UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9361 / September 14, 2012

SECURITIES EXCHANGE ACT OF 1934
Release No. 67860 / September 14, 2012

INVESTMENT ADVISERS ACT OF 1940
Release No. 3464 / September 14, 2012

INVESTMENT COMPANY ACT OF 1940
Release No. 30202 / September 14, 2012

ADMINISTRATIVE PROCEEDING
File No. 3-15024

In the Matter of

WALTER V. GERASIMOWICZ, MEDITRON ASSET MANAGEMENT, LLC, MEDITRON MANAGEMENT GROUP, LLC,

Respondents.

PREHEARING BRIEF OF THE DIVISION OF ENFORCEMENT

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INTRODUCTION

This case involves, along with other violations, the willful misappropriation and misuse of advisory client assets by Dr. Walter V. Gerasimowicz ("Gerasimowicz"), Meditron Management Group, LLC ("MMG"), an unregistered investment adviser, and Meditron Asset Management, LLC ("MAM"), a registered investment adviser – both entities owned and controlled by Gerasimowicz. Gerasimowicz, MMG, and MAM owed duties of candor, loyalty, integrity and full disclosure to their clients – duties that they repeatedly breached in order to evade discovery of their malfeasance and in disregard of their clients' interests.

From at least 2009 to 2011, Respondents misused and misappropriated over $2.7 million belonging to their hedge fund client, the Meditron Fundamental Value/Growth Fund, LLC ("Meditron Fund" or "the Fund"), to provide financial support to a private company that Gerasimowicz effectively controlled, and in which he also had a substantial personal interest, undisclosed to investors and his clients. Specifically, by the end of 2011, Gerasimowicz, MMG, and MAM had funneled approximately 80% of the Fund's assets to SMC Electrical Contracting Inc. ("SMC"), a private contracting company that filed Chapter 11 bankruptcy proceedings in September 2011. Gerasimowicz caused SMC to issue unsecured promissory notes to the Fund for the earlier transfers, but seemingly opted not to similarly document the later transfers of Fund assets to SMC. Those notes, and indeed the Fund's entire SMC "investment," are now close to worthless, given SMC's bankruptcy filing. Moreover, Respondents failed to write down these notes and continued to value the Fund's SMC position at cost despite SMC's deteriorating financial condition and eventual bankruptcy.

While breaching their fiduciary obligations to act in the best interests of the Fund and of MAM advisory clients who also invested in the Fund, Respondents misrepresented or omitted material information to Fund investors concerning:

(i) dramatic deviations from the Fund's stated investment strategy, which was to focus on stocks and provide "controlled risk diversification of investments;"

(ii) deviation from the Fund's disclosed valuation policy, which provided that "reasonable" valuations would be assigned and that the Fund would use a fair value methodology, when in fact SMC was valued at cost despite its deterioration and bankruptcy; and

(iii) Gerasimowicz's and MAM's significant conflict of interest, resulting from their undisclosed investment of approximately $2 million of their own funds in SMC.

Furthermore, when investors attempted to make redemptions, Respondents stonewalled them repeatedly and failed to disclose that the Fund was essentially destitute due to misappropriation of its assets.

In addition to making these direct misstatements and omissions, Respondents marketed themselves through advertisements in *Worth Magazine* that falsely claimed that MAM had over a billion dollars in assets under management ("AUM"), when MAM in fact had only $50 million in AUM according to its Form ADV. MAM, aided and abetted and caused by Gerasimowicz, also violated the advertising and custody rules applicable to registered investment advisers.

I.

RESPONDENTS AND RELATED PARTIES

Respondents

Walter Gerasimowicz, age 60 at the time of filing, resides in New York, New York. He is the Chairman, Chief Executive Officer, Chief Compliance Officer, Chief Investment Officer, and sole owner of MAM, a registered investment adviser. Gerasimowicz is also the sole owner of MMG, an unregistered investment adviser, through which he manages the Meditron Fund. Gerasimowicz is the founder and operating manager of Meditron Real Estate Partners, LLC ("MREP"), a private company, and he serves as President and Chairman of the Board of Directors of SMC, the private electrical contracting company owned by MREP.

MAM is a New York limited liability company and registered investment adviser with its principal place of business in New York, New York. MAM has been registered [redacted] with the Commission since April 9, 2003 and is wholly owned by Gerasimowicz. Gerasimowicz is one of MAM's two employees and he has sole authority to direct the adviser's activities. MAM claimed to have approximately $50 million in regulatory AUM as of March 24, 2012. MAM provides investment advisory services to advisory clients with separately managed accounts, and claims that approximately 10% of its advisory clients also have invested in the Meditron Fund.

MMG is a Delaware limited liability company, formed on March 14, 2003, with its principal place of business in New York, New York. Gerasimowicz is MMG's sole owner and both the Fund's Private Placement Memorandum ("PPM") and its Operating Agreement name MMG as the Fund's manager. (SEC Trial Exs. 39 at 5, 40 at 3, 14.) As such, MMG purportedly serves as the unregistered investment adviser through which Gerasimowicz manages the Meditron Fund. However, Respondents have represented that MMG is used for "branding and marketing purposes" but otherwise exists "as a shell company that has no substantive function" while MAM "performs all substantive investment advisory functions." (SEC Trial Ex. 215 at 4.) MAM and MMG share a common office and a common website, MMG has no bank or brokerage accounts in its name, and advisory fees for managing the Meditron Fund are paid to MAM.

Related Parties

Meditron Fund is a Delaware limited liability company that was formed on March 14, 2003. It is an investment fund managed by Gerasimowicz, MMG and MAM with approximately thirteen investors and a reported $4.2 million in assets as of its March 2012 Form ADV filing.

(SEC Trial Ex. 97 at 18.) The Form ADV represented that MAM was the investment adviser to the Fund and that the Fund had no other investment adviser or sub-adviser. (*Id.* at 18-19.) The Meditron Fund has no board of directors or investment committee, and the PPM and the Operating Agreement endow the manager MMG – effectively Gerasimowicz because of his sole ownership of MMG – with sole investment authority over the Fund. Gerasimowicz controls the Fund's bank and brokerage accounts. The custodian for the publicly-traded securities in the Fund's portfolio was Goldman Sachs Execution & Clearing until July 2010 ("Goldman"), when it was switched to Charles Schwab & Co., Inc. ("Schwab").

MREP is a Delaware limited liability company formed by Gerasimowicz on June 28, 2004 as a vehicle for investments in real estate ventures. According to MREP's Operating Agreement and the first amendment thereto, Gerasimowicz was the operating manager of MREP. MREP has no other employees. In 2007, MREP functioned as a vehicle for Gerasimowicz, the Meditron Fund, and certain individual MAM advisory clients to co-invest in SMC, which is MREP's sole investment.

SMC is a private electrical contracting company and New York corporation headquartered in New York, New York. Gerasimowicz caused MREP to acquire 100% of SMC in two separate transactions: (1) the initial transaction in which MREP purchased 50% of SMC in 2007, and (2) a second transaction by which MREP acquired the remaining 50% in 2008. In addition to his role as investment manager to the Meditron Fund and to MREP, Gerasimowicz became the President and Chairman of the Board of Directors of SMC. On September 30, 2011, SMC filed a petition for relief under Chapter 11 of the Bankruptcy Code in the Southern District of New York (Case No. 11-14599 (Bankr. S.D.N.Y.)). (SEC Trial Ex. 142.)

II.

THE REPRESENTATIONS IN THE MEDITRON FUND OFFERING

Gerasimowicz and MMG formed the Meditron Fund in 2003. According to MAM's March 2012 Form ADV, approximately thirteen investors had membership interests in the Fund at that time, several of whom were also MAM advisory clients. (SEC Trial Ex. 97.) Summary evaluations prepared for Fund investors as of June 30, 2012 similarly indicate that thirteen investors remained in the Fund at that time, including several investors who purchased their interests after Respondents began deviating from Fund strategy and misappropriating assets in September 2009. (SEC Trial Ex. 89.) Gerasimowicz, on behalf of MMG, provided new investors with the Fund's PPM, Operating Agreement, and subscription documents, as well as a one-page document detailing the Fund's historical monthly and annual performance returns.

The PPM (SEC Trial Ex. 39) describes the Fund's investment objective as a stock-centered approach seeking "to outperform the S&P 500 Index through the purchase of undervalued securities and their subsequent sale upon reaching price appreciation targets. The Fund's portfolio is normally comprised of 15 to 50 stocks with expected fair values considerably greater than their current market prices." (PPM at 1; *see also* PPM at 4 ("Fund "seeks to outperform the market by purchasing undervalued securities"); PPM at 19 ("purposes of Fund are to purchase undervalued securities and sell such securities upon their such securities reaching price appreciation targets" (sic)).) The PPM also represents that "the Fund's portfolio ***will be U.S. Equities*** of variable market capitalization," and that "the Fund's portfolio may be heavily weighted in small and mid-cap issues, and is not necessarily composed of stocks which comprise the S&P 500." ((PPM at 1) (emphasis supplied).)

The PPM describes the Fund's methodology for portfolio composition as beginning "with a proprietary quantitative ***stock selection*** methodology centered upon ***fair value calculations*** – the price at which a stock should trade at current market levels." ((PPM at 4) (emphasis supplied).) The PPM further represents that the Fund's investment manager selects investments by considering "other fundamental data such as corporate earnings and growth potential." (*Id.*) The PPM also represents that the manager of the Fund "computes weekly fair values of the securities." (PPM at 4.) The PPM requires the manager to value the Fund's securities based on market prices, and provides that in the absence of such prices, the "value shall be reasonably assigned by the Manager." (PPM at 9-10; *see also* Op. Agmt. at 10-11 ("All other securities held by the [Meditron Fund] will be assigned the value that the Managers in good faith determine.").

