UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16223

In the Matter of

SANDS BROTHERS ASSET MANAGEMENT, LLC, STEVEN SANDS, MARTIN SANDS AND CHRISTOPHER KELLY,

Respondents.

RESPONDENT SANDS BROTHERS ASSET MANAGEMENT, LLC'S OPPOSITION TO THE DIVISION OF ENFORCEMENT'S MOTION FOR SUMMARY DISPOSITION

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STATUTES AND RULES

Respondent Sands Brothers Asset Management, LLC ("SBAM" or "Respondent"), submits its opposition to the Division of Enforcement's (the "Division") Motion for Summary Disposition (the "Division's Motion").

PRELIMINARY STATEMENT

On or about October 29, 2014, the Securities and Exchange Commission (the "Commission") commenced this proceeding with an Order Instituting Administrative Cease-and-Desist Proceedings ("OIP") against Respondent, Steven Sands ("S. Sands"), Martin Sands ("M. Sands") and Christopher Kelly ("Kelly").[1] The OIP alleges violations against SBAM of rule 206(4)-2 (the "Custody Rule") under the Investment Adviser Act of 1940 (the "Advisers Act") by delivering its funds' audited financial statements to investors beyond 120 days after the end of each funds' fiscal year, that S. Sands and M. Sands aided and abetted and caused SBAM's alleged violation. The OIP further alleges that all respondents violated a prior Commission Cease-and-Desist Order relating to violations of the Custody Rule.

On or about December 2, 2014, counsel for SBAM, S. Sands and M. Sands and the Division as well as the Administrative Law Judge ("ALJ") participated in a prehearing conference (the "Conference"). The ALJ issued an Order following the Conference on December 2, 2014 (the "Prehearing Order") setting forth the schedule for motions for summary disposition.

ARGUMENT

I. THE DIVISION'S MOTION FOR SUMMARY DISPOSITION IS BEYOND THE SCOPE

The Division's Motion exceeds the instructions of the ALJ as detailed during the Conference on December 2, 2014. During the Conference, the ALJ proposed to bifurcate this case, stating:

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[1] On November 17, 2014, Respondent submitted its answer to the OIP.

> I would expect anyway that if I were to resolve anything it might resolve the question of liability, [] but I would not necessarily expect that it would resolve the question of sanction if I were to get to the point of sanctions. So we might have to have a hearing in any event but I think that given the fact that the charges are not scienter based that it might be a way of streamlining the case and shortening the hearing if we were to have a round of dispositive motions first and then have a hearing.[2;3]

Counsel for the Division responded,

> That's totally in line with our views, Your Honor, I was going to raise that with **respect to the entity**. Because it's not a scienter based violation we think that it would be a fairly simple matter to establish for summary disposition the entity's valuation of the custody rule.[4;5]

During the Conference, counsel for Respondents advised the Division and the ALJ that the mental state of S. Sands and M. Sands are very relevant to the proceeding.[6]

The Division has exceeded the agreed to parameters for summary disposition against SBAM. The Division improperly asserts conclusions of fact to establish intent of SBAM and the state of mind of S. Sands and M. Sands as well as arguing in favor of third tier sanctions.[7] Crafting its motion in this manner is counter to the purpose of the more streamlined approach proposed by the ALJ. As a result, the Division's Motion raises many material issues of fact that defeat resolution by summary disposition.

II. STANDARDS FOR SUMMARY DISPOSITION

The Commission's Rules of Practice provide that the law judge "may grant the motion for summary disposition if there is no genuine issue with respect to any material fact and the party

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2 Citations to the transcript of the prehearing conference obtained by counsel for SBAM are referenced herein as "TR. at p.___, lines ____).

3 *See* TR. at p. 5, lines 12-22.

4 *See* TR. at pp. 5-6, lines 24-25; 1-4 (*emphasis added*).

5 It appears the Division has unilaterally expanded the scope of the agreed to motion practice addressed during the Conference by including conclusory and unsubstantiated assertions against Martin Sands and Steven Sands in its Motion.

6 *See* TR., p. 5, lines 5-7.

