INITIAL DECISION RELEASE NO. 331
ADMINISTRATIVE PROCEEDING
FILE NO. 3-12429

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	:	
	:	INITIAL DECISION
SCOTT G. MONSON	:	June 15, 2007
	:	
	:	

APPEARANCES: Gregory C. Glynn and Leslie A. Hakala for the Division of Enforcement, Securities and Exchange Commission

Eric Dobberteen of Clark and Trevithick and Shane Tseng of Arnold and Porter, LLP, for Respondent Scott G. Monson

BEFORE: Robert G. Mahony, Administrative Law Judge

INTRODUCTION

The Securities and Exchange Commission (Commission or SEC) initiated this proceeding with an Order Instituting Cease-and-Desist Proceedings (OIP) on September 25, 2006, pursuant to Section 9(f) of the Investment Company Act of 1940 (ICA). The OIP charges that Respondent Scott G. Monson (Monson), while general counsel of JB Oxford Holdings, Inc. (JBOH), and its wholly owned broker-dealer firms JB Oxford & Co. (JBOC) and National Clearing Corporation (NCC)[1], was a cause of JBOC's violations of Rule 22c-1 of the ICA (Rule 22c-1). The OIP alleges that from June 2002 until September 2003 (the relevant period), JBOC's mutual fund department personnel facilitated over 12,000 late mutual fund trades[2] in

[1] For the purposes of this decision, because these two entities are interchangeable and for ease of reference, JBOC will refer to both it and its successors and predecessors.

[2] Mutual funds generally calculate their net asset values (NAVs) at 4:00 p.m. Eastern time by using the closing prices of portfolio securities on the exchange or market on which the securities principally trade. DH2, Inc. v. SEC, 422 F.3d 591, 592 (7th Cir. 2005); Disclosure Regarding Market Timing and Selective Disclosure of Portfolio Holdings, Securities Act Release No. 8343,

over 600 funds, thus violating Rule 22c-1.[3] The OIP also alleges, as JBOC's general counsel, Monson was a cause of these violations based on acts or omissions he knew or should have known would contribute to them. A hearing was held in Los Angeles, California, on January 23-24, 2007.

FINDINGS OF FACT

The findings and conclusions herein are based on the entire record.[4] I applied preponderance of the evidence as the standard of proof. See Steadman v. SEC, 450 U.S. 91, 97-104 (1981). I have considered and rejected all arguments and proposed findings and conclusions that are inconsistent with this Initial Decision.[5]

Background

During the relevant period, JBOH, a publicly traded company headquartered in Beverly Hills, California, provided brokerage and related financial services through its wholly owned subsidiaries. (10-K filed March 30, 2004.) JBOC was JBOH's subsidiary that provided discount

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2003 SEC LEXIS 2937 at *5-9 (Dec. 11, 2003) [hereinafter, Disclosure Regarding Market Timing].

"Late trading" refers to the practice of placing orders to buy or redeem mutual fund shares after a mutual fund has calculated its NAV, but receiving the price based on the previously calculated NAV instead of the NAV next calculated after the orders were placed. Disclosure Regarding Market Timing, 2003 SEC LEXIS at *5-9.

[3] Rule 22c-1 states, in pertinent part: (a) No registered investment company issuing any redeemable security. . . . shall sell, redeem or repurchase any such security except at price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security; . . . (b) For the purposes of this section, (1) the current net asset value of any such security shall be computed no less frequently than once daily, Monday through Friday, at the specific time or times during the day that the board of directors of the investment company sets, in accordance with paragraph [d] of this section, . . . [d] The board of directors shall initially set the time or times during the day that the current net asset value shall be computed, and shall make and approve such changes as the board deems necessary.

[4] Also, pursuant to Rule 323 of the Commission's Rules of Practice, I have taken official notice of information contained within JBOH's filings with the Commission. 17 C.F.R. § 201.323.

[5] Citations to the transcript of the hearing will be noted as "(Tr. __.)." Citations to the Division of Enforcement's (Division) and Monson's exhibits will be noted as "(Div. Ex. __.)," and "(Resp. Ex. __.)," respectively. Citations to the Division's and Monson's posthearing briefs will be noted as "(Div. Post-Hearing Br. at __.)," and "(Resp. Post-Hearing Br. at __.)," respectively. Citations to the Division's and Monson's reply briefs will be noted as "(Div. Reply Br. at __.)," and "(Resp. Reply Br. at __.)," respectively. Citations to Kraig Kibble's investigative testimony of October 8, 2003, will be cited as "(K. Test. at __.)"

and electronic brokerage services to the investing public, as well as clearing and execution services to independent broker-dealers. [6] (Tr. 53-54; 10-K filed April 15, 2003.) JBOC also acted as a market maker in stocks traded on the NASDAQ National Market System and other exchanges. (10-Q filed May 15, 2003.)

