.,* 390 F.3d 952, 957 (7th Cir. 2004) (vacating Commission's order imposing sanctions because the Commission failed to consider, inter alia, the isolated nature of the violation). What Judge Tjoflat said in *Steadman v. S.E.C.,* 603 F.2d 1126, 1141 (5th Cir. 1979), applies directly to this case: "It would be a gross abuse of discretion to bar an investment adviser from the industry on the basis of isolated negligent violations."

This is Montford's first brush with the law. Montford did not know of the SJK fraud, did nothing to advance any of the fraudulent schemes, did not benefit from the fraud, and did not have any incentive to deceive its clients into investing in SJK. If

Ernie Montford did not believe in SJK, Ernie Montford would never have invested his entire retirement account with SJK. Montford had no intent to harm anyone. *See S.E.C. v. Slocum, Gordon, & Co.*, 334 F.Supp.2d 144, 185, 187 (D. R. I. 2004) (for "non-scienter based, technical violations" refused to impose injunctive relief, instead imposed $3,000 civil penalty). The notion that there is a risk that he or his company will commit a future violation has no basis in fact.

In addition, the cease and desist order is unenforceable because it simply commands Montford to obey the law – an injunction that only Congress has the power to issue, not the courts. It is well settled that "obey the law" injunctions, including those issued in securities cases, are unenforceable. *S.E.C. v. Smyth*, 420 F.3d 1225, n. 14 (11th Cir. 2005) ("This circuit has held repeatedly that 'obey the law' injunctions are unenforceable."); *Hughey v. JMS Development Corp.*, 78 F.3d 1523 (11th Cir. 1996); *United States v. Philip Morris USA Inc.*, 566 F.3d 1095 (D.C. Cir. 2009) ("we have held injunctions to be too vague when they enjoin all violations of a statute in the abstract without any further specification, or when they include, as a necessary descriptor of the forbidden conduct, an undefined term that the circumstances of the case do not clarify").

E. No Conflict of Interest

In the Opening Brief, Montford showed that there was no conflict of interest because Montford would have been paid (and was paid) the same by his clients (and by SJK) whether Montford's clients invested with SJK or with another manager. For the ALJ to hold to the contrary, there had to be some evidence that Montford was being paid to direct clients to SJK or would somehow benefit financially from the referral of clients to SJK. But Division, for whatever reasons, decided to not pursue this tact and did not

call any witness or introduce any evidence in support of this proposition. There were a number of potential witnesses – SJK himself, members of SJK staff, the team of forensic experts who were engaged on the SJK fraud – who might have been called to give such testimony had that, in fact, been the case. But there was no such witness and no such testimony.

In its response, Division correctly notes that the Supreme Court in *S.E.C. v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 187 (1963), did emphasize that a conflict of interest could be subconscious, and that a subconscious motivation to favor one's own financial interest was as much a concern behind the 1940 Act as "deliberate intent." But this misses the point. Montford did not have subconscious or conscious motivation to steer clients to or away from SJK. Thus, Division did not make the basic showing required of *Capital Gains* – that Montford's "advice to a client might result in financial benefit to the adviser – other than the fee for the advice." *Id.* As a result, there was no showing of a violation of Section 206, and for this additional reason, the Initial Decision should be reversed.

This 8th day of August, 2012.

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