The PPM is replete with additional references to stocks and securities, further emphasizing the representations to investors that these constitute the Fund's holdings.[1] (*See also* PPM at 19 ("The Fund will have a portfolio that normally consists of 15 to 50 stocks.").) The Fund's Operating Agreement (SEC Trial Ex. 40) further sets out, in relevant part, that the purposes of the Fund are:

> (a) to purchase undervalued securities;
>
> (b) to sell securities owned by the Company upon such securities reaching price appreciation targets;
>
> (c) to acquire and maintain a Company portfolio composed of stocks;
>
> (d) to analyze various potential stocks for purposes of purchasing or selling such stocks"

(Op. Agmt. at 5.)

[1] The PPM did note that prior to investment, proceeds of sales of membership interests might be held in "US Securities, obligations of foreign governments, commercial paper, and certificates of deposit and bankers acceptances issued by domestic branches of US banks." (PPM at 9). Notably, there is no mention here, or anywhere else in any document, of the Fund investing in notes of the kind issued by SMC, or of making loans to private companies.

The PPM repeatedly emphasizes that the Fund maintains a diversified investment portfolio in order to reduce risk. The PPM represents that the Fund's goal is to "seek high economic return through capital appreciation with controlled risk diversification of investments," that "a diversified portfolio of long and short positions is maintained with a long bias," and that "positions will often be hedged selectively to reduce market risk and volatility." (PPM at 4-5.)

The PPM further represents that each member will have a Capital Account "established on the books of the Fund." (PPM at 9; *see also* Op. Agmt. at 7.) For each Capital Account, a "'Fund Percentage' will be determined for each Member . . . by dividing the Member's Capital Account Balance . . . by the aggregate Capital Account Balance of all Members." (*Id.*; *see also* Op. Agmt. at 3 (defining "sharing ratio" for each member).) Thus, any investor could, by reference to these figures, determine for him or herself the total capital amount of the Fund.

Pursuant to the PPM, Fund investors may withdraw from the Fund at the end of any calendar quarter upon prior written notice. (PPM at 11; *see also* Op. Agmt. at 16.) The offering documents provide that the manager will be paid an annual 1% management fee as well as a 20% incentive allocation fee. (PPM at 10; Op. Agmt. at 7, 15.) The Fund is also responsible for "investment-related expenses, such as brokerage commissions, clearing fees, interest, custodial fees, and similar expenses," as well as "[o]rganizational expenses (including legal and accounting fees)." (PPM at 2, 11.) Bank and brokerage records show that Fund fees and expenses were paid directly to MAM. (SEC Trial Exs. 103, 104, 149.)

The Operating Agreement further provides that any member or manager "***may*** engage in and possess interests in other business ventures of any and every type and description," and that the Meditron Fund *may* transact business with any member or manager "***provided the terms of***

those transactions are no less favorable than those the [Fund] could obtain from unrelated third parties [emphasis supplied]." (Op. Agmt. at 18-19.)

III.

RESPONDENTS' DIVERSION OF FUND ASSETS TO AND FROM SMC

In 2007, Gerasimowicz began raising capital through the offer and sale of limited partnership interests in MREP for the specific purpose of investing in SMC. Gerasimowicz, MAM and MMG caused the Meditron Fund to invest $200,000 in MREP in June 2007. During the same period, Gerasimowicz recommended and caused seven individual MAM advisory clients to purchase MREP limited partnership interests totaling $750,000, and Gerasimowicz personally invested $50,000 in MREP in May 2007. (SEC Trial Exs. 7, 44, 45.) In June 2007, Gerasimowicz caused MREP to invest that $1 million in SMC in exchange for a 50% ownership interest in SMC. (SEC Trial Exs. 68, 69.)

Respondents were on notice of SMC's precarious position at least as early as September 2008, when they came to believe there was fraud and malfeasance at SMC. (*See* SEC Trial Exs. 1 and 2, Testimony Transcripts of Walter Gerasimowicz ("WG Tx.") at 145-46). In September 2008, SMC fired its President and CEO, Ted Doumazios, for purportedly diverting jobs and materials to a contracting company owned by Doumazios' sister. In connection with his termination, Doumazios agreed to allow MREP to acquire his 50% share of SMC at no additional cost, and MREP became the sole equity owner of the company. (SEC Trial Ex. 72; WG Tx. at 115-116.) At this time, Gerasimowicz assumed a more active management role in the day-to-day operations of SMC.

By at least the fall of 2008, SMC began experiencing even greater financial difficulties and Gerasimowicz and MAM, directed by Gerasimowicz, began to provide direct financial

support to SMC using their own funds. Between October 2008 and September 2011, when SMC filed for bankruptcy, Gerasimowicz and MAM provided over $2 million to SMC. (SEC Trial Exs. 142, 143, 169.) Gerasimowicz claims that he never documented these transactions as loans to SMC or formalized any repayment terms. (WG Tx. at 118.) There is no record that either Gerasimowicz or MAM ever disclosed their more than $2 million investment in SMC to the Meditron Fund or to any Fund investor.

As SMC's financial condition deteriorated and with its access to operating capital depleted, Gerasimowicz and MMG turned to a new funding source – the Meditron Fund – to meet SMC's funding needs, and to safeguard against the loss of Gerasimowicz's personal investment in SMC. Between September 2009 and September 2011, Gerasimowicz directed 43 separate transfers of assets from the Fund's bank and brokerage accounts, totaling over $2.7 million, either to SMC or directly to SMC's creditors in order to provide SMC with working capital. (*See* SEC Trial Ex. 149.) In order to obtain the money to make these transfers, Gerasimowicz sold publicly-traded, liquid securities held by the Meditron Fund.[2]

Between September 2009 and June 2010, Gerasimowicz, MMG and MAM directed six separate transfers, totaling $1.025 million, from the Meditron Fund's brokerage account at Goldman to SMC. (SEC Trial Exs. 102, 149.) In the letters of authorization, Gerasimowicz represented to Goldman that the monies represented the purchase of the following securities:

- World Trade Center Memorial Development Bond, 12% Coupon;
- Erasmus High School Bond at 9%;
- Brooklyn High School Bond at 9%; and

[2] For example, in September 2009, Gerasimowicz sold 4,900 shares of Altria Group, Inc. for a total of $91,113, and 8,600 shares of U.S. Bancorp Depositary Shares for $195,707. In December 2009, prior to transferring $185,000 to SMC, Gerasimowicz sold 16,200 shares of Conseco Inc. (now CNO Financial Group, Inc.) for $81,298; 1,100 shares of Bristol-Myers Squibb Company for $28,233; and 2,500 shares of eBay Inc. for $55,986.

- Brooklyn PS 225K Bond at 8%

Gerasimowicz directed Goldman to record these alleged "bonds" as private equity investments valued at cost.[3] The letters of authorization failed to specify the issuer of the "bonds," although several of the letters of authorization specifically list SMC as the recipient of the funds (the others list MREP, which subsequently transferred the funds to SMC). (SEC Trial Exs. 18, 20, 21, 23, 25.) The $1.025 million transferred from the Meditron Fund's Goldman account, together with the Fund's 2007 $200,000 investment in SMC through MREP, represented approximately 29% of the Fund's assets as of June 30, 2010. In return, the Meditron Fund received four promissory notes issued by SMC (the "Notes").[4] The Notes have interest rates ranging from 6% to 12%, and require no interest or principal payments until the end of their five-year terms. (SEC Trial Exs. 17, 22, 24, 26.)

Between September 2010 and September 2011, Gerasimowicz, MMG and MAM directed 37 additional transfers of Meditron Fund assets, totaling approximately $1.7 million, to SMC or to its creditors. In November 2010 alone, Gerasimowicz directed seven separate transfers totaling $487,000 from the Meditron Fund's Schwab account to the Fund's Bank of America account. (*See* SEC Trial Ex. 149.) From that bank account, Gerasimowicz almost simultaneously transferred the funds either to SMC's bank accounts or directly to SMC's creditors. (*Id.*) Gerasimowicz claimed during testimony that SMC executed promissory notes for at least some of these transfers, but has produced no documentation to support that assertion.

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[3] The Fund's SMC position does not appear to be reflected in the custodian account statements sent to MAM and the Fund. (SEC Trial Exs. 102, 103.)

[4] The Notes were not always executed contemporaneously with the transfers from the Meditron Fund. For example, Gerasimowicz directed a $315,000 transfer from the Fund to SMC on September 21, 2009, followed by a $185,000 transfer on December 21, 2009, and SMC issued the first Note – for $500,000 – in December 2009. Similarly, Gerasimowicz directed a $50,000 transfer to SMC on March 29, 2010, followed by a $175,000 transfer on June 4, 2010, and SMC issued a $225,000 Note on June 6, 2010.

(WG Tx. at 222-23, 252-53.) In total, between 2009 and 2011, Respondents misappropriated over $2.7 million from the Meditron Fund to support SMC, representing approximately 80% of the Fund's investment portfolio as of December 31, 2011.[5]

Neither Gerasimowicz nor MAM took any steps to protect the Meditron Fund's interests in the SMC-related transactions. It appears that in connection with the Fund's investment in SMC, the adviser never performed the type of disciplined, quantitative-based investment selection strategy that was promised in the PPM. Moreover, neither Gerasimowicz nor MAM vetted whether the terms obtained by the Fund were "no less favorable than those the [Fund] could obtain from unrelated third parties" as required by the Fund's Operating Agreement. (Op. Agmt. at 18-19.)

