

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 4160 / August 6, 2015

INVESTMENT COMPANY ACT OF 1940
Release No. 31742 / August 6, 2015

ADMINISTRATIVE PROCEEDING
File No. 3-15627

In the Matter of

**TRI-STAR ADVISORS,
INC., WILLIAM T. PAYNE,
AND JON C. VAUGHAN,**

Respondents.

**ORDER MAKING FINDINGS AND
IMPOSING REMEDIAL SANCTIONS AND
A CEASE-AND-DESIST ORDER
PURSUANT TO SECTIONS 203(e) AND
203(k) OF THE INVESTMENT ADVISERS
ACT OF 1940 AND SECTION 9(b) OF THE
INVESTMENT COMPANY ACT OF 1940
AGAINST ALL RESPONDENTS**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest to enter this Order Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) and Section 9(b) of the Investment Company Act of 1940 (“Investment Company Act”) against Tri-Star Advisors, Inc. (“TSA”), William T. Payne (“Payne”), and Jon C. Vaughan (“Vaughan”) (collectively, “Respondents”).¹

II.

Respondents have submitted an Offer of Settlement (“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 them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, and Section 9(b) of the Investment Company Act of 1940 Against All Respondents (“Order”), as set forth below.

¹ On November 26, 2013, the Commission instituted against TSA public administrative and cease-and-desist proceedings pursuant to Section 203(e) and Section 9(b) of the Investment Company Act, and against TSA, Payne, and Vaughan cease-and-desist proceedings pursuant to Section 203(k) of the Advisers Act.

III.

On the basis of this Order and Respondents' Offers, the Commission finds that:

A. SUMMARY

1. TSA, an investment adviser registered with the Commission since November 2009, willfully violated the principal transaction prohibitions and compliance provisions of the Advisers Act and the rules thereunder. From July 2009 through July 2011 ("relevant period"), TSA: engaged in thousands of securities transactions with advisory clients on a principal basis through an affiliated broker-dealer, without providing prior written disclosure to, or obtaining consent from, the clients on a transaction-by-transaction basis; and failed to adopt and implement written policies and procedures reasonably designed to prevent such violations of the Advisers Act.

2. Payne and Vaughan caused TSA's violations. During the relevant period, Payne was TSA's CEO, and Vaughan was TSA's President.

B. RESPONDENTS

3. TSA is a Texas corporation based in Houston, Texas. TSA became a Commission-registered investment adviser on November 17, 2009. As of December 2012, it managed 313 accounts on a non-discretionary basis and had approximately \$162 million in assets under management.

4. Payne, age 57, resides in Sugarland, Texas and is the CEO of TSA. He was also the President and 40% owner of Mutual Money Investments, Inc. d/b/a Tri-Star Financial ("TSF"), an affiliated broker-dealer registered with the Commission.

5. Vaughan, age 42, resides in Houston, Texas and is the President of TSA. He was also the Vice President and 20% owner of TSF.

C. OTHER RELEVANT ENTITY

6. TSF is a Texas corporation based in Houston, Texas that is affiliated with TSA. During the relevant period TSF was a Commission-registered broker-dealer and was jointly owned by Payne, Vaughan and another individual.

D. FACTS

7. TSA provides investment advisory services to individuals and entities. TSA's investment strategy focused almost exclusively on fixed income securities, such as mortgage-backed bonds. To execute this strategy, TSA relied on TSF, its affiliated broker-dealer, for fixed income analysis and trade execution.

8. Payne and Vaughan make investment recommendations to TSA clients and, upon the clients' consent, during the relevant period TSF executed the transactions. During the relevant

period, TSF used its inventory account to purchase mortgage-backed bonds for TSA advisory clients and then transferred the bonds to the applicable client account. TSF charged the advisory clients a sales credit for the trades, which was essentially a percentage mark-up (or mark-down). Payne and Vaughan, registered representatives of TSF for the trades, received 55% of the sales credit generated by each trade.

