UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15526

In the Matter of

AMBASSADOR CAPITAL
MANAGEMENT, LLC

and

DEREK H. OGLESBY,

Respondents.

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THE DIVISION OF ENFORCEMENT'S POST-HEARING BRIEF

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I. INTRODUCTION

Respondents Ambassador Capital Management, LLC ("ACM") and Derek Oglesby failed in two of their two most important responsibilities as investment advisers to the Ambassador Money Market Fund ("AMMF" or "the Fund").

First, the Division of Enforcement has offered substantial evidence that Respondents failed to comply with three separate, risk-limiting provisions of Rule 2a-7 under the Investment Company Act. These include the requirement to make and document minimal credit risk determinations for each of the Fund's investments; the requirement to ensure that all of the Fund's investments were made within the 5% issuer diversification limit; and the requirement to conduct the Fund's first, official stress test on a timely basis and in the manner specified by the Rule. By failing to adhere to Rule 2a-7, the Respondents forfeited the Fund's right to identify and market itself as a money market fund, and violated the investment policies of the Fund's municipal investors, who were drawn to the Fund precisely because it was a money market fund, and would have pulled their investments if they had known that the Fund was not in compliance with the Rule.

Second, the Division has offered compelling evidence that the Respondents made false and misleading statements about the Fund's compliance problems, and their investment strategies, to the Fund's Board of Trustees. These misrepresentations included statements by Mr. Oglesby about the Fund's exposure to risky Eurozone investments during the summer and fall of 2011; as well as statements by someone from ACM, either Mr. Oglesby or Mr. Prost regarding the number of investments which had grown to over 5% of the Fund's assets on September 30, 2011. By failing to provide complete and accurate information to the Fund's Board of Trustees, the Respondents deprived them of information which they needed to carry out their own responsibilities under Rule 2a-7.

Finally, the Division has introduced evidence sufficient to show Respondents' motivations for disregarding the requirements of Rule 2a-7 in making investment decisions for the Fund. Based on the evidentiary record, the Court reasonably may conclude that Respondents wanted to maximize the yield on the Fund's investments in order to gain additional clients, which would increase their fees, and to achieve a minimum yield of 2 basis points, which would avoid the need to waive any fees or expenses.

Although the hearing in this matter lasted more than seven days, there are only a few genuine factual disputes about the evidence. Most of the disputes between the parties concern the legal conclusions to be drawn from the evidence. Accordingly, in this brief the Division will simply provide the Court with a summary of the evidence, and present its arguments for holding Respondents liable.

The Commission cannot allow firms and professionals that advise money market funds, like Respondents, to treat their responsibilities in such a cavalier manner. Accordingly, Respondents should be found liable for all of the violations charged in the November 26, 2013 Order Instituting Proceedings, ordered to cease-and-desist from future violations, ordered to pay disgorgement and a significant civil penalty, and be subject to an associational bar.

II. THE UNDISPUTED FACTS

A. <u>The Development of Rule 2a-7</u>

The Commission's 1983 adopting release stated that the provisions of Rule 2a-7 "provide for a special system of safeguards to protect the fund." (Ex. 158 at ¶ 2) One such provision specified that money market funds may only invest in instruments determined to present minimal credit risk. (Tr. 52:5-53:23; Ex. 158 at ¶ 2) A fund's board was responsible for designing and effectuating these safeguards. (Tr. 55:16-57:4; Ex. 158 at ¶ 3) However, the board was permitted to delegate duties and functions to the investment adviser, including the responsibility to determine the quality of portfolio instruments. (Tr. 74:5-14; Ex. 158 at ¶¶ 3-4) But the fund was required to "record, maintain, and preserve" a written record in the meeting minutes of the board's "considerations and actions taken in connection with the discharge of its responsibilities". (Tr. 60:10-61:24; Ex. 158 at ¶ 5)

The rule expressly requires that a minimal credit risk determination be based "on factors pertaining to credit quality *in addition to* any rating assigned to such securities by a Designated NRSRO) and that are at the time of Acquisition Eligible Securities." Rule 2a-7(c)(3)(emphasis supplied).

In 1991, the provisions of Rule 2a-7 were tightened in response to developments in the commercial paper market. (Tr. 50:2-61:24; Ex. 158 at ¶ 8) These amendments limited money market fund investments to no more than 5% per non-government issuer – with a three-day safe harbor of up to 25% for a single security. (Ex. 158 at ¶ 10) The 1991 amendments also prohibited mutual funds from holding themselves out as "money market funds" unless they complied with all of Rule 2a-7's risk limiting conditions. (*Id.* at ¶ 11)

In 1997, the Commission imposed a new record-keeping requirement on money market funds regarding "minimal credit risk" determination. David Joire testified that this requirement, proposed in 1993, became necessary because of the Commission Staff's experience during examinations that "[s]ome funds lacked adequate records to document their analysis and, thus, the Commission could not confirm that these funds had complied with the rule." (Tr. at 59:12 – 62:13; Ex. 158 at Ex. 6 thereto at 68604) Accordingly, money market funds now are required to maintain "[f]or a period of not less than three years from the date that the credit risks of a portfolio security were most recently reviewed, a written record of the determination that a portfolio security presents minimal credit risks..." Rule 2a-7(c)(11)(iii).

In 2010, the Commission adopted a number of additional amendments to Rule 2a-7 in response to the difficulties encountered by money market funds during market events that occurred during 2007-2008. (Ex. 158 at ¶ 13) One new requirement was that money market fund boards adopt procedures for periodic stress testing of the fund's ability to maintain a stable net asset value per share based upon specific hypothetical events. (Tr. 67:22-24; Ex. 158 at ¶ 17) These hypothetical events included: (a) a change in short-term interest rates; (b) an increase in shareholder redemptions; (c) a downgrade of or default on portfolio securities; and (d) the widening or narrowing of spreads between yields on an appropriate benchmark selected by the fund for overnight interest rates and commercial paper and other types of securities held by the fund. *Id.*

B. Money Market Funds Are Subject to Unique Risks

Money market funds differ from other mutual funds in critical respects. (Ex. 112 at 5) A money market fund is permitted to use a fixed $1 share price, which affords investors a safe, short-term investment vehicle. However, money market funds are required to comply with Rule 2a-7's risk-limiting provisions, including minimal credit risk determination, issuer diversification and portfolio stress testing, which are all designed to ensure that money market fund investors always can redeem shares for the full $1 share value on demand.

In money market funds, there is invariably a maturity and liquidity mismatch between a fund's assets and liabilities. (*Id.* at 6) During times of economic stress, however, the mismatch between a money market fund's assets and liabilities can cause unique challenges. *Id.* In a major stress event, money market investors are likely to redeem *en masse*, akin to a bank run, with liquidation of assets at "fire-sale prices" further impairing the value of the remaining assets. (*Id.* at 7) If a fund "breaks the buck," the risks dramatically increase that certain investors will be disadvantaged by earlier redemptions. In addition, such an event can lead to a run on other money market funds, pricing down all money market instruments, and damaging the entire financial system. (*Id.* at 7-8)

The money market fund crisis of 2008 demonstrates how a downward spiral can quickly spread from one money market fund, infecting others. As Professor Russell Wermers noted, one day after Lehman Brother's collapse, the Reserve Primary Fund disclosed that it had broken the buck. (Ex. 112 at 8) In the wake of that announcement, many other money market funds began experiencing vast outflows of investment capital, which ultimately totaled over $300 billion in redemptions. *Id.* As credit markets began seizing up, money market funds struggled to sell securities to meet such redemptions. *Id.* The U.S. Treasury was required to intervene and offer guarantee programs in an effort to stabilize money market funds and other short-term, fixed-income investments. (*Id.*) This credit crisis became the impetus behind the 2010 amendments to Rule 2a-7. (*Id.* at 9)

C. The Ambassador Money Market Fund

Respondent ACM is an investment adviser focused largely on fixed income investments, and between 2009 and 2012 managed approximately $1 billion in assets, including the Ambassador Money Market Fund and other separately managed investments. (Ex. 46 at 5; Ex. 135 at 3) Derek Oglesby was a research analyst, a co-portfolio manager, and eventually the sole portfolio manager for the Ambassador Fund. (May 2, 2014 Joint Stipulation of Facts at ¶ 3)

The Ambassador Money Market Fund was created in 2000, as another investment option for ACM's current advisory clients. ACM served as the Fund's investment adviser from 2000 until the Fund's liquidation in 2012. (May 2, 2014 Joint Stipulation of Facts at ¶ 6) The Fund invested almost exclusively in commercial paper, or asset backed commercial paper, of varying maturity periods. (*Id.* at ¶ 8) Most of the investors in the Fund were Michigan municipalities and other Michigan public entities that used the Fund for a variety of cash flow purposes, including payroll. (May 2, 2014 Joint Stipulation of Facts at ¶¶ 1, 9)

Respondents ACM and Oglesby were fiduciaries to the Fund and its Board of Trustees. As such, they owed to the Fund and its Trustees an affirmative duty of utmost good faith and full disclosure of all material facts. According to the organizational documents of the Fund, the Board delegated a portion of its responsibilities for complying with Rule 2a-7 to ACM, and required ACM to report back to it regarding any violation of the Rule. (*See* Ex. 25 at 20; Tr. 288-296) Service providers like Bisys and Fund Services Group, or FSG, were hired by contract approved by the Board to assist ACM in its compliance functions, because the Board could only delegate compliance responsibilities to an investment advisor. (Tr. 296-297, 299-300)

Conrad Koski, the Chairman of the Fund's Board of Trustees for nearly 10 years, testified that he and the other original Board members were very focused on compliance issues. (Tr. 286:11-16; 325-326) According to Mr. Koski, ACM owed the Fund and its Trustees a duty of a complete and accurate disclosure of the Fund's compliance problems and challenges. (Tr. 302:8-303:10; 328:19-329:15; 345:13-346:23) Both John Guy and Marlene Hodges, who became members of the Board of Trustees in 2010, agreed with Mr. Koski about the importance of compliance issues to the Trustees. (Tr. 436:22-437:14, 530:25-532:3) And all three trustees testified that they would have wanted to know whether the Fund was complying with its own maturity restrictions and whether any of the Fund's investments constituted either active or passive breaches of the 5% issuer diversification limit. (Tr. 345:13-346:23; 463:5-465:20; 466:5-468:13; 531:16-532-3; 537:23-538-10)

D. *<u>The Fund's Investors</u>*

The Fund was designed in order to be marketed to Michigan municipalities, and was tailored to reflect their investment restrictions. (Tr. 291:21-292:3, 1468:8-20; Ex. 25 at 7) The vast majority of the investors in the Fund were Michigan municipalities. (Tr. 308:23-309:6, 636:14-18, 1428:1-3) These included the City of Detroit, Washtenaw County, the City of Flint, Kalamazoo County, Kent County, and the City of Rochester Hills. (Ex. 46 at SP-AMBASSADOR0000111)

The Court heard testimony from treasurers of two municipalities: Kenneth Parrish of Kent County and Kurt Dawson of the City of Rochester Hills. The funds that these municipalities placed with AMMF through ACM included those used to support an array of local services – including law enforcement, fire services, court systems, public health, local transportation hubs, public works, water, libraries, and roads. (Tr. 364:17-365:3, 396:12-20) These municipalities were concerned with safety, liquidity, and yield – in that order – also known as the "SLY Principle." (Tr. 372:14-373-4, 399:2-17, 309:7-24)

Unlike most other investors in money market funds, Michigan municipalities are required to comply with Michigan Public Act 20, which restricts investment by municipalities (directly or *via* a mutual fund) to certain instruments, including government securities, certificates of deposit, and certain kinds of commercial paper. (Tr. 366:2-14) Although Rule 2a-7 permits investment in both "first tier" and "second tier" commercial paper, Public Act 20 only permits investment in "first tier" paper. (*Id.*) Respondent Oglesby was aware of this fact. (Tr. 1429:2-1430-1) Moreover

Public Act 20 also restricts commercial paper to investments with a maturity length of 270 days or fewer, not the 397 days permitted under Rule 2a-7. (Tr. 366:25-367:9)

