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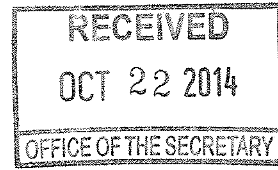
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding
File No. 3-15943



In the Matter of

DAVID J. MONTANINO,

Respondent.

THE DIVISION OF ENFORCEMENT'S PRE-HEARING MEMORANDUM

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Pursuant to SEC Rule of Practice 222(a)(1) and (2) and the Court's Order Setting Prehearing Schedule ("Scheduling Order") dated August 6, 2014, the Division of Enforcement ("Division") respectfully submits this pre-hearing memorandum in advance of the hearing scheduled to begin on November 3, 2014, as to Respondent David J. Montanino ("Montanino").

PRELIMINARY STATEMENT

Montanino misled investors to induce them to invest, later concealed the investments' poor performance and, once the investors learned the truth, lied to cover up his fraud. Montanino's pattern of deception, encompassing several investments over a six-year period, defrauded investors of over $700,000.

The Division's evidence will include testimony and corroborating documents from four investors, Montanino's former supervisor at Fidelity Investments, an employee of a brokerage firm who warned Montanino about very risky trading in one investor's account, and two Commission witnesses who will respectively authenticate documents and summarize voluminous account records. The evidence will show that Montanino misled investors about critical aspects of several investments, including his own prior investment experience, both before and after they invested. Because much of the evidence cannot be disputed, Montanino admits key facts in his Answer.

In 2005, Montanino solicited a $25,000 investment in a private equity fund from one investor by telling her that he was an investor in the fund and by leading her to believe that he was therefore a dispassionate advocate of the fund. As she will testify and as her contemporaneous correspondence shows, he never told her that he in fact worked for the fund. Since then, she has never received a penny of her investment back.

In 2010, Montanino told another investor — whose husband, a veterinarian, cared for Montanino's dog — that he would personally manage her account. Montanino solicited an investment of $299,000 from her in a moderate-risk investment. He never told her that the

investment was in a hedge fund, not a separately-managed account. He never told her that he would not have the authority to make the initial trading decisions. Nor did he tell that her investments would be exposed to significant risk through leveraged margin trading. After she invested, Montanino concealed his lack of trading authority and the risky margin trading from her and, for two months, failed to provide account statements or other basic information about her investments' performance. When she later learned of trading losses, he encouraged her to shake down his (since-deceased) business partner, Tim Sullivan ("Sullivan"), for money from other investors. Within three months of her investment, her entire $299,000 investment was gone.

Finally, in approximately early 2011, Montanino and Sullivan solicited another investor to make an investment of $100,000 — after the investor had already invested approximately $600,000 — in a private equity fund that was to invest in a start-up investment advisory firm. Montanino and his business partner led the investor to believe that his investment would be used solely to recruit financial professionals to work for the advisory firm. In fact, most of the investor's funds never reached the advisory firm, and Montanino used the little that did for his own purposes. Montanino never successfully recruited even a single financial professional.

Through these and other misrepresentations, Montanino violated anti-fraud provisions of the securities laws, including prohibitions on fraud by investment advisers. The Court should order Montanino to cease and desist from future violations, pay full disgorgement, and pay the maximum civil penalty. The Court should also bar Montanino from working in the securities industry. Montanino's pattern of lies and deception over six years renders him a danger to the investing public.

STATEMENT OF FACTS[1]

I. Montanino Begins His Long Association with Sullivan.

In approximately 1998, Montanino met and befriended Sullivan when both worked for the same firm, the Boston Group. (R173 ("David told us he first met Tim Sullivan about 15 years ago, when they both worked at the Boston Group. They were friends for many years until David once lent Tim his car…[and] Tim lent it to someone who got drunk and then abandoned it."); DE 9A- C; DE 10.) From approximately 1999 to 2003, Montanino continued to work with Sullivan at an investment firm called Imagine Venture Capital, LLC ("Imagine Capital"), which Sullivan controlled.[2] (DE 9A-C; DE 129 at 15.)

In March 2005, as Montanino admits, he formed a new firm: Calibourne Capital Management, LLC ("Calibourne"). (*Compare* OIP ¶ 4 *with* Answer ¶ 4.)[3] On August 5, 2005, he registered Calibourne as an investment adviser with the state of California. (*Id.*) Meanwhile, in 2005, Sullivan formed American Private Equity, LLC ("American Equity"), an investment firm. (DE 3; Answer ¶ 30 ("Agree Montanino knew APE was formed in 2005."); DE 1 at 1.) American Equity

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1 The Division expects to prove the facts set forth herein at the hearing based on witness testimony, exhibits introduced into evidence, and Montanino's admissions, including in his Answer and Wells submissions. The Division provides citations herein to exhibits that the Division anticipates offering into evidence (with the prefix "DE") and to exhibits that Montanino has listed (with the prefix "R"). Pursuant to the Scheduling Order, the Division will provide its exhibits to the Court prior to the hearing or at any earlier time the Court requests.

2 Montanino worked for Imagine Capital as a sales agent, albeit without a license to sell securities. (DE 9A-C; DE 3-4.) During that time, Wisconsin securities regulators sanctioned Imagine Capital and Sullivan for securities fraud and for employing a different unlicensed sales agent. (DE 76-82.) Wisconsin regulators later lifted the sanctions based on certain undertakings. (*Id.*)

3 "OIP" refers to the Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Section 21C of the Securities Exchange Act of 1934, Sections 203(f) and (k) of the Investment Advisers Act of 1940, and Section 9(b) of the Investment Company Act of 1940. "Answer" refers to a letter dated July 10, 2014, from Montanino to Chief Administrative Law Judge Brenda P. Murray, that answers the OIP's allegations and appears on the Commission's electronic docket sheet as Montanino's Answer.

owned part of Calibourne, and Montanino and Sullivan worked closely together. (DE 3; Answer ¶ 4 ("APE was an investor in Calibourne.").)

II. Montanino Deceives a Customer to Obtain an Investment in American Equity.

From approximately September 22, 2004 to June 3, 2005, Montanino also worked at Torrey Pines Securities, Inc., a brokerage firm, as a registered representative. (DE 9A-C; DE 11.) In early 2005, in his capacity as a Torrey Pines broker, Montanino solicited Sharon Jones ("Jones") to invest in American Equity, as Jones will testify. As she will also testify — and as she set forth in a written chronology in approximately 2011 — Montanino cold-called Jones in April or May 2005 and told her he was a wealth management advisor. (DE 101A at 2.) He claimed that he usually handled only portfolios of about $500,000 or more, but told her he might be able to establish an account at Torrey Pines for her even though her portfolio was worth only about $125,000. (*Id.*) In one of their meetings, Montanino told Jones that he hoped one day to leave Torrey Pines to start his own investment firm, Calibourne. (*Id.*) In the summer of 2005, after investing most of her portfolio in a Torrey Pines account, Montanino suggested to Jones that she invest the remaining $25,000 in American Equity. (*Id.*) Among other things, he led Jones to believe that he had a personal investment in American Equity. He never told her that he worked for American Equity or that American Equity owned part of Calibourne.

