

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 64288 / April 8, 2011**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 3268 / April 8, 2011**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-14338**

**In the Matter of**

**KENTUCKY ENERGY, INC.,  
EUGENE CHIARAMONTE,  
III AND CLEAR MOUNTAIN  
ASSOCIATES, LLC,**

**Respondents.**

**ORDER INSTITUTING CEASE-AND-DESIST  
PROCEEDINGS PURSUANT TO SECTION  
21C OF THE SECURITIES EXCHANGE ACT  
OF 1934, MAKING FINDINGS AND  
IMPOSING A CEASE-AND-DESIST ORDER**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Kentucky Energy, Inc., Eugene Chiaramonte, III and Clear Mountain Associates, LLC (collectively, “Respondents”).

**II.**

In anticipation of the institution of these proceedings, Respondents have each submitted an Offer of Settlement (an “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over each of them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order (“Order”), as set forth below.

### III.

On the basis of this Order and Respondents' Offers, the Commission finds<sup>1</sup> that:

#### Summary

These proceedings arise out of improper accounting, by Kentucky Energy, Inc., formerly known as Quest Minerals & Mining Corp., for warrants and certain convertible notes for the year ended December 31, 2005. Among other things, Kentucky Energy accounted for warrants it had issued to third parties as an asset with a purported value at the end of the first quarter of 2005 of more than \$13 million. This accounting was not in accordance with generally accepted accounting principles ("GAAP") and was material to Kentucky Energy's financial statements, in that it caused its assets to be overstated by 43% and its net loss to be overstated by 197% for the year ended December 31, 2005. The inaccurate financial statements were prepared by Eugene Chiaramonte, III through his consulting company, Clear Mountain Associates, which had been retained by Kentucky Energy for the purpose of preparing its financial statements.

#### Respondents

1. **Kentucky Energy, Inc.**, formerly known as Quest Minerals & Mining Corp. ("Kentucky Energy") was organized under the laws of the state of Utah in 1985. Since 2004, Kentucky Energy has been in the business of mining coal in Kentucky. It changed its name to Kentucky Energy, Inc. effective June 16, 2010. Kentucky Energy's common stock previously traded on the OTC Bulletin Board under the symbol QMLM.OB and currently trades in the pink sheets under the symbol QMIN.PK and closed at \$.0004 on October 4, 2010.
2. **Clear Mountain Associates, LLC**, a New Jersey limited liability company ("Clear Mountain"), has been employed as a consultant to Kentucky Energy from the fall of 2004 to the present. It was formed by Eugene Chiaramonte, III.
3. **Eugene Chiaramonte, III** is the founder and sole owner of Clear Mountain. He has never been licensed as a certified public accountant. Through his consulting firm Clear Mountain, Chiaramonte prepared the financial statements of Kentucky Energy beginning with its quarter ended June 30, 2004, to the present.

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<sup>1</sup> The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

## Background

### **Inaccurate financial statements.**

4. Beginning in the fall of 2004 and continuing throughout 2005, Kentucky Energy obtained a series of loans from third parties, evidenced by notes convertible into common stock. As an additional incentive to the lenders, Kentucky Energy issued warrants along with each convertible note. The way in which Kentucky Energy accounted for these warrants and for the conversion feature of the notes, however, caused its financial statements for the 2005 year to be materially inaccurate.

5. Chiaramonte formed Clear Mountain for the purpose of running the Kentucky Energy accounting work, its only client, through an entity. Since mid-2004, Chiaramonte, through Clear Mountain, has been preparing the financial statements of Kentucky Energy and its subsidiaries. He has also been making determinations as to the proper accounting for Kentucky Energy's transactions, because the company has not had an officer or employee capable of working in this area. In these ways, he functioned as the CFO of Kentucky Energy. Chiaramonte was solely responsible for deciding how to account for the warrants and convertible notes issued by Kentucky Energy during 2004 and 2005.

