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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 POST-HEARING REPLY MEMORANDUM OF LAW

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The Division respectfully submits this memorandum of law in reply to Respondent David J. Montanino's Post Hearing Memorandum ("Respondent's Brief").[1]

PRELIMINARY STATEMENT

Montanino's self-serving denials of his repeated fraud ring hollow. He contradicts his own hearing testimony, invents facts with no support in the hearing record, and tells an implausible story that is refuted by the documentary evidence, common sense, and his victims' testimony. He even tries to blame Sullivan, whose ghostly presence Montanino keeps conjuring despite Sullivan's limited involvement in Montanino's knowing misrepresentations to investors.

In fact, Montanino is a practiced con man. Just as he admits he lied to Fidelity to get a job, he lied to investors to obtain their investments and he lied under oath at the hearing to escape the consequences of his fraud. He cannot be trusted to work in the securities industry again. The Court should find him liable for securities fraud and impose the maximum relief against him, including full disgorgement and prejudgment interest, the maximum civil penalty, and a permanent industry bar.

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[1] This reply memorandum uses the same short citation forms as the Division's initial post-hearing memorandum ("Division Brief").

ARGUMENT

I. MONTANINO DEFRAUDED YOO.

Montanino's fraud on Yoo results in his liability under the Securities, Exchange, and Advisers Acts. (Div. Br. 39–44, 48–49.) While Montanino does not address the claims' legal elements, he makes implausible factual arguments, contradicts his hearing testimony, and fails to cite evidence supporting his arguments.[2] The Court should reject Montanino's arguments and find him liable for fraud under all three statutes and corresponding rules.

A. Montanino Defrauded Yoo Before She Invested, Establishing His Liability Under the Securities, Exchange, and Advisers Acts.

1. *Montanino Implausibly Testified That He Gave the American Fund Offering Memorandum to the Yoos.*

With respect to his fraud on Yoo, Montanino's primary defense is that he gave Yoo and Dr. Yoo the American Fund Offering Memorandum before they invested. (Resp.'s Br. 16–22.) Montanino's self-serving testimony strains credulity for at least four reasons.

First, if Montanino had actually given the Yoos the Offering Memorandum, he would have had every incentive to create some written record of doing so. As he admits, he understood that every American Fund investor had to receive a copy of the Offering Memorandum before investing. (Tr. 1183.) Indeed, as a Fidelity registered

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[2] Although Montanino never asked the Division to provide a copy of the hearing transcripts, the Division voluntarily did so on January 6, 2015, after receiving Respondent's Brief.

representative for three years beforehand, Montanino routinely had customers sign forms attesting to the customers' receipt and review of fund prospectuses (similar to offering memoranda) before they invested. (Div. Br. 13 & n.4.) He even counter-signed the forms himself. (*Id.*) Yet, although Montanino and Yoo exchanged both emails and texts in 2010, Montanino admits he did not send the Yoos a copy of the Offering Memorandum using those or any other methods that would have left a record. (DE 35, DE 37, DE 39, DE 40 & DE 42 (email and text examples); Tr. 1181–83 (Montanino).)

Furthermore, Montanino knew that the blank line labeled "Name of Offeree" on the Offering Memorandum's cover page was supposed to be filled in with the investor's name. (Tr. 1183–84 (Montanino).) Although Montanino claims he handed the Yoos the Offering Memorandum in their veterinary clinic, which was presumably equipped with a photocopier, he admits he never obtained a copy of the Offering Memorandum from the Yoos with their names on the cover. (Tr. 1184, 1416–17.)

Montanino also removed certain telltale language from the Yoos' signature pages. As Montanino admits, when he gave the two signature pages to the Yoos, he did not attach the Offering Memorandum and subscription agreement or otherwise provide those documents to the Yoos that day. (Div. Br. 22–23; Resp.'s Br. 19.) The original subscription agreement's signature pages contained bold, underlined language informing the investor that her signature affirmed the representations in the subscription agreement — including that she had received and "carefully reviewed"

the Offering Memorandum. (Div. Br. 21–23.) Yet the signature pages signed by the Yoos omitted that language. (*Id.*) If Montanino had provided the Yoos with the Offering Memorandum, he would have retained the signature pages' original language to maintain a record that he had done so. Instead, Montanino removed the language because he had never provided the Yoos with the Offering Memorandum and wanted to omit any reference to the Offering Memorandum or subscription agreement.[3]

Second, if Montanino had given the Yoos the Offering Memorandum, he would have had them fill out both signature pages, rather than handing them one page already filled in. As Montanino admits, the Yoos did not complete the page labeled "Subscription Agreement Signature Page," which referenced "American Private Fund I, LP" and a Series B interest. (Div. Br. 23 & n.10; DE 20 at 2.) Montanino chose not to have the Yoos complete that page, because he did not want them to examine the page closely or ask questions about the fund or the Series B interest. Montanino knew the Yoos, expected them to trust him without paying careful attention to the forms, and hoped they would not read the signature pages closely, as in fact they did not. (Tr. 294–97, 534 ("Dr. Yoo is not a detail person."), 573–74, 589 (Yoo).)