Besides the requirements of Public Act 20, both treasurers also testified that the investment policies of their municipalities only permitted them to invest in mutual funds which maintained a stable $1 per share value – *i.e.* money market funds. (Tr. 370:1-9, 400:19-401:12) In fact, this policy is common among Michigan municipalities. (Tr. 374:5-16) Respondent ACM was made aware of this policy; both treasurers testified that they provided copies of their respective investment policies to ACM prior to investment. (Tr. 376:1-16, 401:13-402:1) ACM then provided the municipalities with a signed acknowledgement of receipt of their investment policies and ACM's intention to comply with them. (Tr. 376:4-11, 401:13-20)

The Treasurers were unequivocal that if Ambassador no longer called their fund a money market fund and had let their share price float, they would have been required to withdraw all of their funds pursuant to their investment policies. (Tr. 380:16-25, 403:22-404-11)

E. ***Declining Fee Income Motivated Respondents to Accept Additional Risks***

According to the minutes of the May 2010 meeting of the Board of Trustees, ACM's Brian Jeffries noted that the Fund's assets had been declining since the prior Fall. (Ex. 30 at 25 (internal p. C-1-2.1)) Jeffries reported that current assets under management were about $190 million, which was down from the Fund's highest level of $550 million. (*Id.;* Tr. 340:18-342:25; 1505:21-1508:15.) Jeffries advised the Trustees that the reduction in the Fund's assets caused a decline in ACM's fee income, which already had forced the adviser to reduce compensation and cut expenses significantly. (Ex. 30 at 25 (internal p. C-1-2.1))

During this Trustee meeting, Jeffries presented two projections based upon different portfolio scenarios – one at $200 million and a worst-case scenario of $150 million. (*Id.* at 27 (internal p. C-1-2.3)) The analysis revealed that at $150 million, the Fund's viability was imperiled – with a projected spike in the Fund's effective expense ratio and a projected *negative* yield to investors. (*Id.* at 134 (internal p. C-11-1)) Accordingly, Jeffries vowed that ACM would return a minimum annualized yield of at least 2 basis points for the Fund's investors, even if that meant waiving fees and expenses. *(Id.* at 27-28 (internal p. C-1-2.3 to C-1-2/4))

The evidence shows that to meet this goal, Respondents were increasingly willing to take on additional risk in order to increase returns. In such a low interest-rate environment, Respondents had to purchase and repurchase the same few profitable securities repeatedly, and in some cases hold them for long periods of time, in order to obtain the desired yield.

F. By the Fall of 2011, the Fund Had a High Tolerance for Investment Risk.

Marita Bartolini led the Commission's compliance examination of AMMF and ACM beginning in November 2011. According to Ms. Bartolini, one of the motivations for the exam was that, at the end of September 2011, during the Eurozone crisis, the Fund was the only money market fund in the entire country holding the commercial paper of Dexia Delaware, Arabella Finance, Romulus Finance and ENI Finance. (Tr. 118:5-119:21, 124:6-125:7; 130:20-131:23)

Dexia was a security supported by a troubled Belgian bank. (Tr. 129:13-130:2; 168:24-25; 180:23-25) Arabella and Romulus were Italian issuers, and ENI was partially owned by the Italian government. (Tr. 130:3-19; 1692:5-7) The Fund also had invested in certain other securities that were exposed to Eurozone risk, including commercial paper issued by Compass Funding, which was related to a German bank, and AGC Capital. (Tr. 131:24-132:9) Finally, 11 of the Fund's 28 holdings were larger than 5% of Fund's net assets, and one of these holdings, Natexis, was over 7% of the Fund's assets. (Ex. 100; Tr. 171:22-24)

These were not occasional purchases. For the eight Eurozone securities which initially were of concern to the Commission's examiners, Respondents had caused the Fund to purchase securities from those issuers 235 times between August and October 2011. (*See* Ex. 173A; Tr. 209-211) In addition, Respondents had caused the Fund to purchase nine other Eurozone securities 184 times during the same period of time. (Ex. 173B; Tr. 211-213) And even after the compliance exam, Respondents caused the Fund to purchase twelve Eurozone securities a total of 161 times in November and December of 2011.[1] (Ex. 173C)

Based on the identity and number of these Eurozone holdings, Ms. Bartolini concluded that ACM was making investment decisions which exposed the Fund to unusual and unnecessary risks of default or a downgrade, in order to secure higher yields. (Tr. 118:5-120:23)

III. THE EVIDENTIARY RECORD ON DISPUTED ISSUES

A. ***Respondents Made Misrepresentations to the Fund's Trustees Regarding Eurozone Investments.***

In June 2011, domestic money market funds found themselves affected by an unfolding financial crisis which originated in European or "Eurozone" countries. The crisis began when Standard & Poor's downgraded Greek sovereign debt to a rating of "CCC." (Div. Ex. 112 at 19) The global economy's reaction was dramatic, and adversely impacted the flow of capital. (*Id.*)

As this crisis unfolded, Derek Oglesby and Greg Prost participated in the August 8, 2011 meeting of the Fund's Board of Trustees as representatives of ACM. According to the meeting minutes, Oglesby spoke and assured the Trustees that "ACM is avoiding Greece, Spain, Italy and other countries seen as higher-risk investments by ACM." (Ex. 98 at 3)

Oglesby claims that he did not make this statement, explaining "it wouldn't have made any sense" because it was not true. (Tr. 1222:7-20) Oglesby also claims that he doesn't think Greg

[1] The Commission's compliance examiners also noted that ACM repeatedly had caused the Fund to hold some of these same securities longer than ACM's internal maturity restrictions. (Ex. 174C; Tr. 213-215)

Prost made that statement either. (Tr. 1223:11-16) Greg Prost at first testified that he had no recollection of the meeting (Tr. 1667:18-25), but when asked by his attorney whether the minutes accurately reflected what Oglesby said, he answered "I don't see how it could be" – because it was not true. (Tr. 1670:1-13) Based on these vague denials, Respondents contend that the minutes must be inaccurate on this point.[2] Neither Jeffries, Prost, nor anyone else testified that the statements attributed to Oglesby were said by someone else.

However, there is no dispute that the subject of Eurozone investments was discussed, that the Board minutes were reviewed by all of the Trustees prior to the next Board meeting, and that they were adopted as the official record of the prior meeting. In fact, Oglesby initially admitted that he told the Trustees ACM was "making efforts" to limit the Fund's exposure to certain European investments. (*See* Answer of Derek Oglesby at ¶ 35)

Marlene Hodges, one of the Fund's Trustees, testified that the minutes were consistent with her recollection of this discussion. (Tr. at 534:1-10) Another Trustee, John Guy, Jr. testified that Oglesby actually made the remarks that the minutes attribute to him during the August 8th meeting. (Tr. at 479:4-17) Moreover, Fund counsel Richard Cutshall testified that he remembered that Oglesby was the speaker and that he used his contemporaneous notes to confirm this while finalizing the draft meeting minutes. (Tr. 820:6-11; 825:19-826:1)

Finally, the earliest draft of the meeting minutes, created by a professional stenographer, reflected that Oglesby told the Trustees that ACM was "trying to stay away from Greece, Spain, Italy and other countries doing poorly in the credit area and are focused on the better countries such as England and Germany." (Ex. 75 at 15)

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[2] Brian Jeffries was unable to testify on this point because he did not even have a general recollection of what was discussed at this meeting and he was unable to refresh his memory even after reviewing the meeting minutes. (Tr. 1474:14-1475:12)

The problem for Respondents is that during this time there is no evidence that ACM ever avoided investing in securities from Italy, or had any intention of doing so. As Oglesby admitted during the Hearing, the *very same day* that he spoke to the Trustees about avoiding investments in certain European countries, ACM caused the Fund to buy $10 million of commercial paper issued by Romulus Funding Corporation, an asset-backed program sponsored by an Italian bank. (Tr. 1414:5-10; Ex. 58 at 18) In Respondents' own credit risk analysis from mid-2011, they wrote: "Italy still remains a concern within the European Union and with Intesa having the same rating as the sovereign, the bank is vulnerable to any downgrade of the country." (Ex. 67 at 144)

But Respondents' subsequent trading in the midst of the crisis revealed no hesitations about accepting such risks. In the three weeks following the Trustee meeting, Respondents made four additional purchases of Romulus commercial paper on the Fund's behalf. (Ex. 58 at 18-23) Because ACM had represented to the Trustees that they were attempting to avoid the credit risks associated with certain Eurozone securities, the Trustees would have found ACM's subsequent actions to be inconsistent with ACM's prior statements – had they known about those purchases. (*See* Tr. at 536:6 – 537:3; 480:8-18, 482:23 – 483:21)

After this Trustee meeting, Respondents continued purchasing other securities that had strong connections to Italy and other troubled Eurozone countries:

- One day after the meeting, Respondents caused the Fund to purchase $11 million of securities issued by ENI Finance USA Inc. (Ex. 58 at 18-23) In their internal risk analysis, Respondents had described ENI's parent as "a Government-Related Issuer (GRI), given its 30.3% direct and indirect ownership by the Italian state." (Ex. 67 at 98)

- A few days after the meeting, Respondents caused the Fund to buy $8 million of securities issued by Arabella Finance LLC. (Ex. 58 at 18-23) In their internal risk analysis, Respondents had described Arabella's sponsor, UniCredit Bank AG, as "an Italy-based, pan-European banking organization." (Ex. 67 at 24) From the time of the August meeting through September 2011, Respondents bought more than $40 million of Arabella securities for the Fund in a series of short-term transactions. (Ex. 58 at 18-23)
- In the weeks that followed the August 8, 2011 meeting, the Fund purchased tens of millions of dollars in other securities with significant Eurozone exposure, including Dexia Delaware, LLC (Ex. 58 at 18-23), which was described in Respondents' internal risk analysis as "one of the top fifteen banking groups in the euro zone" (Ex. 67 at 93), and Compass Securitization, whose sponsor Respondents had described as a "German universal bank" (Ex. 67 at 77)

On November 14, 2011, Prost and Oglesby participated in the next meeting of the Fund's Board of Trustees, during which there was another discussion about the Fund's exposure to Eurozone investments. The minutes of that meeting summarize that discussion as follows:

> Mr. Oglesby assisted in this review, discussing general market conditions, the options available to the Money Market Fund and the foreign and domestic short-term fixed income markets, noting for the Board the Money Market Fund's limited exposure to European markets, including that the Money Market Fund has no assets issued in the Greek marketplace and had minimal second-hand exposure to the Italian market (and that the asset in question would be off the books of the Money Market Fund as of mid-November, after which time the Money Market Fund would have no exposure to the Italian market).