Gerasimowicz testified that he set the interest rates on the Notes "at a premium to lower risk bonding rates that were in existence at the time," the implication being that the Notes were a good investment for the Meditron Fund. However, Gerasimowicz acknowledged that third-party lenders were unwilling to issue loans at any rate to SMC unless Gerasimowicz agreed to personally guarantee repayment. (WG Tx. at 191-94.) Furthermore, when SMC did manage to obtain a short-term loan for $190,000 from a friend of Gerasimowicz in February 2009, the firm paid an annualized rate of approximately 60%, significantly more than the 6%-12% range that Gerasimowicz unilaterally set for the Fund's Notes. (WG Tx. at 128-130; SEC Trial Ex. 12.) To date, SMC has made no payments on the Notes, the first of which comes due in December 2014. Given SMC's bankruptcy filing, and the fact that substantial secured and other creditor claims

[5] SMC's September 2011 bankruptcy filing lists the Meditron Fund as a creditor holding an unsecured, nonpriority claim of $2.5 million. (SEC Trial Exs. 142, 143.)

take priority over the Fund's claims, the Notes, as well as the Fund's subsequent undocumented investments in SMC, are likely now essentially worthless.[6]

Furthermore, the record at trial will demonstrate that Gerasimowicz repeatedly directed that payment be made to himself, in round dollar increments, as "reimbursement" for expenses incurred on behalf of SMC. (*See* WG Tx. at 269; Ex. 36.) Gerasimowicz also transferred funds from MREP to himself. (*See* WG Tx. at 75.) No such "reimbursements" were made to the Meditron Fund.

IV.

RESPONDENTS' LIES AND OMISSIONS TO INVESTORS

Between 2009 and 2011, MAM, MMG and Gerasimowicz made material misstatements and omissions about the Fund's investment strategy, risk, liquidity and portfolio composition. The Respondents also made material misstatements and omissions about the Fund's valuation of the SMC holdings. Finally, Gerasimowicz and MAM failed to disclose their $2 million investment in SMC, which gave rise to a material conflict of interest.

1. Misrepresentations and Omissions By Respondents Regarding Use of Fund Assets to Sustain SMC's Operations

Between 2009 through 2011, Respondents issued "Quarterly[7] Communiques," authored by Gerasimowicz, to Meditron Fund investors which contained false or misleading information, or material omissions, about the increased risk, illiquidity, and concentration of the Fund's portfolio resulting primarily from the Fund's undisclosed SMC investment. Specifically, the Quarterly Communiques repeatedly represented to Fund investors that:

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[6] According to SMC's bankruptcy financials, SMC's net worth is negative and the business is insolvent with liabilities of between $8-$10 million and net assets of approximately $6-$7 million (as that figure includes accounts receivable, SMC's actual net assets are likely to be considerably less than that).

[7] Notwithstanding their titles, these distributions came out on a roughly quarterly basis, although at times up to six months would pass between issues.

- "The majority of assets currently comprise between 1%-3% of the total portfolio on an individual basis. Thus the Fund is well-diversified both in terms of individual position as well as across market sectors." (SEC Trial Exs. 66 at 2 (Dec. 2009); 67 at 2 (June 2010); 30 at 2 (June 2011).)

- "We continue to manage the portfolio in a very vigilant and disciplined manner so that downside risk is minimized" (SEC Trial Ex. 66 at 1.)

- "[T]he [Fund's] risk remains lower than that of the overall marketplace." (SEC Trial Exs. 66 at 2; 67 at 2; 30 at 2; 160 at 3.)

- "[W]hile invested in equity markets, we maintain risk levels associated with bonds." (SEC Trial Exs. 66 at 2; 67 at 2; 30 at 2; 160 at 3.)

Respondents purported to disclose in each Quarterly Communique a listing of the Fund's "Top Ten Long Portfolio Positions." None of these disclosed positions ever represented more than 5% of the overall portfolio. Respondents never included the Fund's SMC position in the "Top Ten" list, even as the Fund's exposure to SMC steadily grew to approximately 18% by January 2010, 29% by June 2010, 48% by March 2011, and 80% by December 31, 2011. (SEC Trial Exs. 30, 66, 67.) Despite the Fund's rapidly increasing and concentrated SMC position, and SMC's deteriorating financial condition, the Quarterly Communiques never mentioned SMC.[8]

MMG represented in the Fund's PPM that the Fund maintained "a diversified portfolio of long and short positions," employed "controlled risk diversification" of investments, and hedged positions to reduce market risk and volatility. (PPM at 4-5.) Although the PPM was originally issued in 2003, several years before the Fund first invested in SMC, investors continued to

[8] Even after testifying in the SEC investigation, Gerasimowicz failed to disclose the Fund's SMC position in the September 30, 2011 "Top Ten" list, but instead merely changed the title to read "Top Ten Long ***Public Equity*** Portfolio Positions." (SEC Trial Ex. 160 at 4 (emphasis supplied).) Gerasimowicz similarly revised the September 30, 2011 Quarterly Communique to state that the "majority of the ***publically-traded*** assets currently comprise between 1%-3% of the total portfolio on an individual basis," yet continued to assert that "the Fund is well-diversified both in terms of individual position as well as across market sectors." (SEC Trial Ex. 160 at 2 (emphasis supplied).)

purchase membership interests in the Fund after the Respondents began diverting Fund assets to SMC, and Respondents continued to provide this same PPM to potential investors. (SEC Trial Exs. 89 at 12-13; 179 (PPM provided to investor in 2010).) Contrary to these disclosures, Respondents proceeded to invest approximately 80% of the Fund's assets in SMC by the end of 2011. Respondents failed to disclose the fundamental change in the Fund's investment strategy, which was investing the majority of its assets in a failing private company with relatively little liquidity that depended on regular infusions from the Fund to finance its operations and ultimately filed for bankruptcy. Nor, at any time, did Respondents inform investors that Gerasimowicz himself had a substantial investment in SMC, an undisclosed and direct conflict of interest, since that debt could never have been repaid (and he would have suffered an immediate, personal economic loss) had Fund assets not been diverted to sustain SMC.

The evidence presented at the hearing in this matter will demonstrate that Gerasimowicz failed to adequately inform Meditron Fund investors about the Fund's investment in SMC. Testimony will establish that Gerasimowicz either misrepresented or omitted to disclose material information regarding the Fund's investment strategy or its SMC position during his discussions with investors. Investors will testify that they would have found it material if the Fund had invested a substantial percentage of its assets in a private company because it would call into question both the strategy and the valuation of the Fund, given the lack of market for such an investment. Investors also will testify that they expected that the Quarterly Communiques would disclose the Fund's largest investments, whether public or private. Investors will further describe how Respondents rebuffed their attempts to redeem their membership interests with a series of ever more flimsy excuses.

The Meditron Fund's annual audited financial statements contain the only written

disclosures concerning the Fund's investments in both MREP and in SMC. However, Fund investors either received these financial statements late or not at all.[9] The Fund's auditor, Joseph Amundsen, did not issue the audit opinions on the Fund's 2008, 2009 and 2010 financial statements until, respectively, August 2010, March 2011 and December 2011. (SEC Trial Exs. 10, 36, 38.) Thus, Fund investors received no written disclosures concerning the 2010 transfers and the Fund's rapidly increasing SMC position (40% of portfolio as of 2010 year-end) until December 2011 at the earliest, by which time the Fund in fact was approximately 80% invested in SMC. There do not appear to be any written disclosures made to investors concerning the 2011 transfers to SMC.[10] Furthermore, investors will testify that they never received the 2010 audited financial statements, or, in the case of some investors, that they never received audited financial statements at all, and thus received no disclosures regarding the Fund's SMC investment. Nor did Respondents disclose that Amundsen, the Fund's auditor, had been subject to disciplinary proceedings and barred from appearing or practicing before the Commission.

Moreover, the 2010 financial statements, for which the auditor's opinion was issued on December 7, 2011, failed to disclose SMC's September 2011 bankruptcy filing. Amundsen testified that Gerasimowicz did not disclose SMC's bankruptcy in his December 7, 2011

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[9] Joseph Amundsen audited the Fund's 2008, 2009, and 2010 financial statements. He is a certified public accountant and has been registered with the Public Company Accounting Oversight Board since March 2009. In 1983, Amundsen was permanently barred from appearing or practicing before the Commission, and in November 2011, the Commission initiated a contempt proceeding against Amundsen for violating the terms of the injunction by repeatedly auditing the financial statements of broker-dealers that were registered with the Commission. *SEC v. Joseph S. Amundsen*, No. 83-cv-00711 (N.D. Cal. Nov. 9, 2011). (SEC Trial Exs. 146, 147.) The Court ordered Amundsen to comply with the 1983 injunction, and clarified that this meant he could not audit broker-dealers or prepare any document to be filed with the Commission, but did not actually hold Amundsen in contempt as the Court seemed sympathetic to Amundsen's pleas for leniency and arguments that a contempt citation would cause him to lose his CPA licenses and as a result, go bankrupt. (SEC Trial Ex. 148.)

[10] Amundsen testified he was retained in April 2011 to audit the Fund's 2010 financial statements, and that the audit opinion was not issued until December 2011 because of Gerasimowicz's health problems, delays in receiving information from the Fund's tax preparer, and disagreements concerning the accounting for one particular $100,000 SMC note. (SEC Trial Ex. 3, Testimony of Joseph Amundsen ("Amundsen Tx.") at 28.) Amundsen testified he was not retained to conduct the 2011 audit. (*Id.* at 18.)

management representation letter provided in connection with Amundsen's audit of the Fund's 2010 financial statements. Amundsen further testified that SMC's bankruptcy was clearly material and should have been disclosed in the "subsequent events" note. (Amundsen Tx. at 10, 38, 70; *see also* Amundsen Tx. at 40 ("My gut feeling, ... is that the fair market value of the Fund – of the assets would be zero.").)