9. Payne and Vaughan are responsible for ensuring that TSA complies with its regulatory requirements, including Advisers Act requirements.

10. From July 2009 through July 2011, TSA, through TSF, engaged in approximately 2,212 principal transactions with its advisory clients (“TSA Principal Transactions”) without providing prior written disclosure to clients that it would effect the trades on a principal basis, or obtaining consent from clients on a transaction-by-transaction basis.

11. TSF collected approximately \$1.9 million in gross sales credits from the TSA Principal Transactions. TSF paid approximately \$1 million to Payne and Vaughan for the TSA Principal Transactions while retaining the rest. None of the gross sales credits was paid to TSA.

12. Payne and Vaughan initiated and executed the TSA Principal Transactions. They knew that TSA did not provide written disclosures to, or obtain consent from, TSA clients before completing the TSA Principal Transactions.

13. During the relevant period, TSA failed to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Advisers Act provision regarding principal transactions. TSA’s compliance manual did not contain any policies and procedures addressing principal transactions.

E. VIOLATIONS

14. As a result of the conduct described above, TSA willfully² violated Section 206(3) of the Advisers Act, which prohibits an investment adviser from executing securities transactions with a client on a principal basis without disclosing to such client in writing, before the completion of such transaction, the capacity in which it is acting and obtaining the consent of the client to such transaction.

15. As a result of the conduct described above, Payne and Vaughan caused TSA’s violations of Section 206(3) of the Advisers Act.

16. As a result of the conduct described above, TSA willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require that an investment adviser adopt and implement written policies and procedures reasonably designed to prevent violation of the Advisers Act and the rules thereunder.

² A willful violation of the securities laws means merely “that the person charged with the duty knows what he is doing.” *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor “also be aware that he is violating one of the Rules or Acts.” *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

17. As a result of the conduct described above, Payne and Vaughan caused TSA's violations of Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

IV.

Undertakings

Respondents have undertaken to do as follows:

Payment to Advisory Clients

18. Respondents undertake, jointly and severally, to distribute, within 60 days of the date of entry of this Order, a total payment in the amount of \$375,000 (the "Distribution") to compensate certain advisory clients who purchased or sold bonds between July 2009 and July 2011. This amount represents an approximation of certain sales credits Respondents Payne and Vaughan received in connection with the principal transactions discussed herein. No portion of the Distribution shall be paid to any account in which any Respondent has a financial interest.

19. If Respondents do not distribute or return any portion of the Distribution for any reason, including an inability to locate an advisory client or any factors beyond Respondents' control, Respondents shall transfer any such undistributed funds to the Commission for transmittal to the United States Treasury after the final accounting provided for in paragraphs 22-23 is approved by the Commission. Any such payment shall be made in accordance with Section VI.F. below.

20. Respondents shall be responsible for administering the payment of the Distribution to certain current and former advisory clients. Respondents shall:

a. deposit the amount of the Distribution into an escrow account (the "Distribution Account") within 10 days of the date of entry of this Order and provide Commission staff with evidence of such deposit in a form not unacceptable to the Commission staff;

b. submit to the Commission staff, within 30 days of the date of entry of this Order, a distribution plan ("Distribution Plan") for the staff's review and approval that identifies: (i) each current and former advisory client who will receive a portion of the Distribution ("Eligible Advisory Client"); (ii) the exact amount of that payment as to each Eligible Advisory Client; and (iii) the methodology used to determine the exact amount of that payment as to each Eligible Advisory Client. Respondents shall provide to the Commission staff such additional information and supporting documentation relating to the Distribution Plan as the Commission staff may request for the purpose of its review. No portion of the Distribution shall be paid to any client account directly or indirectly in the name of or for the benefit of Respondent TSA, Respondent Payne, or Respondent Vaughan. In the event of one or more objections by the Commission staff to Respondents' proposed Distribution Plan and/or any of its information or supporting documentation, Respondents shall submit a revised Distribution Plan for the review

and approval of the Commission staff and/or additional information or supporting documentation within ten (10) days of the date that Respondent is notified of the objection, which revised Plan shall be subject to all of the provisions contained within Paragraphs 18-23 of this Order; and

c. within 60 days of the date of entry of this Order, complete payment of the Distribution to all Eligible Advisory Client pursuant to the Distribution Plan that has been submitted to, reviewed, and approved by the Commission staff. If the total amount otherwise payable to a client is less than \$20.00, Respondents shall instead pay such amount to the Commission for transmittal to the United States Treasury as provided in this Order.