On June 1, 2005, Jones signed a one-page document authorizing a firm called Pensco Trust Company ("Pensco") to transfer $25,000 to a self-directed individual retirement account ("IRA") that Montanino had instructed her to open at Pensco. (DE 107A at 1.) Pensco later transferred $24,800 of Jones's funds to an American Equity account at JPMorgan Chase. (DE 107C, 107D, 107E.)

On June 3, 2005, two days after Jones opened her Pensco account, Montanino resigned from Torrey Pines. (DE 11D.) In September 2005, Torrey Pines contacted Jones to inform her that

Montanino no longer worked there. (DE 101A at 2.) Her new account representatives told her that her $25,000 investment in American Equity was probably gone and that she would not see the money again. (*Id.*) One of the representatives told her that Torrey Pines did not approve of private equity investments and would not have authorized such an investment for her. (*Id.*) The account representatives declined to tell Jones why Montanino had left or where he had gone. (*Id.* at 2–3.)

In early 2006, Jones independently tracked down Montanino, who by then worked at Fidelity. (*Id.* at 3.) Montanino told her that starting up Calibourne had been more work than he had expected, that he had therefore joined Fidelity, and that he hoped to still get Calibourne going sometime. (*Id.* at 3.) Montanino reassured Jones that her American Equity investment was not lost and helped Jones transfer her other investments from Torrey Pines to Fidelity. (*Id.* at 3.) Montanino again did not tell her that he worked for American Equity. (*Id.*)

In August 2006, Jones received a letter from Sullivan. (*Id.*) She mentioned it to Montanino. (*Id.*) Montanino told her that Phillip Redden, who had managed American Equity with Sullivan, had died and that Sullivan had taken over American Equity. (*Id.*) Montanino told Jones that he was only slightly acquainted with Sullivan and did not know Sullivan's background (*id.*) — an outright lie, given Montanino's prior history with Sullivan.

In October 2007, Jones received a Schedule K-1 tax form from an accounting firm, showing that her $25,000 American Equity investment was worth about $11,000. (*Id.*) She called Montanino to ask whether he had received his form, since she had understood he was an investor in American Equity. (*Id.*) He told her he had not received the form, but reassured her that it was a long-term investment. (*Id.* at 4.) He again did not tell her that he worked for American Equity.

In November 2007, Jones called Sullivan about the Schedule K-1 and the investment's drop in value. (*Id.*) Sullivan told her that the forms were just for accounting purposes and that one couldn't place a value on a private equity investment until the final distribution. (*Id.*) He assured her

that she would make a lot of money on the investment. (*Id.*) Sullivan also told Jones that Montanino had worked for him when Montanino recommended the investment, as Jones confirmed several months later in a letter to Sullivan. (DE 101C ("I have become more and more uncomfortable about the fact that David Montanino was, according to you, an 'employee' of yours at the time that he recommended this investment to me. Mr. Montanino told me, when he recommended the investment and again in October, 2007, that he was and is an investor in American Private Equity, not an employee of your company.").

Although Jones repeatedly asked Sullivan to return her funds and redeem her investment in American Equity, he never did. (DE 101A at 4.) In approximately October 2008, Jones received another Schedule K-1 form for her investment in American Equity. (DE 107H.) This time, it showed that her investment had a negative value. (*Id.*) To this day, Jones has never received any of her investment back.

III. Montanino Works at Fidelity But Does Not Manage Customer Assets.

From approximately September 2005 through October 2008, Montanino worked at Fidelity Brokerage Services, LLC as a financial planning consultant. (DE 9A-C; DE 11A-B; DE 125 at 4.) Anne Whatley ("Whatley"), Montanino's direct supervisor throughout his employment at Fidelity, will testify that Montanino's job responsibilities included opening accounts for clients, inputting client information into Fidelity's proprietary software tools, explaining to clients the investment products that the software tools recommended, and referring clients to other Fidelity divisions — such as Fidelity's affiliated investment advisory entity — when appropriate. As Whatley will testify, Montanino never had discretion over client accounts, never had authority to recommend particular stocks to clients, and never had the capability to recommend particular bonds to clients. Other than during a stint in a pilot program, when Montanino served as a dedicated financial planning consultant (with the same responsibilities as before) for a specific group of clients that Fidelity

assigned to him, Montanino did not have his own book of business. As Whatley will testify, Montanino never had a client base with over $1 billion in assets under management. On October 3, 2008, Montanino resigned from Fidelity. (DE 126.)

IV. Montanino Deceives His Veterinarian's Wife To Obtain a $299,000 Investment.

In late 2009, as Montanino admits, he returned to work for American Equity. (Answer ¶ 7 ("Agree that in December 2009, Montanino did return to APE.").) He helped Sullivan launch a new hedge fund called American Private Fund I ("American Fund"), formed in November 2009. (Answer ¶¶ 3, 7 ("Agree Montanino helped launch APF.").)

As Susie Yoo ("Yoo") will testify, she first met Montanino while he worked at Fidelity. She had consulted with him about her investments, and he later began taking his dog to Yoo's husband's veterinary clinic. Yoo and Montanino became friendly, and Yoo introduced him to at least one of her adult children.

In approximately early 2010, Montanino spoke to Yoo about investing with him. He gave her his business card, which bore American Equity's name. (DE 19.) He claimed he did not take investments under $1 million but offered to help Yoo invest her funds as a favor. (R67.) As Yoo will testify, Montanino led Yoo, a relatively inexperienced investor, to understand that her funds would be maintained in her own account — not in a pooled fund. As Montanino admits, Yoo sought and obtained Montanino's explicit oral assurance that he personally would manage her account. (Answer ¶ 13 ("Agree Montanino gave his oral assurance he would manage his client[']s investment.").) As Montanino also admits, he never told her that her investments would involve trading on margin. (*Compare* OIP ¶ 17 ("Montanino had not explained to the investor the concept of margin or its associated risks, or told her that [American Fund] might engage in margin trading.") *with* Answer ¶ 17 ("Agree Montanino did not explain margin to the client.").)

