

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Investment Advisers Act of 1940
Release No. 4823 / December 8, 2017

ADMINISTRATIVE PROCEEDING
File No. 3-18302

In the Matter of

**HORTER INVESTMENT
MANAGEMENT, LLC,**

Respondent.

**ORDER INSTITUTING
ADMINISTRATIVE AND CEASE-AND-
DESIST PROCEEDINGS PURSUANT
TO SECTIONS 203(e) AND 203(k) OF
THE INVESTMENT ADVISERS ACT
OF 1940, MAKING FINDINGS, AND
IMPOSING REMEDIAL SANCTIONS
AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Horter Investment Management, LLC (“Respondent” or “Horter”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “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 Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Advisers Act, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

Summary

1. This matter arises from misstatements made by registered investment adviser Horter to certain of its advisory clients concerning F-Squared Investments, Inc.'s ("F-Squared") materially inflated, and hypothetical and back-tested, performance track record for its AlphaSector strategy.

2. AlphaSector is a sector rotation strategy based on an algorithm that yields a signal indicating whether to buy or sell nine industry exchange-traded funds ("ETFs") that together made up the industries in the S&P 500 Index. Between January 2012 and November 2014, Horter offered the AlphaSector strategy to its clients. Horter's assets under management relating to F-Squared's AlphaSector strategy were approximately \$56 million by September 2013.

3. From January 2012 to October 1, 2013, in reliance on F-Squared's false statements, Horter disseminated AlphaSector advertisements falsely stating: (a) assets had been invested in the AlphaSector strategy from April 2001 to September 2008; and (b) the track record had significantly outperformed the S&P 500 Index from April 2001 to September 2008. In fact, no F-Squared or other client assets had tracked the strategy from April 2001 through September 2008. In addition, F-Squared miscalculated the historical performance of AlphaSector from April 2001 to September 2008 by incorrectly implementing signals in advance of when such signals actually could have occurred. Because of this inaccurate compilation of historical data by F-Squared, Horter advertised the AlphaSector strategy by using hypothetical and back-tested historical performance that was inflated substantially over what performance would have been if F-Squared had applied the signals accurately. As a result, Horter violated Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) thereunder by publishing, circulating, and distributing advertisements that contained untrue statements of material fact.

4. Horter also violated Sections 204(a) and 206(4) of the Advisers Act and Rules 204-2(a)(16) and 206(4)-7 thereunder by (i) failing to make and keep true, accurate and current records or documents necessary to form the basis for or demonstrate the calculation of the performance or rate of returns that it circulated and distributed, and (ii) failing to adopt and implement written policies and procedures regarding the accuracy of performance information it circulated in advertisements and the retention of books and records necessary to support the basis for such performance information.

¹ The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this or any other proceeding.

Respondent

5. **Horter Investment Management, LLC** (SEC File No. 801-67471) is an investment adviser registered with the Commission since January 2007 and is headquartered in Cincinnati, Ohio. Horter had regulatory assets under management of more than \$1 billion as reported in its Form ADV, dated September 13, 2017.²

Other Relevant Entity

6. **F-Squared Investments, Inc.** (SEC File No. 801-69937) was an investment adviser that was registered with the Commission from March 2009 until January 2016, and was headquartered in Wellesley, Massachusetts. In October 2008, F-Squared launched its first AlphaSector index. F-Squared sub-licensed its approximately 75 AlphaSector indexes to unaffiliated third parties who managed assets pursuant to these indexes. On December 22, 2014, the Commission instituted a settled fraud action against F-Squared in which F-Squared admitted, among other things, to making the materially false claims that (a) the signals that formed the basis of the AlphaSector index returns had been used to manage client assets from April 2001 to September 2008; and (b) the signals resulted in a track record that significantly outperformed the S&P 500 Index from April 2001 to September 2008. *See In the Matter of F-Squared Investments, Inc.*, Admin. Proceeding No. 3-16325 (Dec. 22, 2014).