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[3] Montanino otherwise left the signature pages intact, including the page numbers at the bottom. (Resp.'s Br. 18.) He knew American Fund would likely retain the signed signature pages, attached to the subscription agreement, in its files for audit or other purposes. Signature pages with missing page numbers would more likely attract scrutiny than pages with omitted language, which would likely escape notice without a side-by-side comparison with the original. As Montanino had hoped, Yoo trusted Montanino and did not notice the pagination on her signature pages. (Tr. 589 (Yoo).)

Third, Montanino's brief tells a different, albeit even more incredible, version of his story than the one to which he testified. At the hearing, Montanino testified about the signature pages as follows:

> I did provide the Yoos only two pages to sign when they became customers. It is what Sullivan always did. He just said it is something that if they have seen the subscription agreement, they have the offering memorandum, just bring the signature pages. That's what I brought to them.

(Tr. 1451.) In his brief, Montanino embellishes the story with certain inexplicable details:

> I was running late and I asked Sullivan if he had a memorandum that I could bring out with me for [the Yoos] to sign. He said he did not. He then said, 'You don't have to bring the whole memorandum again, just bring the signature pages.' He printed them out and gave them to me.

(Resp.'s Br. 19.) Montanino's revised story — even beyond its lack of evidentiary support in the hearing record — makes no sense. How could Sullivan not have had the Offering Memorandum when he had the two signature pages? The signature pages were part of the subscription agreement, which in turn was attached to the Offering Memorandum. (DE 46 at 101–11.) In any event, Montanino's inability to tell the same story consistently twice (including other inconsistencies pointed out herein and in the Division Brief) show that Montanino simply fabricated his hearing testimony.

Finally, Montanino implausibly claims that he had a "significant relationship" with Dr. Yoo, that he gave the Yoos the Offering Memorandum, and that Dr. Yoo

told him that he would not read it and merely instructed Montanino not to lose his money. (Resp.'s Br. 17, 25–26.) Yet as Yoo testified even under cross-examination, she was the business manager for her husband's veterinary clinics and she handled her and her husband's personal investments. (Div. Br. 17.) In April 2006, she alone walked into Fidelity's office to obtain assistance with opening accounts for both herself and her husband. (*Id.* at 16.) As Yoo also testified, Dr. Yoo would have asked her to read the Offering Memorandum if Montanino had given it to him, based on the couple's marital division of labor. (Tr. 597–98 (Yoo).) Indeed, the documentary evidence corroborates Yoo's testimony about her role in the American Fund investment. After the Yoos invested, Yoo alone exchanged emails and texts with Montanino. (DE 35; DE 37; DE 39; DE 40; DE 42.) There is no evidence that her husband ever did. Indeed, when asked whether he had texted Dr. Yoo before the hearing, Montanino testified that he had only Dr. Yoo's "vet clinic number" in 2011.[4] (Tr. 1639.)

2. *The American Fund Investor Presentation Demonstrates Montanino's Fraudulent Intent.*

Montanino asserts that he gave Yoo the American Fund investor presentation ("American Fund Presentation") before she invested. (Resp.'s Br. 19–22; DE 116A at 4–27.) On that ground, he attempts both to attack Yoo's credibility — he claims that, if she was wrong about the investor presentation, she must be not be "completely

[4] Montanino now claims that his hearing testimony was inaccurate and that he still has Dr. Yoo's 2010 "cell phone number." (Resp.'s Br. 25–26.)

forthcoming" about the Offering Memorandum — and argues that the American Fund presentation disclosed certain key facts about the investment. (*Id.* at 22.) Montanino's arguments are misguided. First, Yoo never testified that she did not receive the American Fund presentation, only that she did not remember whether she received it. Second, assuming Montanino did give Yoo the investor presentation, he had reason to do so without giving her the Offering Memorandum: the investor presentation is an exercise in securities fraud.

a. Yoo's Testimony Was Accurate to the Best of Her Recollection.

Yoo testified that she remembered receiving one or two documents from Montanino, a company brochure and possibly another document, before she invested over four years ago. (Tr. 283–88, 609–10 (Yoo); DE 19B.) She did not testify that those were the only documents she received then, merely that those were the only documents she remembered. (*Id.*) Her hearing testimony is consistent with other statements she has made about what Montanino gave her then. (R201 (potential Brady letter mentioning two brochures); R68 (CFTC declaration not addressing topic).)

Furthermore, Yoo testified that, whatever she received from Montanino before her investment, she did not receive the Offering Memorandum. (Div. Br. 22–23, 28–29.) She first saw that document when Sullivan sent it to her in late July 2010, in response to her lawyer's letter, after Montanino informed her that her investment had been wiped out. (*Id.* at 28–29.) Yoo remembered that clearly, because the Offering

Memorandum — a black-and-white document without graphics that was over one hundred pages long with appendices — looked markedly different from the one or two color-printed marketing brochures Montanino had given Yoo. (Tr. 284–86 (Yoo); *compare* DE 46 *with* DE 19B.) Indeed, in each statement she has made on the subject — including an email to her lawyer in December 2010, about nine months after she invested — she has consistently recalled that Montanino did not give her the Offering Memorandum beforehand. (R67 (Yoo email to lawyer on Dec. 8, 2010) ("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."); R201 (potential Brady letter).)

b. The American Fund Presentation Was a Fraud.