To obtain Yoo's investment, Montanino provided Yoo with the signature page to an American Fund subscription agreement and wire instructions. He never provided her with an American Fund offering memorandum, as Yoo will testify and as she explained to her lawyer several months later. (R67 ("Dave [Montanino] brought in a 1 page document for us to sign, all we saw was the amount $299,000 and we signed. Afterward, when we asked for the contract paper we signed I was surprised to see about 80 pages of documents which we never saw before.").) Yoo and her husband signed the signature page. (DE 20.) As Montanino concedes, Yoo made clear to him that she wanted an investment with moderate to low risk. (Answer ¶ 11 ("Agree investor did select B for Moderate to Low Risk.").) On February 26, 2010, Yoo undisputedly transferred $299,000 to the American Fund. (Answer ¶ 10 ("Agree Montanino raised $299000 from his only [American Fund] investor in February 2010.").)[4]

Dawn Sacco ("Sacco"), a Commission accountant and the Division's summary witness, will testify that Yoo's funds reached the American Fund brokerage account at Lime Brokerage, LLC ("Lime") on approximately March 1, 2010, based on Lime account records. Prior to that time, the American Fund account held no funds or securities. (DE 14B-8.)

Despite Montanino's oral assurance to Yoo that he would personally manage her money, Montanino admits that he was not an authorized trader for the American Fund brokerage account until almost three weeks later, on March 19, 2010. (DE 14B-7 at 12; Answer ¶ 13 ("Agree Montanino was not able at the time to manage her account.... Montanino agrees he was granted trading authority on 03/19/2010.").) As Yoo will testify, Montanino did not tell her that he lacked

[4] There is no dispute that Montanino promised to manage Yoo's account without charging her any fees on her principal and charging instead only 10% of any profits. (Answer ¶ 10 ("Agree Montanino said he would manage account without placement fees."); R67.) After she was nevertheless charged a 10% fee on her principal ($29,900), there is no dispute that Montanino agreed months later to return the fee to her. (Answer ¶ 24 ("Agree Montanino told his client that the 10% fee would be credited back.").) Yoo ultimately never received the fee or any of her principal back.

trading authority over her funds. Just a few weeks later, on April 13, 2010, Montanino lost trading authority over the account. (DE 36.)

From March 19 through April 13, 2010 — the few weeks when Montanino held trading authority — Sal Monaco, a Lime employee, will testify that he sent Montanino and Sullivan at least eleven emails alerting them to repeated margin calls or risk calls on the American Fund account. (DE 25–DE 33; DE 34A; DE 34B.) He sent each of the emails to Montanino's email address at American Equity: dave@apequity.com. (*Id.*) For example, on March 24, 2010, Monaco alerted Montanino to a margin call for $186,100 in the account. (DE 31.) Monaco instructed Montanino and Sullivan that they "must either wire in funds equal to or greater than the call or trade out of it by double the amount of the call…prior to the call settling [in two days]." (*Id.*) Montanino concedes that he received the margin call emails. (Answer ¶ 14 ("Agree he was included in emails for a short period of time detailing margin calls.").) At the very least, these emails alerted Montanino that Yoo's investment — which he had admittedly assured her he would personally manage and which he admittedly understood was supposed to be a moderate-to-low risk investment — had been subject to highly risky, leveraged trades. Yet Montanino did not tell Yoo about the margin trades.

On April 13, Yoo sent an email to Montanino's American Equity email address and asked: "Any way I can get a copy of [a] statement or some kind of proof where the money is?" (DE 35; Answer at ¶ 17.) Montanino replied from the same email address: "The portfolio value is being calculated and it should be available in a week or two." (DE 35.) As he admits, he provided no facts about the performance of her investment. (Answer ¶ 18 ("Agree Montanino did not provide his clients facts about the account.").) He also failed to tell Yoo that he no longer had trading authority over the account.

On May 5, 2010 — almost two months after Yoo had transferred her funds — Montanino forwarded to Yoo a statement prepared by American Fund's administrator, which Montanino had

actually received from Sullivan on April 22. (DE 37.) The statement, dated March 19, 2010, listed the date and amount of Yoo's investment but lacked any information about its performance. (*Id.*) On May 6, 2010, Yoo emailed Montanino again:

> I see that there are no numbers or figures available, however, I'm hoping that those will be available soon[.] Do you have any idea how the money was invested? What funds and what position? I did transfer the funds hoping that you watch the growth bit more closer. Hopefully that's what I'm going to see. You know we know about animals but not much in the area of investment.

(DE 38.)

On May 7, 2010, Lime informed Sullivan that Lime's clearing firm had instructed it to liquidate sufficient stock "to meet the outstanding and overdue margin calls" and that Lime had decided to fully liquidate and close the account. (DE 162.) As Sacco will testify, the American Fund's rate of return for March 2010 was about negative 13.34%, and, in any event, the leverage placed on Yoo's investment effectively erased any nominal gains. (DE 14A-1 & DE 14A-2.)

On or after May 19, 2010, Yoo received a statement from American Fund's administrator. (DE 43.) The statement, dated May 19, 2010, purported to show that her investment had declined in value by over 15% as of March 31, 2010. (*Id.*) Yoo contacted Montanino. Montanino told Yoo that he had initially earned money for Yoo, but that his boss had transferred the money to a different investment that had lost money. (R68 ¶ 10.) Yoo set up a meeting with Montanino and Sullivan to discuss her concerns in person at American Equity's office the next week.

In May 2010, Yoo in fact met with Montanino and Sullivan at their office. Sullivan told Yoo that he thought the investment had lost further value since March. (R68.) But, as Montanino admits, neither he nor Sullivan disclosed the full extent of Yoo's investment losses during the meeting. (Answer ¶ 24 ("Agree Montanino or Sullivan did not disclose to the client the extent of losses in the account during the May 26 meeting.").) Indeed, as Montanino concedes, "Sullivan was unwilling to

provide any details on the trades that led to [Yoo's] losses." (*Id.*) As Yoo will testify, she asked that her remaining funds be returned to her. Sullivan told her she would have to wait until June 30, 2010.

As Yoo will also testify, before or after that meeting began, Montanino told Yoo that if she shook Sullivan hard enough, Sullivan might give her money. (R65.) She asked Montanino how Sullivan could pay her back if the investment had lost money. (*Id.*) Montanino told Yoo that Sullivan would get investments from other investors. (*Id.*)

By May 2010, American Fund had collapsed, as Montanino admits. (Answer ¶ 7 ("Agree the fund did collapse in May 2010.").)