2. Misrepresentations and Omissions Regarding Respondents' Valuation of the Fund's SMC Holdings

Gerasimowicz conceded in his testimony that, notwithstanding SMC's significant deterioration and its inability to find financing in the open market, the Meditron Fund held its SMC investments at cost. (WG Tx. at 47, 143-44, 162, 176-77, 231-34.) In the absence of market prices, the PPM requires the Fund manager to value the Fund's investments based on prices "reasonably assigned by the Manager." (PPM at 9-10.) The notes to the Fund's audited financial statements represented that the Fund followed a fair value methodology (pursuant to ASC 820) to value its investments.[11] (SEC Trial Exs. 10, 36, 38.) The financial statements disclose that the Fund's interests in SMC were all categorized as Level 3, defined in the notes as investments with "prices or valuations that require inputs that are both significant to the fair value measurement and are unobservable." (*Id.*) The financial statements provide no additional detail concerning the valuation methodology applied to the Fund's SMC interests. Respondents rendered these disclosures false and misleading by failing to disclose that they never performed any valuation to value the Fund's SMC interests, nor did they "reasonably assign" a valuation to the SMC interests as provided in the PPM. Amundsen, for example, testified that no valuation analysis was performed on the Fund's SMC investments. (Amundsen Tx. at 32.)

As SMC's financial condition worsened over 2010 and 2011, and the company assumed

[11] FASB Accounting Standards Codification, Fair Value Measurements and Disclosures (ASC 820).

increasing levels of debt, culminating in its September 2011 bankruptcy filing, Respondents had no reasonable basis for continuing to value the Fund's unsecured SMC position at cost. By omitting material information about the SMC bankruptcy from the 2010 audited financial statements, and by continuing to value SMC at cost in calculating the net asset values provided to investors in their quarterly Fund summary evaluation statements, Respondents deprived investors of information about a material event that impaired a significant asset of the Fund and rendered the disclosures about the valuation of the SMC investment false and misleading. (SEC Trial Ex 36; *see, e.g.,* SEC Trial Exs. 176, 177.) As discussed above, Respondents continued to take management fees from the Fund based on the inflated NAV. (SEC Trial Ex. 103, 104.)

3. Misrepresentations and Omissions Regarding Gerasimowicz's and MAM's Personal Investment in SMC

As described above, Gerasimowicz and MAM invested more than $2 million of their own funds in SMC from October 2008 through September 2011. However, at no time during this three-year period did they disclose their personal SMC investment, or the potential and actual conflicts of interest posed thereby. Nor did they disclose that Gerasimowicz authorized numerous disbursements to himself from SMC without documented justification. (*See* WG Tx. at 132, 273-74.)

4. Respondents' False Statements Concerning AUM

MAM's Form ADV, filed March 30, 2010 (SEC Trial Ex. 95 at 8), represented that the adviser had $1 billion in AUM. MAM's subsequent Forms ADV filed on March 31, 2011 and March 24, 2012 both claimed that MAM had $50 million in AUM. (SEC Trial Exs. 96 at 8; 97 at 11.)

Notwithstanding this correction, Respondents continued to claim the far higher figure in communications to investors. Gerasimowicz himself misrepresented MAM's AUM in articles he

wrote for *Worth Magazine*, which advertises itself as a wealth management magazine for high net worth individuals. Gerasimowicz authored fourteen separate magazine articles, dating from Spring 2009 to November 2011, each of which list MAM's AUM at $1.1 billion. (SEC Trial Ex. 137.) These articles were made available on Respondents' website during all relevant times, and were distributed to investors by Respondents as well. Investors will testify as to their receipt of these materials, and their materiality to their investment decisions.

V.

RESPONDENTS' CREATION OF AN AURA OF RESPECTABILITY THROUGH A FRAUDULENT MEDIA CAMPAIGN

Gerasimowicz has promoted himself and his businesses through various media outlets. In addition to authoring articles for *Worth Magazine* from 2009 through September 2012, Gerasimowicz has hosted a weekly radio show, "*The Matter of Money Matters*," on New York-based WOR 710 AM. (See SEC Trial Exs. 121 (listing radio shows), 122 (listing print articles), 137 (Worth articles).)[12]

The evidence to be adduced at trial will show that *Worth* launched its Leading Wealth Advisor Program in late 2008, after being acquired by a new publisher. The purpose of the program was to create a special insert for each issue highlighting, by region, various investment advisers that would pay approximately $30,000 annually to be so showcased. In order to identify advisers appropriate for inclusion, *Worth* decided internally to apply a cut-off of $100M AUM.

Although the Leading Wealth Advisor Program was a form of paid advertising, *Worth* took some care to ascertain the credentials of those advisers included. They required advisers to

[12] What was never disclosed to any investors was that, rather than being independently selected, Gerasimowicz and the other Respondents paid for that privilege. For example, Respondents paid approximately $7,900 per month to host a weekly show on WOR 710 AM, and approximately $2,000 per month for publication in *Worth*. (SEC Trial Exs. 124, 126, 128, 149 (reflecting payments from MAM bank account to WOR Radio between 2010 and 2012).)

submit a detailed questionnaire, and hired an outside service to conduct due diligence on candidates. Respondents filled out the profile questionnaire, in which they represented that they had $1.1 billion of AUM.[13] (SEC Trial Ex. 125 at 7.) When *Worth*'s due diligence consultant investigated, he identified a conflict between that claim and MAM's 2008 Form ADV, which disclosed only $420 million in AUM. When *Worth* raised this discrepancy with Gerasimowicz, he claimed that assets had grown to $1.1 billion in the last year, and that the 2009 Form ADV would reflect the higher AUM. While the due diligence expert questioned how it was possible for a firm to more than double its AUM in one of the worst markets in history, *Worth* accepted Respondents' oral assertion as to his AUM. (SEC Trial Ex. 126.)

Consequently, starting with *Worth*'s first 2009 issue, Respondents were included in the Leading Wealth Advisor Program, and Gerasimowicz authored articles available both in print and via *Worth's* website. (SEC Trial Ex. 137.) Each article listed MAM's AUM at $1.1 billion. These articles were sent to Respondents' clients, as were complimentary *Worth* magazine subscriptions.

Additional issues arose in October 2011 regarding Respondents' AUM. A spot check by *Worth* revealed that Respondents had reported $50 million AUM on their March 2011 Form ADV, yet were still reporting $1.1 billion AUM to *Worth.* (SEC Trial Exs. 96 at 8, 129, 137.) When *Worth* asked their outside due diligence firm to look into this discrepancy, they reported back that there were various disparities between the reported figures, and that further investigation was warranted. (SEC Trial Exs. 129, 130, 131.) *Worth* then decided to give Respondents a chance to correct the disparity, emailing Gerasimowicz to request current AUM

[13] Ironically, in light of the later "investment" in SMC, when asked to identify a "pull quote" for the feature on him, Gerasimowicz wrote that one "must identify securities that are positioned to thrive … The companies must be uniquely positioned, have good prospects, show a competitive advantage and demonstrate continued earnings growth, high cash flow, and an excellent balance sheet unencumbered by debt." (SEC Trial Ex. 125 at 8.)

information and noting that "If your current AUM is at variance with your most recent ADV, please provide an explanation. (Our vetting partner, Investor Watchdog, reviews AUM data annually.)" (SEC Trial Ex. 132 at 3.)

Respondents ignored the inquiry. *Worth* resent the original email, and emphasized that "We are in need of any edits and an updated AUM for Meditron, with 'as of' date, for your Dec/Jan issue profile." Gerasimowicz responded that "AUM remains the same." *Worth* then pointed out that the reported AUM did not reflect the publicly available data, and asked for clarification as to the variance. Again, Gerasimowicz ignored the request, necessitating yet another follow-up in which *Worth* stressed "We do need an answer regarding your AUM today," and suggested that "If you need additional time, we would like to suggest using "Confidential" for the Dec/Jan issue." Gerasimowicz finally replied, "Please use confidential for now." (SEC Trial Ex. 132.)

Concerned, *Worth* set up a Google alert to track information about Respondents. When that Alert indicated that the current action had been filed, *Worth* immediately unpublished all of Respondents' articles from the *Worth* website, removed them from the Leading Wealth Advisor Program, and, via counsel, directed Respondents to remove all references to *Worth* from his website. (SEC Trial Exs. 133, 135.)

VI.

LEGAL ANALYSIS

A. Respondents Violated Section 10(b) and Rule 10b-5 of the Exchange Act and Section 17(a) of the Securities Act

To establish a violation of Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934 ("Exchange Act"), the Commission must show that Respondents: (1) made a misrepresentation or omission of material fact [Rule 10b-5(b)], or used a fraudulent device

[Rules 10b-5(a) and (c)]; (2) with scienter; (3) in connection with the purchase or sale of securities. *See, e.g., SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999).