(Ex. 92 at 8-9) Greg Prost testified that Oglesby did make this statement to the Trustees. (Tr. at 1732:25-1733:17; 1735:9-22) And John Guy, one of the Fund's Trustees at the time, testified that this summary of the discussion was consistent with his recollection. (Tr. at 481:3-482:22)

Critically, Oglesby conceded during the hearing that on the *same day* of the meeting Respondents made a $4 million investment for the Fund in ENI Finance securities. (Tr. at 1415:23-1416:5; Ex. 92 at 60) That investment was *on top of* the $5 million of ENI securities already owned by the Fund. (*Id. at* 61) Respondents themselves had previously stated, in their internal credit risk documentation, that ENI's parent corporation had "direct and indirect ownership by the Italian state." (Ex. 67 at 98)

Respondents also claim that the foregoing representations about limiting the Fund's exposure to the Eurozone were accurate since as of November 14, 2011 – the maturity of the Fund's existing investments would expire in " mid-November" 2011 and "the Money Market Fund would have no exposure to the Italian market" from those existing investments. (Tr. at 1414:20-1415:22) Moreover, they argue, for a 12-day period in late November 2011 Respondents did in fact avoid purchasing any Italian securities. (Tr. at 1417:2-8)

What Respondents never told the Trustees, however, was that after a brief 12-day hiatus they were back at it again, exposing the Fund to risk from the purchase of securities from Italian issuers. In December 2011 alone, Respondents bought more than $70 million of ENI securities for the Fund. (Ex. 92 at 63-67) Their rationale was that "during that 12-day period… the world was changing." (Tr. at 1417:8-11)

Critically, however, Respondents never shared with the Fund's Trustees that changed circumstances warranted the Fund's renewed exposure to the Italian market. (*See* Tr. 1774:16-22) Moreover, nothing in Respondents' written credit reports and analysis supports their contention that the exposure to the Eurozone, or Italy, suddenly presented only a minimal risk. (Tr. at 880:11-21) According to Professor Wermers, certain objective metrics, such as the value of the Euro to the Dollar, suggested that during that in early December 2011 the market didn't share Respondents' renewed enthusiasm for Italian investments. (Tr. at 881:24 – 882:22.) In this regard, it is instructive to note that by late 2011 no other prime institutional money market fund appeared to share Respondents' sentiment that circumstances – either longstanding or recently changed -- warranted a prime money market fund's exposure to Italian investments. (Ex. 112 at 20-21)

B. ACM Made Misrepresentations to the Fund's Trustees Regarding Issuer Diversification.

On September 30, 2011, the City of Detroit made a $25 million redemption which caused an approximate 10% decline in the Fund's total net assets. (May 2, 2014 Joint Stipulation of Facts at ¶ 12) This large withdrawal triggered "passive breaches" for 10 of the Fund's 21 holdings. (*Id.* at ¶ 13; Ex. 69; Tr. 773:14-775:9) In a letter entitled "To Whom It May Concern," Oglesby insisted that the "situation was unavoidable and unintentional," and that "the Fund was back in compliance" by the following business day. (Ex. 54) According to the minutes of the November 14, 2011 Board meeting, someone from ACM made a similar representation at the next board meeting, assuring the Trustees that the passive breach which occurred on September 30th was only limited to securities of "a single issuer," and that by the next business day that investment had reverted below the 5% threshold. (Ex. 92 at 11 (internal A-1 / p. 31 of 41))

This representation by ACM to the Fund's Trustees was inaccurate and misleading in two important respects. First, the multiple, passive breaches of the 5% issuer diversification limitation persisted well beyond October 3, 2011. (Tr. 865:7-866:6) Second, the breaches were not limited to the securities of "a single issuer", but extended to 10 of the 21 issuers represented in the Fund's holdings. (Ex. 69) The Trustees were never informed of the truth of this situation. (Tr. 530:1-17, 530:25-531:9) The Trustees thought that passive breaches were significant and should be brought to the Board's attention. (Tr. 472:1 – 12; 525:23 – 528:10)

ACM claims that none of its personnel made any such representation because Oglesby and Prost may have discontinued their conference call link to the meeting before those words were spoken. (Respondents' Pre-Hearing Brief at 8-10) Instead, ACM has attributed the statements that appear in the Board minutes either to Maria De Nicolo, the Fund's Chief Compliance Officer ("CCO"), or to a misunderstanding of the October 3, 2011 Oglesby letter which was part of the Board package. (See ACM's Answer at ¶ 43)

These arguments are not persuasive for several reasons. First, John Guy and Marlene Hodges both testified that they remember someone from ACM making those statements. (Tr. 475:12-476:8; 529:22 – 531:24) Second, Maria De Nicolo has denied making those statements. She recalls being asked about the unexpected redemption and answering that it was unique. (Tr. 780:10-20) But she testified that she would not have told the Board that the Fund's investments were back below 5% as of October 3rd because it was not correct. (Tr. 780:21-781:2) Third, the statements contained in the Board minutes are more detailed than the information which could be gleaned from Oglesby's letter. (See Ex. 54, Ex. 92 at 11 (internal A-1 / p. 31 of 41))

Fund counsel Richard Cutshall disagrees, and has testified that the Board minutes were topical rather than chronological. (Tr. 826:13-827:1) Cutshall also believed that the speaker identified as "ACM" in the minutes was Oglesby, although he could not be certain it was someone else from ACM speaking from Detroit. (Tr. 828:6-829:10) Finally, Cutshall testified that ACM would have known the most about the unexpected redemption event and would have been in the best position to answer the Board's questions – they were thus the most likely persons to speak on this issue. (Tr. 838:13-25)

C. ***<u>Respondents Failed to Perform or Document Minimal Credit Risk Determinations, Disregarded Their Internal Maturity Restrictions, and Failed to Disclose Those Failures to the Fund's Board of Trustees.</u>***

As an investment adviser to the Ambassador Fund, ACM was required by Rule 2a-7 and the Fund's own compliance procedures to make a determination that each of the Fund's investments posed a minimal credit risk. (*See* Ex. 20 at 5) ACM also was required, by the Rule and the Fund's own procedures, to document this determination in writing and maintain that record for several years. Further, during the SEC's 2009 compliance examination, Brian Jeffries received a letter from the examiners, reminding ACM that the written analysis should be prepared prior to the Fund's initial purchase of a particular security. (*See* Ex. 159 at 2)

1. Respondents Failed to Perform or Document Minimal Credit Risk Determinations.

It was ACM's practice to maintain a list of securities that it considered to be eligible for investment by the Fund, which would be ratified by the Trustees on a quarterly basis. (May 2, 2014 Joint Stipulation of Facts at ¶ 11) This document contained some bare-bones information about the issuer and its support institution, including the issuer's national rating by S&P and Moody's, which always was A-1 or P-1. (*Id.*)

ACM eventually prepared a credit research report for each approved issuer and support institution, which was much more detailed, and contain additional information about the issuer and an analysis of factors other than the national ratings. (*See* Ex. 19; Ex. 67) But ACM prepared these credit reports only *after* placing an issuer on the "approved" list (and presumably after purchasing the issuer's securities) – a number of months could pass by before a report was prepared. (*Compare* Ex. 19 and Ex. 67 for date of report and date of information used in report) Respondent Derek Oglesby signed nearly all of these research reports, either as an analyst or as the Fund's portfolio manager. (*See* Ex. 19; Ex. 67)

A review of ACM's research reports from 2009, and 2010-2011 reveals that a research reports reveal that reports often were prepared using data that was months old and were updated no more than once per year. (*See* Ex. 19; Ex. 67) For example, Exhibit 89 shows that ACM was late in documenting its decisions regarding 5 issuers of commercial paper, including White Point Funding, by periods of one month to over a year.

But perhaps the most perplexing feature of ACM's credit reports is the large number of reports which attribute to a security a level of risk which is something other than "minimal," or which contain no conclusions about risk at all. (See Ex. A hereto and Ex. B hereto) During 2009, ACM prepared 36 out of 100 credit reports which contain the conclusion that the risk is "minimal." (*See* Ex. A (minimal risk determinations shown in green - all others in orange)) Another 49 reports describe the risk of the security using words such as "low," "slight," "some," "moderate" or "slightly moderate." (*Id.*) And there are 15 reports which do not contain any conclusion about risk at all. (*Id.*) During the years 2010-2011, which Oglesby was the principal preparer, ACM created reports which were much more uniform, and which usually reached the conclusion that a credit's risk was "minimal." (*See* Ex. 67) However, ACM still prepared 52 reports in which the conclusion was something other than "minimal." (See Ex. B) In no case did ACM analyze or document whether an investment could be said to present a minimal credit risk if it accounted for more than 5% of the Fund's portfolio.

2. Respondents Failed to Adhere to ACM's Internal Maturity Restrictions.

During 2009, ACM's credit research reports rarely indicate whether there was any maturity period associated with a particular security. But there were exceptions which indicated that ACM had determined that the minimal credit risk for an investment required it to be held for no more than three days. For example, a June 2009 risk analysis signed by Oglesby warned that commercial paper offered by White Point Funding, Inc. was "structured with some risk factors due to its lack of diversification and the current credit crisis taking place globally." The analysis stated that this security "should only be purchased between 1-3 days to avoid long-term risk exposure. This credit represents risk." (*See* Ex. 19B)

However, Respondents' trading activity reveals that ACM often ignored its own written risk analyses for such securities. In the five months after Respondents created the White Point Funding credit risk analysis, they caused the Fund to purchase millions of dollars of White Point commercial paper, at least 16 times with a maturity period that exceeded the 1-3 day maximum:

- On June 29, 2009 – the same month as the risk analysis – ACM caused the Fund to buy $12 million of White Point with a 16-day maturity period.
- On August 19, 2009, ACM caused the Fund to buy $11 million of White Point with a maturity period of 90 days.
- And on December 21 of 2009, ACM caused the Fund to purchase White Point with a maturity period of 63 days.

(*See* Ex. 174A)

Sometime during 2010, ACM added another feature to its internal credit risk analyses by designating issuers as Tier 1(A), Tier 1(B), or Tier 1(C). "Tier 1(A)" reflected ACM's assessment that a security could be held for up to 397 days; "Tier 1(B)" reflected an assessment that the security be held for a maximum of 30 days; and, "Tier 1(C)" reflected Respondents' assessment that the credit risk was sufficiently significant to warrant a seven-day maturity restriction. (*See* Ex. 172) In other words, in ACM's judgment, securities that ACM rated in these tiers constituted a minimal credit risk, provided they were purchased within the designated maturity restrictions.[3]

We know from the credit research files that ACM went back and updated some of these reports, downgrading issuer securities from Tier 1(B) to Tier 1(C) to reflect concerns about Eurozone exposure. But it does not appear that the credit reports were updated more than once a year, even if changing economic conditions altered the risk for a particular issuer's securities. And from time to time, ACM also disregarded its own maturity restrictions for Tier 1(B) and Tier 1 (C) securities. (*See* Ex. 174B and 174C)

Now, in this proceeding, Respondents contend that the maturity restrictions found in the 2009 credit reports, or the ones associated with ACM's internal rankings, were mere guidelines, representing flavors of "good," "better" and "best" for securities that always qualified as a minimal credit risk, and that maturity restrictions could be disregarded for convenience, or if a security's yield curve was trending upwards.

This makes no sense. Greg Prost conceded that the ACM "internal ratings" corresponded to relative levels of risk and that Tier 1(C) was the riskiest category of the three ratings. Labelling an issuer's securities as Tier 1(C), but making no effort to hold them for a shorter period of time than Tier 1(A) or Tier 1(B) securities, would mean that ACM was deliberately accepting an elevated investment risk for an extended period of time. The only reason to do this would be to pursue an attractive yield – this also would explain why ACM would disregard a shorter maturity period.

In order to determine whether the tier rankings should be viewed as restrictions or guidelines, the Court should consider how Respondents described the rankings and maturity

[3] Inexplicably, ACM produced numerous credit reports during 2010 and 2011 that did *not* assign a tier ranking to a portfolio security, and many of these reports without tiers are the ones with a risk determination that is something other than "minimal." *See* Ex. A hereto.

restrictions to others at the time. First, Standard & Poor's asked how ACM was able "mitigate the credit risk to the fund with respect to the large number of names on the approved list". (Tr. 617:8-25) In response, ACM told Standard & Poor's that the Tier 1(A), 1(B), and 1(C) designations "determined how long the maturities of that particular security could be in the fund." (Tr. 618:1-7) ACM used the word "restrictions" and never told S&P that they were only guidelines. The SEC compliance examiners were told the same thing; the tiers are joined with real maturity restrictions – not guidelines. (*See* Ex. 172) And the Fund's Trustees, John Guy and Marlene Hodges, both were aware of ACM's tier system, and the accompanying maturity restrictions, and understood that ACM was following those restrictions with respect to portfolio securities. (Tr. 456:21-25; 458:16-459:2; 521:10-522:2; 523:21-524:12) Mr. Guy testified that he expected ACM to follow these restrictions because ACM itself set up the tier ranking system, and following the maturity restrictions obviously would help mitigate portfolio risk. (Tr. 463:5-14, 21-24)

3. Respondents' Failure to Advise the Fund's Trustees about ACM's Problems in Determine Minimal Credit Risk Was Material.