Facts

7. In approximately August 2011, F-Squared introduced Horter to its AlphaSector strategies. Horter began considering whether it would enter into a model manager agreement with F-Squared whereby Horter would establish an investment product that followed F-Squared's AlphaSector sector rotation strategy. F-Squared marketed AlphaSector to Horter as an ETF sector rotation strategy that was based on an algorithm that yields a "signal" indicating whether to buy or sell nine industry ETFs.³ If the algorithm produced buy signals for three or fewer sector ETFs, the AlphaSector strategy provided for some or all of the assets to be invested in cash equivalents.

8. F-Squared described the strategy falsely to Horter by, among other things, representing that: (a) the AlphaSector strategy had been used to manage client assets from April

²Regulatory assets under management include the securities portfolios for which Horter provides continuous and regular supervisory or management services.

³ F-Squared created several AlphaSector strategies and sub-licensed approximately 75 AlphaSector indexes. The AlphaSector Premium index that is the subject of this matter is based on investments in U.S. equity ETFs. As with all indexes, the performance of the AlphaSector Premium Index is inherently hypothetical in the sense that the index does not purport to reflect the performance of any particular client or account. However, the AlphaSector Premium Index was advertised as being based on a strategy that had been in place since 2001 and therefore the performance of this index was advertised as "not backtested" when in fact the performance *was* back-tested.

2001 to September 2008, often calling it a “live” track record; and (b) the track record had significantly outperformed the S&P 500 Index from April 2001 to September 2008. In reality, no assets tracked the strategy until 2008 and the back-tested track record was substantially overstated. F-Squared’s AlphaSector sales and marketing materials, which it shared with Horter, claimed falsely that clients actually achieved these performance returns for the April 2001 to September 2008 time period.

9. In September 2011, Horter entered into a model manager agreement allowing the firm to invest client assets pursuant to the AlphaSector Premium strategy. In December 2011, after reviewing the disclosures in F-Squared’s AlphaSector marketing slide presentation, one Horter employee suspected that F-Squared’s AlphaSector performance results from April 2001 to September 2008 were back-tested, as opposed to performance resulting from the “live” trading of actual assets. Horter took insufficient steps to determine whether F-Squared’s buy or sell signals were generated or used in any trading decisions during the April 2001 through September 2008 period. As a result, Horter knew or should have known that it did not have a reasonable basis to believe that AlphaSector’s advertising claims were accurate prior to recommending the AlphaSector strategy to clients.

Horter’s Advertisements Contained Misstatements

10. Horter advertised the strategy by incorporating portions of F-Squared’s advertisements, including claims concerning the live nature of the track record and the significant outperformance claim, into its own advertisements. Horter then disseminated these advertisements to its clients and prospective clients without having a reasonable basis to conclude that F-Squared’s exceptional performance claims between 2001 and 2008 were the result of live trading. For example, from January 2012 through October 1, 2013, Horter, in advertising its own advisory services, disseminated AlphaSector performance advertisements for its own separately managed account strategies that failed to disclose the AlphaSector track record for the period April 2001 to September 2008 was hypothetical and back-tested. In fact, these Horter advertisements described the historical performance of AlphaSector as “not backtested.” Horter’s AlphaSector advertisements also substantially overstated the performance of the back-tested track record for the strategy during this period based on the false information provided by F-Squared. Horter advised clients to invest in the AlphaSector strategies based on their historical performance. In October 2013, F-Squared notified Horter that F-Squared was removing all performance track records for the time period April 2001 to September 2008. Horter removed the references in its advertising materials to any performance information of F-Squared for periods prior to September 2008. In November 2014, Horter suspended new sales of F-Squared products.

Horter Failed to Adopt and Implement Adequate Policies and Procedures

11. Horter was required to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and its rules. As an adviser that often relied on subadviser or other third-party-produced performance and marketing materials, both in hiring or retaining subadvisers and in marketing a subadviser to its own clients or

prospective clients, Horter should have adopted and implemented policies and procedures reasonably designed to address the accuracy of such materials. However, Horter had no written policies and procedures for evaluating and monitoring the accuracy of such materials that it provided to other persons. As a result, Horter failed to adopt and implement reasonably designed written policies and procedures regarding the retention of books and records necessary to support the basis for performance information in advertisements directly or indirectly circulated or distributed by Horter.

Horter Failed to Maintain Adequate Books and Records

12. Horter was required to make and keep true, accurate and current records or documents necessary to form the basis for or demonstrate the calculation of the performance or rate of return that it circulated or distributed to ten or more persons. In marketing its own advisory services, Horter circulated and distributed the 2001-2008 historical performance of the AlphaSector strategy in client presentations and marketing materials and other communications to numerous clients, investors, and potential investors. However, Horter never made or kept records or documents sufficient to form the basis for or demonstrate the calculation of the historical performance or rate of return of the AlphaSector strategy.

Retention of a Compliance Consultant

13. In determining to accept Respondent's Offer, the Commission considered Horter's retention of a compliance consultant in February 2015. Among other things, Horter hired a compliance consultant to conduct a comprehensive review of Horter's written compliance policies and procedures addressing: (i) with respect to separately managed accounts, the publication, circulation, communication, or distribution of third-party marketing materials or materials that include third-party-produced performance information, and (ii) with respect to the initial and continuing due diligence into and retention of subadvisers, policies and procedures related to appropriate oversight of subadviser compliance with Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, as appropriate.

Violations

14. As a result of the conduct described above, Respondent willfully⁴ violated Section 206(2) of the Advisers Act, which prohibits any investment adviser from engaging in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client. A violation of Section 206(2) may rest on a finding of simple negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research*

⁴ 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)).

Bureau, Inc., 375 U.S. 180, 195 (1963)). Proof of scienter is not required to establish a violation of Section 206(2) of the Advisers Act. *Id.*

15. As a result of the conduct described above, Respondent willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) thereunder, which makes it a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of Section 206(4) of the Advisers Act to, among other things, directly or indirectly publish, circulate, or distribute an advertisement which contains any untrue statement of material fact, or which is otherwise false or misleading. A violation of Section 206(4) and the rules thereunder does not require scienter. *Steadman*, 967 F.2d at 647.

16. As a result of the conduct described above, Respondent willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder by failing to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and its rules.

17. As a result of the conduct described above, Respondent willfully violated Section 204(a) of the Advisers Act and Rule 204-2(a)(16) thereunder. Section 204(a) of the Advisers Act requires investment advisers to make and keep certain records as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors. Rule 204-2 under the Advisers Act requires investment advisers registered or required to be registered to make and keep true, accurate and current various books and records relating to their investment advisory business, including all accounts, books, internal working papers, and any other records or documents that are necessary to form the basis for or demonstrate the calculation of the performance or rate of return of any or all managed accounts or securities recommendations in any notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication that the investment adviser circulates or distributes, directly or indirectly, to 10 or more persons.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent's Offer.

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

A. Horter shall cease and desist from committing or causing any violations and any future violations of Sections 204(a), 206(2), and 206(4) of the Advisers Act and Rules 204-2(a)(16), 206(4)-1(a)(5), and 206(4)-7 thereunder.

B. Horter is censured.

C. Horter shall pay disgorgement of \$482,595, prejudgment interest of \$46,209, and a civil money penalty in the amount of \$250,000 to the Securities and Exchange Commission for

transfer to the general fund of the United States Treasury, subject to Securities Exchange Act of 1934 Section 21F(g)(3), as follows: \$194,701 within 10 days of the entry of this Order and the remaining \$584,103 to be paid in three payments of \$194,701 within 180 days, 270 days, and 360 days of the entry of this Order. 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) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent 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
- (3) Respondent 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 Horter as the 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 Corey A. Schuster, Assistant Director, Asset Management Unit, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549-5012.

D. 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, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall 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, Respondent agrees that 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 Securities and Exchange Commission. 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