Monson is an attorney licensed to practice law in Utah, California, Texas, and the District of Columbia. He has been licensed to practice law since 1985. (Tr. 48.) Monson joined JBOH's predecessor, OTRA Securities Group, in 1989, serving as legal counsel. In 1994, Monson was made associate general counsel and, in September 1997, was appointed general counsel of JBOH. (Tr. 51-52, 55.) Monson served as general counsel for JBOH until he left the company in April 2003.[7] During the relevant period, he reported directly to James Lewis (Lewis), the president and CEO of JBOH. (Tr. 52, 127-29.) Prior to joining JBOH in 1989, Monson was a solo practitioner in family law. (Tr. 148-49.) However, from the time he was hired in 1989, Monson tried to develop a "comprehensive knowledge of the securities industry and regulatory requirements for broker-dealers." (Tr. 63-65; Div. Ex. 303.) Monson has never held any securities licenses. (Tr. 150.)

As general counsel of JBOH, Monson's duties included compiling corporate records and overseeing the preparation and filings of JBOH and its subsidiaries with the Commission. Monson also reviewed leases for office space and was responsible for public relations, which consisted of responding to investors and media with respect to JBOH. By 2000, Monson also held the title of corporate secretary of JBOH. He took minutes at board meetings and circulated them to the board of directors to finalize. (Tr. 54-56.)

From 2000 until he left in 2003, Monson was JBOC's in-house legal counsel, with the title of general counsel, and also was its corporate secretary. Monson's duties for JBOC included overseeing customer complaints, customer arbitrations, and litigation matters, whether they were handled in-house or by outside counsel.[8] Monson also reviewed contracts and other documents for JBOC. (Tr. 55-58, 61.) Monson spent up to ninety-five percent of his time dealing with subpoenas, arbitrations, production of documents, customer litigation and complaints. He also served as a resource to the JBOC compliance and operations departments, when either of those departments requested his opinion about specific legal questions. However,

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[6] In 2003, JBOC transferred its name and accounts to a wholly owned subsidiary of JBOH, Stocks 4 Less, Inc., and the entity previously known as JBOC was renamed NCC. As a result, there was a split in services: JBOC became an introducing broker offering discount and electronic brokerage services to investors; NCC provided clearing and execution services to broker-dealers as well as market-making activities, but no longer maintained retail accounts. NCC did business as JBOC until the split was completed. (10-Q filed August 14, 2003.)

[7] Monson received notice on February 1, 2003, that his contract with JBOH would not be renewed; he left the office in April 2003, but remained on the payroll until June 2003. (Tr. 151-52.)

[8] By 2000, the majority of JBOC's litigation matters were handled by outside counsel. (Tr. 56.)

the compliance department did not look to Monson for resolution of compliance issues. (Tr. 222.) In addition to Monson, JBOC utilized law firms as general outside counsel and for specific areas of law. On several occasions, Monson contacted outside counsel to ask questions about legal issues. (Tr. 60-62, 151, 222.)

The Procedural Agreement

In May and June of 2002, new business came into the JBOC Mutual Fund Department. (Tr. 168; Div. Exs. 287, 349.) E-mails on May 6 and 24, 2002, establish that this "new business" was for clients who wanted to "market time" mutual funds.[9] (Div. Exs. 222, 240, 281, 286.) Prior to signing a procedural agreement, these potential clients wanted to know how late in the day they could submit mutual fund trades to the ADP-SIS system. Lewis asked Kraig Kibble (Kibble),[10] the Assistant Vice-President of the JBOC Operations Department, to look into the trading times in order to have a draft agreement prepared that would define the terms of the mutual fund trading that Lewis negotiated with a European client and the JBOC fees. (Tr. 131-32.)

On May 24, 2002, Kibble called John Conley (Conley), the Customer Service Manager at ADP-SIS. Kibble wanted to know what the mutual fund trade submission cutoff time was for

[9] Market timing involves frequent purchases and sales of mutual fund shares, often with the intent of earning arbitrage profits if the NAV of the mutual fund differs from the value of its underlying portfolio holdings. This discrepancy in valuation may occur if the prices used to calculate the daily NAV become stale. See DH2, Inc. v. SEC, 422 F.3d 591, 592 (7th Cir. 2005); In re Mutual Funds Inv. Litig., 384 F. Supp. 2d 845, 852 n.1 (D. Md. 2005); SEC v. PIMCO Advisors Fund Mgmt., LLC, 341 F. Supp. 2d 454, 458 (S.D.N.Y. 2004).

Although market timing is not per se illegal, the practice can harm a fund's shareholders in several ways. For example, market timing may dilute the value of long-term shareholders' interests in a mutual fund if the fund calculates its NAV using closing prices of its portfolio securities that are no longer accurate. Market timing also may cause a fund to manage its portfolio in a disadvantageous manner, such as maintaining a larger percentage of its assets in cash or liquidating certain portfolio securities prematurely to meet higher levels of redemptions due to market timing. Additionally, a mutual fund also may incur increased brokerage and trading costs, as well as tax liabilities, related to the frequent purchases and redemptions associated with market timing. PIMCO Advisors, 341 F. Supp. 2d at 458; First Lincoln Holdings, Inc. v. Equitable Life Assurance Soc'y, 164 F. Supp. 2d 383, 390-94 (S.D.N.Y. 2001); Disclosure Regarding Market Timing, at *5-9 (Dec. 11, 2003). Accordingly, the potential for market timing to harm the interests of mutual fund investors led many mutual funds to adopt policies intended to limit market timing within their family of funds. PIMCO Advisors, 341 F. Supp. 2d at 459. These policies vary from fund to fund.