7 *See* Division's Motion, Section I(C), (D) and Section II.

making the motion is entitled to a summary disposition as a matter of law."[8] "At the summary disposition stage, the hearing officer's function is not to weigh the evidence and determine the truth of the matter, but rather to determine whether there is a genuine issue for resolution at a hearing."[9] Determining a motion for summary disposition the summary disposition record as well as the reasonable inferences that may be drawn from them, must be viewed in the light most favorable to the non-moving party.[10]

Summary disposition prior to a hearing in an enforcement or disciplinary proceeding is less likely to be appropriate. "Typically, enforcement and disciplinary proceedings that reach litigation involve genuine disagreement between the parties as to material facts. [] While partial disposition may be appropriate in some cases, a hearing will still often be necessary in order to determine *a respondent's state of mind* and the need for remedial sanctions if liability is found."[11] This is contrasted with the granting of summary disposition in cases where there are no material facts at issue such as follow-on proceedings or solely issues of sanctions to be determined.[12]

The only allegation in the Division's Motion appropriate for summary disposition which, SBAM concedes, is that the audited financials for year-end 2010, 2011 and 2012 were not distributed within the 120 days as required by the Custody Rule.

SBAM contests the factual conclusions asserted in the Division's Motion that SBAM recklessly disregarded the Custody Rule. Evidence presented at the hearing will demonstrate that SBAM employees responsible for obtaining information for the audited financial statements

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8 *See* 17 C.F.R. § 201.250.

9 *See* In the Matter of Amalgamated Explorations, Inc., Areawide Cellular, Inc., Genomed, Inc., Global Maintech Corp., Military Resale Grp., Inc., Verado Holdings, Inc., & World Transp. Auth., Inc., Release No. 397, 2010 WL 2233767, *1 (June 3, 2010).

10 *See* In the Matter of Michael Lauer, Release No. 369, 2009 WL 211383, *3 (Jan. 29, 2009).

11 *See* Rules of Practice, Exch. Act Release No. 35833, 1995 WL 368865, *66 (June 9, 1995) (*emphasis added*).

12 *See e.g.,* Seghers v. SEC, 548 F.3d 129, 134-35 (D.C. Cir. 2008); Brownson v. SEC, 66 Fed. Appx. 687, 688 (9th Cir. 2003).

engaged in continuous and concerted efforts to obtain valuation information for underlying fund assets necessary for the preparation of audited financials. SBAM, through its employees, acted in good faith to meet the Custody Rule deadlines and provide accurate and complete valuations in the audited financials. SBAM's failure was the result of relying on a misinterpretation of the Custody Rule that compliance with the 120 requirement was excused due to the need for completeness of valuations.

There is no basis in the instant matter that justifies SBAM being denied a hearing. The concept of third tier penalties in circumstances where no gain was obtain, no member of the public was damaged and the year-end audited financials were distributed more than demonstrates the Division's overreaching. A review of the OIP indicates that the Commission did not authorize the third tier penalties or the related draconian remedies sought by the Division.[13]

III. MATERIAL FACTS TO BE DETERMINED AT A HEARING IN ORDER TO DETERMINE ANY SANCTIONS

The sanctions sought by the Division are based on conclusory facts asserted by the Division which are not supported by the investigatory record. The Division asserts that SBAM's conduct in failing to distribute audited financials on time was "egregious" in light of prior violations, that "SBAM and [S. Sands and M. Sands] viewed the Custody Rule as a "mere technicality,"[14] neither SBAM, S. Sands and M. Sands "did anything to ensure no custody violations occurred,"[15] and that SBAM, "acting through [S. Sands and M. Sands] knew that it was not distributing the audited financials by the deadline."[16] As set forth more fully herein, the evidence will demonstrate that

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13 As set forth in the Division's Motion, revocation of SBAM's registration requires a finding of "willful" conduct by S. Sands and M. Sands. The division has failed to establish sufficient proof of S. Sands and M. Sands' mental state and therefore, the requested sanction against SBAM cannot be granted.

14 *See* the Division's Motion, p. 27.

15 *Id.* at p. 6.

16 *Id.* at p. 26.

SBAM acted in good faith to comply with the Custody Rule deadlines and that any failures were not the result of egregious or willful conduct.

A. SBAM's Compliance Initiatives and Structure Belie the Division's Factual Assertions

The Division attempts to paint SBAM as a rogue entity that flouts the rules, as none of the respondents did anything to ensure there were no custody violations.[17] In support of this factual conclusion the Division seeks to draw a negative inference from Kelly's testimony before the Commission wherein, he stated that he did not recall any changes to SBAM's policies and procedures after the October 2010 Consent Cease and Desist Order (the "2010 Order").[18] In fact, the questioning by the Commission's staff was fundamentally flawed on this point as they did not seek information as to whether Kelly made any changes to the compliance structure or procedures at SBAM.