In June 2010, Yoo and her husband signed and faxed a form redemption request to Sullivan. (DE 41 ("Please process a full redemption of our account as of June 6, 2010.").) After that, Yoo spoke with Montanino again to try to obtain whatever was left of her investment. Montanino then told her for the first time that the investment had gone bad and that all her money was gone. (R68.) She has never received any of her investment back.

V. <u>Montanino Obtains More Investments With Lies and Baseless Projections.</u>

Just two months after American Fund collapsed, Montanino and Sullivan began working together on a new investment scheme. This time, Montanino and Sullivan decided that American Equity would purportedly finance Calibourne's operations as an investment adviser and its efforts to recruit professional advisers, who would move their clients' assets to Calibourne. (Answer ¶ 34 ("Agree the strategy was for APE to invest in Calibourne to recruit experienced financial professionals to Calibourne.").) On July 22, 2010, Montanino filed an application to re-register Calibourne, whose registration had previously lapsed, as a California investment adviser. (Answer ¶ 8 ("Agree in July 2010 Montanino filed an application to re-register Calibourne as a California Registered Investment Adviser.").)

As Montanino admits, he had no prior experience supervising investment professionals. (Answer ¶ 31 ("Montanino agrees he had not supervised investment professionals.").) Nor had he ever recommended stocks or bonds to Fidelity clients, as Whatley will testify. To the extent that he had played any role in investing Yoo's funds, the results were disastrous: within three months, risky trades dissipated her entire investment and American Fund collapsed. And Montanino knew — in part because he had solicited Jones's original investment in American Equity in 2005 — that American Equity had remained entirely unsuccessful during its five-year existence.

By at least late 2010, Montanino also knew, as he admits, that American Equity's and Calibourne's finances were precarious. (DE 55 at 5; Answer ¶ 32 ("Agree Montanino knew APE was in precarious financial position.... Agree Montanino told graphic designer she could not be paid until more money came in. Agree Montanino told consultant to cash check right away.") & ¶ 28 ("Agree that Calibourne had significant financial issues.").)

Yet Montanino prepared marketing documents for American Equity that predicted enormous future profits for investors based on the Calibourne strategy, without any legitimate basis. As he admits, "Montanino prepared documents that projected that if [American Equity] was to raise $5 million that money could be used to acquire $300–400 million in assets and if sold could yield a return of 7–10x" the investments. (Answer ¶ 29; DE 56 at 36-39.) These documents — which projected a seven- to ten-fold return for investors — were used to market American Equity to potential investors, as Montanino knew. (Answer ¶ 9 ("Agree Montanino did prepare marketing documents for APF and APE.") & ¶ 28; DE 56.)

Montanino's marketing documents also misrepresented his relevant experience. Among other things, the same American Equity marketing presentation represented that, while at Fidelity Investments, Montanino "was tasked with...providing investment management services for a client

base with over $1 Billion in assets under management." (DE 56 at 40.) As Whatley will testify, that representation was false.[5]

In approximately 2010, Bill Pankey ("Pankey") invested first $100,000 and later $500,000 in American Equity. After his first two investments, Montanino and Sullivan solicited a third investment in American Equity from Pankey. As Pankey will testify, Montanino and Sullivan represented to Pankey that his entire third investment would be used to fund Calibourne's hiring of professional investment advisers. (R178; *cf.* Answer ¶ 35 ("Agree Montanino told investor A in the Summer/Fall 2010 that a portion of the capital invested in Calibourne would be used to recruit financial advisors but denies ever saying that is all that money raised for Calibourne would be used to recruit advisors.").) With that understanding, Pankey invested a final installment of $100,000 in American Equity in March 2011. (DE 73; DE 74; Answer ¶ 35 ("Agree APE investor A made an additional $100000 investment.").)

Of Pankey's $100,000 investment, American Equity transferred $11,000 directly to Montanino. (DE 17C-4 at 8.) Montanino does not dispute that he used about half of the $11,000 for personal purposes and the rest for purposes unrelated to Calibourne. (Answer ¶ 35 ("Agree $11000 was transferred to Calibourne. Agree Montanino transferred at least a percentage of that capital for his own use.").)

On April 17, 2011, Sullivan died. (DE 85 (email from Montanino dated May 17, 2011) ("Tim passed away on 4/17.").) On June 20, 2011, Pankey emailed Montanino to ask him where his funds were: "To start with: the investment of $100k March 24 investment was not spent as specified at the

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[5] Montanino further represented that Fidelity awarded him "the prestigious Chairman's Circle of Excellence Award." (DE 56 at 40.) In fact, as he admits, he did not receive a Chairman's Circle of Excellence Award, but rather a Chairman's Award that was provided annually to the top 35% of Fidelity's financial planning consultants. (DE 108; DE 120 at 14; Answer ¶ 40 ("Montanino agrees he did not receive the prestigious 'Chairman's Circle of Excellence Award.'").)

time of investment (ie, for acquisition of investment advisers for Calibourne). Where are those funds? How w[ ]ere those funds spent?" (DE 111.) Pankey never received a clear answer.

As investors' concerns mounted after Sullivan's death, other American Equity investors contacted Montanino. On June 8, 2011, one investor, Jeff Tilem, met with Montanino in person. Tilem had previously invested $50,000 in American Equity. (DE 86.)

Tilem recorded his June 8 meeting with Montanino in an email two days later to his father. Montanino "explained how the deal between APE and Calibourne was formed. They [Montanino and Sullivan] had worked together since 2009 and they were going to set up 3 hedge funds, none of which succeeded." (R173.) Montanino admitted to Tilem that he knew Sullivan had a disciplinary history: "David said that Tim was not very smart, but was very skilled in persuading people to make investments. Tim had had his Series 7 NASD license forfeited." (*Id.*) Montanino further admitted that he knew Sullivan had had serious financial issues: "David said Tim was months behind on the rent. Tim had such bad credit toward the end that the US Bank (Century City Branch) tagged him on a Federal Check System watch list so Tim could not open another bank account anywhere." (*Id.*) Montanino told Tilem that, by December 2010, Sullivan had become hostile towards Montanino: "In December 2010, Tim threatened David that he would shut him down. He said that Tim tried to 'hijack' his project, and was refusing David [Montanino] access to the office. Tim and David had fights, including one fist fight in the office with screaming." (*Id.*) Montanino "characterized Tim as an alcoholic, a user of Xanax and some other drugs" and told Tilem that the drugs were found on Sullivan when he died. (*Id.*) Despite his poor track record, Montanino told Tilem that he was trying to start up another firm and that he had talked to another investor "who might put up $800,000.... [Montanino] will use the legal documents already drafted and only change the names to the new company, if he is able to start it." (*Id.*)

Montanino also represented to Tilem that he had Sullivan's computer, which Montanino had taken from the office after Sullivan's death. (*Id.*) Tilem asked to see the hard drive so he could trace his investment. (*Id.*) Montanino refused. (*Id.*) Montanino told Tilem that he "would give the hard drive to the authorities if they asked him for it." (*Id.*)

In fact, Montanino no longer had Sullivan's computer in his possession on June 8, 2011. On May 25, 2011, Montanino had pawned his own computer, along with Sullivan's computer. (DE 96 at 4–5; DE 97 ("[M]y client (Mr. Montanino) indeed pawned two computers. One…was his, and…one was Tim Sullivan's.") (emphasis omitted).)