None of the Trustees who testified had any idea that Respondents were not following ACM's internal maturity restrictions in 2009, 2010 or 2011. They all would have wanted to know if Respondents failed to follow those maturity restrictions in managing the Fund's portfolio. (Tr. 333:22-334:22; 463:25-464:8; 465:13-22; 524:13-17) Accordingly, Respondents' repeated failure to advise the Fund's Trustees of ACM's lack of compliance with maturity restrictions was an omission of material facts.

D. *ACM Caused the Fund to Commit Active Breaches of Rule 2a-7's Issuer Diversification Limitation.*

It is uncontested that on at least three occasions, ACM made purchases of securities from a single issuer that caused the Fund's holdings of those securities to exceed 5% of its holdings on the day of purchase. (*See* Ex. 70; Ex. 466A) Through its prior counsel, ACM identified certain securities and admitted to the Commission that purchases from a single issuer in excess of 5% of the Fund's portfolio took place on August 19, December 7, and December 18, 2009. (Ex. 70 at 1-2) However, the letter from ACM's counsel did not contain any details about the exact amounts invested in these securities, their respective maturity dates, or the total percentage of the Fund's portfolio that each investment constituted. (*See Id.*) That problem was remedied during the parties' hearing, when Respondents' expert witness identified a spreadsheet created by ACM showing the securities, dates of purchase, maturity dates, the percentage of investments in a single issuer, and the number of days that a position existed over 5% of the Fund's portfolio, along with other supporting data. (*See* Ex. 466A)

However, Respondents contend that they did not cause the Fund's failure to comply with Rule 2a-7 because Maria De Nicolo, the CCO for both the Fund and ACM, had a mistaken understanding of the law on this point. (*See* Respondents' Pre-Hearing Brief at 13-14; Ex. 70) And Ms. De Nicolo has conceded that she did not understand Rule 2a-7's requirement on this point until at least January 2010. (Tr. 723:21-725:3) However, Ms. De Nicolo was not the adviser to the Fund, did not select any investments for the Fund, and did not determine the amounts that the Fund should invest in any particular issuer. (Tr. 727:21-728:22) That was ACM's job, so the active breaches of Rule 2a-7 were its responsibility. Moreover, at the time of these breaches in 2009, Ms. De Nicolo was acting as the CCO of both the Fund *and* ACM. (Tr.

671:12-23) Consequently, even if she did cause the active breaches of Rule 2a-7, ACM would still ultimately be liable for her actions.

E. Respondents' Initial Stress Testing Failed to Comply with Rule 2a-7.

In 2010, the Commission adopted a number of amendments to Rule 2a-7 designed to address the problems encountered by money market funds during market events in 2007 and 2008. (Ex. 158 at ¶ 13 and Ex. 7 thereto) One such amendment, codified as Rule 2a-7(c)(10)(v), requires regular stress testing of a money market fund's investment portfolio. Stress testing was intended to serve as an "early warning system" of potential trouble, allowing a money market fund to analyze the impact of potential events that would present "moderate" to "extreme" stress to its portfolio. (Ex. 112 at 22)

Rule 2a-7(c)(10)(v) now requires money market fund boards to adopt procedures for periodic stress testing of the fund's ability to maintain a stable net asset value per share based upon specific hypothetical events. (Ex. 158 at ¶ 17 and Ex. 7 thereto) These hypothetical events include: (a) a change in short-term interest rates; (b) an increase in shareholder redemptions; (c) a downgrade of or default on portfolio securities; and (d) the widening or narrowing of spreads between yields on an appropriate benchmark selected by the fund for overnight interest rates and commercial paper and other types of securities held by the fund. (*Id.*; Ex. 158 at Ex. 8 thereto)

The stress testing requirement, like the 2010 amendments generally, was enacted along with the other components of that release in March 2010, and became "effective" on May 5, 2010, which is also the "compliance date" for the stress testing requirement. (Tr. at 67:25-69:12; Ex. 158 at Ex. 7 thereto) ACM first discussed the new stress testing requirement with the Fund's Trustees more than six months after the May 5, 2010 compliance date; the Trustees immediately passed a resolution authorizing the performance of such testing on an annual basis. (Ex. 468 at 5)

On December 28, 2010, Maria De Nicolo emailed Oglesby a reminder that "per the discussion at the last Board meeting … a stress test needs to be performed on the Money Market Fund as of 12/31/10." (Ex. 63) Nothing in the record reflects Oglesby doing so in the month that followed De Nicolo's reminder.

On February 9, 2011, Oglesby received another reminder about the stress testing. (Ex. 168) The next day, he emailed a one-page document to Brian Jeffries and Greg Prost, writing: "This is what I came up with for the stress test for the Board. Tell me what you think… should we go with it? Thanks." (Ex. 168) The following day Oglesby forwarded a revised version of the one-page document to De Nicolo and her colleague, Christina Curtis. (Ex. 64) Oglesby's "stress test" was discussed at the Board meeting that occurred the following week. (Ex. 97 at 7)

During the hearing, Oglesby claimed that his first stress test did include testing for hypothetical redemptions. He argued that one aspect of the test was sufficiently broad that, conceptually, it captured the information regarding redemptions. However, Oglesby was forced to concede that, during the Division's investigation, he had testified that his initial stress test did not account for hypothetical redemptions and purchases. (Tr. 1397:18-1401:13) At the time, Oglesby had speculated that the reason his test did not include redemptions was that "we were not instructed to do so." (Tr. 1401:6-10)

In any event, Oglesby's self-serving, revisionist history is contradicted not only by his earlier testimony, but also by the testimony of the Division's expert. Professor Wermers opined that Oglesby's initial stress test "failed to include at least two elements expressly set forth in Rule 2a-7 – including an analysis of the impact of the unexpected investor redemptions and an analysis of 'concurrent' stress events." (Ex. 112 at 22) Moreover, Professor Wermers testified that nothing about the stress testing which Oglesby performed in February 2011 addressed or captured the possibility of customer redemptions. (Tr. at 894:10-895:2)

IV. THE OPINIONS OF THE PARTIES' EXPERTS

A. The Division's Expert Offered Opinions that Were Both Relevant to the Issues in this Case and Helpful to the Court.

Professor Wermers' expert report sets forth his opinions on several important issues, including: (1) the Fund was uniquely vulnerable to risk; (2) on numerous occasions Respondents either had failed to make the required "minimal credit risk" determination, or to keep the records of such a determination; (3) that the Fund's active and passive breaches of the 5% issuer diversification requirement increased the risk of investor loss; (4) the initial stress testing conducted by ACM in February of 2011 did not include redemptions and did not test multiple variables simultaneously; and (5) by the Fall of 2011 the Fund was an outlier, holding very risky securities with a significant number of holdings over 5%. (*See* Ex. 112 at 3-4)

1. The Fund Was Uniquely Vulnerable to Inherent Risk.

First, although all money market funds carry inherent risks, the Fund was particularly vulnerable to these risks. Professor Wermers explained that this was due to: (1) the Fund's relatively small number of investors (some of whom represented very large proportion of the Fund's liabilities); (2) the fact that nearly all shareholders were Michigan municipalities and thus subject to similar and correlative market pressures; and (3) the relatively small number of issuers in the Fund's portfolio. (*See* Ex. 112 at 10-11)

Second, Professor Wermers noted that money market funds rely on the "Law of Large Numbers" during normal market conditions, which make it is unlikely that a large number of small investors will demand liquidity and redeem their shares at the same time. (Ex. 112 at 10) However, because the Fund had a relatively small number of investors, and disproportionate holdings by a few of them, the Fund did not enjoy the protections afforded by this phenomenon. (*Id.*) The fact that the City of Detroit and Washtenaw County owned (as of September 30, 2010) approximately 40% of the Fund's shares exposed the Fund to some unusual redemption risks. For example, a complete or substantial redemption by a single shareholder could have materially impacted the ability of the fund to honor that redemption without selling substantial securities in the market (resulting in potential "fire sale" losses). (*Id.)* In fact this scenario very nearly occurred when the City of Detroit made its unexpected $25 million redemption in September 2011 – an event that threatened to break the buck.

Third, Professor Wermers noted that the Fund's shareholders were not sufficiently diverse so as to reduce the risk of mass redemptions – as a result, there was an unusually high degree of correlation among shareholders' likely reasons for, and timing of, redemption. Nearly all of the Fund's shareholders were Michigan municipalities, who generally experienced similar economic pressures and conditions and the same investment restrictions. (*Id.* at 10) In particular, all of the municipal shareholders shared an acute aversion to risk and were likely to redeem *en masse* from the Fund at the first perceived sign of trouble. (*Id.)* Professor Wermers also explained that the Fund's breaches of the 5% diversification limit, active or passive, added risk to the portfolio – especially considering the Fund's unique risk of "lumpy redemptions". (*Id.* at 17) This also increased the volatility of the assets under management of the Fund.

Finally, Professor Wermers noted that the Fund held only a small number of investments in its portfolio at any given point in time. For example, on September 30, 2011 (after the $25 million redemption by Detroit), the Fund held only 21 issuers (plus a nominal amount of cash). *Id.* at 10. This small number of issuers increased the risk that credit issues or illiquidity for a single issuer could drastically affect the liquidity of the entire portfolio.

2. *The Fund's Portfolio Was at Risk because Respondents Failed to Make Minimal Credit Risk Determinations.*

Professor Wermers also noted that there was risk to the Fund's portfolio because of its repeated failure to make determinations that certain portfolio securities constituted minimal credit risk, which was crucial given the inherent fragility of money market funds. Professor Wermers examined all of Respondents' credit research reports on portfolio securities, as well as the "approved list." (Ex. 112 at 13 and Ex. 2 at ¶¶ 6, 7, 13, and 37) As Oglesby testified, these documents are the only records Respondents maintained to reflect ACM's credit risk conclusions. (Tr. 1328:5-1330:9; Ex. 112 at 13 (citing Oglesby's investigative testimony)) Professor Wermers concluded, based on his review of the relevant records, that ACM did not always perform the in-depth analysis required by Rule 2a-7, including the numerous factors specified in the "McGrath Letters," such as:

i. "macro-economic factors which might affect the issuer's or guarantor's current and future credit quality;
ii. the strength of the issuer's or guarantor's industry within the economy and relative to economic trends;
iii. the issuer's or guarantor's market position within its industry;
iv. cash flow adequacy;
v. the level and nature of earnings;
vi. financial leverage;
vii. asset protection;
viii. the quality of the issuer's or guarantor's accounting practices and management;
ix. the likelihood and nature of event risks.

(*See* Ex. 112 at 12-13) Professor Wermers noted that there was also risk due Respondents' failure to follow their internal system of "subratings" and the maturity restrictions associated with each rating. (*Id.* at 13-15) Professor Wermers further noted that ACM had represented to S&P that these ratings were part of its credit risk determination, and therefore ACM's failure to adhere to these maturity restrictions for Tier 1(C) securities, or conduct additional due diligence when holding securities beyond the maturity restriction Tier 1(C), added additional risk to the Fund's portfolio. (Ex. 112 at 14)

3. The Fund Was Subject to Increased Risk because of Its Active and Passive Breaches of the 5% Issuer Diversification Requirement.