[10] Kibble held Series 7 and Series 24 licenses. (Tr. 132.) He was called as a witness at the hearing, but invoked his Fifth Amendment right against self-incrimination with regard to his employment and duties at JBOC. (Tr. 334-38.) However, portions of Kibble's investigative testimony of October 8, 2003, have been admitted into the hearing record.

ADP-SIS in order for the trades to go through to Fund/SERV.[11] Conley advised that ADP-SIS transmitted to the National Securities Clearing Corporation (NSCC) all night, but NSCC required that the last trade transmission had to be by 5:00 p.m. Mountain time, which would be no later than 7:00 p.m. Eastern time. (Div. Ex. 77 at 1-7; Resp. Ex. 512 at 3.) Kibble told Conley that this was "good news" and it was "really important to the people we are trying to bring in." (Div. Ex. 77 at 1-7.) Kibble said he would "talk it over with Jamie [Lewis]." (Div. Ex. 77 at 4.) Absent a computer server error, Kibble understood that having the mutual fund trades submitted by 7:00 p. m. Eastern time would allow the trade to get that day's NAV. (Div. Ex. 77 at 5-6.)

After speaking with Conley, Kibble sent Lewis an e-mail with a copy to Jonathan Cotledge (Cotledge),[12] who worked under Kibble in Operations in the Mutual Funds Department, stating, in pertinent part:

> Today, John Conley . . . told me SIS will allow us to enter mutual fund trades until 3:50 PM Pacific Time so they can transmit to NSCC (Fund/SERV) to meet NSCC's cut off time of 4:00 p. m. That represents an improvement over what SIS had been telling us (3:00 PM Pac Time deadline.)

(Div. Ex. 240.)

Lewis then e-mailed Kibble and Cotledge:

> this is great news! i will tell them that we need preliminary during the day and final orders by 6:30 pm EST . . . and we will continue working on getting a later time entry on orders. i will tell them we want $25MM to start and would like to do more once we show them the great CX we are going to deliver!

(Div. Ex. 240)

That afternoon, after receiving Lewis's e-mail, Kibble e-mailed Conley:

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[11] Fund/SERV is an acronym for the Mutual Fund Settlement, Entry and Registration Verification Service. "Fund/SERV provides a central processing system that collects order information from clearing brokers and others, sorts all the incoming order information according to fund, and transmits the order information to each fund's primary transfer agent." (Resp. Ex. 512. at 3 & n.13) Only NSCC members who are Fund/SERV participants may use the system. Although purchase and redemption orders must be submitted to retail dealers and other intermediaries by 4:00 p.m. to receive that day's price, [SEC] rules permit those intermediaries to forward the order information to Fund/SERV or fund primary transfer agents at a later time. (Resp. Ex. 512 at 3 & n.13.)

[12] Cotledge began working at JBOC in Client Services in January 2000. (Tr. 224.) Sometime in early 2001, Cotledge was asked to switch to Operations in the Mutual Funds Department. (Tr. 225, 250.) His duties included processing retail client trades, reconciling accounts, dealing with different fund transfer agents, and acquiring agreements, as well as selling and networking agreements. Cotledge left JBOC in February 2003 to pursue other opportunities. (Tr. 224-26.)

> Thank you for your helpful information today. I send this email to confirm what we discussed. [JBOC] is bringing in some new business. It is important to the new people involved that JBOC be able to transmit orders to NSCC's Fund/SERV later in the day than JBOC had been doing.
>
> Based on my conversation with you today, I understand that NSCC has a cut off time at 5:00 PM Mtn Time (4:00 PM Pac Time.) Thus SIS has a deadline that broker-dealers must enter mutual fund orders before 4:50 PM Mtn Time (3:50 Pac Time) so those orders can be transmitted to NSCC by NSCC's 5:00 PM Mtn Time cutoff.
>
> I do not yet have a date of when JBOC will begin sending mutual fund orders between 4:00 PM and 4:50 PM Mtn Time. However, please ensure that the SIS employees who are involved with the cutoffs and transmissions of orders to Fund/SERV around that time period will support JBOC during that period . . . .

(Div. Ex. 281.)

Thereafter, during May and early June of 2002, Lewis asked Monson to prepare the draft agreement. It was titled: Mutual Fund Investment Procedural Agreement (Procedural Agreement). Lewis gave Monson instructions on what he wanted in the Procedural Agreement and provided Monson with documents to assist in drafting the document.[13] (Tr. 66-68, 130-31;

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[13] Previously, on May 6, Monson sent Lewis an e-mail about "load fees":

> Jonathan [Cotledge] informs me that most "market timers" are registered reps, and if so, they don't pay load fees. Is this client a registered rep? Also, he said that most market timers trade only in no-load funds. There is not a way to "code" the account for no-load fees otherwise. With that in mind, do you still want the 'commercially reasonable efforts' language in?
>
> Lewis e-mailed Monson with a copy to Kibble:
>
> they are not RRs. they are in London and Switzerland. they usually only trade no loads because they have to pay a "load" on other types of trades-if we waive the load, they will trade them. i would like to use the commercially reasonable language.
>
> kraig, this is an important opportunity for our firm. i want you to make sure your mutual fund team is very strong and 'gets it' when it comes to business thinking, etc. i have been working with Jonathan a good bit lately on this mutual fund opportunity, i think you need to get involved to make sure you understand what the best way to serve the client. scott or i can give you some details. thanks.