Yoo does not recall whether she received the American Fund Presentation beforehand, because she trusted Montanino and did not read the marketing material she received closely. (Tr. 283–88, 609–10, 612–13 (Yoo); DE 116A at 4–27.) However, her lawyer's letter to Sullivan and Montanino, on July 21, 2010, quoted certain language from the "promotional literature" the Yoos had received from Montanino before they invested:

> Positive nonmarket correlated returns for its investors, emphasizing capital preservation, strict risk control, and low volatility.

(DE 44.) As Montanino admits, that language does not appear in the Offering Memorandum but does appear in the American Fund Presentation. (Resp.'s Br. 21 ("To my knowledge, [that language] only appears in the Investor Presentation for

APF."); *compare* DE 44 *with* DE 46; DE 116A at 7.) Montanino may therefore have given the Yoos the American Fund Presentation before they invested.

If Montanino did so, the American Fund Presentation is a "smoking gun," although not for the reasons he suggests. (Resp.'s Br. 21–22.) The presentation proves beyond any doubt that Montanino intended to defraud the Yoos. Far from disclosing the truth, the presentation was false and misleading in many ways, which Montanino knew. He therefore had every reason to give the Yoos the presentation but not the Offering Memorandum to induce them to invest.

First, the presentation did not use the term "hedge fund" to describe the American Fund. (DE 116A at 4–27.) Instead, the presentation favorably compared American Fund's fee structure to a typical mutual fund. (*Id.* at 8.) An unsophisticated investor like Yoo would not have known that the American Fund was a hedge fund upon reading the presentation.

Second, the presentation did not disclose that American Fund would use margin trading or leverage. (DE 116A at 4–27.) Instead, buried in the second appendix, in tiny type, the presentation contained a disclosure about "any securities of any investment vehicle," not American Fund specifically. (*Id.* at 20.) Underneath, referring generically to any securities investment, it stated: "Securities trading is speculative and involves substantial risk. *Securities trading may be leveraged.*" (*Id.* (emphasis added).) This language did not disclose that the American Fund itself would use margin trading.

Third, the American Fund Presentation provided highly misleading information about the fund's past returns. The presentation prominently displayed a chart, entitled "Fund Performance — Pro Forma (1997-2009)," showing that a $1 million investment in 1997 in the S&P 500 stock index would have resulted in more than $1.5 million in 2009, while the same investment in American Fund in 1997 would have resulted in almost $3.5 million in 2009. (*Id.* at 11.) From 1997 through 2009, it showed a "Cumulative" "Net Performance" for the American Fund of 333.66%. (*Id.*) In minuscule type underneath the chart, it stated: "The returns reflected above are pro forma calculations that reflect hypothetical allocations. Hypothetical or simulated performance results have certain inherent limitations. Unlike an actual performance record, simulated results do not represent actual trading." In fact, as Montanino knew, not only were the results "hypothetical," but the chart was complete fiction. American Fund had no assets until Yoo invested in February 2010 and no performance results whatsoever. (Div. Br. 18–19, 23.)

Fourth, the American Fund Presentation materially misrepresented its risk control processes. For instance, it represented:

> APF portfolio managers undergo a rigorous screening process that includes a thorough examination of their track record, pedigree, return and risk expectations, and overall ability to enhance portfolio diversification.

(DE 116A at 10.) In fact, as Montanino knew, Sullivan had offered him a job as the sole American Fund portfolio manager without any due diligence whatsoever. (Div.

Br. 18; Tr. 1155, 1158 (Montanino).) Nor did Montanino have any "track record" or "pedigree" because he had admittedly never managed a hedge fund before. (Div. Br. 18.) The presentation further represented that "APF managers are required to consult with the APE investment committee on a daily basis." (DE 116A at 7.) Yet, as Montanino knew, no such investment committee existed, and he never consulted with anyone other than Sullivan. (Tr. 1454–55 (Montanino) (testifying that he picked the initial American Fund positions in consultation with Sullivan).)

Finally, Montanino's biography in the American Fund Presentation was even more misleading than his biography in the American Equity Presentation. (Div. Br. 10–13, 33.) The American Fund Presentation claimed — using the present tense — that "[h]igh net worth individuals, small business owners, and families who desire the assistance of a credentialed financial advisory specialist call upon Mr. Montanino's expertise to coordinate retail banking, estate planning, legal resources, tax professionals, and investment management." (DE 116A at 14.) In fact, Montanino had been unemployed for over a year before joining the American Fund, and American Fund had no assets or clients before the Yoos invested. (Div. Br. 17–19, 23.) Nor had Montanino provided any investment advisory or management services at Fidelity. (Div. Br. 9–10, 11–13.) The presentation further claimed that, at Fidelity, Montanino "was responsible for developing financial planning strategies for an $800 million affluent client base." (DE 116A at 14.) In fact, Montanino's Fidelity customer base, to the extent he had one, held about half as much: $400 million to $500 million

in Fidelity assets. (Div. Br. 11–13.) Finally, the presentation claimed that Montanino held a four-year "Bachelors of Business Administration." (DE 116A at 14.) In fact, Montanino held only a two-year Associate's Degree.[5] (DE 110 at 5.)

3. *Greed Motivated Montanino's Fraud on Yoo.*

Montanino contends that he had no motive to solicit and defraud Yoo, because he would have earned an annual performance fee of only $2990 if her investment returned a 10% profit.[6] (Resp.'s Br. 28.) In fact, Montanino had two reasons to defraud Yoo: his employment with Sullivan hung in the balance, and he hoped to reap larger fees as Yoo's investment grew and returns compounded.