Professor Wermers also explained that breaches of the 5% diversification limit, whether active or passive, adds risk to the Fund's portfolio. (Ex. 112 at 16-17) These events also increased the volatility of the assets under management of the Fund, and as the Trustees themselves understood, the existence of such breaches posed increased and undesirable risk to the fund and its shareholders. (*Id.* at 19) Adherence to the diversification limit on holdings of a single issuer would have ensured that the Fund would not be exposed to this type of excessive credit risk. (*Id.*) Professor Wermers further noted that to the extent these passive breaches occurred because ACM did not anticipate the large shareholder redemptions, they further reflected ACM's failure to follow Rule 2a-7's "Know Your Customer" requirement. (*Id.* at 24) ACM could have responded to these unexpected redemptions by formalizing and improving communication with, and knowledge of, the fund's investors, and taking steps to reduce overall portfolio concentration and reduce the number of future passive breaches. But as Professor Wermers observes, Respondents took no steps to mitigate this continued risk. (*Id.*)

4. The Fund's Investments Also Were at Risk because of ACM's Failure to Conduct Adequate Stress Testing.

Professor Wermers also noted that the Fund was at risk resulting from its failure to conduct meaningful stress testing on the Fund's portfolio. Money market funds now are required to conduct periodic stress tests, and to produce and maintain written documentation of these procedures and the outcome of such stress tests to the fund's board. (Ex. 112 at 22) The purpose of these stress tests is to analyze the impact of potential events that would present "moderate" to "extreme" stress to the money fund portfolio, in order to inform the advisor and the board of the risks such events pose to shareholders of the fund. (*Id.*) Professor Wermers noted that stress tests essentially serve as an "early warning system" to predict potential problems. (*Id.*)

However, ACM apparently failed to take this requirement seriously, at least at first. The initial stress test, based on data for year-end 2010, clearly failed to include at least two elements expressly set forth in Rule 2a-7 – including an analysis of the impact of unexpected investor redemptions and an analysis of "concurrent" stress events. (*Id.* at 22) Professor Wermers analyzed this stress test and concluded that it contained only a very limited analysis of the credit risk exposure, and that this assumption significantly diminished the reliability of the stress testing. (*Id.* at 22-23)

5. The Fund was at Risk due to its unique Eurozone investments and lack of diversification in late 2011.

Professor Wermers also observed that the Fund was an outlier in its Eurozone holdings and lack of diversification in late 2011. By September 2011, Ambassador stood alone as the *sole* U.S. Prime institutional money market fund holding the risky Eurozone securities at issue in this case. (Ex. 112 at 20-21) This created additional risk that, in the event of large redemptions and the need to liquidate such holdings, the Fund might find it difficult to find counterparties for these securities. Moreover, according to publicly filed Forms N-MFP, the Fund was the only Prime money market fund to hold 13 issuers in excess of 5% on June 30, 2011, and 15 issuers in excess of 5% on September 30, 2011 and January 31, 2012. (*Id.* at 24) No other fund, during November 2010 to December 2013, held this number of issuers in excess of the 5% limit. (*Id.)*

B. ***The Respondents' Expert Offered Opinions that Were Neither Relevant to the Parties' Claims and Defenses Nor Helpful to the Court.***

The Defendant's sole expert witness, Professor Eric Zitzewitz, offered the following opinions: (1) that on certain days during 2009 when the Fund's portfolio exceeded the 5% issuer diversification requirement, the Fund's risk of loss was only slightly higher than the risk of an alternative, compliant portfolio; (2) that on these same occasions the Fund was not close to "breaking the buck;" (3) that the Fund's diversification of investments generally was lower than what Rule 2a-7 permitted (as measured by a proxy calculation); and (4) that the credit quality of the Fund's holdings was comparable to or higher than its "peers." (*See* Ex. 466 at ¶¶ 1-5)

However, these opinions are not reliable, shed no light on whether Respondents violated the federal securities laws, and do not help the Court resolve any of the disputed issues in the case. For example, Professor Zitzewitz:

- admitted that he was not trying to impose a materiality threshold on Rule 2a-7 (Tr. 1021:25-1022:23);
- offered no opinion regarding the risk of loss posed by the Fund's numerous passive breaches of the 5% issuer diversification requirement (Tr. 109:15-19);
- did not review any of the Respondents' records, other than a spreadsheet that listed purchases "Over 5 percent at time of purchase" (Ex. 466-A; Tr. 1036:18-1038:15); and
- admitted that his opinion covered only a "specific set of issues" and did not address many of the issues raised in this action. (Tr. 1004:1-1005:12)

In addition, for the portion of his opinion that favorably compared the credit ratings of the Fund's holdings to a "peer group" of other prime money market funds, Professor Zitzewitz admitted that:

- the timeframe for this review was almost entirely comprised of the period following the SEC's exam of ACM and the Fund (Tr. 1054:5-11);
- the other funds in AMMF's "peer group" were not required to report the credit ratings of their holdings (Tr. 1055:22-1057:1);
- his peer group analysis was based on the credit rating of fund investments, despite the fact that Rule 2a-7 explicitly precludes funds from basing a minimal credit risk determination on ratings; and
- he had no idea if any of the funds in the "peer group" were also compliant with Michigan Public Act 20 or the equivalent, and therefore not even permitted to purchase lower-quality credits.

As a result, this peer group analysis was wholly unreliable because it was based upon incomplete and unreliable data.

For all of these reasons, the Court should not give Zitzewitz's opinions any weight in reaching its Initial Decision.

V. LEGAL ARGUMENT

A. *ACM Willfully Violated Sections 206(1) and 206(2) of the Advisers Act*

Section 206(1) of the 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. The Supreme Court has held that Section 206 establishes a statutory fiduciary duty for investment advisers to act for the benefit of their clients. *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 17 (1979). An adviser's fiduciary duties include "an affirmative duty of utmost good faith, and full and fair disclosure of all material facts." *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963).

Materiality under the Advisers Act is defined by the same standard used under the antifraud provisions of the Securities Act and the Exchange Act. *Steadman v. SEC*, 603 F.2d 1126, 1130 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981). In that context, materiality does not require proof that an accurate disclosure would have caused a reasonable investor to change his decision, only that the omitted fact would have assumed actual significance in the deliberations of the reasonable investor. *TSC Industries, Inc. v. Northway*, Inc., 426 U.S. 438, 449 (1976). Investment advisers to registered investment companies "owe to the board… of the funds they manage the highest fiduciary duties." *SEC v. Treadway*, 430 F. Supp. 2d 293, 338 (S.D.N.Y. 2006).

Scienter is required for a violation of Section 206(1), but not for 206(2). *See Steadman*, 603 F.2d at 1134; *see also Capital Gains,* 375 U.S. at 184–92. Recklessness satisfies the *scienter* requirement of Section 206(1). *Vernazza v. SEC*, 327 F.3d 851, 860 (9th Cir. 2003). Proof of *scienter* need not be direct, but may be a matter of inference from circumstantial evidence. *See Herman & Maclean v. Huddleston*, 459 U.S. 375, 390 n. 30 (1983).

Here, Respondents owed a fiduciary duty to the Fund's Board of Trustees, which required Respondents to make full and fair disclosure of all material facts to the Trustees during the Board's quarterly meetings. Respondents violated their fiduciary duty when communicating with the Trustees about compliance matters and various risks to the Fund's portfolio during quarterly Board meetings.

First, Oglesby and ACM sought the Trustees' ratification of ACM's investment decisions without informing the Trustees that: (1) they had caused the Fund to purchase numerous securities without making or documenting a determination that the securities presented "minimal credit risk"; and (2) that they routinely had purchased and held Fund securities for longer than the appropriate maturity period, including White Point Funding and securities which ACM had rated Tier 1(B) and Tier 1(C). These issues were material because the Trustees testified that they had delegated responsibility for making minimal credit risk determinations to ACM, that they were aware of ACM's internal rating and maturity restrictions, and that they would have wanted to be informed if these restrictions were instead being ignored.

Second, throughout the summer and fall of 2011, Respondents continually purchased securities issued by Italian-affiliated entities, despite assuring the Trustees that ACM would be staying away from Italy and was avoiding even "second hand" Italian issuers. However, this was not true, except for a brief period in November following the Commission's compliance examination. Respondents claim that by early December, conditions in Europe had changed enough that they decided to resume buying securities with Italian exposure. However, Respondents did not inform the Trustees about this about-face.[4] Nor did Respondents make any record of their supposed re-evaluation of the credit risk these securities posed, as required by the recordkeeping provisions of Rule 2a-7.

[4] By failing to disclose to the Trustees that they had reconsidered their decision to avoid Italian securities, Respondents engaged in securities fraud. *See SEC v. Syron,* 934 F. Supp. 2d 609, 629 (S.D.N.Y. 2013) (defendants' half-truths constituted viable claim for securities fraud because they created a materially misleading impression); *SEC v. Radius Capital Corp.,* 2012 U.S. Dist. LEXIS 26648 at *19-20 (Mar. 1, 2012) (same); *SEC v. True North Finance Corp.,* 909 F. Supp. 2d 1073, 1115 (D. Minn. 2012) (same); *id.* at *1101 ("The law requires 'an actor to provide complete and non-misleading information with respect to the subjects on which he undertakes to speak.'"); *SEC v. Mudd,* 885 F. Supp. 2d 654, 666 (S.D.N.Y. 2012) ("'half-truths' – literally true statements that create a materially misleading impression... will support claims for securities fraud.'"). Accordingly, Respondents were obligated to disclose to the Trustees in some form or fashion that Respondents had decided to re-expose the Fund to the risks of Italian securities. Their claim, that somehow the "world changed" during the 12 days when the Fund was out of Italian securities, and that they didn't need to inform the Trustees that their views had changed, must be rejected.

Third, ACM also falsely reassured the Trustees about the Fund's portfolio composition following a large redemption by the City of Detroit on September 30, 2011. This redemption caused ten out of the twenty-one issuers in the Fund to exceed 5% of the portfolio. During the November 2011 Board meeting, someone from ACM assured the Trustees that, by the next business day after the redemption, no issuer represented more than 5% of the portfolio. In reality, many of these issuers that were over 5% on September 30th lingered at greater than 5% for several weeks. The Trustees testified that this fact would have been important to them – had they been told the truth.

All of these misleading statements and omissions by Respondents were material. These facts related to the quality of the Fund's portfolio, a crucial area for the Trustees' oversight. Respondents' failure to inform the Trustees about the heightened risks to the Fund's portfolio, which Trustees would have found significant, interfered with their ability to exercise appropriate oversight.

Similarly, Respondents interfered with the Trustees' oversight by making misleading statements during Board meetings. Respondents provided the Trustees with false reassurance regarding the Fund's Eurozone exposure at a time when the Trustees openly expressed concern regarding the impact of the Eurozone crisis on the Fund. Respondents' false statements to the Trustees regarding the issuer diversification of the Fund in the wake of the City of Detroit's unanticipated large redemption likewise interfered with the Trustees' oversight of the Fund's portfolio.

B. *Oglesby Aided and Abetted and Caused ACM's Violations of 206(1) and 206(2)*

Oglesby aided and abetted and caused ACM's violations of Section 206(1) and 206(2). Aiding and abetting liability may be imposed when the Division can demonstrate: (1) the existence of an independent primary wrong; (2) actual knowledge or reckless disregard by a respondent of the wrong and of his/her role in furthering it; and (3) the respondent substantially assisted in the accomplishment of the primary violation. *In the Matter of vFinance Investments, Inc., et al.*, Exchange Act Rel. No. 62448, 2010 SEC LEXIS 2216, *41 (July 2, 2010). In administrative proceedings, the Commission applies a "recklessness" standard for aiding and abetting liability. *See Voss, et al. v. SEC*, 222 F.3d 994, 1004 (D.C. Cir. 2000). The recklessness standard can be satisfied where a respondent fails to use due diligence to investigate a circumstance with unusual factors or ignores red flags and suggestions of irregular conduct. *See Howard v. SEC*, 376 F.3d 1136, 1143 (D.C. Cir. 2004). Further, "[a] defendant provides substantial assistance only if [he] affirmatively assists, helps conceal, or by virtue of failing to act when required to do so enables the fraud to proceed." *SEC v. Espuelas*, 698 F. Supp. 2d 415, 433 (S.D.N.Y. 2010) (internal quotation marks and citations omitted).

For "causing" liability, three elements must be established: (1) a primary violation; (2) an act or omission by the respondent that was a cause of the violation; and (3) that the respondent knew, or should have known, that his act or omission would contribute to the violation. *In the Matter of Robert M. Fuller*, Exchange Act Rel. No. 48406, 2003 SEC LEXIS 2041 (Aug. 25, 2003), *pet. denied*, 95 F. App'x. 361 (D.C. Cir. 2004). A finding that a respondent willfully aided and abetted violations of the securities laws necessarily makes that respondent a "cause" of those violations. *See In re Clarke T. Blizzard, et al.*, Advisers Act Rel. No. 2253, 2004 SEC LEXIS 1298, at *16 n.10 (June 23, 2004); *In re Sharon M. Graham*, 53 S.E.C. 1072, 1085 n.35 (1998), *aff'd* 222 F.3d 994 (D.C. Cir. 2000).