(Div. Ex. 222.)

Div. Ex. 287.) Specifically, Lewis wanted Monson to look into excess SIPC insurance and research and draft the indemnification provisions. (Tr. 131-32; Div. Ex. 339, 342-43.) Lewis wanted Monson to ensure that the company was protected and well indemnified. (Tr. 131-32.) Included in the documents provided by Lewis was a term sheet that contained handwritten notes that listed terms Lewis wanted included in the Procedural Agreement. The notes included the terms: "time, market, close/buy or sell, (when is Fund/SERV sent) . . . cancellation service after market . . . [Bank of America] 7:00 p. m. NYC time." (Div. Ex. 75 at 2.)

In addition to meeting with Lewis and reviewing the documents he provided, Monson also used a model mutual fund procedural agreement, provided by a potential JBOC client and created by another broker-dealer, as well as some JBOC agreements to modify the indemnification language. (Tr. 69-71, 77; Div. Ex. 220, 345, 349.) Monson understood that Lewis was trying to come up with the time that the trading would be conducted, which would be the times entered on the Procedural Agreement. (Tr. 66-69, 131-32, 141-44; Div. Ex. 75 at 2.) At the time he was preparing the Procedural Agreement, Monson understood that it would be used as a template and would be available on the office computer for the staff to use with other JBOC customers. (Tr. 107-08, 134.)

The transaction times for engaging in mutual fund trades in the model agreement used by Monson to draft the Procedural Agreement were proposed trades submitted to the broker-dealer before 3:30 p.m. New York time, trade confirmation via telephone 4:00 p.m. New York time. (Div. Ex. 220.) Monson incorporated those times into his draft and added indemnification language and some additional provisions. (Div. Ex. 221.) Later trade submission times were inserted in the Procedural Agreements based on instructions to him from Lewis, Kibble, and Cotledge. (Tr. 71, 77, 132-33; Div. Ex. 221.) [14] The final version of the Procedural Agreement

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[14] Monson did not understand mutual fund trading, but he asked Kibble about it so he could draft the Procedural Agreement. The questions Monson asked Kibble related to meeting the needs of the operations department and the company's need for indemnification and fees. (Tr. 118-19.) Kibble denied talking to Monson about the Procedural Agreements or providing him with any information so he could draft them. (K. Test. at 44-45.) Kibble believed that the [trade submission] 4:15 p.m. time was a practical consideration so the staff could process the trades before going home. (K. Test. at 61-62.) I do not credit Kibble's testimony that he did not provide Monson with information about trade submission time. Kibble discussed the trade submission times with Conley and informed him that later trade times were important to the clients.

In fall 2002, Cotledge requested that the trade submission times in subsequent procedural agreements be changed to a proposed transaction time of 2:00 p.m., New York time, and a confirmation and activation time of 4:15 p.m., New York time. (Tr. 96, 98; Div. Ex. 206.) Cotledge, concerned about his workload and being inundated with trades at the end of the day, recalled asking Monson whether trading after 4:00 p.m., New York time, was permissible; however, he could not recall whether Monson ever answered his question. (Tr. 231-33, 260.) Cotledge assumed the trade submission times in the Procedural Agreements complied with the securities laws and never discussed late trading with anyone in the Compliance Department. (Tr.

prepared by Monson and used by JBOC for its market timing clients contained transaction time language stating that:

> Each day that Customer intends to engage in mutual fund transactions, Customer shall send via Excel spreadsheet or other mutually acceptable means to [JBOC] a list of proposed transactions before 4:15 p.m. New York time. Transaction detail shall include mutual fund names and symbols, plus all other information necessary to effect the transaction(s) as agreed to by the parties. Customer intends to confirm and activate such trade communication via telephone by 4:45 p.m., New York time, which shall be deemed made upon oral or written verification by [JBOC].
>
> [JBOC] shall use its best efforts to execute transactions in the normal course of business via subsequent file transfers to mutual fund companies. Customer is responsible for reviewing such transactions and shall report any corrections due to error to [JBOC]. [JBOC] will use its best efforts to make any corrections with the appropriate mutual fund company, but cannot and does not guaranty that such changes will be made or, if made, will reflect the previous day's fund net asset value . . . .
>
> [JBOC] shall use commercially reasonable efforts to eliminate any load charge or load fee associated with Customer's mutual fund transactions.

(Div. Exs. 205, 222.)

During the time he was drafting the Procedural Agreement, Monson was unaware of Rule 22c-1 and did not know how mutual funds were priced. (Tr. 111-12.) While preparing the Procedural Agreement, Monson never addressed or discussed the trade submission deadlines with anyone in the Compliance Department and never consulted with anyone in the Operations Department to determine if JBOC had a manual regarding mutual fund trading. (Tr. 82-83, 112, 114, 137-38.) Monson also never asked anyone either at or outside of JBOC if the post-4:00 p.m. trade submission times were consistent with the federal securities laws, but he could have contacted outside counsel and inquired. (Tr. 85-86, 92-94, 117, 119.) Monson did not consult any dealer agreements, mutual fund prospectuses, or do any research to determine if accepting trades after the market closed at 4:00 p.m. was prohibited. (Tr. 92-93, 117-18; 234-36.) He was aware, however, that the equity stock markets closed at 4:00 p.m. New York time. (Tr. 94, 97.) It never occurred to him to take any of these steps because he had no concerns as to the legality of the trade times, and that issue was never raised. (Tr. 85-86, 91-92.)

While Monson never asked anyone at JBOC if the trade submission times were proper, he did recall asking Kibble if he was comfortable with them. (Tr. 83.) Kibble, who held securities licenses, was overseeing the market timing project from an operations standpoint.

234, 257-58, 260-63.) When he joined the Mutual Fund Department, his training led him to believe that post 4:00 p.m. trading was not illegal. (Tr. 258.)

Monson's inquiry was related solely to confirming that the trade times accurately reflected the agreement with the customer because the trade submission times were frequently changed. (Tr. 83-84, 93.) In fact, Monson did not know if it was JBOC or the client that wanted post-4:00 p.m. Eastern trade times. (Tr. 93.)

Transactions at Issue

The evidence establishes that the Procedural Agreement drafted by Monson served as the template for the mutual fund investment procedural agreement for seven JBOC clients.[15] (Div. Exs. 73, 204-06, 277-78, 305.) As directed by their individual Procedural Agreements, Cotledge testified that JBOC institutional clients would first send a list of funds they wanted to trade, at or before a preliminary cutoff time. (Tr. 227-29; Div. Exs. 73, 205.) After receiving the trades, the JBOC mutual fund department would research to ensure the CUSIPs[16] and symbols were accurate and would transmit properly when executed. (Tr. 227-28.) The institutional clients would then contact the JBOC Mutual Fund Department, by phone or e-mail, to confirm, cancel, or modify their trading instructions. (Tr. 228-30.) Although JBOC's cutoff time to submit mutual fund trades for retail clients was 4:00 p.m. Eastern time, Cotledge testified that, on a daily basis, JBOC allowed several institutional clients to confirm, cancel, or modify their trading instructions after 4:00 p.m. Eastern time and still receive that day's NAV price. (Tr. 227-48; Div. Exs. 55-60, 72, 206, 305-11, 313-36.) Those institutional clients very rarely confirmed, cancelled, or modified trades before 4:00 p.m.[17] (Tr. 91-92, 181-82, 227-30, 271-72; Div Exs. 55-71, 306-36.)

In July 2003, after Monson left the firm, JBOC received a subpoena from the New York State Attorney General (Subpoena). (Tr. 151-52, 161-62; Div. Ex. 216.) Among other things, the Subpoena requested documents concerning or showing late trading as well as the identity of

[15] The seven clients, the date the Procedural Agreements were signed, and the trading cutoff times are as follows: NetFund, Inc., July 10, 2002, 4:15 p.m. and 4:45 p.m. (Div. Ex. 73); Boston Pipes, LLC, July 22, 2002, 4:15 p.m. and 4:45 p.m. (Div. Ex. 278); LP Advisors, Inc., August 13, 2002, 4:15 p.m. and 4:45 p.m. (Div. Ex. 305); Cockatoo Capital, LLC, August 14, 2002, 4:15 p.m. and 4:45 p.m. (Div. Ex. 205); Samaritan Global Fund, L.P.., October 14, 2002, 4:15 p.m. and 4:45 p.m. (Div. Ex. 277); HC Domestic Fund, LP, October 31, 2002, 2:00 p.m. and 4:15 p.m. (Div. Exs. 206, 207); Wadson Family Ltd. and Winterbottom Family Ltd., December 9, 2002, 2:00 p.m. and 4:15 p.m. (Div. Ex. 204.)

[16] CUSIP is a unique nine-character number assigned to identify each company or issuer and class of security and is used to facilitate the clearing and settling process.

[17] JBOC trading data and e-mails, including their attachments, were reviewed and analyzed by the Division to create a list of transactions for two clients, Kaplan and Company (Kaplan) and David Cooper, showing that JBOC frequently executed late mutual fund trades from August 2002 until August 2003. (Tr. 297, 300-05; Div. Exs. 1-71, 91-92, 111-12, 238, 250-51, 257, 260-62, 264-65, 301-02.) However, the Division represents that Kaplan did not have a Procedural Agreement because it was a clearing broker. (Tr. 180, 282.)

people who engaged in or facilitated late trading. (Div. Ex. 216.) Brad Treichler (Treichler),[18] the Chief Compliance Officer at JBOC, began gathering documents and interviewing JBOC employees in an effort to comply with the Subpoena. (Tr. 161-63, 169-70, 199-202.) Treichler also looked for a rule regarding late trading but was unable to find one. (Tr. 187-88.) Upon initial review of the Subpoena, Treichler did not think that late trading would be an issue because he did not think JBOC would be engaging in such a practice. (Tr. 172-73.) Thus, Treichler was unaware that JBOC was accepting mutual fund trades after 4:00 p.m. Eastern time prior to gathering information and speaking with people from the Mutual Fund Department. (Tr. 164, 168, 172-73.)

Treichler was also unaware of the existence of the Procedural Agreement, in any version, prior to receiving the Subpoena.[19] (Tr. 161-65, 168, 207-08.) It was not until he began gathering documents in an effort to comply with the Subpoena that Treichler discovered the Procedural Agreements in the files. (Tr. 173-74, 176-77.) Treichler was surprised when he learned that JBOC was engaged in post-4:00 p.m. Eastern time mutual fund trading because it seemed obvious from his experience in the securities industry that JBOC could not engage in that sort of activity. (Tr. 172-73, 216.) However, he was also surprised that the Subpoena called for information about market timing because he did not believe that there was anything about market timing that could involve compliance issues. (Tr. 198-99.) Shortly after discovering the late trading, Treichler told JBOC to cease all late trading. (Tr. 221-22.) [20]

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[18] Treichler began working for JBOC in 2002 as the Assistant Vice President of Operations in New Accounts. (Tr. 156-58.) After Treichler was with JBOC for about one or two months, Lewis asked him to become the Chief Compliance Officer. (Tr. 158, 177, 199-200.) He held both roles until October 2002, when he was told he would no longer be in operations. (Tr. 167.) Treichler reported to Lewis, until Barry Fischer joined JBOC as general counsel, whereupon Treichler reported to him. (Tr. 195.) During the time of his employment at JBOC, Treichler held several securities licenses, including Series 4, 8, 9, 10 and 24 licenses. (Tr. 156, 196-97.) Treichler created a compliance manual for JBOC in 2002. (Tr. 166, 190-91.) Treichler left JBOC in September of 2004. (Tr. 156.)

[19] As Chief Compliance Officer, Treichler was aware of some of the new mutual fund business coming to JBOC. However, he did not believe that he had to know the details of any new agreements to ensure compliance with the securities laws. He viewed these accounts as the same as those that came in on a daily basis. (Tr. 191-92.)

As a typical part of his duties, Treichler reviewed the new account applications and paperwork for customers to ensure they were completed properly. (Tr. 158-60, 168.) Treichler testified that none of the new account agreements he reviewed contained the Procedural Agreement at the time of his initial review. (Tr. 158-60, 218; Div. Exs. 202, 203, 205.) However, Monson testified that he gave Treichler the Procedural Agreement after they were signed by the customer. (Tr. 80-82). Whether Treichler saw the Procedural Agreements or not, I credit Monson's testimony that he gave the Procedural Agreement to Treichler as part of the clients' application.

[20] In August 2004, the Commission filed a civil action in the United States District Court for the Central District of California against JBOH, JBOC, Lewis, Kibble, and James Y. Lin. SEC v. JB

Expert Testimony

Steven Thel

Steven Thel (Thel), the Division's expert witness, is the Wormser Professor of Law at Fordham University School of Law, where he has been employed since 1988. (Tr. 360-61.) He teaches contracts, securities regulation, corporate finance, and a seminar in advanced business law. He also co-authored "Investment Management Law and Regulation." (Tr. 361.) He graduated from Harvard Law School in 1979 and has extensive professional experience practicing in the securities industry. (Tr. 361-63; Div. Ex. 269.)

Thel testified that a reasonable lawyer employed as the general counsel to a registered broker-dealer that does business in mutual funds would have known of Rule 22c-1, what it prohibited, and would have looked at the dealer agreements and the prospectuses referenced therein. (Tr. 370, 377-78.) Thel testified that any lawyer who was asked to draft a new account agreement should review the dealer agreement to ensure that all contractual obligations are being complied with. (Tr. 374-75, 381.) Thel testified that any lawyer taking a quick glance at the dealer agreement and prospectuses referenced therein would have realized that the Procedural Agreement contemplated trading that violated the policies of the various mutual funds, regardless of whether the lawyer had any knowledge of Rule 22c-1. (Tr. 375; Div. Exs. 79-83.)

In the event a lawyer was unaware of Rule 22c-1, Thel testified that a reasonable lawyer would have inquired into secondary sources such as JBOC's manual on mutual funds, consulted or called someone at the fund's trading offices or legal department, or consulted a professional who specializes in fund work. (Tr. 382-84.) Thel testified that any of these steps would have resulted in discovery of Rule 22c-1. Thel testified that Monson's actions fell far short of what a reasonable lawyer would have done. (Tr. 388.)

Keith Bishop

Keith Bishop (Bishop), Respondent's expert witness, has a Bachelor of Arts from Harvard College and a Juris Doctor from the University of Southern California Law Center and is currently a shareholder in the Irvine, California, office of Buchalter Nemer (Tr. 416-17.) Bishop has been a practicing attorney since 1981 with extensive professional experience in corporate governance and professional responsibility with respect to attorneys in California. (Tr. 417-19.) He is an adjunct professor at Chapman University Law School. (Tr. 419-20.)

Oxford Holdings, Inc., No. CV 04-7084 PA (VBKx) (C.D. Cal.). On August 24, 2005, the district court granted the Commission's motion for partial summary judgment against JBOC and found that JBOC's conduct facilitated late trading and violated Rule 22c-1 of the ICA. (Div. Ex. 267.) Ultimately, JBOC and the other defendants settled the district court action and administrative proceedings brought by the Commission. JB Oxford Holdings, Inc., 87 SEC Docket 473 (Jan. 18, 2006); James G. Lewis, 87 SEC Docket 911 (Feb. 2, 2006); Kraig L. Kibble, 86 SEC Docket 1998 (Nov. 3, 2005); James Y. Lin, 87 SEC Docket 909 (Feb. 2, 2006). 17 C.F.R. § 201.323 (official notice).

Bishop is of the opinion that when Monson drafted the Procedural Agreement he did not fail to exercise the degree of skill, prudence, and diligence that lawyers of ordinary capacity and skill commonly possess. (Tr. 429-30.) Bishop bases his opinion on Monson's duties as the general counsel of JBOC, the plain language of Rule 22c-1, and the Procedural Agreement and other underlying documents.

As general counsel for JBOC, Monson was responsible for overseeing litigation, arbitration, and filings made under the federal securities laws. Bishop opines that because Monson, as general counsel, had no supervisory responsibilities over JBOC's compliance department, he had no duty to ensure that the Procedural Agreement was not used by JBOC, to avoid compliance with the federal securities laws. Thus, it was the duty of the Chief Compliance Officer, Treichler, to ensure operational compliance with the federal securities laws. (Tr. 434-36.)

Bishop further opines that the Procedural Agreement, on its face, does not contemplate a per se violation of Rule 22c-1. (Tr. 439-41.) Rule 22c-1 does not mention specific times, only that trades be priced at the NAV "next computed" after the order is received. Thus, according to Bishop, the post-4:00 p.m. Eastern time in the Procedural Agreement does not give rise to a violation. (Tr. 439-41.) According to Bishop, the Procedural Agreement merely states when an order will be deemed activated and is silent on what NAV will be given to the transaction. (Tr. 440.) Bishop believes that looking at the selected dealer agreements and the prospectuses would not have resulted in finding a violation of Rule 22c-1 because "the prospectuses themselves don't even say that 4:00 p.m. Eastern is an absolute time." (Tr. 439-40.) Bishop's opined that one would have to know when the NAVs were calculated to determine if Rule 22c-1 was violated. (Tr. 441.)

CONCLUSIONS OF LAW

The Division seeks a cease-and-desist order pursuant to Section 9(f) of the ICA under the theory that Monson caused JBOC to violate Rule 22c-1. Section 9(f) of the ICA provides for secondary causing liability if a respondent is a cause of another's violation where the respondent knew or should have known that his or her act or omission would contribute to such violation.

The Commission has determined that causing liability requires finding that: (1) a primary violation occurred; (2) an act or omission by the respondent contributed to the violation; and (3) the respondent knew, or should have known, that his or her conduct would contribute to the violation. See Erik W. Chan, 55 S.E.C. 715, 724-26 (2002); Robert M. Fuller, 80 SEC Docket 3539, 3545 (Aug. 25, 2003), pet. denied, 2004 U.S. App. LEXIS 12893 (D.C. Cir. Apr. 23, 2004); Harrison Sec., Inc., 83 SEC Docket 2986, 3037 (Sept. 21, 2004), final, 84 SEC Docket 117 (Oct. 29, 2004).

Negligence is sufficient to establish liability for causing where, as here, the primary violation is non-scienter based. KPMG Peat Marwick LLP, 74 SEC Docket 384, 421 (Jan. 19, 2001), recon. denied, 74 SEC Docket 1351 (Mar. 8, 2001), pet. denied, 289 F.3d 109 (D.C. Cir. 2002); Edward D. Jones & Co., 66 SEC Docket 3086, 3094-95 (April 15, 1998). Negligence is

the failure to exercise reasonable care or competence. Byron G. Borgardt, 80 SEC Docket 3559, 3577 & n.35 (Aug. 25, 2003).

Primary Violations

Rule 22c-1, also known as the "forward pricing" rule, requires mutual funds, their principal underwriters, dealers, and any person designated in the fund's prospectus, as authorized to consummate transactions in the fund's securities, to sell and redeem fund shares at a price based on the NAV next computed after receipt of an order to buy or redeem. Rule 22c-1(b) generally requires mutual funds to compute their NAVs at least once daily, Monday through Friday, at a specific time or times as set by their board of directors. Most funds calculate NAV when the major U.S. stock exchanges close at 4:00 p.m. Eastern time.

The time of receipt of an investor's order by an intermediary, rather than the time of receipt by the fund or the underwriter, is the time for determining the price the order will receive. (Resp. Ex. 512 at 3.) Thus, an investor's order must be priced based on the mutual fund's NAV that is next computed after the intermediary receives or confirms that order.

In the instant proceeding, the funds' prospectuses show that the funds' NAV was to be calculated at 4:00 p.m. Eastern time. (Tr. 331-33; Div. Exs. 79-83, 93-110.) It follows, therefore, that orders to buy or redeem shares of a mutual fund placed at or before 4:00 p.m. Eastern time on a given day must receive that day's NAV, but orders placed after 4:00 p.m. Eastern time, must be priced at the NAV that is calculated the following day.[21] To establish a violation of Rule 22c-1, the evidence must show that JBOC received or confirmed orders after 4:00 p.m., but allowed customers to receive the NAV already determined as of 4:00 p.m. that same day.

The evidence proving that JBOC violated Rule 22c-1 is overwhelming. The Division submitted numerous e-mails with attachments showing that these JBOC clients, who had a Procedural Agreement in effect, placed or confirmed mutual fund orders after 4:00 p.m. Eastern time. (Div. Exs. 1-71, 306-36.) Referencing those e-mails with the individual customer's trade blotter shows that the trades in the e-mails were executed by JBOC after 4:00 p.m. Eastern time, and that these customers still received that same day's NAV. (Tr. 297-327; Div. Exs. 91, 111-12.) Based on this trading pattern, I conclude that JBOC violated Rule 22c-1.