In late 2009, when Montanino re-encountered Sullivan, he had been unemployed for over a year. (Div. Br. 17.) Sullivan flaunted his luxurious lifestyle, and Montanino hoped "to be a part of" it, as he testified. (*Id.* at 17–18.) Although Montanino had never worked at a hedge fund before — and had not even picked stocks in at least the preceding four years — Sullivan offered Montanino a job as American Fund's portfolio manager. (Div. Br. 11–13, 18.)

Sullivan promised Montanino he would "take care of" Montanino financially, but in return Sullivan asked Montanino to bring clients into the new hedge fund. (*Id.*

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[5] The American Fund Presentation contains other apparently false or misleading statements. For instance, there is no evidence that several individuals listed as "Directors or Advisers" — including a Stanford University professor emeritus and the director of the Center for Research in Financial Mathematics and Statistics — had any relationship with American Equity or American Fund. (DE 116A at 15–18.)

[6] Montanino uses the figure $2900, but a 10% performance fee on a 10% profit on a $299,000 investment would be $2990, not $2900. (Resp.'s Br. 28.)

at 18.) Indeed, the American Fund Presentation that Montanino contends he gave Yoo described Montanino's role as "work[ing] on fundraising efforts and new business initiatives" and listed his name as American Fund's sole "Investor Relations" contact. (DE 116A at 14, 27.) Not having visited the Yoos' veterinary clinic or spoken to Yoo since leaving Fidelity in October 2008, Montanino returned to the clinic in January 2010. (Tr. 269–71 (Yoo); 1135–36 (Montanino); Div. Br. 17.) He then lured Yoo into American Fund because he knew that his job managing the fund would be imperiled if he could not obtain any investors for the new fund.

Montanino also knew that Sullivan would pay him more if he did obtain investors. Indeed, Montanino hoped to earn money by investing the Yoos' funds. As Montanino contends, a 10% performance fee on a 10% profit on a $299,000 investment would result in $2990 in the first year. (Resp.'s Br. 28.) Over time, Montanino hoped that the Yoos' profits would be re-invested and generate larger fees. For example, in the second year, if the Yoos re-invested their profit (after paying fees) in the American Fund and the fund returned a 10% profit, his fee would be $3259. In several years, as the returns compounded, Montanino's fees would have been substantial. Montanino did not solicit Yoo's investment out of friendship: he did so because he wanted to make money.

B. Montanino Also Defrauded Yoo After She Invested and Thereby Violated the Advisors Act.

1. *Montanino's Own Admissions Establish His Liability.*

While Montanino broadly contends that he did not violate "any securities law," (Resp.'s Br. 42), there can be no dispute that he defrauded Yoo under Advisers Act Sections 206(1) and (2) after she became his advisory client. (Div. Br. 39–44 (describing elements of these claims).) His own admissions establish his liability.

First, although Montanino asserts that he had no fiduciary duty to American Equity's individual investors (which the Division does not dispute), Montanino does not contest that he was Yoo's investment adviser and therefore had a fiduciary duty to her. (*Compare* Resp.'s Br. 9–28 (referring to the Yoos as "clients") *with* 31; Div. Br. 40–42.)

Second, Montanino admits that, at least after Yoo invested in American Fund, he knew material facts about her investment, knew he had to disclose them, and chose not to disclose them reasonably promptly. Specifically, he admits that by March 24, 2010, he knew both that Sullivan had "completely reckless[ly]" traded on margin in American Fund and that Sullivan's recklessness would affect the Yoos' investment. (Div. Br. 24–25.) Montanino admits that by April 13, 2010 — the day Sullivan de-authorized him from the American Fund account — he knew that the Yoos had lost

$35,000 to $40,000 of their $299,000 investment.[7] (*Id.* at 25.) Montanino further admits that by April 13, 2010, he "realized that [he] needed to inform the Yoos[ ] about what had transpired in the account" (Resp.'s Br. 11) — an acknowledgement that he knew the information was extremely important to Yoo and therefore material. Yet when Yoo asked him by email that day how "[her] portfolio [was] performing," Montanino misled her. (Div. Br. 25.) Rather than disclosing that he was no longer managing her investment, that Sullivan had made reckless margin trades, and that her investment had lost over 11% of its value, he told her only that her "portfolio value [wa]s being calculated" and misled her into believing she had no reason for concern. (Div. Br. 24–25; DE 35; Resp.'s Br. 11–12 (admitting he decided not to tell Yoo the truth then while claiming he told her nine days later, on April 22).)