ARGUMENT

I. Montanino Violated the Antifraud Provisions of the Advisers Act.

A. Montanino Violated Sections 206(1) and 206(2).

Sections 206(1) and (2) of the Investment Advisers Act of 1940 ("Advisers Act") prohibit an investment adviser from using any device, scheme, or artifice to defraud clients or engage in any transaction, practice, or course of business that defrauds clients. 15 U.S.C. § 80b-6(1) & (2).[6] These provisions impose an affirmative obligation on investment advisers to disclose all material facts to prospective and existing advisory clients — to whom advisers owe a fiduciary duty — even after a client invests money. *See Washington Inv.*, 475 F.3d at 404 ("Section 206 prohibits failures to disclose material information, not just affirmative frauds."); *SEC v. Moran*, 922 F. Supp. 867, 895–96 (S.D.N.Y. 1996) ("Section 206 of the Advisers Act establishes a statutory fiduciary duty for investment advisers to act for the benefit of their clients, requiring advisers to exercise the utmost good faith in dealing with clients, to disclose all material facts, and to employ reasonable care to avoid misleading clients.") (citing, *inter alia*, *Capital Gains*, 375 U.S. at 191–92); *David Henry Disraeli*,

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[6] Violations of Section 206 do not require actual injury to any client. *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963).

A.P. File No. 3-12288, 2007 WL 4481515, at *8 (Dec. 21, 2007). These Advisers Act provisions prohibit fraud throughout the advisor-client relationship, not just "in connection with" the offer or sale of securities. *See* Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles, Advisers Act Rel. No. 2628, 2007 WL 2239114, at *5–6 (Aug. 3, 2007) (Final Rule); *see also SEC v. Washington Inv. Network*, 475 F.3d 392, 403–05 (D.C. Cir. 2007) (failure to disclose to investment firm's existing clients that firm's principal had been barred from industry constituted fraud under the Advisers Act).

1. *Montanino Was an Investment Adviser to American Equity and Yoo.*

Section 202(a)(11) of the Advisers Act defines an "investment adviser" to include any person "who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities." 15 U.S.C. § 80b-2(11); *see also Abrahamson v. Fleschner,* 568 F.2d 862, 870 (2d Cir. 1977) ("[I]nvestment adviser" reaches all persons who manage "the funds of others for compensation."). "Compensation" is any economic benefit or expectation of an economic benefit and includes misappropriation. *See Brendan E. Murray,* A.P. File No. 3-12436, 2008 WL 4964110, at *5 (Nov. 21, 2008); *SEC v. Fife*, 311 F.3d 1, 10 (1st Cir. 2002); *SEC v. Olsen*, 243 F. Supp. 338, 339 (S.D.N.Y. 1965).

For fraud under Sections 206(1) and (2), an adviser to a fund will generally have a fiduciary duty only to the fund, his client. *See Goldstein v. SEC*, 451 F.3d 873, 881–82 (D.C. Cir. 2006). Montanino was an adviser to and had a fiduciary duty to American Equity, a private equity fund. Montanino admits he prepared investment reports for American Equity and Calibourne about trends in the securities market, as well as fund-specific marketing documents describing the strategy, which he knew would be distributed to investors. As a result, Montanino obtained at least $95,000 in compensation directly from American Equity, including a portion of Pankey's final investment in

American Equity, which Montanino and Sullivan had told Pankey would be used solely to hire new Calibourne investment professionals. *See Alexander V. Stein*, A.P. File No. 3-8112, 1995 WL 358127 (Jun. 8, 1995) ("compensation" element satisfied by diverting funds for personal use).

Yoo was also Montanino's advisory client, notwithstanding her investment in the American Fund hedge fund. Several United States Circuit Courts of Appeal and District Courts have recognized an exception to *Goldstein*. These courts have held that a fund adviser may be an adviser to an individual investor in the fund when the adviser provides personalized advice to the investor. *See United States v. Lay*, 612 F.3d 440, 446–47 (6th Cir. 2010); *SEC v. Lauer*, 478 Fed. Appx. 550, 556–57 (11th Cir. 2012); *SEC v. ICP Asset Management, LLC*, 2012 WL 2359830, at *3 (S.D.N.Y. June 21, 2012); *Goldenson v. Steffens*, 802 F. Supp. 2d 240, 268 (D. Me. 2011).

In *Lay*, the Sixth Circuit denied defendant's motion for an acquittal or new trial following a criminal conviction under the Advisers Act and held that the jury was properly instructed that the defendant, an adviser to a hedge fund, could have a fiduciary duty to an investor in the fund. 612 F.3d at 445–46. The court found that certain factors, such as the fact that the investor was the only investor in the fund at the relevant time and that the investor had an active role in the fund, as indicated by the adviser's meeting with the investor, supported the jury's conclusion that such a fiduciary duty existed. *Id.* The court noted that *Goldstein* "did not hold that no hedge fund adviser could create a client relationship with an investor, but rather held only that the SEC had 'not justified treating *all* investors in hedge funds as clients.'" *Id.* at 446–47 (emphasis in original). Similarly, in *Lauer*, the Eleventh Circuit held that "a client-adviser fiduciary relationship can arise when a hedge fund investor receives direct investment advice from a hedge fund adviser." 478 Fed. Appx. at 557 (noting as an example that defendant "proffered advice directly to the Funds' investors when he hosted meetings and teleconferences with investors"). In *Goldenson*, the district court likewise declined to dismiss claims pleading an investment adviser relationship between an adviser to

a fund and individual fund investors. 802 F. Supp. 2d at 267. The court pointed to a number of factors showing an advisory relationship between the adviser and the fund investors: "a long course of dealing between the [investors] and [the adviser], a personal friendship, a switch whereby they followed him when he changed investment firms, a request for investment advice, a recommendation to invest in a relatively esoteric form of investment concerning which he professed specialized knowledge, and repeated assurances of his personal involvement with and monitoring of the investments." *Id.*

Montanino's individualized relationship with Yoo falls squarely within the *Lay* exception. As Yoo will testify, she and Montanino had a prior professional and personal relationship, when he assisted her with her investments at Fidelity, took his dog to her husband's veterinary practice, and socialized with her and her family. As Montanino admits, he then "gave his oral assurance he would manage [Yoo's] investment." (Answer ¶ 13.) As Yoo's testimony and documentary evidence will show, Montanino spoke with Yoo repeatedly before she invested, led her to believe it would be an investment in a separate account — not a hedge fund — and communicated with her about the investment afterwards. Montanino therefore acted as Yoo's adviser and owed her a fiduciary duty.