A manipulative or deceptive fraud occurs "in connection with the purchase or sale of any security" when the fraud and the securities transaction are part of the same fraudulent scheme. *SEC v. Zandford*, 535 U.S. 813, 825 (2002); *United States v. O'Hagan*, 521 U.S. 642, 655-656 (1997). For purposes of Rule 10b-5(b), the "maker" of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. *Janus Capital Group, Inc. v. First Deriv. Traders*, 131 S. Ct. 2296 (2011); *In re Optimal U.S. Litig.*, 2011 WL 4908745, at *2 (S.D.N.Y. Oct. 14, 2011). A fact is material if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision. *Basic, Inc. v. Levinson*, 485 U.S. 224, 231 (1988); *SEC v. DiBella*, 587 F.3d 553, 565 (2d Cir. 2009). Scienter is a "mental state embracing intent to deceive, manipulate, or defraud." *VanCook v. SEC*, 2011 WL 3437663, at *7 (2d Cir. Aug. 8, 2011). Proof of reckless conduct or motive and opportunity to commit fraud establishes scienter. *SEC v. Aragon Capital Advisors, LLC*, 2011 WL 3278907, at *11 (S.D.N.Y. July 26, 2011). Courts impute the scienter of corporate directors, officers and employees to the entity for purposes of establishing the entity's primary liability. *See SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1089 n.3 (2d Cir. 1972).

Sections 17(a)(1), (2) and (3) of the Securities Act of 1933 ("Securities Act") prohibit similar conduct in the offer or sale of securities, except that subsection (2) – the counterpart to Rule 10b-5(b) – does not require attribution to a statement's "maker." *See SEC v. Stoker*, 865 F. Supp.2d 457, 464-65 (S.D.N.Y. 2012) (defendant liable under Section 17(a)(2) if he obtains money or property by use of a false statement, whether prepared by himself or by another).

Section 17(a)(2) of the Securities Act prohibits any person engaged in the offer or sale of securities from "directly or indirectly" obtaining money or property "by means of any untrue statement of a material fact or any omission to state a material fact." To establish liability under Section 17(a)(2), the Commission need only show that a respondent was "sufficiently responsible for the statement – in effect, caused the statement to be made – and knew or had reason to know that the statement would be disseminated to investors." *SEC v. KPMG LLP*, 412 F. Supp. 2d 349, 375 (S.D.N.Y. 2006); *see also Stoker*, 865 F. Supp.2d at 464 (requiring a showing only that defendant obtained money or property by use of a false statement, rather than the higher *KPMG* standard). Scienter is not an element of Sections 17(a)(2) or (3). *SEC v. Kelly*, 765 F. Supp. 2d 301, 319 (S.D.N.Y. 2011).

In addition, "[f]or the purpose of rule 10(b)-5, an investment adviser is a fiduciary and therefore has an affirmative duty of utmost good faith to avoid misleading clients. This duty includes ***disclosure of all material facts and all possible conflicts of interest***." *Laird v. Integrated Resources, Inc.*, 897 F.2d 826, 835 (5th Cir. 1990) (*citing SEC v. Blavin*, 760 F.2d 706 (6th Cir. 1985) (emphasis supplied)). It has long been the rule that if an investment adviser "chooses to assume a role in which she is motivated by conflicting interests" that she must make full disclosure. *In the Matter of Arleen W. Hughes*, Exchange Act Release No. 4048, 1948 WL 29537, at *6 (Feb. 18, 1948) (Commission opinion affirming the finding of willful violations of, among other provisions, Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder) (cited with approval in *In the Matter of Marc N. Geman*, Exchange Act Release No. 43963, 2001 WL 124847 (Feb. 14, 2001), *aff'd*, *Geman v. SEC*, 334 F.3d 1183 (10th Cir. 2003)).

1. Liability for Material Misrepresentations and Omissions

Gerasimowicz, MAM and MMG are liable for violations of Section 10(b) and Rule 10b-5(b) thereunder for materially misstating and omitting material information in PPMs concerning the Meditron Fund's investment strategy in connection with the purchase and sale of Meditron Fund membership interests by investors after the Fund began deviating from its stated strategy. Respondents solicited investors in the Meditron Fund by creating and disseminating PPMs that misrepresented the Fund's investment strategy. Instead of disclosing to those investors who purchased membership interests after the Fund began investing in SMC that the Meditron Fund had changed its investment strategy, the offering documents describe the Fund as maintaining a diversified portfolio of long and short positions and using hedges to reduce market risk. But these statements were false – Gerasimowicz, MAM and MMG instead took over $2.7 million from the Meditron Fund to make concentrated, illiquid investments in SMC. *See, e.g., In the Matter of Gualario & Co., LLC and Ronald Gualario*, Release No. 452, 2012 WL 627198 (Feb. 14, 2012) (investment adviser's failure to disclose radical change from conservative to high-risk trading strategy violated antifraud provisions); *see also SEC v. Scott,* 565 F. Supp. 1513, 1526-27 (S.D.N.Y. 1983), *aff'd sub nom, SEC v. Cayman Island Reinsurance Corp., Ltd.,* 734 F. 22 118 (2d Cir. 1984) (investment outside scope of prospectus constitutes fraud).

In addition to his control of MAM and MMG, Gerasimowicz made oral representations to investors, and continued to market and offer interests in the Fund to prospective investors after he began diverting Fund assets to SMC.

These misstatements and omissions of fact are material. Investors continued to invest in the Fund after Respondents began funneling Fund assets into SMC. These investors would have considered it important to know that the Meditron Fund's investment adviser departed from its

well-diversified, hedged investing strategy and in fact, by December 31, 2011, had concentrated approximately 80% of the Fund's portfolio in illiquid investments in a single financially-challenged private company, which filed Chapter 11 bankruptcy in September 2011. These investors also would have considered it important to know that the investment adviser was not making disinterested investment decisions for the Meditron Fund and that Gerasimowicz and MAM had their own substantial financial interests in SMC. False statements and omissions about a fund's use of proceeds, investment model, objectives, strategies, and risks are material because they concern the fundamental nature, safety and profitability of the investment. *SEC v. Research Automation Corp.*, 585 F.2d 31, 35-36 (2d Cir. 1978); *SEC v. Championship Sports Mgmt., Inc.*, 599 F. Supp. 527, 532-33 (S.D.N.Y. 1984).

Nor did Respondents disclose the material facts regarding the significant conflicts of interest regarding their diversion of Fund assets to SMC. Among these material omissions are the facts that:

- Gerasimowicz himself was owed millions of dollars by SMC, which he stood to lose unless SMC was propped up by additional infusions of capital;
- Gerasimowicz had personally diverted funds from SMC's cash flow without proper or, in fact, any documentation; and
- Gerasimowicz had directed numerous purported "investments" in SMC not to SMC, but to its creditors. (*See* SEC Trial Exs. 105, 149.)

Gerasimowicz knew the representations concerning the Fund's investment strategy were false because he controlled the Fund's bank and brokerage accounts, made all investment decisions on behalf of the Fund and personally directed each transfer of Meditron Fund assets to SMC or its creditors. Gerasimowicz also knew, or was reckless in not knowing, that Meditron Fund investors were unaware of the Fund's radical change in investment strategy, its significant position in SMC and Gerasimowicz and MAM's own SMC investments. The misrepresentations

and omissions of material fact Gerasimowicz made in connection with the purchase and sale of the Meditron Fund membership interests to investors demonstrate he acted with the highest degree of scienter required for primary liability under Section 10(b) of the Exchange Act and Rule 10b-5(b). Since entities can only act through their agents, Gerasimowicz's scienter is properly imputed to MAM and MMG, the entities over which he exercised sole control, for purposes of those entities' primary violations of the same provisions. *See Manor Nursing*, 458 F.2d at 1089 n.3; *In re Sunbeam*, 89 F. Supp. 2d 1326, 1340 (S.D. Fla. 1999).

2. Liability For Engaging In A Fraudulent Scheme

Furthermore, Respondents are primarily liable under Section 10(b) of the Exchange Act, Rules 10b-5(a) and (c) thereunder, and Sections 17(a)(1) and (3) of the Securities Act for altering the Fund's investment strategy and misappropriating and misusing over $2.7 million of Fund assets to invest in SMC. *See SEC v. Boock*, 2011 WL 3792819, at **22-23 (S.D.N.Y. Aug. 25, 2011) (scheme liability extends to misappropriated assets). The facts above describe the timing and circumstances of the misappropriations. Gerasimowicz, MAM and MMG used deceptive acts to conceal their theft, including issuing Quarterly Communiques to investors that misrepresented the Fund's holdings, diversification, and investment strategy. *See Zandford*, 535 U.S. at 820-21 (misappropriation of client asset constitutes scheme to defraud).

In addition, beginning in September 2009, Gerasimowicz, MAM and MMG engaged in a manipulative and deceptive course of business by altering the Fund's stated investment strategy and investing the Fund's money in SMC. Investors in the Meditron Fund who purchased membership interests after September 2009 had an expectation that the Fund's investment adviser was following the stated investment strategy and was not misusing the Fund's assets. The Fund's offering documents depict it as diversified and hedged. Gerasimowicz, MAM and

MMG, however, drastically deviated from the Fund's disclosed strategy and instead invested the majority of the Fund's assets in SMC, thereby defrauding investors of the investment choice they believed they were making. As discussed above, Gerasimowicz acted with scienter and his scienter is properly imputed to MAM and MMG, the entities over which he exercised sole control. Accordingly, Gerasimowicz, MAM and MMG violated Rules 10b-5(a) and (c) and Sections 17(a)(1) and (3).

B. Gerasimowicz Aided and Abetted and Caused MAM's And MMG's Violations of Section 10(b) and Rule 10b-5 of the Exchange Act and Section 17(a) of the Securities Act

Gerasimowicz is liable for aiding and abetting and causing MAM's and MMG's violations of Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder, and Section 17(a) of the Securities Act. Aiding and abetting liability requires proof of three elements: (1) a securities law violation by a primary wrongdoer; (2) knowledge of the violation by the person sought to be charged; and (3) proof that the person sought to be charged substantially assisted in the primary wrongdoing. *Armstrong v. McAlpin*, 699 F.2d 79, 91 (2d Cir. 1983).