As will be demonstrated at the hearing, the reason that Kelly did not implement changes after the 2010 Order was because Kelly overhauled SBAM's compliance program upon being hired in 2008.[19] Such overhaul included, without limitation compliance with the Custody Rule and addressed the conduct at issue in the 2010 Order, which occurred in 2007.

Significantly, Kelly's revised procedures clearly delineate the responsibilities for compliance at SBAM:

> Steven Sands, the Firm's Mangers, shall be responsible for ensuring that the Firm provides adequate resources to the persons with the responsibilities for implementing an effective compliance program for the Firm. [] Where the Firm maintains possession or custody of client funds/securities, the **Chief Compliance Officer** shall ensure compliance

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17 *Id.* at p. 6

18 *Id.*

19 The Division concedes that in 2008, Kelly made substantial changes to the firm's compliance manual. *See* the Division's Motion, p. 14.

with the restrictions and requirements of *Rule 206(4)-2 adopted under the Advisers Act*.[20]

The evidence presented at a hearing in this matter will demonstrate there was a clear and reasonable delegation of responsibility to Kelly as Chief Compliance Officer for all compliance matters and his authority as Chief Operating Officer empowered Kelly to oversee the audit process.[21] The Division does not assert that Kelly did not possess the necessary expertise and experience to act as Chief Compliance Officer at SBAM. As Chief Compliance Officer, and as an attorney advising investment advisers on regulatory matters, Kelly was required to understand and had the ability to understand the Custody Rules as they applied to SBAM. Kelly testified that he would remind SBAM employees about audit deadlines, [22] participated in communicating with auditors and assisting in obtaining information for valuations of the underlying assets of the various funds for the audited financials.[23]

Kelly should have known about the Commission's guidance relating to preparing audited financials set forth in the release of the final rule which addressed the scenario involving difficulty in valuing privately-offered securities. Kelly's failure to comport SBAM's conduct with the Custody Rule prevented SBAM employees, who were responsible for preparing valuations, from learning of the alternative methodology for distributing audited financial statements.

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[20] The Division's Motion, p. 14, quoting Ex 39 (2009 Compliance Manual) at 1, 18-19 (*emphasis in original*).

[21] The Division's Motion states that Kelly's simultaneous role as Chief Operating Officer made him responsible for all of SBAM's "operations which do not involve investment decision-making." *See* the Division's Motion, p. 24, quoting Ex 9, at 3 and Ex 10.

[22] The Division's Motion states that Kelly "testified that he repeatedly reminded everyone in the working group-including the Sands—of the Custody Rule deadlines." *See* The Division's Motion, p. 20, citing Ex 6, p. 15, lines 15-22 and p. 20, lines 23-21, and p. 5.

[23] The Division's Motion states that "Kelly engaged the auditors, and the email correspondence reflects, he was on of the auditors' primary contacts at SBAM." *See* The Division's Motion, p. 24, referencing Exs 17, 25-27, 29, 32-33, 37 and 41.

SBAM employees relied in good faith on Kelly's misinterpretation of the valuation and completeness requirement for the distribution of audited financials under the Custody Rule. Evidence will be presented at the hearing that will demonstrate that SBAM employees engaged in continuous and ongoing efforts to obtain valuation information for the underlying assets of the subject funds. SBAM employees believed in good faith that complete and accurate valuation information was necessary for preparation of audited financials.

Further evidence of SBAM's commitment to compliance will be demonstrated through the evidence of reports submitted by SBAM's independent compliance consultant, Richard Slavin, Esq. ("Slavin"). During the relevant time period, pursuant to an agreement with the Connecticut Department of Banking (the "Department"). Slavin was tasked to audit, make recommendations and submit reports of his conclusions to the Department relating to SBAM's compliance structure and procedures. Slavin provided testimony during the Commission investigation, which led to this matter. Slavin testified that he reviewed the new compliance manual and interviewed Kelly.[24] As part of Slavin's initial review, he created an outline of the Investment Advisers Act of 1940 and specific rules and an outline of the new compliance manual and tested Kelly and the compliance system.[25] Slavin understood that if he found any deficiencies or weaknesses he was to put them in a report, which he did.[26] Slavin testified that he was made aware of the 2010 Order and discussed it with Kelly.[27] Slavin testified that he was required to highlight any compliance deficiencies and make recommendations and if there had been a violation of the 2010 Order it may have been a compliance deficiency.[28]

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24 *See* the Division's Motion, Ex 10, p. 28.
25 *See* the Division's Motion, Ex 10, p. 29.
26 *Id.* at Ex 10, p. 41-42.
27 *Id.* at Ex 10, p. 82.
28 *Id.* at Ex 10, p. 91.