2. *Montanino Deceived His Clients In Material Ways.*

The Division's evidence will show that Montanino deceived his clients in numerous ways. As just one example, Montanino deceived Yoo — as set forth above, an advisory client to whom he owed a fiduciary duty — about the fact that he would personally manage her account, that she would have an individual account rather than an investment in a hedge fund, and that her funds would be in invested in assets involving moderate to low risk. In fact, her investment was in a hedge fund, Montanino had trading authority over the hedge fund account for less than a month, and, as Montanino knew, the account made high-risk, leveraged trades and received almost a dozen margin and risk calls during the short time he had trading authority over the account. Afterwards,

Montanino continued the charade by failing to reveal these material facts to Yoo and indeed failed to give her even the most basic account information until after her funds were entirely gone. *See, e.g., Hennessee Group LLC*, A.P. File No. 3-13454, 2009 WL 1077451, at *9 (Apr. 22, 2009) (settled order) (advisers breached their fiduciary duties "to not misrepresent the services that they were providing and to disclose all material departures from the representations that they made to their clients"); *SEC v. Sentinel Mgmt. Group, Inc.*, 2012 WL 1079961, at *3 (N.D. Ill. Mar. 30, 2012) (adviser's failure to disclose fund's excessive use of leverage and associated risks to clients was material as a matter of law); *Gualario & Co.*, 2012 WL 627198, at *13 (failure to disclose risky investment strategy, including borrowing heavily on margin, was a material omission); *Goldenson*, 802 F. Supp. 2d at 263 (adviser's assurances that he would personally manage investors' account were material).

3. *Montanino Had the Requisite Scienter.*

Violations of Section 206(1) require a finding of scienter.[7] *See, e.g., SEC v. Steadman*, 967 F.2d 636, 641 n.3 (D.C. Cir. 1992); *Steadman v. SEC*, 603 F.2d 1126, 1134 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981). The scienter requirement is satisfied by "extreme recklessness," an "extreme departure from the standards of ordinary care, ...which presents a danger of misleading buyers or sellers that is either known to the [respondent] or is so obvious that the actor must have been aware of it." *SEC v. Steadman*, 967 F.2d at 641.

The Division will show that Montanino knew — or recklessly disregarded — that he was deceiving his advisory clients in many different ways. For example, Montanino knew that Yoo's investment would be in a pooled hedge fund, not a separate account. In fact, he gave Yoo — an unsophisticated client who did not understand its import — a signature page that showed the fund's name and reflected a fund "Series B" moderate-to-low risk investment, but failed to give her an

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[7] Violations of Section 206(2) require only a finding of negligence, not scienter. *See, e.g., Washington Inv.*, 475 F.3d at 396 ("[A]ppellants deny Radano acted with the negligence required to make out a violation of section 206(2).").

offering memorandum, as she will testify. Similarly, he failed to inform her before she invested that he would not have trading authority over the account immediately and failed to advise her even afterwards, when he knew he did not have trading authority. Finally, after Montanino received repeated margin and risk call emails, he knew the account had been subject to risky, leveraged trades, but once again failed to inform Yoo.

B. Montanino Violated Section 206(4) and Rule 206(4)-8.

Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder prohibit an adviser from making material misrepresentations or omissions to, or otherwise defrauding, existing or prospective investors in a pooled investment vehicle, such as a hedge fund or a private equity fund. 15 U.S.C. § 80b-6(4); 17 C.F.R. § 275.206(4)-8. These provisions, like Section 206(2), require a finding of only negligence, not scienter. *See SEC v. Steadman*, 967 F.2d at 647 ("[S]cienter is not required under section 206(4)."); *In re Reserve Fund Sec. & Deriv. Litig.*, 2013 WL 5432334, at *12 (S.D.N.Y. Sept. 30, 2013) (citing "well-established law...that a verdict for the Commission on the...Section 206(4) claim, could be based either on a finding of scienter or negligence").

Montanino defrauded investors in American Equity, a private equity fund, in several ways. For example, he falsely represented to potential investors that he had managed a book of business worth over $1 billion while at Fidelity, which he knew or recklessly or negligently disregarded was not true. He prepared marketing material for American Equity investors that projected returns of seven to ten times on an American Equity investment when, among other things, he knew that American Equity and Calibourne's finances were precarious and that he had no relevant experience that could possibly justify such a projection. He and Sullivan also represented to Pankey that his final American Equity investment would be used only to hire Calibourne's new investment professionals. But after Pankey invested, very little of his funds ever reached Calibourne, and

Montanino admittedly used at least a portion of those funds for his own purposes. Indeed, Montanino never hired any investment professionals at Calibourne.[8]

II. Montanino Violated Anti-Fraud Provisions of the Securities Act and Exchange Act.

To establish that Montanino committed a primary violation of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5, the Division must show that Montanino: (1) used a fraudulent scheme or device or made a material misrepresentation or omission, (2) in connection with "the offer or sale," under Section 17(a), or "the purchase or sale," under Section 10(b) and Rule 10b-5, of any security, (3) with scienter.[9] *See Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 152–53 (1972) (liability under Rule 10b-5 for fraudulent schemes or devices); *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999); 15 U.S.C. §§ 77q(a) & 78j(b); 17 C.F.R. § 240.10b-5.[10]

A. Montanino Engaged in Fraudulent Conduct.

Montanino violated Section 17(a), Section 10(b), and Rule 10b-5(b) by making materially false statements and omissions to induce investors to invest and engaging in fraudulent schemes. For example, as the Division will show, Montanino made material misrepresentations and omissions to Yoo — including about his personal management of her investment, the fact that the investment would be not be in a pooled fund, and the leveraged nature of the investment — to obtain her

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[8] For the reasons set forth above, the Division's evidence will show that Montanino was Yoo's investment adviser. If the Court finds otherwise, then Montanino would be liable for his fraud on Yoo under Section 206(4) and Rule 206(4)-8, rather than Sections 206(1) and 206(2), because she was an investor in American Fund, a pooled investment vehicle.