Where, as here, the alleged aider and abettor is a fiduciary, a showing of recklessness is sufficient to establish liability. *Id.* According to the Second Circuit's recent decision in *SEC v. Apuzzo*, "to satisfy the 'substantial assistance' component of aiding and abetting, the SEC need only show that the defendant 'in some sort associate[d] himself with the venture, that he participate[d] in it as in something that he wishe[d] to bring about, [and] that he [sought] by his action to make it succeed.'" *SEC v. Apuzzo*, 689 F.3d 204, 206 (2d Cir. 2012) (citation omitted). A finding that a person aided and abetted a violation necessarily makes the person a cause of that violation. *See In re Zion Capital Mgmt. LLC*, Exchange Act Release No. 48904, 2003 WL 22926822 (Jan. 29, 2003). MMG and MAM violated the federal securities laws by using PPMs

containing materially misleading information about the Fund's investment strategy to solicit investors who purchased membership interests after the Fund began investing in SMC. Gerasimowicz, as the sole owner of both MMG and MAM, knew that the PPMs contained material misleading statements and provided substantial assistance to MMG and MAM in soliciting investors.

C. MAM, Gerasimowicz and MMG Violated the Antifraud Provisions of the Advisers Act

1. Respondents Violated Sections 206(1) and (2) of the Advisers Act

Section 206(1) of the Investment Advisers Act of 1940 ("Advisers Act") prohibits any investment adviser from, directly or indirectly, employing any device, scheme, or artifice to defraud any client or prospective client. Section 206(2) of the Advisers Act prohibits any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client. Conduct that violates the antifraud provisions of the Exchange Act, when done by an investment adviser to his or her clients, also violates Sections 206(1) and 206(2) of the Advisers Act. *SEC v. Haligiannis*, 470 F. Supp. 2d 373, 383 (S.D.N.Y. 2007). Scienter is required for a violation of Section 206(1), but not for Section 206(2). *See Steadman v. SEC*, 603 F.2d 1126, 1134 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981). When dealing with investment pools, the adviser's client is only the fund and not the investors in the fund. *Goldstein v. SEC*, 451 F.3d 873, 883-84 (D.C. Cir. 2006).

As fiduciaries, investment advisers have an affirmative duty of utmost good faith, full and fair disclosure of all material facts and an obligation to employ reasonable care to avoid misleading clients. *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963) ("Congress has recognized investment adviser[s] to be [fiduciaries] . . . . Courts have imposed on a fiduciary the affirmative duty of 'utmost good faith, and full and fair disclosure of all material

facts,' as well as an affirmative obligation 'to employ reasonable care and to avoid misleading' his clients.") (citations omitted). In particular, an investment adviser has a duty under Section 206 to disclose to clients all material information concerning potential or actual conflicts of interest which might incline the adviser consciously or unconsciously to render advice which is not disinterested. *Id.* at 191-92. This fiduciary duty requires investment advisers to act for the benefit of their clients, and precludes them from using their clients' assets to benefit themselves. *In re Performance Analytics, Inc.*, Release No. 2036, 2002 WL 1308305, at *3 (June 17, 2002) (settled action) (*citing In the Matter of Kingsley, Jennison, McNulty & Morse, Inc.*, Release No. 24, 1991 WL 288369, at *11 (Nov. 14, 1991) (litigated proceeding)); *see also SEC v. Mannion*, 789 F. Supp. 2d 1321, 1341 (N.D. Ga. 2011) ("the Advisers Act obligates [investment advisers] to act for the benefit of the Fund rather than diverting Fund assets for personal use.")

Gerasimowicz, MAM and MMG violated Sections 206(1) and (2) by intentionally misappropriating and misusing Fund assets to invest in SMC. Misappropriation or misuse of fund assets constitutes a fraud on the fund in violation of Sections 206(1) and 206(2). *See, e.g., SEC v. Lloyd V. Barriger*, Release No. 21968, 2011 WL 1825038 (May 13, 2011) (charging adviser with Sections 206(1) and (2) violations based upon misuse of fund assets) (consent judgment entered Dec. 2011); *SEC v. Alero Odell Mack, Jr., et al.*, Release No. 21731, 2010 WL 4388290 (Nov. 4, 2010) (same) (default judgment entered May 2011 against entity adviser, consent judgment entered March 2012 against individual adviser).

Respondents deviated dramatically from the Fund's stated investment strategy by investing over $2.7 million – approximately 80% of the Fund's total assets as of December 2011 – in SMC. These investments clearly benefited SMC, as well as Gerasimowicz and MAM (which had a significant economic interest in SMC), while providing the Meditron Fund with a

concentrated, undiversified, and illiquid position in a struggling company that ultimately filed for bankruptcy. In addition, they misstated the Fund's NAV by keeping the Fund's investment in SMC at cost, despite SMC's deteriorating financial condition and eventual bankruptcy. By taking management fees based on inflated Fund NAV, Gerasimowicz, MAM and MMG also misappropriated Fund assets in violation of Sections 206(1) and (2). Furthermore, MAM and Gerasimowicz defrauded MAM's pre-existing advisory clients who invested in the Meditron Fund by failing to disclose not only their conflicts of interest but also the dramatic deviations from the Fund's stated investment strategy and valuation processes.

Gerasimowicz, MAM and MMG's misuse of the Meditron Fund's money and change in investment strategy were material. Their clients – the Fund and those MAM advisory clients who invested in the Fund – or any other reasonable investor in their positions would consider it material that their money was being misused by their investment adviser. The Meditron Fund was hijacked by its investment adviser and turned into SMC's piggy bank. It was also material to the Fund that Gerasimowicz was making investment decisions for the Meditron Fund based on his relationship with and interest in SMC. *See SEC v. Gabelli*, 653 F.3d 49, 57-58 (2d Cir. 2011). Gerasimowicz – and by extension, MAM and MMG – were at least reckless in abandoning the Fund's disclosed investment strategy and were making investment decisions that were not in the best interests of the Meditron Fund or of those MAM advisory clients invested in the Fund. Gerasimowicz may be charged with direct violations of the Advisers Act's antifraud provisions because he meets the definition of an investment adviser.[14]

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[14] *See In the Matter of John J. Kenny and Nicholson/Kenny Capital Management, Inc.*, Exchange Act Release No. 47847, 2003 WL 21078085, at *17 n.54 and accompanying text (May 14, 2003) (litigated proceeding) (associated person may be charged as primary violator under Section 206 where he/she meets the definition of an investment adviser, for example, where adviser is an alter ego of or controlled by the associated person) (*citing SEC v. Berger*, 244 F. Supp. 2d 180, 192-93 (S.D.N.Y. 2001) (finding associated person liable under Sections 206(1) and (2) based on control of investment adviser)).

Finally, Respondents violated the Advisers Act by distributing Quarterly Communiques to investors that purported to list the Fund's largest holdings, while omitting any reference to its investments in SMC. *See Valicenti Advisory Services, Inc. v. SEC,* 198 F.3d 62 (2d Cir. 1999) (distribution to investors of chart that omitted performance of portion of adviser's account violated Sections 206(1), (2), and (4), as well as the advertising rule, 206(4)-1(a)(5)).

2. Respondents Violated Section 206(4) of the Advisers Act and Rule 206(4)-8

Section 206(4) of the Advisers Act prohibits an investment adviser from, directly or indirectly, engaging in any deceptive act, practice, or course of business. Rule 206(4)-8(a)(1) prohibits an investment adviser to "pooled investment vehicles" – such as hedge funds – from making an untrue statement of material fact or omitting to state a material fact necessary to make the statements made not misleading to investors or prospective investors in those pools. Rule 206(4)-8(a)(2) provides that it is a fraudulent practice for an investment adviser to a pooled vehicle to engage in "fraudulent, deceptive, or manipulative" conduct with respect to any investor or prospective investor in a pooled investment vehicle. *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles,* Release No. 2628, 2007 WL 2239114 (Aug. 3, 2007).[15] Scienter is not required – negligent conduct is sufficient. Pooled investment vehicles include hedge funds, private equity funds, and other types of offered pools that invest in securities. *Id.* As noted above, MAM, Gerasimowicz and MMG made investment decisions on behalf of the Meditron Fund – a pooled investment vehicle – for a fee, and thus each is considered an investment adviser to the Fund.

MAM, Gerasimowicz and MMG violated Section 206(4) and Rule 206(4)-8(a)(1) and (a)(2) thereunder. As discussed above, Respondents defrauded Fund investors by changing the

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[15] With the exception of the Fund's initial $200,000 investment in MREP in 2007, which is not at issue here, all of the Fund's investments in SMC occurred after September 10, 2007 – the effective date of Rule 206(4)-8.

fundamental nature of the Meditron Fund without disclosure, as well as by siphoning off Fund assets to SMC. Gerasimowicz, MAM and MMG represented to investors – both in writing and in discussions – that the Meditron Fund was well-diversified and low risk. MMG similarly represented in the Fund's PPM that the Fund maintained "a diversified portfolio of long and short positions," employed "controlled risk diversification" of investments, and hedged positions to reduce market risk and volatility. However, through the SMC investments, Respondents radically changed the Fund's strategy to invest the majority of its assets in a failing private company with relatively little liquidity that ultimately filed for bankruptcy. Given Gerasimowicz's representations to investors regarding the Fund's strategy, his failure to disclose the fundamental change in the nature and strategy of the Meditron Fund was fraudulent. *See In the Matter of Gualario & Co.*, 2012 WL 627198 (investment adviser's failure to disclose radical change from conservative to high-risk trading strategy violated antifraud provisions).