21. Respondents shall be responsible for any and all tax compliance responsibilities associated with the Distribution and shall retain any professional services necessary. The costs and expenses of any such professional services shall be borne by Respondents and the payment of taxes applicable to the Distribution Account, if any, shall not be paid out of the Distribution funds. Respondents shall not be responsible for payment of any income taxes investors owe on the portion of the Distribution they receive.

22. Within 90 days after the date of entry of this Order, Respondents shall submit to the Commission staff for its approval a final accounting and certification of the disposition of the Distribution not unacceptable to the Commission staff. The final accounting and certification shall include, but not be limited to: (i) the amount paid to each payee; (ii) the date of each payment; (iii) the check number or other identifier of money transferred or proof of payment made; (iv) the date and amount of any returned payment; (v) a description of any effort to locate a prospective payee whose payment was returned; (vi) an affirmation that the amount paid to the current and former Eligible Advisory Client represents a fair calculation of the Distribution; and (vii) any amounts to be forwarded to the Commission for transfer to the United States Treasury. Respondents shall submit proof and supporting documentation of such payments to the Commission staff upon request. Respondents shall cooperate with reasonable requests for information in connection with the accounting and certification.

23. After Respondents have submitted the final accounting to the Commission staff, the staff shall submit the final accounting to the Commission for approval.

Independent Compliance Consultant

24. Respondent TSA currently retains a compliance consultant (the "Consultant") to render compliance services. TSA shall continue to retain either the Consultant or an independent compliance consultant ("ICC") not unacceptable to the staff of the Commission, to render compliance services for a period of at least one (1) year from the entry of this Order. The expenses of the consultant or of the ICC shall be borne exclusively by TSA.

25. Respondent TSA shall require the Consultant or ICC to conduct a comprehensive compliance review designed to prevent and detect prohibited principal transactions and to ensure the adoption and implementation of written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder, including but not limited to, violations of Sections 206(3) and 206(4) of the Advisers Act and Rule 206(4) under the Act.

26. Respondent TSA shall provide to the Commission staff, within 30 days of this Order or within 30 days of retaining an ICC, a copy of an engagement letter detailing the Consultant or ICC's responsibilities, which shall include the review described above in paragraph 25.

27. At the end of the review, which in no event shall be more than 180 days after the date of the entry of this Order, Respondent TSA shall submit a report approved by the Consultant or the ICC (the "Report") to the staff of the Commission. The Report shall address the issues described above in paragraph 25, and shall include a description of the review performed, the conclusions reached, the Consultant or ICC's recommendations for changes in or improvements to TSA's policies and procedures, a procedure for implementing the recommendations or changes in or improvements to those policies and procedures, and the Consultant or ICC's approval of the foregoing.

28. Respondent TSA shall adopt all recommendations contained in the Report. Within 210 days after the date of the entry of this Order, TSA shall, in writing, advise the Consultant or ICC and the staff of the Commission of any recommendations for changes or improvements to TSA's policies on which TSA and the Consultant or ICC did not agree and the resolution of such disagreement. In the event that TSA and the Consultant or ICC are unable to agree on a resolution, TSA will abide by the recommendations of the Consultant or ICC. To the extent the Consultant has already made recommendations for changes in or improvements to TSA's policies and procedures and/or disclosures to clients, TSA shall adopt and implement all such recommendations.