6. All of Kentucky Energy's inaccurate 2005 financial statements were the responsibility of Chiaramonte. He had no prior experience with accounting for warrants, the beneficial conversion feature of a convertible note, or derivative accounting. Chiaramonte consulted the company's audit firm for guidance. He did not seek other outside expertise regarding the proper accounting for the convertible notes and warrants.

7. Kentucky Energy's auditor told Chiaramonte that he should use the Black-Scholes option pricing model to value the warrants. While he had heard the term before, Chiaramonte had no experience with Black-Scholes. He used a search engine to find a Black-Scholes calculator on the internet. This calculator called for inputs for the "equity price," "strike price," "volatility," "rate/year," and "term," and would then generate a figure for "option value." Chiaramonte then applied the resulting valuation to the warrants in Kentucky Energy's financial statements.

8. In using the Black-Scholes calculator he had found on the internet, Chiaramonte did not input the actual volatility and interest rate applicable to Kentucky Energy's common stock. Instead, he chose the generic example for volatility and interest rate provided by the website, and inserted those numbers into the formula. In the case of the volatility figure, Chiaramonte used the generic input suggested by the website, which was 30%, for each quarter in 2005. In fact, the actual volatility of Kentucky Energy's common stock was well in excess of 200% for each quarter. This difference was material.

9. In its 2005 financial statements, Kentucky Energy recorded the warrant valuation as an asset on the company's balance sheet, and amortized that valuation over the life of the

underlying convertible note. In fact, no portion of the loan proceeds represented by the warrants should have been recorded as an asset. Instead, this portion of the loan proceeds should have been recorded in stockholders' equity as paid-in capital, with an offsetting amount treated as a debt discount and amortized. In addition, the company did not account for the beneficial conversion feature of the notes themselves. Kentucky Energy should have allocated the loan proceeds first to the notes and the warrants, and then allocated a portion from the resulting note amount to the beneficial conversion feature of the notes.

10. As a result of this improper accounting, Kentucky Energy's assets were materially overstated for each quarter in 2005 and for the 2005 year. For example, its assets were overstated by approximately \$13.8 million, or 213%, in the financial statements contained in the Form 10-Q for the first quarter of 2005.

11. As a result of the amortization of the warrant asset, Kentucky Energy's statement of operations was also materially false for each quarter in 2005 and for the 2005 year. For example, this amortization caused its net loss to be overstated by approximately 174% for the second quarter of 2005.

12. For its year ended December 31, 2005, as a result of its improper accounting for the warrants and convertible notes, Kentucky Energy recorded a warrant asset in the amount of \$3,097,903 on its balance sheet, net of that which was amortized as an expense on its statements of operations. In so doing, the company overstated total assets by 43% and overstated its net loss by 197%. Along the way it materially overstated paid-in capital, retained deficit, stockholders' equity and expenses. Its recording of the warrants as an asset, and the subsequent amortization of that asset, was material to both its balance sheet and its statement of operations contained in all of its periodic filings for 2005, and caused those financial statements to be false and misleading.

## **Violations**

13. As a result of the conduct described above, Kentucky Energy committed violations of Section 13(a) of the Exchange Act, which requires registrants to file certain periodic and other reports, and of Rules 12b-20, 13a-1 and 13a-13. Rules 13a-1 and 13a-13 require, respectively, the filing of annual and quarterly reports. Rule 12b-20 provides that, in addition to information specifically required to be included in reports, registrants are obligated to include any material information necessary to make the statements made in the reports not misleading.

14. As a result of the conduct described above, Kentucky Energy committed violations of Section 13(b)(2)(A) and (B) of the Exchange Act. Section 13(b)(2)(A) of the Exchange Act requires every issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act to "make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer . . . ." Scienter is not required to establish a violation of Section 13(b) or the rules thereunder. Section 13(b)(2)(B) requires an issuer to "devise and maintain a system of internal accounting controls sufficient to

provide reasonable assurances that . . . (ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets.”