This undisputed conduct establishes Montanino's liability under Advisers Act Sections 206(1) and (2), which impose a fiduciary duty on investment advisers "to

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[7] Montanino now attempts to make two internally inconsistent arguments. He contends the American Fund account suffered no losses before he was de-authorized on April 13, 2010, *but also* that he knew the Yoos had sustained losses of $40,000 by that date. Initially he claims — contrary to his own hearing testimony and the documentary evidence — that the Yoos' losses occurred only after he was de-authorized from the account on April 13, 2010. (Resp.'s Br. 13 ("But during the short period of time while I was authorized on the account, the account was only in negative territory for a day or two in the month of March 2010.... [A]t least while I was authorized, the situation was not nearly as dire as the Commission had made it out to be."); Tr. 1226; DE 43.) Later he admits, as he testified, that he knew of the Yoos' loss of $40,000 by the time he lost trading authority on April 13. (Resp.'s Br. 11, 23 (acknowledging that Sullivan gave him no information about the account value after de-authorizing him on April 13 yet claiming he told Yoo on April 22 that she had lost "roughly $40,000"); Tr. 1226 (Montanino).) The Court should not credit Montanino's recent fabrications.

exercise the utmost good faith in dealing with clients, to disclose all material facts, and to employ reasonable care to avoid misleading clients." (Div. Br. 39–42 (quoting *SEC v. Moran*, 922 F. Supp. 867, 895–96 (S.D.N.Y. 1996)).) Once Montanino knew that the Yoos' investment had lost a significant amount of money and that he no longer managed the investment — information of the utmost importance to Yoo and any reasonable investor — he had a duty to disclose that information as promptly as he reasonably could. Indeed, Montanino could have told Yoo within the next day or week, and he does not contend otherwise. (Resp.'s Br. 16 (labeling his decision a "judgment call").) In short, Yoo had a right to know the truth to decide what action to take in response. By misleading her and failing to provide the information to her reasonably promptly, Montanino violated Advisers Act Sections 206(1) and 206(2).

2. *Montanino's Testimony That He Told the Yoos About Their Losses On April 22, 2010 Is Implausible.*

Relying on his hearing testimony, Montanino argues that he told the Yoos on April 22, 2010 — nine days after he first learned the information — that their investment had suffered "roughly $40,000" in losses and that Sullivan had "fired" him. (Resp.'s Br. 22–25; Tr. 1232–33, 1283, 1285.) Montanino accuses Yoo of lying when testifying that he did not tell her until mid-May 2010. (*Id.* at 8, 22–25 ("Yoo was at the very least not forthcoming, and possibly outright dishonest."); Tr. 331–38, 343–50 (Yoo).) The documentary evidence, which corroborates Yoo's truthful testimony, belies Montanino's self-serving story and accusations against the victim of his fraud.

On Tuesday, April 13, 2010, Yoo sent Montanino a four-paragraph email. (DE 35.) In the first paragraph, Yoo asked Montanino about his dog Munky. (*Id.*) In the second paragraph, she asked about her portfolio value and requested written confirmation of her investment. (*Id.*) In the third paragraph, she told Montanino that her son was on break, asked if they could all get together for dinner with her son at a restaurant called Piccolo, and told Montanino that she would show him "the progress of my home" — the new house she and Dr. Yoo were building — the night of the dinner. (*Id.*; Tr. 521 (Yoo).) While Yoo was nervous about her investment, she was careful not to annoy Montanino — "rock the boat" — because he had her money and was "already in the driver's seat." (Tr. 316–17 (Yoo).) In response, Montanino wrote: "The portfolio value is being calculated and it should be available in a week or two." (DE 35.) He proposed dinner on Thursday that week, two days after their email exchange and well before he claimed the portfolio value would be available. (*Id.*)

On April 22, Yoo, her husband, and her son had a social dinner with Montanino at Piccolo. (Tr. 318–21; *cf.* Resp.'s Br. 23 ("That evening may have been in part about me meeting her son Josh."); DE 35.) Montanino told her that her portfolio value was still being calculated, as he had told her nine days earlier. (Tr. 319–20 (Yoo); DE 35.)

On May 5, Montanino forwarded Yoo an investment confirmation with no information about her investment's value. (DE 37.) The next day, Yoo emailed Montanino again:

> Thank you for working hard to set my account up... 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 positions? 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.
>
> Thank you and I appreciate your personal attention.

(DE 39.) As Montanino admits, he did not reply to her email. (Tr. 1245–46.)

Montanino's testimony that he told the Yoos at the April 22 dinner — two weeks before Yoo's May 6 email — that her investment had lost at least $35,000 in value and that he had been fired from managing her account defies credulity. (Tr. 1232–33, 1283, 1285 (Montanino).) Why would Yoo email Montanino questions about her portfolio's value and investments if he had already told her that (1) he had been fired from managing it and (2) the portfolio had lost over 10% of its value? Montanino's only response is that, in May 2010, Yoo "strategically" created a false "paper trail." (Resp.'s Br. 23.) But if her email had been false and Montanino had in fact disclosed the truth to Yoo, Montanino would have immediately emailed Yoo back, corrected her, and reiterated in writing what he claims he had already told her orally. Montanino did no such thing. (Tr. 1245–46 (Montanino).) The evidence points

to only one conclusion: Yoo told the truth, and Montanino now seeks to discredit her.[8]

3. *Montanino Delayed Telling the Yoos the Truth To Conceal His Fraud.*

Montanino also contends that his delay in telling the Yoos the truth about their investment was not "outcome determinant" and that he had the best intentions in doing so. (Resp.'s Br. 16.) Nothing could be further from the truth.