The change in the Meditron Fund's investment strategy was also deceptive and manipulative. The change in investment strategy was not disclosed to investors until December 2011 at the earliest, when the 2010 audited financial statements finally were completed, by which time the Fund already was approximately 80% invested in SMC and SMC had filed for bankruptcy, a material fact which was not disclosed in the audited financial statements. Investors also will testify, however, that they never received those audited financial statements. Gerasimowicz, MMG and MAM also failed to disclose to investors that they caused the Fund to invest in a company in which they had a significant economic interest based on their own sizeable investments in SMC. Finally, the *Worth Magazine* articles sent to investors and linked to on the Meditron website falsely reported that MAM had $1 billion in AUM.

Gerasimowicz acted with scienter. As the sole owner of MAM and MMG, he was

responsible for all aspects of the Meditron Fund and had sole investment authority. He caused the Fund to invest over $2.7 million in SMC. He knew that he told investors the Fund employed a diversified, hedged strategy and thus that investing most of the Fund's assets in SMC was an undisclosed and significant change of investment strategy.

Additionally, Gerasimowicz is liable for aiding and abetting and causing MAM's and MMG's violations of Section 206(4) and Rule 206(4)-8 thereunder. As sole owner of MAM and MMG, he substantially assisted them in abandoning the disclosed investment strategy and concentrating the Fund's portfolio in SMC.

D. MAM Violated, and Gerasimowicz Aided, Abetted and Caused MAM's Violations of, the Advisers Act Custody and Advertising Rules

MAM violated, and Gerasimowicz aided, abetted, and caused MAM's violations of, Advisers Act Section 206(4) and Rules 206(4)-1 and 206(4)-2 thereunder.

1. Rule 206(4)-2 (custody rule)

Rule 206(4)-2 of the Advisers Act requires registered investment advisers with custody of client funds or securities to adequately safeguard those assets by implementing specific procedures. Rule 206(4)-2 was amended, effective March 12, 2010, and thus the custody violations discussed here span both the old custody rule (in effect from 2003 until March 2010) and the amended rule. Under amended Rule 206(4)-2(d)(2)(iii), an adviser has custody if it acts in any capacity, including as managing member of a limited liability company, that gives the adviser or its supervised person legal ownership of or access to client funds or securities. An adviser with custody of client funds or securities violates Section 206(4) and amended Rule 206(4)-2 thereunder unless a qualified custodian maintains those funds and securities; the custodian sends quarterly account statements to each member of the limited liability company; and the adviser is subject to an annual surprise examination by an independent public accountant.

Rule 206(4)-2(a)(1), (3), (4), (5). The same requirements applied under the "old" rule, except that either the qualified custodian or the adviser could issue the quarterly account statements to investors. Under both the "old" and amended rules, advisers with custody of the assets of pooled investment vehicles are exempt from the requirement to distribute quarterly account statements and undergo an annual surprise examination *if* the pooled investment vehicle distributes annual, audited financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") to pool investors within 120 days of fiscal year end. Rule 206(4)-2(b)(4).

MAM and Gerasimowicz had access to client funds or securities because as the managing member and investment adviser of the pooled investment vehicle, they had the authority to withdraw funds from the pooled vehicle's accounts. Therefore, they are deemed to have had custody of Fund assets for purposes of Rule 206(4)-2. Investors received quarterly statements from Gerasimowicz and MAM, rather than from the qualified custodian, and MAM was never subject to a surprise exam. Accordingly, MAM failed to comply with the requirements of either the amended or the old Rule 206(4)-2(a). Nor did MAM use the alternative audit approach to comply with the custody rule because, although the Fund was audited annually, the audited financials were not distributed in a timely manner, and the 2010 audited financials were not GAAP-compliant because they failed to disclose the material subsequent event of the SMC bankruptcy.

The Meditron Fund's 2008 audited financial statements were not completed until August 1, 2010. The Fund's 2009 audited financial statements were not completed until March 31, 2011, and its 2010 audited financial statements were not completed until December 7, 2011, all well beyond the 120 days required under the custody rule. As Meditron Fund investors did not receive GAAP-compliant, audited financial statements for 2008 through 2010 within the required

120 days, if at all, MAM cannot rely on the exemption afforded to pooled investment vehicles under either amended Rule 206(4)-2(b)(4) or the old custody rule. As a result of this conduct, MAM violated Section 206(4) and Rule 206(4)-2 and Gerasimowicz, who exercised sole control over MAM and the Fund and bore responsibility for obtaining and distributing the Fund's audited financials to Fund investors, aided, abetted and caused MAM's violations.

2. Rule 206(4)-1 (advertising rule)

Rule 206(4)-1(a)(5) prohibits any registered investment adviser, directly or indirectly, from publishing, circulating or distributing "any advertisement . . . which contains any untrue statement of a material fact, or which is otherwise false or misleading." Proof of scienter is not required to establish a violation of Section 206(4). *See SEC v. Steadman*, 967 F.2d 636, 647 (D.C. Cir. 1992). Rule 206(4)-1(b) broadly defines an "advertisement" to include any written communication addressed to more than one person that offers any investment advisory service with regard to securities." Material that promotes investment advisory services for the purposes of inducing potential clients to subscribe to those services is an advertisement covered by the rule. *SEC v. C.R. Richmond & Co.*, 565 F.2d 1101, 1105 (9th Cir. 1977).

The MAM website contains links to numerous *Worth Magazine* articles written by Gerasimowicz, dating from April 2009 to November 2011, which materially misrepresented MAM's AUM at $1.1 billion. These articles constituted "advertisements" within the meaning of Rule 206(4)-1(b). *See In the Matter of Delta Global Advisors, Inc.,* Exchange Act Release No. 65356, 2011 WL 4364106 (Sept. 20, 2011) (settled order finding Section 206(4) and Rule 206(4)-1 violations where adviser provided links on its website to third-party articles that overstated firm's assets under management); *In the Matter of Nevis Capital Management, LLC,* Release No. 2214, 2004 WL 236571 (Feb. 9, 2004) (same); *see also In the Matter of Isaac*

Sofair, Release No. 2245, 2004 WL 1238258 (June 4, 2004) (settled order finding Section 206(4) and Rule 206(4)-1 violations where brochures overstated firm's assets under management). By publishing these materially misleading articles on its website, MAM violated Section 206(4) and Rule 206(4)-1(a)(5) thereunder. Furthermore, these articles were distributed to investors in the Fund.

Gerasimowicz substantially assisted and caused MAM's violation because he knowingly authored these articles and linked to them on MAM's website to promote the firm, and distributed them to Fund investors. He did not remove the articles even after reporting only $50 million in AUM in MAM's March 2011 Form ADV filing. In fact, *Worth Magazine* articles were still accessible on MAM's website until *Worth* directed Respondents to remove them in September 2012. Accordingly, Gerasimowicz aided, abetted and caused MAM's violations of Section 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) thereunder.

VII.

RELIEF SOUGHT

The assessment of whether a particular sanction recommended by the Division is in the public interest is derived from the Court's analysis in *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981), which includes the following elements: (1) the egregiousness of the defendant's actions; (2) the isolated or recurrent nature of the infraction; (3) the degree of scienter involved; (4) the sincerity of the defendant's assurances against future violations; (5) the defendant's recognition of the wrongful nature of his or her conduct; and (6) the likelihood that the defendant's occupation will present opportunities for future violations. In addition, the Commission has listed three additional factors to be considered in making the public interest determination concerning sanctions: (1) the age of the violation;

(2) the degree of harm to investors and the marketplace as a result of the violations (*see In the Matter of Marshall E. Melton, et al.*, Release No. 2151, 2003 WL 21729839, at *2 (July 25, 2003)); and (3) the "extent to which the sanction will have a deterrent effect" (*see McCarthy v. SEC*, 406 F.3d 179, 189 (2d Cir. 2005); *see also Schield Management Co. and Marshall L. Schield*, Exchange Act Release No. 53201, 2006 WL 231642, at *8 (Jan. 31, 2006)). Based on these factors, this Court should impose the sanctions against Respondents that are recommended below on account of the violations complained of herein.

A. <u>A Cease and Desist Order Should Issue</u>

Section 21C of the Exchange Act (15 U.S.C. § 78u-3), Section 8A of the Securities Act (15 U.S.C. § 77h-1), and Section 203(k) of the Advisers Act (15 U.S.C. § 80b-3(k)), authorizes the Commission to order any person to cease and desist from violating, or causing any future violation of, any securities law or rule that the person has been found to have violated. *In the Matter of Rita J. McConville*, Exchange Act Release No. 51950, 2005 WL 1560276, at *15 (June 30, 2005). *See* 15 U.S.C. §§ 77h-1, 78u-2; 15 U.S.C. § 80b-3(i). In considering whether to impose a cease-and-desist order, a Court should consider the Steadman factors discussed above. *See In the Matter of Herbert Moskowitz*, Exchange Act Release No. 45609, 2002 WL 434524, at *8 (March 21, 2002). In addition, although some risk of future violations is necessary, it need not be very great to warrant issuing a cease-and-desist order. *See In the Matter of KPMG Peat Marwick, LLP*, Exchange Act Release No. 43862, 2001 WL 47245, at *24 (Jan. 19, 2001), *recon. denied*, Exchange Act Release No. 44050, 2001 WL 223378, at *6-7 (Mar. 8, 2001), *petition for review denied, KPMG, LLP v. SEC*, 289 F.3d 109 (D.C. Cir. May 14, 2002) *rehearing en banc denied*, (July 16, 2002). Absent evidence to the contrary, a finding of past violations raises a significant risk of future violation. *See id.*

While the Commission will only impose a cease-and-desist order where it determines that there is some risk of future violation, the risk of future violations required to support a cease-and-desist order "is significantly less than that required for an injunction." *Id.* at *15 n.66. *See also In the Matter of Fuller*, Exchange Act Release No. 48406, 2003 WL 22016309, *9 (Aug. 25, 2003) ("risk [of future violations] . . . need not be very great").