Oglesby acted with "extreme recklessness" when he misled the Trustees about the Fund's Eurozone investments and ACM's failure to perform minimal credit risk determination of portfolio investments. Extreme recklessness can be demonstrated by evidence that he ignored red flags that indicated misconduct, or if there was a danger so obvious that he must have been aware of the danger. *Howard*, 376 F.3d at 1143-1144. Here, Oglesby personally managed the day-to-day investments of the Fund and thus knew that the Fund: (1) routinely purchased securities beyond the maturity restrictions; (2) purchased securities for which ACM had not made determinations of minimal credit risk; and (3) continued to have extensive Italian exposure during the Eurozone crisis despite his contrary assurances to the Trustees.

Oglesby was aware that he reported to the Trustees to assist their oversight of the Fund, including the quality of the portfolio securities, and that the Trustees depended upon him for accurate information. So the danger of misleading the Trustees was obvious. Despite this, Oglesby made material misstatements to the Trustees and failed to report other material facts regarding compliance matters and risks to the Fund's portfolio.

C. ACM and Oglesby caused the Fund's Failure to Comply with the Risk-Limiting Conditions of Rule 2a-7

Rule 2a-7 contains a number of risk-limiting provisions that all money market funds must strictly follow. Although there is no direct cause of action for failing to comply with Rule 2a-7, a failure to comply with the Rule exposes an investment company to other causes of actions for violations of other Investment Company Act. For example, an investment company may hold itself out as a money market fund and use the amortized cost method of valuing portfolio securities only if it abides by the risk-limiting provisions of Rule 2a-7. When a money market fund fails to follow these provisions, it: (a) must price its shares according to Rule 22c-1 of the Investment Company Act; and (b) may no longer hold itself out as a money market fund per Section 35(d) of the Investment Company Act. Accordingly, by failing to ensure that the Fund complied with Rule 2a-7, but continuing to price and market the Fund as a money market fund, ACM and Oglesby caused the Fund to violate these other provisions.

1. *The Fund failed to comply with Rule 2a-7(c)(3)— Portfolio Quality*

The Fund failed to limit investments to securities that were determined to present minimal credit risk. The fund cannot rely solely on credit ratings; it must make an independent determination that the portfolio security presents a minimal credit risk. Here, the Fund's Trustees delegated this "minimal credit risk" determination to ACM, and ratified ACM's determinations at Trustee meetings.

Pursuant to its delegated obligations under this provision, ACM imposed internal maturity restrictions on certain portfolio securities. Respondents represented to the Commission's compliance examiners, and to Standard & Poor's, that these designations constituted a part of ACM's independent credit analysis – and thus part of their determination that these holdings posed only a minimal credit risk. However, ACM regularly caused the Fund to exceed these maturity restrictions. Respondents never disclosed to the Commission's examiners, to Standard & Poor's, or to the Trustees that they treated the maturity restrictions as mere guidelines and routinely disregarded them. ACM also lacked any policies or procedures ensuring adherence to its own restrictions. Moreover, Respondents sometimes purchased portfolio securities without having made or documented any determination regarding minimal credit risk.

2. *The Fund failed to comply with Rule 2a-7(c)(4) – Portfolio Diversification*

A money market fund may invest no more than 5% of its portfolio in the securities of any one issuer immediately after acquisition of the security, subject to a safe harbor of three days. Respondents have conceded that, on three separate occasions during 2009, ACM made purchases of securities for the Fund that violated the 5% issuer diversification limitation at the time of purchase.

3. *The Fund failed to comply with Rule 2a-7(c)(10)(v) – Stress Testing*

After the 2010 amendments to Rule 2a-7, a money market fund was required to have written procedures providing for periodic stress testing of the fund's ability to maintain a stable net asset value per share based upon specified hypothetical events, including:

- a change in short-term interest rates;
- an increase in redemptions;
- a downgrade of or default on portfolio securities;
- the widening or narrowing of spreads between yields on an appropriate benchmark the fund has selected for overnight interest rates and commercial paper and other types of securities held by the fund; and
- concurrent occurrences of these events.

Despite ACM's knowledge of the Rule's amendment, the Fund conducted no stress testing whatsoever until February, 2011. Moreover, this initial stress test, conducted by Oglesby, failed to test for an increase in redemptions. Further, the Fund did not adopt written procedures regarding stress testing procedures until May 2012, almost two years after the stress testing requirement became effective.

D. *ACM and Oglesby Caused Violations of Rule 22c-1 of the Investment Company Act*

Respondents caused violations of the pricing provisions of the Investment Company Act by continuing to use pricing rules only available to Rule 2a-7-compliant funds. Investment Company Act Rule 22c-1 requires investment companies to sell and redeem shares only "at a price based on the current net asset value of such security." Rule 2a-7, however, provides an exception to this requirement, permitting a fund to instead use the amortized cost method, which allows securities to be valued at cost adjusted for any premium paid or discount received at purchase. Only using the amortized cost method can money market funds generally maintain a stable price of $1 per share. A fund that does not meet the conditions of Rule 2a-7 is ineligible to use the amortized cost method. There is no *scienter* requirement for a violation of 22c-1; negligence is thus sufficient to establish liability. *In re Pritchard Capital Partners, LLC, et al.*, Initial Decision Rel. No. 350 (July 10, 2008) 2008 SEC LEXIS 1593 at *43 n. 6, citing *SEC v. Steadman,* 967 F.2d 636, 643 n. 5 (D.C. Cir. 1992). Further, Rule 22c-1 does *not* have a materiality element. *In re Parnassus Investments, et al.*, Initial Decision Rel. No. 131 (September 3, 1998) 1998 SEC LEXIS 1877 at *48 (Finality Order - Exchange Act. Rel. No. 40,534 (Oct. 8, 1998)).

ACM repeatedly failed to comply with Rule 2a-7 while continuing to use the amortized cost method to value shares. As a result, ACM violated Rule 22c-1. On each day that the Fund did not meet the conditions of 2a-7, the Fund was required to provide redeeming shareholders a share price calculated with the current market NAV instead of the amortized-cost price of $1 per share. Similarly, purchasing shareholders should have bought shares at the daily NAV rather than $1 per share.

E. *ACM and Oglesby Caused Violations of Section 35(d) of the Investment Company Act*

Respondents also caused the Fund to violate the naming provisions of the Investment Company Act. Under Section 35(d), a registered investment company is prohibited from adopting as a part of its name or title any materially deceptive or misleading words. Rule 2a-7(b)(2) provides that using the term "money market" as part of a fund's name is materially deceptive or misleading unless the fund is in compliance with Rule 2a-7. There is no *scienter* requirement under Section 35(d); negligence is sufficient for liability. *In the Matter of Vaughn*

Weimer, IC Act Release No. 27313, IA Act Release No. 2512, 2006 SEC LEXIS 1019 at *12 (May 5, 2006). As noted above, Respondents caused the Fund's failure to comply with the conditions of Rule 2a-7(c)(3) and (c)(4) but continued to hold the Fund out as a money market fund. Accordingly, ACM and Oglesby caused the Fund's violations of Section 35(d).

F. *ACM and Oglesby Caused Violations of Section 34(b) of the Investment Company Act*

Respondents also caused the Fund to violate the filing provisions of the Investment Company Act. Section 34(b) prohibits making any untrue statement of a material fact in any report, account, record, or other document filed or required to be kept under Section 31(a) of the Investment Company Act. There is no *scienter* requirement under Section 34(b). *In re Fundamental Portfolio Advisors, Inc.*, Advisers Act Release No. 2146; 2003 SEC LEXIS 1654 at *29 (July 15, 2003). Rule 2a-7(b)(1) provides that a money market fund which is not in compliance with Rule 2a-7 makes an untrue statement of material fact by holding itself out as a money market fund in any registration statement, application, or other document filed or transmitted pursuant to the Investment Company Act. Respondents caused the Fund to violate Section 34(b) by identifying the Fund as a money market fund in numerous Commission filings despite the Fund's failure to comply with the provisions of Rule 2a-7.

G. *ACM Caused Violations of Rule 38a-1of the Investment Company Act*

ACM's operation of the Fund also led to a number of violations of the compliance rule under the Investment Company Act. Rule 38a-1 requires investment companies to adopt and implement written policies and procedures reasonably designed to prevent the fund's violation of the federal securities laws and to provide for oversight of compliance by the fund's investment adviser. *See Compliance Programs of Investment Companies and Investment Advisers*, Investment Company Act Release No. 26299, 2003 SEC LEXIS 2980 (Dec. 17, 2003) (38a-1

Adopting Release). In the adopting release, the Commission plainly stated that an investment company's failure "to have adequate compliance policies and procedures in place will constitute a violation of our rules independent of any other securities law violation." *Id.* at *8. The Rule permits the Commission to address the failure of an adviser or fund to have in place adequate compliance controls *before* that failure has a chance to harm clients or investors. *Id.*

ACM violated this provision when it failed to enact any written procedures providing for periodic stress testing until nearly two years after the 2010 amendments to Rule 2a-7. The 2010 Rule 2a-7 amendments had a compliance date of May 2010. (Tr. 68:20-69-6) ACM was aware of the amendments but did not cause the Fund to adopt any written procedures regarding stress testing. In fact, those procedures were not created until November 2011, after the Commission's compliance examiners reported to ACM that the Fund's written compliance procedures were out of date. But these newly-drafted procedures were not adopted by the Trustees until May 2012, nearly two years after the 2010 amendments.

Additionally, ACM failed to comply with its own written compliance policies and procedures for the fund. These procedures specified that ACM bore responsibility for the Fund's compliance with Rule 2a-7 and for keeping the Trustees fully informed about any compliance failures. As noted above, Respondents repeatedly failed to make sure that the fund maintained its compliance with Rule 2a-7, and failed to keep the Trustees informed of those compliance issues. Accordingly, ACM caused violations of Rule 38a-1.

H. ACM and Oglesby Caused the Fund's Violations of Section 31(a) of the Investment Company Act and Rule 31(a)-1 thereunder

Finally, ACM and Oglesby also caused the Fund's failure to maintain books and records required by Section 31(a) of the Investment Company Act and Rule 31(a)-1. The rule requires registered investment companies to maintain and keep current records required under all applicable rules. Rule 2a-7(c)(11)(iii) applies to all money market funds, and required ACM to maintain a written record of its determination of minimal credit risk for all portfolio securities for a period of at least three years. However, between 2009 and 2011, numerous credit files for portfolio securities lacked a record of a minimal credit risk determination. ACM and Oglesby were responsible for creating these records, and thus they caused the Fund's failure to comply with this recordkeeping requirement.

VI. SANCTIONS

The public interest requires that Respondents each be sanctioned for their misconduct. In determining the sanctions to be imposed in the public interest, courts and the Commission consider: the egregiousness of the actions; the isolated or recurrent nature of the infractions; the degree of *scienter* involved; the sincerity of a respondent's assurances against future violations; a respondent's recognition of the wrongful nature of his or her conduct; and the likelihood that a respondent's occupation will present opportunities for future violations. *See Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981) (*quoting SEC v. Blatt*, 583 F.2d 1325, 1334 n.29 (5th Cir. 1978)). The Commission also may consider a sanction's deterrent effect. *See In the Matter of Schield Management Co., et al.*, Exchange Act Rel. No. 53201 (Jan. 31, 2006), 2006 WL 23162, at *8.

Here, Respondents have violated the law repeatedly, and did so recklessly (if not intentionally), in order to protect their ability to earn management fees or a salary. Under the conditions that prevailed during the fall of 2011, Respondents were exposing the Fund to dangerous levels of risk. The Fund easily could have broken the buck, and investors could have suffered losses. However, even now Respondents have not acknowledged any impropriety in their actions or offered any assurances against future misconduct. Both Respondents are currently acting as investment advisers and their positions provide them with the opportunity to commit similar violations in the future. Finally, Respondents have not testified, or offered any documentary evidence, that they are unable to afford to pay disgorgement or an appropriate monetary sanction.