Montanino's decision to delay telling Yoo — and instead to secretly try to convince Sullivan to redeem her investment (Resp.'s Br. 16) — did not stem from any benevolent motive. Had he genuinely had Yoo's best interests at heart, he would have revealed the truth immediately. Yoo would likely have hired a lawyer promptly and pursued legal action against Sullivan and Montanino to get her money back before Sullivan recklessly gambled away her entire investment. In fact, the Yoos ultimately retained a lawyer just days after Montanino disclosed to them in July 2010 that their investment had been wiped out. (Div. Br. 29.) But by then it was too late. (*Id.*)

Montanino hid the truth from Yoo for over a month because he hoped that Sullivan would quietly return her money before she hired a lawyer and discovered

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[8] Montanino also seeks to cast doubt on Yoo's testimony by attacking her recollection of the timing of certain events in 2010. (Resp.'s Br. 22–25.) Few witnesses have perfect recollection of the timing of events over four years before. Nevertheless, Yoo's central timeline was accurate, as emails and other documentary evidence corroborate. (Div. Br. 19–30.)

Montanino's fraud. Montanino's decision not to tell Yoo was not the "best decision" for her (Resp.'s Br. 16), but for himself.

II. MONTANINO DEFRAUDED AMERICAN EQUITY AND ITS INVESTORS.

Montanino's fraud on American Equity, Pankey, and other American Equity investors further results in Montanino's liability (either as a primary violator or as an aider and abettor) under the Securities, Exchange, and Advisers Acts. (Div. Br. 31–36, 45–51.) Montanino's factual defenses again rely on misstatements of the hearing evidence and his own implausible, self-serving testimony.[9]

A. Montanino's American Equity Presentation Defrauded Investors.

1. *Montanino Knew That the Presentation's Profit Projections Had No Rational Basis.*

The American Equity Presentation — which Montanino wrote knowing it would be used to solicit investors — represented that "Company Management believes that American Private Equity, LLC will become profitable very quickly and may only be in a cash flow negative position for 12 months or less." (DE 56 at 36; Div. Br. 32.) The presentation similarly projected that, if American Equity raised $5 million from investors, it would use the money to purchase "between $300–400 Million in financial assets within the first year" and be able to sell Calibourne for $35

[9] While Montanino contends — and the Division does not dispute — that he never served as an investment adviser to individual American Equity investors such as Pankey, Montanino does not address his advisory role as to American Equity, the private equity fund. (Resp.'s Br. 31.) In fact, Montanino served as an investment adviser to American Equity. (Div. Br. 45.)

million to $70 million — a seven- to fourteen-fold increase. (DE 56 at 37–39.) While Montanino argues that the Division offered no expert opinion that these projections lacked any reasonable basis, Montanino in fact proffered no basis, other than his own purported "belie[f] in [his] plan, and [his] own abilities." (Resp.'s Br. 40–41.)

To prove that the projections were fraudulent, the Division need only show that Montanino did not "reasonably believe the positive opinions [he] touted (i.e., the opinion was without a basis in fact or the speaker[ ] w[as] aware of facts undermining the positive statements)." *Lapin v. Goldman Sachs Group, Inc.*, 506 F. Supp. 2d 221, 239 (S.D.N.Y. 2006). Montanino could not have reasonably believed in his projections because he had no basis for them and knew "of facts undermining" them. *Id.* First, he knew Sullivan had made "completely reckless" trades in the American Fund earlier that year, causing the American Fund to collapse in about four months. (Div. Br. 24–25, 27.) Second, he knew that Sullivan had substance abuse problems. (*Id.* at 31.) Third, he knew that American Equity's and Calibourne's finances were precarious. (*Id.*) Finally, he knew that American Equity's plan to make money through Calibourne depended on Calibourne's ability to sell investments in American Fund II, American Fund's successor, to Calibourne's own advisory clients. (*Id.* at 30–31.) To do so, Montanino knew that he and Sullivan would have to conceal their track record — American Fund's quick collapse and Sullivan's reckless trading — from potential American Fund II investors, Calibourne's clients. (*Id.*) As Montanino knew or

recklessly disregarded, his projections therefore presented a deceptively rosy picture of Calibourne's prospects.

Indeed, Montanino's brazen contention that these projections must have been reasonable for Pankey to have invested $700,000 in American Equity defies credulity. (Resp.'s Br. 41.) Pankey believed in the projections because Montanino never told him the truth. As Pankey testified, Montanino never told him that Montanino had first formed Calibourne in 2005 and that American Equity and Calibourne had failed at their first venture in 2005. (Div. Br. 34.) That information alone would have raised questions about the investment in Pankey's mind. (Tr. 883 (Pankey).) Nor did Montanino tell Pankey that Sullivan had engaged in "completely reckless" trading at American Fund or that Montanino had worked for American Fund for less than a month before Sullivan had de-authorized him from its account. (Div. Br. 34.) No reasonable investor would have invested after such a disclosure.

2. *Montanino Knew the Biography He Wrote Was Misleading.*

Montanino also contends that his biography in the American Equity Presentation was either true or unintentionally misleading. (Resp.'s Br. 37–38 ("I possibly could have been clearer.").) Neither claim has any merit.

First, Montanino's biography misleadingly claimed that he "was recruited to be part of a team to open" Fidelity's Santa Monica investor center. (DE 56 at 40.) In fact, Montanino knew that Fidelity had not "recruit[ed]" him. (Div. Br. 11.) As Montanino

admits, he had lied on both the resume and certified job application he sent Fidelity, because he knew Fidelity would not otherwise have hired him. (Div. Br. 10–11.)