29. Respondent TSA shall cooperate fully with the Consultant or ICC and shall provide the Consultant or ICC with access to files, books, records, and personnel as reasonably requested for the review.

30. If TSA retains an ICC, TSA undertakes to require the ICC to enter into an agreement that provides that for the period of engagement and for a period of two years from completion of the engagement, the ICC shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with TSA, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. The agreement will also provide that the ICC will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the ICC in performance of his/her duties under this Order shall not, without prior written consent of the Fort Worth Regional Office of the SEC, enter into any employment, consultant, attorney-client, auditing or other professional relationship with TSA, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

31. TSA shall certify, in writing, compliance with the undertakings set forth above. The certification shall identify the undertaking, 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 agrees to provide such evidence. The certification and supporting material shall be submitted to David Peavler, Assistant Regional Director, 801 Cherry Street, Suite 1900, Fort Worth, Texas 76102, 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.

Notice to Advisory Clients

32. Within ten (10) days of the entry of this Order, TSA shall post prominently on its principal website a summary of this Order in a form and location acceptable to the Commission staff, with a hyperlink to the entire Order. TSA shall maintain the posting and hyperlink on its website for a period of nine (9) months from the entry of this Order. Within thirty (30) days of the entry of this Order, TSA shall provide a copy of the Order to each of TSA's existing advisory clients as of the entry of this Order via mail, email, or such other method as may be acceptable to the Commission staff, together with a cover letter in a form not unacceptable to the Commission staff.

Deadlines

33. For good cause shown, the Commission staff may extend any of the procedural deadlines relating to the undertakings.

V.

TSA's Remedial Efforts

34. In determining to accept the offer, the Commission considered the remedial acts promptly undertaken by Respondent TSA.

VI.

In view of the foregoing, the Commission deems it appropriate, in the public interest and for the protection of investors to impose the sanctions agreed to in Respondents' Offer.

Accordingly, pursuant to Sections 203(e) and 203(k) of the Advisers Act, and Section 9(b) of the Investment Company Act, it is hereby ORDERED that:

A. TSA shall cease and desist from committing or causing any violations and any future violations of Sections 206(3) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

B. Payne shall cease and desist from committing or causing any violations and any future violations of Sections 206(3) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

C. Vaughan shall cease and desist from committing or causing any violations and any future violations of Sections 206(3) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder.

D. TSA is censured.

- E. TSA shall comply with the undertakings enumerated in Section IV, above.
- F. Respondents shall make payment as follows:
 - (1) TSA shall pay a civil money penalty in the amount of \$150,000;
 - (2) Payne shall pay disgorgement of \$142,500, which represents profits gained as a result of the conduct described herein, prejudgment interest of \$3,235.21, and a civil money penalty in the amount of \$50,000, for a total payment of \$195,735.21; and
 - (3) Vaughan shall pay disgorgement of \$232,500, which represents profits gained as a result of the conduct described herein, prejudgment interest of \$5,278.50, and a civil money penalty in the amount of \$50,000, for a total payment of \$287,778.50.

The disgorgement amounts of \$142,500 and \$232,500 described in sub-paragraphs (2) and (3), above, shall be deemed satisfied by the payment described above in paragraphs 18-23. All other amounts shall be paid within 20 days of the entry of this order to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 and 31 U.S.C. § 3717. Payment must be made in one of the following ways:

- (1) Respondents may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (2) Respondents may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Respondent as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to: David Peavler, Associate Regional Director, Securities and Exchange Commission, 801 Cherry Street, Fort Worth, TX 76102.

G. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, each Respondent agrees that in any Related Investor Action, Respondent shall not argue that Respondent is entitled to, nor shall he/it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's

payment of a civil penalty in this action (“Penalty Offset”). If the court in any Related Investor Action grants such a Penalty Offset, each Respondent agrees that he/it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission’s counsel in this action and pay the amount of the Penalty Offset to the United States Treasury or to a Fair Fund, as the Commission directs. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a “Related Investor Action” means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary