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.

DIVISION OF ENFORCEMENT'S REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF ITS MOTION FOR SUMMARY DISPOSITION AGAINST RESPONDENTS

DIVISION OF ENFORCEMENT
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Dated: February 23, 2015

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The Division of Enforcement (the "Division") respectfully submits this Reply Memorandum of Law in Further Support of its Motion for Summary Disposition Against Respondents.

Preliminary Statement

Respondents' opposition briefs make clear why Sands Brothers Asset Management, LLC ("SBAM") continued, year after year, in the face of a Cease-and-Desist Order, to violate the Custody Rule: Everyone with responsibility for ensuring SBAM's compliance with the Rule disclaims that responsibility. Steven Sands ("S. Sands") and Martin Sands ("M. Sands") (collectively, "the Sands") say that it was Christopher Kelly's ("Kelly") job to ensure compliance. Kelly says that it was the Sands who had control over SBAM's compliance.

The record shows that they all shared responsibility and they all failed to satisfy it. On this record – which is undisputed as to all material facts – summary disposition should be granted against all Respondents and the appropriate relief the Division seeks should be awarded. On this undisputed record, there is no need for a hearing.

ARGUMENT

I. SBAM CONCEDES THAT IT VIOLATED THE CUSTODY RULE, MAKING SUMMARY DISPOSITION AGAINST IT APPROPRIATE

Not one Respondent contests that, for the three years after SBAM entered into a Cease-and-Desist Order with the Commission, it delivered audited financial statements to investors in SBAM-managed funds after the 120-day Custody Rule deadline. See 17 C.F.R. § 275.206(4)-2(b)(4) (the "Custody Rule"); (SBAM Br. [1] at 3; Kelly Br. at 10-11; Sands Br. at 14).

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[1] "SBAM Br." refers to SBAM's Opposition to the Division of Enforcement's Motion for Summary Disposition, dated Feb. 12, 2015. "Sands Br." refers to the Sands' Opposition to the Division of Enforcement's Motion for Summary Disposition, dated Feb. 13, 2015. "Kelly Br." refers to Kelly's Opposition to the Division of Enforcement's Motion for Summary Disposition, dated Feb. 3, 2015. "Mov. Br." refers to the Division's Motion for Summary Disposition

In fact, SBAM explicitly acknowledges that it violated the Rule: "SBAM concedes . . . 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 Br. at 3.) It even concedes that summary disposition would be appropriate against it on this issue. (Id.)

As SBAM concedes its liability, the Court should enter judgment against it for violating the Rule.

II. SUMMARY DISPOSITION IS APPROPRIATE AS TO THE SANDS

A. The Sands Have Not Met Their Burden of Presenting Evidence to Demonstrate a Genuine Issue of Material Fact

Although provided with an opportunity to respond to the Division's Motion and evidence, the Sands have offered no evidence at all to create any issue of disputed fact. In fact, in much of their brief, they implicitly or explicitly concede the facts and evidence supplied by the Division: for example, they do not deny that they knew that SBAM had not complied with the 120-day delivery requirement (Sands Br. at 14); and they do not deny that they participated in the audit process or that M. Sands refused to allow financial statements to go out by the deadline because he wanted to wait to review all of the financial statements at once (id. at 15 n.56; see generally id. at nn.2-16 (citing Division's Motion and attached exhibits)). At most, the Sands offer their lawyer's unsupported argument and promises to present evidence later, at a hearing, to support their primary defense: that they were simply "unaware that SBAM's efforts to comply with the Custody Rule were not successful during the relevant period," because the Compliance Manual delegated the sole responsibility for compliance to Kelly alone. (Sands Br.

Against Respondents SBAM, the Sands and Kelly and Memorandum of Law in Support, dated Jan. 15, 2015.

at 10, 12.) But the Commission has been clear that such unsupported argument and vague promises will not defeat summary disposition where the Division's evidence goes unrebutted.

As we noted in our Moving Brief (Mov. Br. at 17), the Commission has not solely reserved summary disposition for follow-on proceedings or instances where the only issue is sanctions, as both SBAM and the Sands argue. (Sands Br. at 6-7; SBAM Br. at 2-3.) Indeed, as recently as December 2014, the Commission overturned an ALJ's decision to deny summary disposition in a non-follow-on proceeding just like this one, where sufficient undisputed evidence existed to grant the Division's motion. Matter of S. W. Hatfield, CPA, No. 3-15012, 2014 WL 6850921 (S.E.C. Dec. 5, 2014); see also Rule of Practice 205(b).[2]

The Sands cannot create an issue of material fact through attorney argument. Once the Division carried its burden to show that the Sands intentionally or recklessly aided, abetted and caused SBAM's violations (Mov. Br. at 18-23, 25-26), the burden shifted to the Sands to "'present facts demonstrating a genuine issue of fact that is material to the charged violation'" to defeat summary disposition. Matter of Absolute Potential, Inc., No. 3-14587, 2014 WL 1338256, at *5 (S.E.C. April 4, 2014) (citations omitted). The opposing party "may not rest upon mere allegations or denials of [the movant's] pleadings." Matter of Executive Registrar & Transfer, Inc., No. 3-12996, 2008 WL 5262371, *1 (Initial Decision Dec. 18, 2008); accord Matter of China-Biotics, Inc., No. 3-14581, 2013 WL 5883342, at *16 (S.E.C. Nov. 4, 2013) (in

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[2] Contrary to the Sands' claim that the Court "acknowledged" that a motion for summary disposition would be inappropriate as to the individual respondents at the December 2, 2014 pre-hearing conference (Sands Br. at 7-8), the Court actually confirmed the propriety of such a motion. When the Division said at that conference that it had planned to raise the issue of summary disposition as to SBAM, the Court stated, "I'm not sure that I see the distinction between the entity and the individuals since the entity only acts through the individual officers . . . ." (Declaration of Janna I. Berke in Support of the Division's Opposition to Kelly's Motion for Summary Disposition, executed Feb. 12, 2015 ("Berke Feb. 12, 2015 Decl."), Ex O at 6:5-7.)

opposition to summary disposition the respondent must do more than proffer "bare allegations or denials").

The Sands' unsworn references to unspecified evidence, together with their promise to present it later at a hearing, are not facts demonstrating a genuine issue of material fact. (E.g., Sands Br. at 1 ("there is ample evidence that . . . the Sands exercised reasonable care by relying on SBAM's qualified and experienced Chief Compliance Officer"); 9 ("evidence will be presented at hearing which will demonstrate that M. Sands and S. Sands took significant steps to institute a robust compliance structure at SBAM"); 17 ("Evidence will be presented at the hearing that investors in the various funds were provided periodic financial updates."). As the Commission has ruled, Rule 250 excuses a respondent's obligation to present evidence in opposition *only* where the party shows that he cannot "for good cause shown." Matter of Robert L. Burns, No. 3-12978, 2011 WL 3407859, at *6 (S.E.C. Aug. 5, 2011) (rejecting Respondent's claim that summary disposition was improperly entered against him where he argued that he would have presented evidence at a hearing sufficient to defeat the Division's claims, but offering no reason why he could not do so in opposing the Division's Motion).[3] The Sands had the opportunity to present their evidence, and they declined to take advantage of it, or show why they could not.

For those reasons alone, the Division's motion against the Sands should be granted.

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[3] SBAM makes the same ineffective promises to present evidence at a hearing. (E.g., SBAM Br. at 9 ("there is [sic] substantial 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.") But in SBAM's case, because the violation is non-scienter based, SBAM's good faith is irrelevant to its liability. As to remedies, SBAM's failure to adduce evidence now in opposition cannot defeat summary disposition for the reasons set out in Burns.

B. The Sands Cannot Delegate Away Their Custody Rule Functions

Even if the Sands had submitted sworn declarations or other evidence, it would not defeat the Division's Motion. At bottom, the Sands' whole argument is premised on their claim that they signed over Custody Rule compliance duties to Kelly, and thought he was executing them. (Sands Br. at 9-10, 12-15.) If true, that conduct alone is sufficient to support a finding of recklessness because those in charge of Investment Advisers – those who are, as in this case, the firm's named co-partners, co-principals and co-chief executives – cannot simply delegate a duty without ever inquiring whether their delegate is properly performing.

As a starting point, the Sands' only evidence that Kelly retained sole and exclusive authority for SBAM's compliance with the Custody Rule is the Compliance Manual. But, as the Division noted in its Moving Brief, that same Compliance Manual places compliance responsibility on the Sands as well, assigning them overall authority to ensure that the compliance program has sufficient resources, and requiring their yearly certification that they are familiar with, and have abided by, all applicable laws and regulations and that they have carried out all duties imposed on them under the Manual. (Mov. Br. at 14-15; Declaration of Nancy A. Brown in Support of the Division's Motion for Summary Disposition, executed Jan. 15, 2015 ("Brown Jan. Decl."), Ex. 39 at Section I.B, I.E; Ex. 40 ¶¶ 2-3, 8; accord Affidavit in Support of Kelly's Opposition to the Division's Motion for Summary Disposition, sworn to Feb. 3, 2015 ("Kelly Aff.") ¶ 14.) Thus, while the Compliance Manual assigned Kelly specific responsibility for compliance with the Custody Rule, it equally assigned responsibility for compliance with all rules and regulations to the Sands. If they made no efforts in that regard, they cannot shift all of the blame to Kelly.

The undisputed evidence –further corroborated by Kelly – also shows that the Sands wielded over-arching control over SBAM. (See Kelly Aff. ¶¶ 9-11.) The Sands do not dispute that their families own the firm, or that they acted as principals, co-partners, and co-chief executives of SBAM. (Brown Jan. Decl., Ex. 3 (SBAM website profiles); Ex. 9 (2012 Slavin Report) at 3).)[4] They were also each designated a "control person" on SBAM's ADV filings in each of the years at issue, along with Kelly. (Id., Ex. 5 (2012 ADV) at 125-26.) Under the ADV Glossary of Terms, "control" is defined as "the power, directly or indirectly, to direct the management or policies of a person," and notes that "[e]ach of your firm's officers, partners, or directors *exercising executive responsibility* . . . is presumed to control your firm." Available at http://www.sec.gov/about/forms/formadv-instructions.pdf. None of this is disputed by the Sands.

Notwithstanding this evidence, the Sands contend that whatever responsibility they had to assure SBAM's compliance with the Custody Rule they delegated to Kelly and blindly trusted that he was satisfying that obligation. (E.g., Sands Br. at 10 ("Kelly—and not The Sands—had full authority for compliance at SBAM."); 12 ("The Sands themselves had no duty to ensure compliance").) This argument fails as a matter of law. The Commission has long held that a firm's principal always retains a duty to follow-up on his delegation to ensure that it is being properly exercised; he may not "'simply wash his hands of the matter until a problem is brought to his attention.'" Matter of Midas Secs., LLC, No. 3-14308, 2012 WL 169138, at 13 (S.E.C. Jan. 20, 2012) (holding president of brokerage firm responsible for failure to supervise despite

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[4] SBAM was a small adviser and never employed more than 12 people, including the Sands, their mother (as a consultant) and two drivers. (Berke Feb. 12, 2015 Decl., Ex. C (Slavin 2009 Report), at SB000004-05; Ex. E (Slavin June 2010 Report), at SB 000224; Ex. G (Slavin Dec. 2010 Report), at SB000245; Ex. I (Slavin 2011 Report), at SB000579.) Thus, SBAM was not a financial conglomerate, where an executive could argue that it would be impossible to monitor thousands of employees individually.

his claim that he delegated his duties to another) (citations omitted); Matter of Angelica Aguilera, No. 3-14999, 2013 WL 3936214, *21-24 (Initial Decision July 31, 2013) (same).[5]

In a case close to the one at hand, the CEO of a brokerage and advisory firm was held liable for the firm's record-keeping failures because he had delegated all record-keeping responsibility without checking to make sure that his delegate had satisfied his obligations. Matter of Marc N. Geman, No. 3-9032, 2001 WL 124847, at *17 (S.E.C. Feb. 14, 2001), aff'd, 334 F.3d 1183 (10th Cir. 2003). The Commission held:

> Despite Geman's direct knowledge of [a] change in the Firm's reporting procedures, he took no steps to ensure that – or inquire whether – [the firm] was making alternative arrangements to satisfy recordkeeping obligations. Geman's inaction, which was at the very least reckless, amply supports a finding that he willfully aided and abetted the Firm's recordkeeping violations.

Id.

So it is here. The Sands admit that they each consented to a Cease-and-Desist Order in 2010 that found that "SBAM violated the Custody Rule by not timely distributing year end 2007 audited financials to investors and that The Sands aided and abetted and caused SBAM's violations." (Sands Br. at 4.) But, according to their Opposition Brief, in the wake of that Order, they did nothing more than leave it to Kelly to assure that SBAM would comply with the Rule going forward. If that is so, they offer no grounds to defeat the Division's motion because, in the face of an Order holding them responsible for SBAM's compliance with the Custody Rule, they were at least reckless to transfer that obligation to Kelly without taking any steps to make sure he was complying.

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[5] In their 2009 Wells Submission, the Sands conceded that the law applicable to delegation by supervisory personnel in broker dealer cases under the Exchange Act applied with equal force in the Adviser Act context to delegation of compliance duties. (Declaration of Janna I. Berke in Support of the Division's Reply Brief, executed February 23, 2015 ("Berke Feb. 23, 2015 Decl."), Ex. 1, at 6.)

The Sands' failure to follow up on their purported delegation was especially reckless in light of the obvious red flags that existed as to SBAM's Custody Rule violations. See Midas Secs., 2012 WL 169138, at *12-13; Geman, 2001 WL 124847, at *17 n.72; Matter of James L. Owsley, Rel. No. 34-32491, 1993 WL 226056, at *1, 9-10 (S.E.C. June 18, 1993) (holding that CEO, and President and CCO could not avoid liability for delegated compliance responsibilities where both encountered red flags). They knew or were reckless in not knowing that one of the Custody Rule violations sanctioned by the 2010 Order was SBAM's untimely distribution of audited financial statements.[6] (Brown Jan. Decl., Ex. 16 (Sands Offer of Settlement leading to 2010 Order, signed by the Sands) at 8.) They knew or were reckless in not knowing that the Custody Rule imposed a 120-day deadline. (Id., Ex. 39 at Section IX.D.5 (Compliance Manual provision citing 120-day deadline); Ex. 40 (Acknowledgments that the Sands had "read and understand[] the information contained in the [Compliance] Manual") at SB 000027, SB 000029; Ex. 6 (Kelly Tr.) at 15:15-22 (Kelly "remind[ed] people of deadlines" vis-à-vis the Custody Rule).) They knew that the audited financial statements were being delivered after the 120-day deadline. (Sands Br. at 14; Brown Jan. Decl., Ex. 31 (Management Representation Letters, all signed after April 30).) And they knew at least as of June 2012 that the SEC was making inquiries about the timing of the distribution of the Funds' audited financial statements. (Brown Jan. Decl., Ex. 38.) All of these were sufficient red flags to trigger the Sands' responsibility to at least inquire how SBAM was complying with the Rule.[7]

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[6] The Sands do not argue that they did not understand the 2010 Order. Nor could they. As the court held in Executive Registrar, 2008 WL 5262371, at *30, if a respondent claims not to understand a prior Commission order, it merely "demonstrates [respondent's] indifference to following the rules and regulations . . . and his apathy toward the importance of abiding by such rules and regulations." Id.

[7] In attempting to distinguish it, the Sands mischaracterize Hatfield, claiming that, there, the respondents had "actual knowledge of their wrongful conduct." (Sands Br. at 9.) In fact,

Finally, the Sands' alleged wholesale abdication of their responsibility to Kelly after 2010 is even more reckless in light of their history and pattern of unquestioning delegation and the regulatory trouble that decision had already brought them. In their 2009 Wells Submission, like here, the Sands claimed that they should not be blamed for SBAM's earlier compliance violations because they had delegated all responsibility for compliance to SBAM's CCOs:

> Martin and Steven Sands believed that their delegation to the various Chief Compliance Officers was reasonable and appropriate. At no time during their respective tenures were either Martin or Steven Sands notified nor did they have reason to believe that each of the various Chief Compliance Officers were not doing their jobs in a competent way.

(Berke Feb. 23, 2015 Decl., Ex. 1 at 7; see generally id. at 3-7.) To explain their faith in those CCOs, they highlighted the sterling reputations of each of them, just as they try to impress Kelly's reputation on the Court now. (Id. at 3-5.)

The Sands do not explain here, however, how they could have reposed the same blind trust in Kelly after they consented to aiding and abetting liability in the 2010 Cease-and-Desist Order. Although the Sands blamed their unquestioning, but unwise, faith in their former compliance officers for SBAM's compliance failures found in the 2010 Order, they maintain now that they did nothing after that to make sure that this CCO was properly doing his job. Nor do they explain why they, like the CEO in Geman, *never even asked* Kelly how it was that SBAM could miss the 120-day deadline year after year and still be in compliance. They simply

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however, the Commission found that the Hatfield respondents, like the Sands, were "at least reckless." "It is implausible," the Commission found, "that Respondents did not know that having a valid license was a prerequisite for holding themselves out as CPAs." (Id.) Moreover, authorities had previously warned respondents that their licenses were going to expire and of the consequences of non-renewal. Under these circumstances, the Commission found sufficient scienter for summary disposition. Here, too, the Sands' refusal to investigate obvious red flags that SBAM was violating the Custody Rule makes them at least reckless, and provides the basis for summary disposition.

argue that they were "unaware that SBAM's efforts to comply with the Custody Rule were not successful." (Sands Br. at 10.) If so, like the CEO in Geman, and especially after their faith in previous CCOs had proved misguided, their inaction was reckless.

The Sands' delegation argument is a demonstration of willful blindness and recklessness in the extreme in light of their prior violations, and supports entry of judgment against them.[8]

III. SUMMARY DISPOSITION IS APPROPRIATE AS TO KELLY

Kelly's brief raises two main arguments, both of which are flawed as a matter of fact and a matter of law.

Kelly's contention that the IM Q&A provided an exemption from the Custody Rule for SBAM is the same one he made in his own Motion for Summary Disposition, and he offers little new to support it. (Kelly Br. at 2-3.) As the Division argued in Opposition, his reading of the Q&A is wrong, and any reliance he placed on it was rendered unreasonable by the Q&A's warnings against such reliance. More to the point, Kelly's reading of the Q&A would make the Custody Rule meaningless. (Opp. Br.[9] at 12-17.) As the Adopting Release makes clear, the Commission sees the Custody Rule as an important mechanism to protect investors (Mov. Br. at 27-28); it is therefore unlikely to agree with Kelly's interpretation of the Q&A, which would so easily exempt Advisers from its requirements, particularly those like SBAM which had already been ordered to comply.[10]

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[8] Because their delegation argument fails, so too does the Sands' attempt to distinguish the case law cited in the Division's Motion under the rubric that those respondents had a duty to act, but the Sands did not. (Sands Br. at 12-14.) Since their arguments against causing are based on the same flawed delegation premise (id. at 16-17), they too are inapposite.

[9] "Opp. Br." refers to the Division's Opposition to Kelly's Motion for Summary Disposition, dated Feb. 12, 2015.

[10] Kelly argues that the Custody Rule cannot mean what it says because "fund of funds" are given 180 days to circulate audited financial statements, a provision not found in the text of the Rule itself. However, the Commission implicitly adopted that exception in implementing the

Contrary to his claim that he was not a control person (Kelly Br. at 6-7, 9-10), the ADV Kelly prepared (and certified under penalty of perjury) identifies him as one, along with the Sands. (Brown Jan. Decl., Ex. 5 (2012 ADV) at 125-28, 146.) To the extent that he argues that he lacked the authority to bring SBAM in line, his titles of CCO and COO tell a different story. And he does not deny that the Compliance Manual that he rewrote assigned the Custody Rule compliance responsibility to him.[11] (Id., Ex. 39, at 18.) That he had no background in finance is irrelevant. (Kelly Br., passim.) If SBAM could not circulate its audited financial statements on time year after year, Kelly had a responsibility to do something about it – to seek out other ways to comply with the Custody Rule, such as through a surprise examination during the fiscal year; to hire additional personnel; to hire new auditors or lawyers or administrators; to implement new policies. He did none of that. For that, Kelly bears responsibility. (See Opp. Br. at 3-6.)

Kelly's arguments that he had none of the authority his titles would suggest further fail as a matter of law. In Matter of Aguilera, the President and Financial and Operations Principal of a broker-dealer was charged with failure to supervise a registered representative and a back office employee, who were alleged to have engaged in a markup/markdown scheme to defraud two

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Custody Rule Amendments enacted in 2010. (Custody of Funds or Securities of Clients by Investment Advisers, Rel. No. IA-2968, 2009 WL 5172038, at *6 n.45 (Dec. 30, 2009) (Final Rule) ("Adopting Release") (citing ABA Committee on Private Investment Entities, 2006 WL 5440662 (Aug. 10, 2006)). Moreover, the IM Q&A is prefaced by warnings that it is not binding on the Commission.

[11] Kelly, who previously touted his overhaul of the Compliance Manual because it had simply been "based on an off-the-shelf template," (Brown Jan. Decl., Ex. 8 at 6), now argues that the Custody Rule provision in the *revised* manual is "stock Compliance Manual language found in many Compliance Manuals." (Kelly Br. at 6.) Whatever revisions he did make, however, his overhaul of "the firm's compliance policies" (Sands Br. at 2) did not make any change to the assignment of Custody Rule Compliance; it still remained the responsibility of the CCO, as it did pre-Kelly. (Berke Feb. 23, 2015 Decl., Ex. 2 at SEC-NY8127-000155789.) That assignment did not preclude the Commission from finding that the Sands were responsible for SBAM's Custody Rule violations, and it should not here.

Brazilian pension funds. 2013 WL 3936214 . In contesting her liability, the Respondent – similar to Kelly here – argued that she did not have the training or background to carry out responsibilities assigned to her in the firm's policies, and that she was a "figurehead" who deferred to those with effective control of the firm. Id. at *21-24. The Court rejected those arguments, holding that if the firm's policies were inaccurate, she should have rewritten them. Id. at *23-24. It further held that her claim that she lacked training and was a "figurehead" were arguments long rejected by the Commission. "'We recognize that [respondent] was more or less a figurehead president. However, once he accepted that title, he was required to fulfill the obligations attached to his office for as long as he occupied the position, a duty he failed to discharge.'" (Id. at *24 (quoting Matter of Kirk A Knapp, No. 3-7231, 1992 WL 40436, at *5 (S.E.C. Feb. 21, 1992).)

As CCO and COO, Kelly had a duty to bring SBAM into Compliance with the Custody Rule. That was a duty he failed to discharge.

IV. SANCTIONS SHOULD BE GRANTED

A. The Division's Request for Sanctions Is Appropriate

Both SBAM and the Sands argue that the Division exceeded the scope of the Court's authorization to move for summary disposition by requesting sanctions. (SBAM Br. at 1-2; Sands Br. at 7-8.) The Court was very clear that its motive was to streamline the case and shorten any hearing that might be necessary through motions for Summary Disposition. (Berke Feb. 12, 2015 Decl., Ex. O (Dec. 2, 2014 Hearing Tr.) at 5:17-22, 7:4-8 (discussing the need for a hearing, if any).) The Division's motion satisfies that goal. The Court put no limitation on the content of the Division's motion and, as such, the Division's submission of a motion that

potentially resolves all issues in this case is fully in keeping with the language and spirit of the parties' discussion at the December 2 Court Conference.[12]

B. SBAM's Registration Should Be Revoked under Section 203(e)

SBAM's registration should be revoked. SBAM concedes that it violated the Custody Rule. All Respondents concede that it missed the 120-day deadline in the wake of the Commission's 2010 Order which ordered SBAM to cease-and-desist from further violations. And all agree that SBAM's failure to deliver timely its financials occurred repeatedly for each of the next three years. No one disputes that SBAM's violations were willful, under that term's legal definition. Accordingly, based on these undisputed facts, revocation of SBAM's registration is in the public interest.

Under Section 203(e), revocation may ordered where the investment adviser has "willfully violated any provision of . . . this title," 15 U.S.C. § 80b-3(e)(5), and "revocation is in the public interest." Id. § 80b-3(e). SBAM argues that, in order to find that it "willfully" violated the Custody Rule, the Division must show scienter on the part of the Sands. (SBAM Br. at 4 n.13.) This the Division has already done. (Mov. Br. at 18-23 and supra, Section II.B.) But, even if it had not, a finding of willfulness does not require a finding of "intent to violate the law, but merely intent to do the act which constitutes a violation of the law." Matter of Peak Wealth Opportunities, LLC, No. 3-14979, 2013 WL 812635, at *7 (Order Making Findings on Default March 5, 2013); accord Hatfield, 2014 WL 6850921, at *9 ("The intent to deceive, *i.e.*, scienter, is different from the intent to the [sic] commit the act, *i.e.*, willfulness").

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[12] SBAM's argument that the Commission did not, through the OIP, authorize third-tier penalties (SBAM Br. at 4) is refuted by the OIP itself, which ordered that proceedings be instituted "to determine . . . whether Respondents should be ordered to pay civil penalties pursuant to Section 203(i) of the Advisers Act." (OIP Section III.D.) That Section includes third-tier penalties. Section 203(i)(2)(C).

In fact, ignorance or confusion of one's obligations under the law – which the Sands now claim to have suffered – cannot insulate a respondent from willfulness liability. Matter of Duo Yuan Printing, Inc., No. 3-15389, 2014 WL 3706544, at *3 (Initial Decision July 28, 2014) (citing Burns, 2011 WL 3407859, at *12 n.60); see also Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000) (willfulness does not require that the actor "'be aware that he is violating one of the Rules or the Acts.'" (internal citations omitted)). Similarly, "good faith efforts" to interpret or comply with the law do not undermine willfulness." Geman, 2001 WL 124847, at *17 (holding that securities professionals are "required to know the law that is applicable to their conduct within that industry.")

Finally, as this Court has held, where the conduct at issue is an omission, as opposed to an affirmative act, it may be willful, "even though inadvertent." Matter of BDO China Dahua, No. 3-14872, 2014 WL 242879 at *69 (Initial Decision Jan. 22, 2014) (noting that some courts have dispensed entirely with a knowledge requirement) (internal citations omitted), review granted, Rel. No. 3553, 2014 WL 1871078 (S.E.C. May 9, 2014). Indeed, willfulness may be found where the "respondent was on actual or constructive notice that action was required." Id.

As SBAM has already acknowledged, the audited financial statements were intentionally sent to investors after the Custody Rule deadline, and SBAM did so after it had consented to the 2010 Order requiring it to cease and desist from that precise conduct. Even if SBAM's three-year long violations could somehow be deemed "inadvertent," SBAM had actual notice in the 2010 Order that it was required to deliver its audited financial statements within the 120-day timeframe.

As to whether revocation of SBAM's registration as an investment adviser is in the public interest, the Commission considers the factors identified in Steadman v. SEC, 603 F.2d 1126,

1140 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981). No one factor is determinative. Matter of Gary M. Kornman, No. 3-12716, 2009 WL 367635, at *6 (S.E.C. Feb. 13, 2009). Those factors are:

> [T]he egregiousness of the respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his or her conduct, and the likelihood that the respondent's occupation will present opportunities for future violations.

Peak Wealth, 2013 WL 812635, at *8.

Here, the factors weigh decidedly in favor of revocation. With conceded violations in three successive years, no serious argument can be made that the violation was isolated or not recurrent. SBAM offers no assurance – despite an opportunity to do so – against future violations. Nor could it, credibly, given that SBAM's violations continued after it had consented to a Cease-and-Desist Order requiring it to comply, and even after learning that the Division had launched yet another investigation into its compliance. (See Brown Jan. Decl., Ex. 38 (2012 Subpoenas); Mov. Br. at 9 (Chart showing delivery of FY 2012 audit reports between July 23 and August 1, 2013).) And the Sands, who continue to own and operate SBAM, offer no assurances either, and appear even to contest that SBAM's conduct was violative. (Sands Br. at 16 (calling SBAM's violations "alleged").) With the Sands still at the helm, and still unwilling to acknowledge that SBAM violated any rule, SBAM's continuation in the industry provides it with every opportunity for future violations. In fact, future violations seem all but inevitable given the Sands' position that they are entitled to hand off all responsibility for the firm's compliance to their appointed Compliance Officer. (Sands Br. at 10, 12.) As noted in their 2009 Wells Submission, SBAM has engaged a long succession of Compliance Officers, none of whom has been up to the job. (Berke Feb. 23, 2015 Decl., Ex. 1 at 3-4.)

SBAM's violations were egregious, and particularly so since the violations entailed its repeated disregard of a Commission Order. Neither the fact that investors ultimately got the audited financials (Sands Br. at 1; SBAM Br. at 4), nor that the audits were delayed to ensure accurate valuations (SBAM Br. at 7), nor that investors received "periodic financial updates" (SBAM Br. at 8) is mitigating.[13] As noted in the Division's Moving Brief, the Commission views timely reporting as critical for investors. (Mov. Br. at 28 (citing China-Biotics, Inc., 2013 WL 5883342, at *13).) And the Commission's focus in adopting the Custody Rule was on asset verification, not asset valuation. (Adopting Release, 2009 WL 5172038 at *3, 9 n.67) (noting that amendments are designed to "prevent those assets from being lost, issued, misappropriated or subject to advisers' financial reverses" and "although valuation is a very important issue closely related to client assets, it covers an area that goes beyond custody"). SBAM did not have to issue audited financial statements to comply with the Custody Rule; it could have satisfied the Rule by submitting to a surprise examination of its assets within the fiscal year. But when it determined to use the audited financial statement option, it undertook to deliver them within 120 days of the end of its fiscal year. Its failure to do so, even after being sanctioned for previous failures to do so, was egregious.

C. Third Tier Penalties Are Appropriate as to All Respondents

Third tier civil money penalties are appropriate here and Respondents offer nothing but vague promises to produce evidence at some later date to show why they are not. Having had

[13] SBAM's arguments in this regard are unclear, possibly intentionally so. SBAM obliquely contends that the violations stemmed from a "lack of awareness of the alternative methodology for allowing a non-current asset valuation to be included in an audited financial report." (SBAM Br. at 9.) This "alternative methodology," goes uncited and unexplained. The Division is, itself, unaware of any such "alternative."

the opportunity to present that evidence now, and having foregone it, Respondents' arguments provide no reason to deny the Division the relief it seeks, which is in the public interest.

Apparently ignoring the very language of the precedent that they cite, both SBAM and the Sands argue that "third tier sanctions requires [sic] a showing of public harm and investor loss." (SBAM Br. at 8; see also Sands Br. at 17.) Nonetheless, both briefs actually quote the text of Advisers Act Section 203(i)(2)(C), which permits third tier penalties even where the violation creates only a *risk* of investor loss. Neither cites any precedent for the added proposition that an actual showing of public harm is required. That is because Respondents have misstated the legal standard. As pointed out in the Division's Moving brief, the Custody Rule's very purpose was to minimize the risk of investor loss by adviser misuse or misappropriation. (Mov. Br. at 27-28.)

The Division has also shown that the conduct at issue involved "deliberate or reckless disregard of a regulatory requirement," (Section 203(i)(2)(C)(i); Mov. Br. at 18-24; supra at Points II.B and III), and Respondents have presented no evidence to rebut that showing.

Finally, SBAM argues that "the Division purposely overstates the number of violations engaged in by SBAM" and that "[t]his is one good faith misunderstanding, not thirty." (SBAM Br. at 9; see also Sands Br. at 19.) But the math is simple: SBAM had an obligation to send out audited financial statements for each of its 10 managed funds under the Custody Rule – an obligation that it now concedes it failed to fulfill for at least three years. That amounts to thirty violations.

Moreover, the undisputed evidence shows that in certain years, the obligation *could have* been fulfilled if SBAM principals had simply signed the management representation letters that the auditors required to release the audits for several of the 10 Funds. (Mov. Br. at 10-11, 21-22;

see also Kelly Br. at 4.) That failure was certainly not the result of a misunderstanding; it was the result of deliberate or reckless conduct, and the Sands do not offer an alternative explanation. Each time SBAM failed to send out audited financial statements to investors, investor assets were put at risk.

D. Permanent Collateral Bars Are Appropriate as to the Sands

Nothing in the Sands' brief refutes the facts cited by the Division in support of its Motion for full collateral bars against them.

The Sands argue that their conduct merits no sanction at all because (i) they reasonably relied on Kelly to bring SBAM into compliance with the Custody Rule; and (ii) the Sands' "efforts to completely overhaul SBAM's compliance structure" (Sands Br. at 18-19) reflect their desire to bring SBAM into compliance, thus making them undeserving of meaningful sanctions. For the reasons discussed above, the Sands could not shift their responsibilities to Kelly and then wash their hands of them. Nor is there any evidence in the record that the Sands made any efforts, other than hiring Kelly, to "completely overhaul SBAM's compliance structure." (Sands Br. at 18.)

E. Cease-and-Desist Orders as to All Respondents, and a Permanent CCO Bar as to Kelly, Are Appropriate Sanctions

Aside from addressing liability, Respondents do not contest that Cease-and-Desist Orders are appropriate under the circumstances, nor do they contest that Respondent Kelly should be permanently barred from acting as CCO.

For the reasons laid out in the Division's motion, these uncontested sanctions are appropriate.

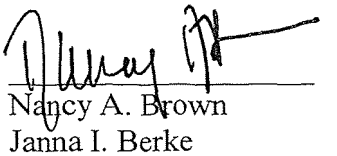
CONCLUSION

For the reasons discussed above and those cited in the Division's Moving Brief, the Court should grant the Division's Motion for summary disposition in all respects.

Dated: New York, New York
February 23, 2015

Respectfully submitted,

DIVISION OF ENFORCEMENT

By: 

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