Second, Montanino's biography claimed that he had been "tasked with developing financial planning strategies, and providing investment management services for a client base with over $1 Billion in assets under management." (DE 56 at 40.) Montanino argues that, while his job description may have been unclear, Whatley "verified that my client base in the first two years of my employment at Fidelity very well could have been over $1 Billion." (Resp.'s Br. 35, 37–38.) Montanino mischaracterizes Whatley's testimony. Both Whatley's testimony and a Fidelity document Montanino offered into evidence show that, to the extent that Montanino had a customer base, those customers held about half as much: $400 to $500 million in assets at Fidelity. (Div. Br. 13.) While Montanino might have referred customers with $1 billion of assets to Fidelity's investment management division, he did not "provide services" to those customers. (Tr. 225–27 (Whatley).) Montanino deliberately misled investors into thinking that he had managed — picked stocks and other investments for — over $1 billion of Fidelity's customer assets. (Div. Br. 9–10, 11–13.)

B. Montanino Misappropriated $11,000.

After previously investing $600,000 in American Equity without any return, Pankey agreed to invest a final $100,000 in American Equity as long as his funds would be used solely to pay signing bonuses to Calibourne's newly hired investment

advisers. (Div. Br. 33–35.) Although Pankey made this clear to both Montanino and Sullivan in a phone call, Montanino tries to sidestep his misappropriation of $11,000 of Pankey's investment by denying that he participated in the call. (*Id.*; Resp.'s Br. 32; Tr. 1570–71 (Montanino).)

As Montanino admits, Pankey was a "highly successful business owner." (Resp.'s Br. 41.) Pankey initially invested $100,000 in American Equity based on Sullivan's representations. (Div. Br. 33.) In June 2010, Pankey invested another $500,000 in American Equity "as a vehicle for investing in Calibourne." (Div. Br. 33–34.) Montanino was an "active participant" in soliciting that investment. (*Id.*) As Montanino admits in his Answer (but refused to concede at the hearing), he and Sullivan assured Pankey in the "Summer/Fall 2010" that "a portion of" his investment would be used for Calibourne's formation expenses, including recruiting advisers to Calibourne. (*Compare* DE 138 ¶ 35 *with* Tr. 1274–77.)

When Montanino and Sullivan approached Pankey in early 2011 for a third investment to pay Calibourne's signing bonuses, Pankey had already sunk $600,000 into American Equity. (Div. Br. 34–35.) Pankey believed that, if he did not invest more, Calibourne would be unable to hire advisers, the venture would fail, and his entire $600,000 investment would be lost. (*Id.*) On a call with both Montanino and Sullivan, Pankey therefore agreed to invest $100,000 as long as his funds would be used solely to pay signing bonuses. (*Id.*)

Montanino's testimony that he did not participate in the call defies common sense. Pankey was a sophisticated businessman whose investment had so far returned nothing, and he knew that Montanino was Calibourne's chief executive officer. (Resp.'s Br. 41; Tr. 1280 (Montanino); Div. Br. 34–35; Tr. 799 (Pankey).) As Pankey testified, he would not have made a third investment without an explicit understanding with Montanino that Calibourne would use the funds only to pay signing bonuses. (Tr. 799–803 (Pankey).) Had Pankey told only Sullivan, Pankey would have had no assurance that Montanino — Calibourne's top officer — would agree to use Pankey's funds solely for signing bonuses and therefore would not have invested. Tellingly, Montanino admits that he did not tell Pankey he would use some of Pankey's investment to pay himself.[10] (Tr. 1280 ("That topic never came up.").)

C. There Is No Dispute That Montanino Received At Least $88,500 from American Equity.

By Montanino's own best estimate, he concedes that he received $88,500 for his role at American Equity, including $11,000 from Pankey's final investment. (R94 ("Estimate was derived to the best of my ability."); Resp.'s Br. 2 ("roughly $87,000") (citing R94); Tr. 1280–81.) Notwithstanding Montanino's inaccurate assertion that the

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[10] Montanino also claims that Pankey did not invest in American Equity based on Montanino's solicitation — that is, that Pankey did not rely on Montanino's misrepresentations and omissions. (Resp.'s Br. 5.) In fact, Pankey testified that he did rely on them. (Div. Br. 33–35.) Regardless, the Division need not show investor reliance to prove securities fraud. *See, e.g., SEC v. North Am. Research & Development Corp.*, 424 F.2d 63, 84 (2d Cir. 1970).

Division fails to credit him for the amount he transferred back to American Equity, the Division's precise calculation of ill-gotten gains — $89,340 — exceeds Montanino's estimate by only $840.[11] (Resp.'s Br. 29; Div. Br. 36–37.)