A. *Cease and Desist Orders*

Section 203(k) of the Advisers Act and Section 9(f) of the Investment Company Act authorize the Court to issue cease-and-desist orders for violations of the Advisers Act and Investment Company Act. Respondents' violations raise a sufficient risk of future violations to support the entry of such an order. *See In the Matter of KPMG Peat Marwick LLP*, Exchange Act Rel. No. 43862, 54 S.E.C. 1135, 1185 (Jan. 19, 2001) ("a finding of [a past] violation raises a sufficient risk of future violation," because "evidence showing that a respondent violated the law once probably also shows a risk of repetition that merits our ordering him to cease-and-desist.").

Here, there is a significant risk of repetition. Respondent ACM has not acknowledged any wrongdoing or offered any assurances against future misconduct, and continues to act as an investment adviser to clients such as pension funds and insurance companies. Greg Prost, ACM's Chief Investment Officer and one of its owners, testified that even though ACM currently is not acting as an investment adviser for a mutual fund, ACM may want to do so in the future. (Tr. 1701:20-23) Respondent Oglesby still works for ACM in a responsible position. Although Oglesby is no longer a portfolio manager, there is nothing to prevent him from assuming such a position after the conclusion of this case.

B. Disgorgement and Prejudgment Interest

Section 203(k)(5) of the Advisers Act and Section 9(f)(5) of the Investment Company Act authorize the Court to impose disgorgement and reasonable interest of ill-gotten gains. To determine the appropriate amount of disgorgement, the Division need only show a reasonable approximation of the profits from the violative conduct. *See SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989). Here, Respondent ACM received management fees from the Fund despite the numerous undisclosed violations of the federal securities laws, and Respondent Oglesby received a salary based on his work as management of the Fund's portfolio.

Respondents were able to continue receiving such compensation only by concealing their violations of the securities laws from their municipal investors and the Board of Trustees. *See, e.g., SEC v. Black,* No. 04 C 7377, 2009 WL 1181480, at *2 (N.D. Ill. Apr. 30, 2009) ("Disgorgement of salaries and other forms of compensation may be an appropriate remedy"). In every quarter during the period of time at issue, the Respondents either failed to comply with the provisions of Rule 2a-7, made misrepresentations to the Trustees about material issues, or did both. Accordingly, the Respondents should be ordered to disgorge some or all of their earnings (in management fees or salary) for each of those quarters in which they violated the law, or caused the Fund to violate the law.

In the table on the following page, the Commission has noted the various ways in which Respondents violated the Advisers Act, or aided and abetted or caused violations of the Investment Company Act during each of the quarters between August of 2009 and May of 2012. The table also shows the corresponding management fees or salary earned by Respondents during that same period of time.

Quarter	Violations	ACM Fees[5]	Oglesby Salary[5]
2009 Q3	Minimal Credit Risk (Whitepoint) Credit Reports 1 Active Breach	$133,547	N/A
2009 Q4	Minimal Credit Risk (Whitepoint) Credit Reports 2 Active Breaches	$200,321	N/A
2010 Q1	Credit Reports	$156,744	$23,565
2010 Q2	No procedures for Stress Testing Credit Reports	$105,915	$23,565
2010 Q3	Minimal Credit Risk (Tiers) Credit Reports	$100,159	$23,565
2010 Q4	Minimal Credit Risk (Tiers) Credit Reports	$93,336	$23,565
2011 Q1	Minimal Credit Risk (Tiers) Credit Reports Noncompliant Stress Test	$145,168	$37,800
2011 Q2	Minimal Credit Risk (Tiers) Credit Reports	$168,982	$37,800
2011 Q3	Minimal Credit Risk (Tiers) Credit Reports Misrepresentations to Trustees	$126,481	$37,800
2011 Q4	Minimal Credit Risk (Tiers) Misrepresentations to Trustees	$102,682	$37,800
2012 Q1	Minimal Credit Risk (Tiers)	$102,260	N/A
2012 Q2	Minimal Credit Risk (Tiers)	$21,156	N/A

C. *Civil Penalties*

The public interest would be served by imposing significant civil penalties upon the Respondents for their misconduct. In assessing the public interest of imposing civil penalties, the

[5] ACM's fees for 2009Q3 and 2010Q4 are calculated by using a proportionate share of the fees described in the May 12, 2014 Joint Stipulation of Facts for the time frame August 2009-December 2009. ACM's fees for all other quarters (2010 Q1-2012 Q2) are taken from the June 20, 2014 Joint Stipulation of Facts. Oglesby's salary is calculated by using a proportionate share of the salary stipulated to in the May 12, 2014 Joint Stipulation of Facts.

following factors may be considered: (1) the egregiousness of the violations at issue, (2) Respondents' *scienter*, (3) the repeated nature of the violations, (4) Respondents' failure to admit to their wrongdoing; (5) whether Respondents' conduct created substantial losses or the risk of substantial losses to other persons; (6) Respondents' lack of cooperation and honesty with authorities, if any; and (7) whether the penalty that would otherwise be appropriate should be reduced due to Respondents' demonstrated current and future financial condition. *See SEC v. Lybrand*, 281 F. Supp. 2d 726, 730 (S.D.N.Y. 2003), *aff'd on other grounds*, 425 F.3d 143 (2d Cir. 2005).

Respondents engaged in violations of the law by making misrepresentations to the Trustees regarding significant compliance matters, which they either knew, or were reckless in not knowing, were misleading and untrue. Further, Respondents' reckless failure to comply with the risk-limiting provisions of Rule 2a-7 repeatedly caused the Fund's shareholders to unwittingly violate their own investment policies and bear a substantial risk of loss. The Respondents have refused to admit to any wrongdoing or even to any missteps. In fact, Respondent Oglesby testified that he did not regret <u>any</u> of his actions at issue in this case. (Tr. 1431:1-1432:3)

First, Respondents made misrepresentations to the Trustees regarding the Fund's exposure to Eurozone investments. The Trustees made clear their interest and concern regarding the risk of these investments during the August 2011 Trustee meeting; Respondents assured the Trustees that they were avoiding investments in Italy. Yet the Respondents continued to make investments in commercial paper with exposure to Italy. In so doing, the Respondents exposed the Fund to serious risks, including substantial loss of investor principal, that the Trustees were seeking to avoid. Consequently, for this conduct Respondents should be subject to third tier penalties, which are appropriate when violations involve "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement" and the violations ". . . 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."[6] *See* Advisers Act Section 203 (i)(2)(C).

Second, Respondents made misrepresentations to the Trustees, and failed to make disclosures to them, regarding the Fund's passive breaches of the 5% issuer diversification limit. These violations were serious, they involved risk of investor losses, and were material to the Trustees' oversight of the Fund. Consequently, for this conduct Respondents should be subject to second tier penalties, which apply when violations involve "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement," but no significant losses or risk of losses.[7] *See* Advisers Act Section 203 (i)(2)(B).

Third, Respondents repeatedly failed to comply with the risk-limiting provisions of Rule 2a-7 which, in turn, caused numerous violations of the Investment Company Act naming rules, Section 24(b) and 35(d), as well as the pricing rule, Rule 22c-1. Respondents' violations of these provisions involved a "reckless disregard of a regulatory requirement," and thus each of these violations are deserving of second-tier penalties.

Fourth, Respondents violated the compliance rule under the Investment Company Act when they: (1) failed to enact written procedures for stress testing until 2011, despite a May 2010 compliance date; and (2) failed to adhere to ACM's own internal maturity restrictions. *See* Rule 38a-1. Respondents also violated the books and records provision under the Investment Company Act when they repeatedly failed to make and keep a record of a determination that a

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[6] The violations took place after March 2009 but before March 2013, so the maximum civil penalties for third tier violations by an individual and a corporation are $150,000 and $725,000, respectively.

[7] Based on the dates of the violations, the maximum civil penalties for second tier violations by an individual and a corporation are $75,000 and $375,000, respectively.

security posed a minimal credit risk. *See* Section 31(a) and Rule 31(a)-1. Respondents should be subject to a first-tier penalty for each of these violations.[8]

D. *Associational Bars*

Under Section 203(f) of the Advisers Act and Section 9(b) of the Investment Company Act, as amended by Section 925 of the Dodd-Frank Act, the Commission may bar or suspend registered persons from being associated with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization. *See In the Matter of John W. Lawton*, Advisers Act Rel. No. 3513 (December 13, 2012), 2012 WL 6208750 (collateral bars imposed pursuant to Section 925 of Dodd-Frank may be applied in proceedings based on pre-Dodd-Frank conduct).

Respondent ACM should be barred from any further association with an Investment Company. Such a bar would not preclude ACM from continuing to advise clients with respect to separately managed accounts; it would only prohibit operating or advising a mutual fund. ACM has offered no evidence that being subject to such a bar would result in the departure of any of its clients or put any of its employees out of work. (*See* Tr. 1595-1601)

On the other hand, Respondent Derek Oglesby should be subject to an associational bar in order to preclude his continued employment in the securities industry. Although such a sanction clearly would be a significant setback to his career, it is consistent with sanctions imposed by the Commission in similar cases. *See, e.g.*, *In re Fundamental Portfolio Advisors, Inc. et al.*, Securities Act Rel. No. 8251 (July 15, 2003), 80 SEC Docket 1851 (permanent associational bar ordered against portfolio manager who misled investors about a risky investment strategy).

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[8] The maximum civil penalties for first tier violations by an individual and a corporation are $7,500 and $75,000, respectively.

VII. CONCLUSION

For all of the foregoing reasons, the Division of Enforcement respectfully requests that the Court accept all of the documentary and testimonial evidence presented at the hearing, and issue an Initial Decision: (1) finding that Respondents Ambassador Capital Management, LLC and Derek H. Oglesby committed all of the violations described in the Order Instituting Proceedings; and (2) imposing appropriate sanctions against each Respondent.

Dated: June 20, 2014.

By: ____________________

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EXHIBIT

A

2009 ACM Credit Risk Determination

Document Date	Date As Of	Name of Issuer	Risk Determination	Bates No.
Jan-09	30-Sep-08	BASF SE	Minimal	12270
Jan-09	No date	Allianz Finance	No conclusion	12256
Jan-09	No date	Allianz Finance	No conclusion	12257
Feb-09	Feb-09	Golden Funding Corporation	Minimal	12299
Apr-09	Apr-09	Bunge Asset Funding Corporation	Moderate	12275
May-09	31-Dec-08	Standard Chartered Bank	Low	12341
Jun-09	Dec-08	Norddeutsche Landesbank Girozentrale	Moderate	12323
Jun-09	31-Jan-09	Edison Asset Securitization, LLC (EDISEC)	Minimal	12291
Jun-09	Feb-09	Straight-A Funding LLC	Minimal	12343
Jun-09	Apr-09	Gotham Funding Corporation	Minimal	12300
Jun-09	Apr-09	Sydney Capital Corporation, Inc. (SYDCAP)	Some	12344
Jun-09	Apr-09	Variable Funding Capital Corporation LLC	Moderate	12351
Jun-09	Apr-09	White Point Funding, Inc	Some	12354
Jun-09	Apr-09	White Point Funding, Inc	"Risk" (hold 1-3 days)	Ex. 31
Jun-09	May-09	LMA-Americas LLC	Minimal	12315
Jun-09	May-09	The Bank of Tokyo-Mitsubishi UFG, Ltd.	Some	12347
Jul-09	Dec-08	Jupiter Securitization Corporation	Minimal	12311
Jul-09	Mar-09	AllianceBernstein	Moderate	12255
Jul-09	Mar-09	Florida Group Capital, Inc. (FPL)	Minimal	12295
Jul-09	Mar-09	Hannover Funding Company, LLC	Low	12304
Jul-09	31-Mar-09	Danske Corporation	Minimal	12287
Jul-09	31-Mar-09	PACCAR Financial Corp	Minimal	12325
Jul-09	Apr-09	Citigroup Inc.	Moderate	12282
Jul-09	Apr-09	RBS Holdings USA Inc.	Moderate	12333
Jul-09	Apr-09	Yorktown Capital Corporation	Minimal	12356
Jul-09	21-Apr-09	The Bank of New York Mellon	Moderate	12346

*Source of Information is Division's Exhibit 19.