[9] The Division need not establish scienter to prove violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. *See Aaron v. SEC*, 446 U.S. 680, 685, 696 (1980).

[10] The Division must also show that the fraud was committed "by the use of any means" or instrumentality of "interstate commerce." 15 U.S.C. §§ 77q & 78j(b). The use of phone calls, emails or wire transfers "in some phase" of the fraud is sufficient to satisfy this requirement. *See SEC v. Stanard*, 2009 WL 196023, at *25 (S.D.N.Y. Jan. 27, 2009) (phone); *SEC v. Ramoil Mgmt., Ltd.*, 2007 WL 3146943, at *8 (S.D.N.Y. Oct. 25, 2007) (email); *SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 861, 865 (S.D.N.Y. 1997) (wire transfers). There can be no dispute that, at a minimum, Montanino communicated with Yoo by email.

investment. Similarly, he and Sullivan misrepresented to Pankey that his final investment in American Equity would be used solely to recruit Calibourne's new investment professionals. In fact, Calibourne received little of Pankey's funds, and Montanino admittedly took a portion of Pankey's funds for Montanino's own personal use. The Division's evidence will show that these misrepresentations and omissions were material — indeed, critical — to Yoo's and Pankey's decisions to invest. In addition, Montanino and Sullivan engaged in a scheme, among other things, to make baseless projections about American Equity's future rates of return and to exaggerate Montanino's investment advisory experience in order to solicit investor funds that they could use for their own purposes. *See, e.g., SEC v. Kelly,* 817 F. Supp. 2d 340, 344 (S.D.N.Y. 2011) (scheme liability encompasses deceptive acts).

B. Montanino Had the Requisite Scienter.

Montanino acted with scienter. For the reasons set forth above in Part I.A.3, the Division will show that Montanino knew or recklessly disregarded the falsity of his misrepresentations and omissions and knew or recklessly disregarded that his schemes were deceptive. In addition, Montanino's lies and omissions to investors after they had invested — including his misrepresentation to Jones that he did not know Sullivan's background, his failure to tell Yoo that her investment had been leveraged, his concealment from Yoo of the true extent of her losses, and his representation to Tilem that he had Sullivan's computer, when in fact Montanino had already pawned it — will demonstrate Montanino's scienter. *See, e.g., United States v. Kelley,* 551 F.3d 171, 176 (2d Cir. 2009) (broker's concealment of his fraud through further misrepresentations was admissible to show his intent).

C. Montanino Acted In Connection With the Purchase or Sale of Securities.

The "in connection with" requirement should be construed broadly "to encompass the entire selling process." *United States v. Naftalin,* 441 U.S. 768, 773 (1979). The Division's evidence will

show that Montanino's misrepresentations, omissions, and deceptive schemes occurred during the process of his sale of securities — investments in American Equity, a private equity fund, and American Fund, a hedge fund — to investors.

III. Montanino Aided and Abetted and Caused American Equity's Fraud

Montanino willfully aided and abetted and caused American Equity's violations of Section 17(a)(2) of the Securities Act, Section 10(b) of the Exchange Act, Rule 10b-5(b) thereunder, and Sections 206(1) and (2) of the Advisers Act by incorporating materially false statements and omissions into the American Equity investor presentation he prepared. To prove that Montanino aided and abetted a fraud, the Division must prove: (1) the existence of a fraud; (2) Montanino's general awareness, knowledge or reckless disregard of the fraud; and (3) Montanino's substantial assistance to advance the fraud's commission.[11] *See SEC v. Subaye, Inc.*, 2014 WL 448414, at *9 & n.3 (S.D.N.Y. Feb. 4, 2014) (addressing aiding and abetting liability under Exchange Act Section 20(e)); *SEC v. Apuzzo*, 689 F.3d 204, 206–07 (2d Cir. 2012). Substantial assistance "can be established by showing that the [respondent] joined the specific venture and shared in it, and that his efforts contributed to its success, or, in other words, by showing that [he] consciously assisted the commission of the specific [violation] in some active way." *SEC v. DiBella*, 587 F.3d 553, 566 (2d Cir. 2009) (quoting *United States v. Ogando*, 547 F.3d 102, 107 (2d Cir. 2008)); *see also Armstrong v. McAlpin*, 699 F.2d 79, 91 (2d Cir. 1983) (holding that even "inaction on the part of the alleged aider

[11] Under Sections 203(e)(6) and (f) of the Advisers Act, the Commission may bar a person who "at the time of the alleged misconduct [was] associated with an investment adviser" from enumerated securities industry roles if the person has "willfully aided, abetted, counseled, commanded, induced or procured the violation by any other person of any provision of the Securities Act of 1933, the Securities Exchange Act of 1934,…this title, [or] the rules or regulations under any of such statutes." 15 U.S.C. § 80b-3(e)(6) & (f).

and abettor" may be "treated as substantial assistance…when it was designed intentionally to aid the primary fraud or it was in conscious and reckless violation of a duty to act").[12]

The Division's evidence will show that Montanino aided and abetted the anti-fraud provisions by including baseless projections about American Equity's returns and misrepresentations about his investment management experience in American Equity's marketing material for potential investors, as set forth above in Part I.B. First, these statements were fraudulent because they were false and material to a reasonable investor's decision to invest. *See, e.g., Lapin v. Goldman Sachs Group, Inc.,* 506 F. Supp. 2d 221, 239 (S.D.N.Y. 2006) ("[O]ptimistic statements may be actionable upon a showing that the defendants did not genuinely or reasonably believe the positive opinions they touted (i.e., the opinion was without a basis in fact or the speakers were aware of facts undermining the positive statements), or that the opinions imply certainty."); *Marbury Mgmt., Inc. v. Kohn,* 470 F. Supp. 509, 513 (S.D.N.Y. 1979) (false statements concerning professional expertise in the securities field qualified as securities fraud), *rev'd in part on other grounds,* 629 F.2d 705 (2d Cir. 1980). Second, the Division's evidence will show that Montanino knew or recklessly disregarded that these statements by American Equity were false and therefore had the requisite scienter. Finally, Montanino's preparation of the marketing materials constituted substantial participation.