Slavin's testimony along with his reports that will be presented as evidence at the hearing demonstrates that SBAM was aware of its compliance obligations including, the Custody Rule. Slavin's testimony, as well as his reports, will demonstrate that SBAM was willing and did implement recommendations from Slavin to improve its compliance program. Moreover, Slavin's testimony and reports will confirm that Kelly was unequivocally responsible and sufficiently empowered effectuate the compliance program at SBAM. Based on such evidence, the Division will fail to prove that SBAM's conduct in failing to timely distribute the audited financials was the result of a disregard of the rules or in any way egregious.

B. Third Tier Sanctions Require a Showing of Public Harm or Loss to Investors

Third tier penalties are appropriate if a respondent willfully violated the Adviser Act and a penalty is in the public interests.[29] As set forth in the Division's Motion, "the third (highest)" tier is reserved for conduct involving a 'deliberate or reckless disregard of a regulatory requirement," and "such act or omission...created a significant risk of substantial losses to the other persons.'"[30]

Third tier sanctions are inappropriate in this matter. As a threshold matter, third tier sanctions requires a showing of public harm and investor loss. The Division concedes there was no evidence of investor loss.[31] None of the respondents had any pecuniary gain as a result of the untimely distribution of the audited financial statements. In addition, the Division has not proven that there is a public harm. Evidence will be presented at the hearing that investors in the various funds were provided periodic financial updates which kept them apprised of their investment. Therefore, the Division has failed to meet its burden to substantiate third tier sanctions.

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29 *See* 15 U.S.C. § 80b-3(i).

30 *See* the Division's Motion, p. 31 quoting 15 U.S.C § 80b-3(i)(1)(B)(2)(C)(i) and (ii).

31 *See* the Division's Motion, p. 32.

Moreover, the statutory language requires a finding of an actor's state of mind, "deliberate" or "reckless." Summary disposition of the penalty to allow third tier sanctions in inappropriate because a finding of intent is required. As set forth herein, there is substantial factual matters that must be presented at a hearing to establish SBAM's good faith effort to comply with the Custody Rule and its continuous efforts to revise its compliance. Such evidence will prove the Division's conclusory statements, that SBAM's "flagrant disregard for their Custody Rule obligations," is untrue.[32]

The Division purposely overstates the number of violations engaged in by SBAM to enflame the nature of the violation. As set forth above, the violations complained of stemmed from a misunderstanding of the Custody Rule and lack of awareness of the alternative methodology for allowing a non-current asset valuation to be included in an audited financial report. This is one good faith misunderstanding, not thirty.

CONCLUSION

Wherefore, Respondents SBAM respectfully request an order be issued denying the Division's request for summary disposition against it and for such other and further relief deemed appropriate by the Administrative Law Judge.

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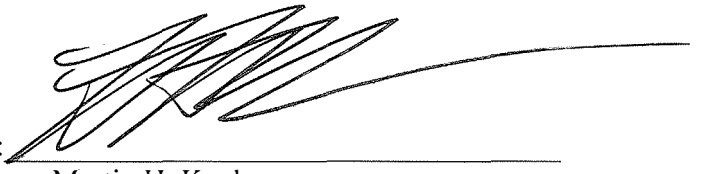
32 *Id.*

Respectfully submitted,

Dated: New York, New York
February 12, 2015

GUSRAE KAPLAN NUSBAUM PLLC

By: 

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Re: Administrative Proceeding File No. 3-16223

Dear Hon. Cameron Elliot,

This firm represents Respondent Sands Brothers Asset Management, LLC ("SBAM") in the above-referenced matter. Enclosed herewith for filing is an original and three (3) copies of Respondent SBAM's Opposition to the Division of Enforcement's Motion for Summary Disposition.

Should you have any questions please contact me or in my absence, my associate Robyn D. Paster, Esq.

Very truly yours,

Martin H. Kaplan /DH

Martin H. Kaplan

Encl.

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