15. As a result of the conduct described above, Chiaramonte committed violations of Section 13(b)(5) of the Exchange Act, which provides that “no person shall . . . knowingly falsify any book, record, or account . . .” described in Section 13(b)(2). Chiaramonte knowingly falsified the financial statements of Kentucky Energy by improperly accounting for the warrants and convertible notes.

16. As a result of the conduct described above, Chiaramonte committed violations of Rule 13b2-1 under the Exchange Act, which generally prohibits the falsification of books and records.

17. As a result of the conduct described above, Chiaramonte and Clear Mountain caused Kentucky Energy’s violations of Sections 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 thereunder.

## **Undertakings**

18. Kentucky Energy has undertaken to:

- a. Maintain at least two independent directors on its Board of Directors so that not less than two-thirds of the members of the Board of Directors will be independent directors;<sup>2</sup>
- b. Employ a Chief Financial Officer qualified to prepare financial statements in accordance with GAAP;

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<sup>2</sup> For a director to be considered independent within the meaning of these undertakings, the board must determine that the director has no material relationship with Kentucky Energy (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company) that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. A director is not independent if (1) he is, or has been within the last three years, an employee of the company, or if an immediate family member is, or has been within the last three years, an executive officer of the company; (2) the director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than \$120,000 in direct compensation from the company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service); (3) the director or an immediate family member is, or has been with the last three years, employed as an executive officer of another company where any of Kentucky Energy’s present executive officers at the same time serves or served on that company’s compensation committee; or (4) the director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the company, other than those payments to or from the company arising solely from investments in the company’s securities or payments under non-discretionary charitable contribution matching programs, for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of \$1 million, or 2% of such other company’s consolidated gross revenues. In addition, references to “Kentucky Energy” or “the company” include any parent or subsidiary in a consolidated group with the company.

c. Notify the Division of Enforcement if its chief financial officer resigns or is terminated, or if one or more board members leave the company, such that the board as a whole is no longer independent. Such notification shall be submitted to Karen L. Martinez, Assistant Director, Securities and Exchange Commission, 15 West South Temple Street, Suite 1800, Salt Lake City, Utah 84101, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of such event;

d. Within three months of the date this order is instituted, adopt a system of written internal controls, and identify and implement actions to improve the effectiveness of its disclosure controls and procedures and internal controls, including plans to enhance its resources and training with respect to financial reporting and disclosure responsibilities, and to review such actions with its independent auditors; and

The above undertakings shall automatically expire three years from the date this order is instituted.

#### IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondents' respective Offers.

Accordingly, pursuant to Section 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondent Kentucky Energy cease and desist from committing or causing any violations and any future violations of Sections 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 thereunder.

B. Respondent Kentucky Energy comply with its undertakings as enumerated in Section III above. Any undertaking set forth in Section III above which were implemented prior to the date of this Order shall be maintained.

Respondent Kentucky Energy shall certify, in writing, compliance with the undertakings enumerated in Section III above. The certification shall identify the undertakings, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent Kentucky Energy agrees to provide such evidence. The certification and supporting material shall be submitted to Karen L. Martinez, Assistant Director, Securities and Exchange Commission, 15 West South Temple Street, Suite 1800, Salt Lake City, Utah 84101, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of the completion of the undertakings.

Any undertakings set forth in Section III above which were implemented prior to the date of this Order shall be maintained.

C. Respondent Chiaramonte cease and desist from committing or causing any violations and any future violations of Section 13(b)(5) of the Exchange Act and Rule 13b2-1 thereunder. Respondents Chiaramonte and Clear Mountain cease and desist from committing or causing any violations and any future violations of Section 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 thereunder.

By the Commission.

Elizabeth M. Murphy  
Secretary

Service List

Rule 141 of the Commission's Rules of Practice provides that the Secretary, or another duly authorized officer of the Commission, shall serve a copy of the Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings and Imposing a Cease-and-Desist Order ("Order") on the Respondents and their legal agent.

The attached Order has been sent to the following parties and other persons entitled to notice:

Honorable Brenda P. Murray  
Chief Administrative Law Judge  
Securities and Exchange Commission  
100 F Street, N.E.  
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