IV. <u>The Court Should Impose Meaningful Remedies.</u>

A. The Court Should Order Montanino to Cease and Desist.

Section 8(A) of the Securities Act, Section 21C of the Exchange Act and Section 203(k) of the Advisers Act authorize the imposition of a cease-and-desist order on any person who has violated any provision of the Securities Act, Exchange Act, Advisers Act or the rules and regulations

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[12] A respondent "causes" a violation if: (1) a primary violation occurred; (2) an act or omission by the respondent served as a cause of the violation; and (3) the respondent knew or should have known that his conduct would contribute to the violation. *See Robert M. Fuller*, Admin. Proc. File No. 3-10576, 2003 WL 22016309 (Aug. 25, 2003). Negligence suffices where the primary violation does not require scienter. *See KPMG, LLP v. SEC*, 289 F.3d 109, 120 (D.C. Cir. 2002).

thereunder. 15 U.S.C. §§ 77h-1, 78u-3 & 80b-3(k). In determining whether a cease-and-desist order is appropriate in the public interest, the Commission considers the following factors, often called the "*Steadman* factors": (1) the egregiousness of the violator's actions, (2) the isolated or recurrent nature of the violations, (3) the degree of scienter, (4) the sincerity of the violator's assurances against future conduct, (5) the violator's recognition of his wrongful conduct, and (6) the likelihood that the violator's occupation will present opportunities to commit future violations. *Steadman v. SEC*, 603 F.2d at 1140 (citing *SEC v. Blatt*, 583 F.2d 1325, 1334 n.29 (5th Cir. 1978)), *aff'd on other grounds*, 450 U.S. 91 (1981); *Steven E. Muth*, Initial Decision, Rel. No. 262, 2004 WL 2270299, at *38 (Oct. 8, 2004) (citing *Steadman*). The Commission further considers the following factors in determining whether to impose a cease-and-desist order: "whether there is a risk of future violations, whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being sought in the same proceedings." *Muth*, 2004 WL 2270299, at *38 (citing *KPMG Peat Marwick LLP*, 74 SEC Docket 384, 436 (Jan. 19, 2001)).

The Division's evidence will show that these factors warrant a cease-and-desist order. First, Montanino's actions were egregious and committed with a high degree of scienter. He flagrantly disregarded his fiduciary duties to his clients by materially misleading them both before and after they invested and otherwise engaged in a six-year pattern of deception. Second, Montanino has failed to recognize his unlawful conduct. Third, the violations are relatively recent and the harm to investors — who collectively lost hundreds of thousands of dollars from Montanino's fraud — was significant. A cease-and-desist order is therefore necessary, appropriate, and in the public interest to prevent Montanino from future violations of the securities laws.

B. The Court Should Issue a Permanent, Collateral Bar Against Montanino.

Section 203(f) of the Advisers Act authorizes the Commission to bar from the securities industry a willful violator of the federal securities laws (whether a primary violator or an aider and abettor) who was associated with an investment adviser during his misconduct. A collateral bar prohibits such an individual "from being associated with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization." 15 U.S.C. § 80b-3(f).

The *Steadman* factors should be applied to determine whether a bar is appropriate and, if so, its length and whether a full collateral bar is appropriate. *See John W. Lawton*, Rel. No. 3513, 2012 WL 6208750, at *10–13 (Dec. 13, 2012) (Commission opinion); *Tzemach David Netzer Korem*, Rel. No. 70044, 2013 WL 3864511, at *4–7 (July 26, 2013) (Commission opinion); *Alfred Clay Ludlum, III*, Rel. No. 3628, 2013 WL 3479060, at *4–6 (July 11, 2013) (Commission opinion). For the reasons set forth above in Part IV.A, the Division's evidence will show that the *Steadman* factors weigh heavily in favor of a bar. Indeed, Montanino's egregious fraud — involving many different deceptions over a six-year period, the loss of hundreds of thousands of dollars to investors, and attempts to conceal his fraud from investors afterwards — requires that a full, collateral bar be imposed against him. "[F]idelity to the public interest requires a severe sanction when a respondent's misconduct involves fraud because the securities business is one in which opportunities for dishonesty recur constantly." *Phillip J. Milligan*, Rel. No. 61790, 2010 WL 1143088, at *4 (Mar. 26, 2010) (Commission opinion) (internal quotation marks and citation omitted).[13]

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[13] A collateral bar under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") would not be retroactive. *See* 15 U.S.C. § 78o(b)(6)(A); Pub. L. No. 111-203, 124 Stat. 1376 (2010). Montanino's fraud continued into 2011, well after the effective date of the relevant Dodd-Frank Act provisions.

C. <u>The Court Should Order Montanino To Disgorge All Ill-Gotten Gains.</u>

Section 8A(e) of the Securities Act, Section 21C(e) of the Exchange Act, and Section 203(j) of the Advisers Act authorize the Commission to order disgorgement of ill-gotten gains, including prejudgment interest, based on willful violations of any of those statutory acts or rules or regulations thereunder. 15 U.S.C. §§ 77h-1(e), 78u-3(e) & 80b-3(j). The Division's evidence will show that Montanino obtained ill-gotten gains as a result of his fraud and that he should disgorge those gains.

D. <u>The Court Should Order Montanino to Pay a Substantial Civil Penalty.</u>

Section 8A of the Securities Act, Section 21B of the Exchange Act, and Section 203(i) of the Advisers Act authorize the Commission to order civil monetary penalties based on willful violations of any of those statutory acts or rules or regulations thereunder. 15 U.S.C. §§ 77h-1, 78u-2 & 80b-3(i). To order payment of monetary penalties, the Commission must find that such penalties are in the public interest, based on the following relevant factors: (1) deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; (2) harm to others; (3) unjust enrichment; (4) prior violations; (5) deterrence; and (6) such other matters as justice may require. 15 U.S.C. §§ 78u-2(c) & 80b-3(i)(3). "Not all factors may be relevant in a given case, and the factors need not all carry equal weight." *In re Robert G. Weeks*, Initial Decision, Rel. No. 199, 2002 WL 169185, at *58 (Feb. 4, 2002).

A three-tier system identifies the maximum amount of civil penalties, depending on the severity of the respondent's conduct. 15 U.S.C. §§ 78u-2(b) & 80b-3(i)(2). Second-tier penalties are imposed in cases involving fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement. *Id.* Third-tier penalties are imposed in cases where such state of mind is present *and* where the conduct directly or indirectly (i) resulted in substantial losses, (ii) created a significant risk of substantial losses to other persons, or (iii) resulted in substantial pecuniary gain to the person who committed the act. *Id.* Because the evidence will show that Montanino's violations

involved intentional misconduct that posed a significant risk of substantial losses to Yoo, Pankey, and other investors, third-tier penalties are appropriate against Montanino.

CONCLUSION

For the foregoing reasons, the Division's evidence will demonstrate that Montanino violated, and aided and abetted violations of, the anti-fraud provisions of the securities laws and that the Court should impose meaningful sanctions and other remedies against Montanino.

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DIVISION OF ENFORCEMENT

By: ______________________________

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