A cease and desist order is appropriate here because Respondents' violations were egregious, recurrent, and extremely harmful to investors. Respondents' *scienter* here is not even a close issue. They deliberately chose not to reveal information that investors will testify would have been highly material to them. They deliberately and significantly misstated the liquidity of their highly illiquid holdings. Their conduct persisted over the entire relevant period, and caused substantial harm to investors and their clients.

When called to account for their misconduct, moreover, their response was to refuse to accept responsibility for their own acts, and lay it at the feet of others. *See, e.g.*, Respondents' Wells Submission, at 7 (blaming investor losses on a "fraud committed by SMC's previous owners and employees" and on "intentional and deliberate acts by" these persons). A cease-and-desist order is appropriate in this case as it "will serve the remedial purpose of encouraging [Respondents] to take [their] responsibilities more seriously in the future." *McConville*, 2005 WL 1560276, at *16.

B. <u>Disgorgement</u>

The Court enjoys broad equitable power to order Respondents to disgorge the profits from their illegal activities. First Jersey Sec.'s Litig., 101 F.3d 1450, 1474 (2d Cir. 1996). "The effective enforcement of the federal securities laws requires that the SEC be able to make violations unprofitable. The deterrent effect of an SEC enforcement action would be greatly

undermined if securities law violators were not required to disgorge illicit profits." Id. The primary purpose of disgorgement is to deprive violators of their ill-gotten gains, thereby maintaining the deterrent effect of the federal securities laws. Id. The amount of disgorgement ordered "need only be a reasonable approximation of profits causally connected to the violation," and "any risk of uncertainty [in calculating disgorgement] should fall on the wrongdoer whose illegal conduct created the uncertainty." Id. at 1475 (citations omitted). *See also In the Matter of John A. Carley*, Exchange Act Release No. 57246, 2008 WL 268598, *24 (Jan. 31, 2008) (citations omitted); *In the Matter* of *Thomas C. Bridge*, Exchange Act Release No. 60736, 2009 WL 3100582, at *23-24 (Sept. 29, 2009) ("The disgorged amount must be causally connected to the violation, but it need not be figured with exactitude.").

Once the Division establishes that its disgorgement figure reasonably approximates the amount of unjust enrichment, the burden of going forward shifts to the respondent, who is then obliged clearly to demonstrate that the disgorgement figure was not a reasonable approximation. *John A. Carley,* 2008 WL 268598, at *104 (quotation omitted). Where disgorgement cannot be exact, any risk of uncertainty should fall on the wrongdoer whose illegal conduct created that uncertainty. *Id.* (quotation omitted).

Here, Respondents should disgorge the proceeds they received from the Fund, which were obtained by false pretenses. These consist of the following:

- Funds diverted from the Meditron Fund to SMC between approximately September 2009 and September 2011, totaling over $2.7 million;
- Management, performance and other fees paid to Respondents by the Meditron Fund between approximately September 2009 through the present, totaling approximately $895,000; and
- Funds paid to Respondents by SMC between approximately September 2009 through the present, in amounts to be established at hearing.

An award of prejudgment interest (and the rate used) is within the discretion of the Court, and is appropriate here. See First Jersey Secs. Litig., 101 F.3d at 1476.

C. Civil Penalties

Section 8A(g) of the Securities Act, [15 U.S.C. § 77h-1(g)], Section 21B of the Exchange Act [15 U.S.C. § 78u-2], and Section 203(i) of the Advisers Act [15 U.S.C. § 80b-3(i)] authorize the Commission to seek civil penalties in administrative proceedings, not to exceed $130,000 against an individual defendant, and $650,000 against entities, per act or omission for violations occurring after February 14, 2005, and $150,000 against individual defendants, and $725,000 against entities, per act or omission for violations occurring after March 3, 2009. *See* 17 C.F.R §§ 201.1003, 201.1004 (adjusting penalties for inflation).

These provisions permit the Court to impose civil monetary penalties that fall into one of three tiers, which increase with the seriousness of the violation. "Civil penalties are designed to punish the violator and deter future violations of the securities laws." SEC v. Opulentica, LLC, 479 F. Supp. 2d 319, 331 (S.D.N.Y. 2007). "Disgorgement alone is an insufficient remedy, since there is little deterrent in a rule that allows a violator to keep the profits if [he] is not detected, and requires only a return of ill-gotten gains if [he] is caught." *Id.* at 331-32 (citation omitted).

The Division respectfully requests that the Court order Respondents to pay civil penalties on account of their misconduct as follows. Respondents should be ordered to pay a Third Tier penalty for their willful violation of Section 17(a) of the Securities Act. Section 8A(g) of the Securities Act [15 U.S.C. § 77h-1(g)] authorizes the Commission to impose a civil penalty upon a finding, with notice and opportunity for a hearing, that any person or entity is violating or has violated any provision, rule or regulation issued under the Securities Act and that such penalty is

in the public interest. A Third Tier penalty of a maximum amount of $150,000 for each such act or omission may be imposed against a natural person (and $725,000 for an entity) if:

> (i) The act or omission ...(1) involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; and
>
> (ii) Such act or omission directly or indirectly resulted in
>
> > (I) Substantial losses or created a significant risk of substantial losses to other persons; or
> >
> > (II) Substantial pecuniary gain to the person who committed the act or omission.

Respondents should also be ordered to pay similar Third Tier penalties on account of their willful violations of the Exchange Act. Section 21B of the Exchange Act provides that civil penalties may be imposed in any proceeding instituted pursuant to Section 15(b)(4) of the Exchange Act on any person who has willfully violated the federal securities laws.

Respondents should also be ordered to pay a Third Tier penalty on account of their violation of Sections 206(1), 206(2) and 206(4) of the Advisers Act and Rules 206(4)-1, 206(4)-2 and 206(4)-8 thereunder. Section 203(i) of the Advisers Act authorizes the Commission to impose a civil penalty against any person upon a finding, with notice and opportunity for a hearing, that such penalty is in the public interest and that has willfully violated any provision of the Securities Act, the Exchange Act or subchapter II of the Advisers Act or the rules or regulations thereunder. The criteria for imposing a Third Tier penalty under Section 203(i) of the Advisers Act are the same as the criteria for imposing a Third Tier penalty under Section 8A(g) of the Securities Act and Section 21B of the Exchange Act as quoted above. *See* 15 U.S.C. § 203(i)(2)(C)(i), (ii).

Third Tier penalties for Respondents' violations of Section 17(a) of the Securities Act, Section 15(a) of the Exchange Act and Sections 206(1) and 206(2) of the Advisers Act are in the

public interest because these violations created a significant risk of substantial losses to other persons. In accordance with *Steadman v. SEC*, Third Tier penalties are also in the public interest in order to deter Respondents or other persons from perpetrating prime bank securities frauds in the future. Furthermore, Respondents have not provided assurances that they will not continue or repeat their violations of the securities laws. (*See, e.g.*, Respondents' Answer, at 12 ("Dr. Gerasimowicz contributed significant personal funds on an ongoing basis to aid . . . [SMC and to], help it overcome the financial difficulties that arose from the fraud of Mr. Doumazios").

D. Industry Bars

Exchange Act Section 15(b)(6)(A), as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, authorizes bars from association with a "broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization." 15 U.S.C. § 78o(b)(6)(A). The same holds true for Advisers Act Sections 203(e)(5) and 203(f).

The Commission has long held that "the fact that a person has been enjoined from violating the antifraud provisions has especially serious implications for the public interest." *See In the Matter of Harold F. Harris et. al.*, Release No. 286, 2005 WL 1307739, at *6 (June 1, 2005). The existence of such an injunction may indicate that it is in the public interest to bar respondents from participation in the securities industry. *See id.*

The Commission treats violations occurring within the context of fiduciary relations with particular seriousness and due regard for the relationship of trust and confidence. *In the Matter of James C. Dawson*, Release No.3057, 2010 WL 2886183, at *3 n.16 (2010); *In the Matter of Don Warner Reinhard*, Exchange Act Release No. 63720, 2011 WL 121451, at *6 n.27 (Jan. 14, 2011) ("[T]he importance of honesty for a securities professional is so paramount that we have

barred individuals even when the conviction was based on dishonest conduct unrelated to securities transactions or the securities business").

The Commission has long held that there is a presumption that prior misconduct may provide the basis for inferring that the risk of probable future misconduct is sufficient to exclude respondents from the securities industry. *See In the Matter of Arthur Lipper Corp.*, Exchange Act Release No. 11773, 1975 WL 163472, at *16 (Oct. 24, 1975); *see also In the Matter of Robert W. Armstrong, III*, Release No. 248, 2004 WL 737067, at *16 (Apr. 6, 2004) ("In the ordinary case and absent evidence to the contrary, a finding of past violation raises a risk of future violation."). This is true even where respondents claim that they will not commit any future violations. *See In the Matter of Castle Securities Corp.*, Release No. 244, 2004 WL 115193, at *11 (Jan. 23, 2004) (inferring that, as a result of past misconduct, respondents remained "a threat to commit future misconduct, in spite of their assurances to the contrary.").

CONCLUSION

The Division of Enforcement will demonstrate, by clear, unambiguous, and overwhelming evidence, that Respondents committed numerous violations of the Securities, Exchange, and Advisers Acts. Consequently, the Division requests that the Court make findings of fact with regard to the misconduct discussed above and impose the sanctions requested.

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New York, New York

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