III. THE COURT SHOULD IMPOSE THE MAXIMUM RELIEF.

Montanino's fraud on Jones ten years ago demonstrates his high degree of scienter, the recurrent, egregious nature of his fraud, and the likelihood that he will commit fraud again. (Div. Br. 51–56 (analyzing *Steadman* factors).) Montanino's contention that he never defrauded Jones is implausible. (Resp.'s Br. 39–40.) First, he claims that, before Jones invested in American Equity, he told her that American Equity was funding Calibourne. (*Id.*; Div. Br. 6–8, 13–15.) That claim makes no sense, given his admission that he told Jones that Calibourne was a future plan with no clients and no revenue. (Div. Br. 6.) As Jones testified, she would never have invested one-fifth of her retirement savings in American Equity, if she had known it was investing in Calibourne, a start-up. (Div. Br. 6–7.) Second, as Montanino admits, when he "took" Jones' investment in American Equity one month later, Calibourne was already a "dead idea." (Tr. 1404, 1619–20.) This admission leaves only two possibilities: either Montanino failed to tell Jones that Calibourne was already a "dead idea," or he failed to tell her that American Equity was investing in Calibourne. Either way, Montanino defrauded Jones.

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[11] Montanino apparently does not dispute that prejudgment interest is warranted if the Court orders him to pay disgorgement. The Division's mathematical calculation of prejudgment interest (Div. Br. 54) is attached as Exhibit A.

Furthermore, Montanino continues to deny responsibility for his fraud. He tries to deflect blame for his own misrepresentations on Sullivan and Anthony Klatch.[12] (Resp.'s Br. 1–4, 42.) Having defrauded Yoo, Montanino even accuses her of lying. (*Id.* at 8, 18, 26.) Indeed, Montanino's story — implausible and inconsistent — defies credulity. His lies under oath show his past and future willingness to defraud victims into making worthless investments to benefit himself. For the safety of investors, the Court should impose the maximum relief against Montanino, including permanent industry and investment company bars.

CONCLUSION

For the reasons described above and in the Division Brief, the Court should hold Montanino liable for securities fraud, as alleged, and impose the maximum relief.[13]

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[12] In a complete reversal, Montanino now contends that Sullivan was an "active investor" in Calibourne. (Resp.'s Br. 31.) Both after Sullivan's death and in his hearing testimony, Montanino claimed that Sullivan was a "silent investment partner" in Calibourne. (DE 83 at 2; Tr. 1656–57.) Montanino also repeatedly invokes Klatch (Resp.'s Br. 1–2), whose name hardly appears in the hearing record.

[13] Although Montanino apparently seeks "lost wages" and "all expenses" incurred in his defense (Resp.'s Br. 43), sovereign immunity bars any such purported counter-claim for money damages. *See, e.g., Sprecher v. Von Stein*, 772 F.2d 16, 18 (2d Cir. 1985). Montanino's sole recourse would be to make an application under 5 U.S.C. § 504, which permits fees and other expenses to be awarded to a "prevailing party" in an administrative proceeding when, among other things, the Division's position is not "substantially justified." As described above, Montanino should not prevail and, regardless, the Division's position would be substantially justified. Montanino cannot therefore obtain any monetary award.

Dated: New York, New York
January 16, 2015

DIVISION OF ENFORCEMENT

By: _____

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Exhibit A

U.S. Securities and Exchange Commission

Division of Enforcement

Prejudgment Interest Report

Quarter Range	Annual Rate	Period Rate	Quarter Interest	Principal+Interest
Violation Amount				$89,340.00
12/01/2009-12/31/2009	4%	0.34%	$303.51	$89,643.51
01/01/2010-03/31/2010	4%	0.99%	$884.16	$90,527.67
04/01/2010-06/30/2010	4%	1%	$902.80	$91,430.47
07/01/2010-09/30/2010	4%	1.01%	$921.82	$92,352.29
10/01/2010-12/31/2010	4%	1.01%	$931.11	$93,283.40
01/01/2011-03/31/2011	3%	0.74%	$690.04	$93,973.44
04/01/2011-06/30/2011	4%	1%	$937.16	$94,910.60
07/01/2011-09/30/2011	4%	1.01%	$956.91	$95,867.51
10/01/2011-12/31/2011	3%	0.76%	$724.92	$96,592.43
01/01/2012-03/31/2012	3%	0.75%	$720.48	$97,312.91
04/01/2012-06/30/2012	3%	0.75%	$725.86	$98,038.77
07/01/2012-09/30/2012	3%	0.75%	$739.31	$98,778.08
10/01/2012-12/31/2012	3%	0.75%	$744.88	$99,522.96
01/01/2013-03/31/2013	3%	0.74%	$736.20	$100,259.16
04/01/2013-06/30/2013	3%	0.75%	$749.88	$101,009.04
07/01/2013-09/30/2013	3%	0.76%	$763.79	$101,772.83
10/01/2013-12/31/2013	3%	0.76%	$769.57	$102,542.40

Prejudgment Violation Range	Quarter Interest Total	Prejudgment Total
12/01/2009-12/31/2013	$13,202.40	$102,542.40

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SECURITIES AND EXCHANGE COMMISSION
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January 16, 2015

BY FACSIMILE & UPS OVERNIGHT DELIVERY

Ms. Denise Miller
Senior Program Information Specialist
Office of the Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: *In the Matter of David J. Montanino*, AP File No. 3-15943

Dear Ms. Miller:

Please find enclosed for filing in this matter (i) the Division's Post-Hearing Reply Memorandum of Law and Exhibit A thereto, and (ii) a certificate of service. The overnight delivery contains an original and three copies of each.

Respectfully submitted,

Danielle Sallah
Senior Counsel

Encls.

cc: Administrative Law Judge James E. Grimes (by email) (w/ encls.)
David J. Montanino (by email) (w/ encls.)