*Information in the "Risk Determination" column comes from the Conclusion section of each credit report. While most reports also include a Credit Risks section, these sections generally do not contain any conclusions or findings regarding the overall risk of the security.

Jul-09	30-Apr-09	Galleon Capital Corporation	Some	12297
Jul-09	May-09	Barton Capital Corporation	Small	12269
Jul-09	May-09	Beethoven Funding Corp.	Moderate	12271
Jul-09	May-09	Commerzbank	Slightly moderate	12284
Jul-09	May-09	Govco Inc.	Minimal	12301
Jul-09	May-09	Grampian Funding LTD	Minimal	12302
Jul-09	May-09	Old Line Funding Corp.	Minimal	12324
Jul-09	May-09	Silver Tower US Funding, LLC	Moderate	12339
Jul-09	28-May-09	Bank of Nova Scotia/ScotiaBank	Minimal	12268
Jul-09	31-May-09	Market Street Funding Co	Moderate	12317
Jul-09	Jun-09	General Electric Capital Corp.	Minimal	12298
Jul-09	Jul-09	Halkin Finance LLC	Minimal	12303
Jul-09	15-Jul-09	FCAR Owner Trust Series I	Moderate	12294
Aug-09	Feb-09	Seven Eleven, Inc.	Minimal	12337
Aug-09	Mar-09	Amstel Funding Corporation	Some	12258
Aug-09	31-Mar-09	Royal Bank of Scotland Group	Moderate	12335
Aug-09	30-Apr-09	Bank of Montreal	Minimal	12267
Aug-09	30-Apr-09	Fairway Finance Corporation (FAIRPP)	Minimal	12292
Aug-09	May-09	Campbell Soup Company	No conclusion	12276
Aug-09	May-09	CRC Funding LLC	Minimal	12285
Aug-09	May-09	Royal Bank of Canada	Minimal	12334
Aug-09	Jun-09	Amsterdam Funding Corporation	Some	12259
Aug-09	Jun-09	Bryant Park Funding LLC	Slight	12273
Aug-09	Jun-09	Coca-Cola Co	Minimal	12283
Aug-09	Jun-09	HSBC Holdings PLC	Slightly moderate	12305
Aug-09	Jun-09	Illinois Tool Works Inc. (ITW)	Slightly moderate	12306
Aug-09	Jun-09	Liberty Street Funding Co	Moderate	12313
Aug-09	Jun-09	Thames Asset Global Securitization	Moderate	12345
Aug-09	Jun-09	United Technologies Corporation (UTXPP)	No conclusion	12350
Aug-09	Jun-09	Westpac Banking Corporation	Minimal	12353

Aug-09	30-Jun-09	Autobahn Funding Company	Minimal	12264
Aug-09	30-Jun-09	BNP Paribas Finance Inc.	Minimal	12272
Aug-09	30-Jun-09	CBA (Delaware) Finance Inc.	Moderate	12278
Aug-09	30-Jun-09	Credit Agricole S.A.	Slightly moderate	12286
Aug-09	30-Jun-09	DZ Bank AG Group	No conclusion	12289
Aug-09	30-Jun-09	Falcon Asset Securitization Corporation	Minimal	12293
Aug-09	30-Jun-09	ING Bank N.V. (ING Groep NV)	No conclusion	12307
Aug-09	30-Jun-09	ING Funding LLC	Minimal	12308
Aug-09	30-Jun-09	Lloyds TSB Bank	Some	12314
Aug-09	30-Jun-09	Louis Dreyfus Corporation	Slightly moderate	12316
Aug-09	30-Jun-09	Metlife Short Term Funding	Moderate	12318
Aug-09	30-Jun-09	State Street Corporation	Moderate	12342
Aug-09	30-Jun-09	UBS Finance Delaware	Some	12349
Aug-09	30-Jun-09	Windmill Funding Corporation (WINFUN)	Slightly moderate	12355
Aug-09	Jul-09	Chrysler Financial Conduit Auto Rec'v (Daimler Chrysler Revolving Auto)	Moderate	12281
Aug-09	31-Jul-09	Chesham Finance LLC	Minimal	12280
Aug-09	31-Jul-09	Ebury Finance LLC	Minimal	12290
Aug-09	Aug-09	Kitty Hawk Funding Corporation	Moderate	12312
Aug-09	Aug-09	Procter & Gamble Co./Procter & Gamble International Finance	No conclusion	12330
Aug-09	Aug-09	Ranger Funding Company LLC	Minimal	12332
Aug-09	Aug-09	Société Généralo	Moderate	12340
Aug-09		Fortis Funding LLC	Moderate	12296
Sep-09	Mar-09	National Australia Funidng (Delaware) Inc.	Some	12319
Sep-09	31-Mar-09	Australia and New Zealand Banking Group Limited	No conclusion	12263
Sep-09	31-Mar-09	Natixis US Finance Co.. LLC/Natexis Banques Populaires U.S. Finance Company, LLC	No conclusion	12320
Sep-09	31-May-09	Cargill, Inc.	Minimal	12277
Sep-09	Jun-09	APRECO, Inc.	Minimal	12260

Sep-09	Jun-09	Atlantis One Funding	No conclusion	12262
Sep-09	Jun-09	Charta Corporation	Some	12279
Sep-09	Jun-09	Pfizer Investment PLC	Minimal	12327
Sep-09	Jun-09	Rabobank Netherland	No conclusion	12331
Sep-09	Jun-09	SE Banken AB	No conclusion	12336
Sep-09	30-Jun-09	AstraZeneca PLC	Moderate	12261
Sep-09	30-Jun-09	Dexia Delaware LLC	No conclusion	12288
Sep-09	30-Jun-09	Nestlé Capital Corporation	No conclusion	12321
Sep-09	30-Jun-09	Novartis Finance Corporation	Moderate	12322
Sep-09	30-Jun-09	Pfizer Incorporated (PFE)	Minimal	12326
Sep-09	30-Jun-09	Sharp Electronics Corp	No conclusion	12338
Sep-09	31-Jul-09	Wal-Mart Stores, Inc. (WMT)	Minimal	12352
Oct-09	Aug-09	TSL (USA) Inc.	Moderate	12348
Oct-09	26-Aug-09	BTM Capital Corporation	Moderate	12274
No date	31-Dec-09	Bank of America Corporation	Moderate downside	12265-6
No date	31-Dec-09	JPMorgan Chase & Co.	Moderate downside	12309-10
No date	31-Dec-09	PNC Financial Services Group, Inc.	Low	12328-9

Summary:

Minimal	36 instances
Low/slight	5 instances
Some	10 instances
Moderate/slightly moderate	33 instances
"Risk"	1 instance
No conclusion	15 instances
	100 total

EXHIBIT

B

2010-11 ACM Credit Risk Determination

Document Date	Date As Of	Name of Issuer	Tier	Risk Determination	Bates No.
Mar-10	Dec-09	Korea Development Bank	1(A)	Low	9314
Mar-10	Dec-09	Landesbank Hessen-Thuringen	None	No conclusion	9329
Apr-10	Dec-09	Royal Bank of Scotland Group	None	Moderate	7069
May-10	Dec-09	Intesa Sanpaolo	None	No conclusion	9187
May-10	Dec-09	Mitsubishi UFJ	None	Solid	8865
May-10	Dec-09	Rabobank Netherland	None	No conclusion	7678
Jun-10	Dec-09	ANZ Bank	None	Solid	7294
Jun-10	Mar-10	BTM Capital Corporation	None	Moderate	7976
Jun-10	Dec-09	Commerzbank	None	Slightly moderate	7894
Jun-10	Dec-09	DZ Bank AG Group	None	No conclusion	7749
Jun-10	Dec-09	Norddeutsche Landesbank GZ	None	Solid	9140
Jun-10	Dec-09	Sumitomo Mitsui Fin'l Group	None	Solid	9560
Jun-10	Dec-09	UniCredit Bank AG	None	No conclusion	7453
Jun-10	Dec-09	Westdeutsche Landesbank GZ (WestLB AG)	None	No conclusion	8334
Jul-10	Jun-10	Dexia Delaware, LLC	1(A)	No conclusion	8464
Aug-10	Dec-09	Bank of Nova Scotia	None	No conclusion	7757
Aug-10	Dec-09	ING Bank N.V. (ING Groep NV)	None	No conclusion	9176
Aug-10	Dec-09	Lloyds TSB Bank	None	Moderate	7526
Aug-10	Dec-09	Natixis	None	Stable	9665
Aug-10	Dec-09	Société Générale	None	Moderate	7292
Sep-10	Dec-09	Credit Agricole S.A.	None	Slightly moderate	7566
Sep-10	Jun-10	United Technologies Corporation (UTXPP)	1(A)	No conclusion	10900
Sep-10	Jun-10	United Technologies Corporation (UTXPP)	None	No conclusion	10905
Dec-10	Sep-10	BASF SE	1(A)	Some	7827
Mar-11	Dec-10	Landesbank Hessen-Thuringen	None	No conclusion	9330

*Source of Information is Division's Exhibit 67.

*All duplicate credit reports have been eliminated. The version with the lowest Bates number is listed.

*Information in the "Risk Determination" column comes from the Conclusion section of each credit report. While most reports also include a Credit Risks section, these sections generally do not contain any conclusions or findings regarding the overall risk of the security.

Apr-11	Dec-10	AllianceBernstein	1(A)	No conclusion	6805
Apr-11	Mar-11	Dexia Delaware, LLC	1(A)	No conclusion	8465
Apr-11	Dec-10	Royal Bank of Scotland Group	None	Moderate	7070
May-11	Apr-11	Hannover Funding	1(B)	Low	9087
May-11	Dec-10	Mitsubishi UFJ	None	Solid	8866
May-11	Dec-10	Rabobank Netherland	None	No conclusion	7679
May-11	Apr-11	Romulus Funding Corporation	1(C)	Moderate	10161
Jun-11	Dec-10	ANZ Bank	None	Solid	7295
Jun-11	Dec-10	HSBC Holdings PLC	None	Moderate	7975
Jun-11	Dec-10	Intesa Sanpaolo	None	No conclusion	9188
Jun-11	Dec-10	Sumitomo Mitsui Fin'l Group	None	Solid	9561
Jun-11	Dec-10	Westdeutsche Landesbank GZ (WestLB AG)	None	No conclusion	8335
Jul-11	Dec-10	DZ Bank AG Group	None	No conclusion	7750
Jul-11	Dec-10	Norddeutsche Landesbank GZ	None	Solid	9141
Jul-11	Dec-10	SE Banken AB	None	No conclusion	10506
Jul-11	Dec-10	Société Générale	None	Moderate	7293
Aug-11	Dec-10	Bank of Nova Scotia	None	No conclusion	7758
Aug-11	Dec-10	Commerzbank	None	Solid	7895
Aug-11	Dec-10	Commonwealth Bank of Australia	None	Low	8136
Aug-11	Dec-10	Lloyds TSB Bank	None	Moderate	7527
Aug-11	Dec-10	Natixis	None	Stable	9666
Aug-11	Dec-10	Standard Chartered Bank	None	Low	10554
Aug-11	Jun-11	United Technologies Corporation (UTXPP)	1(A)	No conclusion	10908
Sep-11	Mar-11	BTM Capital Corporation	None	Moderate	7977
Sep-11	Aug-11	Compass Securitization	1(C)	Moderate	8333
Sep-11	Dec-10	Credit Agricole S.A.	None	Slightly moderate	7567
Sep-11	Dec-10	UniCredit Bank AG	None	No conclusion	7454

Summary:

Low	4 instances
Solid/stable	11 instances
Some	1 instance
Moderate/slightly moderate	14 instances
No conclusion	22 instances
	52 total