Did Monson contribute to and cause JBOC's violations of Rule 22c-1?

Monson can be found to have caused JBOC's violations of Rule 22c-1 if he was responsible for an act or omission that he knew or should have know would contribute to the violation. See Rita J. McConville, 85 SEC Docket 3127, 3145 (June 30, 2005); Fuller, 80 SEC Docket at 3545.

[21] See e.g. Staff Interpretive Positions Relating to Rule 22c-1, 1968 SEC LEXIS 979 (Dec. 27, 1968).

The first question to address is whether Monson committed an act or omission that contributed to the primary violation. The Division does not need to prove that Monson was the proximate cause of the primary violation. McConville, 85 SEC Docket at 3146. Monson drafted the Procedural Agreement and knew that it would be used as a template for JBOC to contract with clients. (Tr. at 94-95.) The Procedural Agreement allowed several JBOC clients to trade as late as 4:45 p.m. Cotledge testified that the times in the Procedural Agreement "guided" his understanding of how late he could accept trades. (Tr. at. 239.) Therefore, I conclude that Monson committed an act that contributed to JBOC's primary violations.

The only remaining question is whether Monson knew or should have known that drafting the Procedural Agreement would contribute to JBOC's late trading. The Division proposes two theories for how Monson caused JBOC's violations. The first theory is that Monson was negligent in preparing the Procedural Agreement template because he did not "spot the issue" that Rule 22c-1 could be implicated in relation to the Procedural Agreement trade submission times. Therefore, the Division contends, Monson is directly responsible for the late trading by JBOC clients who signed a Procedural Agreement. (Div. Post-Hearing Br. at 14-19.) The second theory of causation is that the Procedural Agreement created a "culture" wherein the Operations Department believed that late trading was not a problem for JBOC clients, like Kaplan, who never signed a Procedural Agreement. (Tr. 282-84; Div. Post-Hearing Br. at 13.)

I find that the Division's "culture" theory of causing liability is not supported by the record. Monson was the general counsel and corporate secretary of JBOC. However, he supervised only his secretary; he did not control the daily activities of the Operations Department or decisions made by JBOC's Compliance Department. Cotledge was in the Operations Department dealing with mutual funds from 2001 to February 2003. (Tr. 225-26.) Based on the training Cotledge received when he joined the mutual fund department, at no time during his employment at JBOC did he believe that 4:00 p.m. had any particular significance in mutual fund trading. Even though he had access to the Mutual Fund Manual, Cotledge did not believe that giving that day's NAV to an order entered after 4:00 p.m. was illegal. (Tr. 257-58.) In light of Cotledge's testimony, I find that the Procedural Agreement template did not contribute to or cause any "culture" about the appropriate NAV to give in mutual fund trading. The "culture" preceded the use of the Procedural Agreements and apparently it was a standard practice to give the same day's NAVs for late trading. Specifically, I find that Monson did not cause JBOC to violate Rule 22c-1 in any of the late trading transactions involving clients, such as Kaplan, who did not have a Procedural Agreement.

The Division does not allege that Monson knew the Procedural Agreement violated Rule 22c-1, and the record clearly shows that Monson did not intentionally violate Rule 22c-1. Therefore, in order to prove Monson was a cause of JBOC's violation the Division must prove that Monson should have known that his conduct would result in JBOC's late trading. For several reasons, I find that the Division has not met its burden.

Monson's scope in drafting the Procedural Agreement was limited. In May or early June 2002, at their initial meeting to discuss preparing a draft of the Procedural Agreement, Lewis charged Monson with the specific tasks of obtaining excess SIPC insurance and researching and drafting the indemnification and fee provisions. At approximately the same time, Lewis gave

Kibble the responsibility of determining the mutual fund trade submission cutoff times. Monson was never given the task of determining whether the times in the Procedural Agreement were a violation of any securities regulations. Monson's draft initially included times that, had they been kept in, very likely would have prevented violations of Rule 22c-1. (Div. Ex. 221.) It was not until Monson was directed by Lewis, Kibble, or Cotledge, at the behest of Kibble, that the times were changed. There is no evidence that Monson decided independently to change the trade submission times. Based on Monson's limited scope in drafting the Procedural Agreement and his reliance on Lewis, as CEO, Kibble, as Assistant Vice President of Operations, and Cotledge, who had operations experience, Monson did not act negligently in accepting the trade times that they instructed.

Monson's daily duties as the sole in-house counsel for JBOC consisted of managing outside counsel, reviewing non-securities related issues (e.g., leases), and preparing JBOC's corporate documents and filings with the Commission, but did not include any responsibilities for operations or compliance. The Division provided no evidence to show that Monson assigned an NAV to any trades or knew what NAV trades were receiving. In fact, the first time a Procedural Agreement was used that forms the basis of the charge in this proceeding was July 10, 2002, more than a month after Monson completed his work on the draft. His duties did not require him to anticipate what might happen in the future or to search for prospectuses or other documents for any of the seven clients who were apparently unknown to him when he did the draft.

Further, the Procedural Agreement, on its face, does not raise sufficient "red flags." The Procedural Agreement defines when JBOC's clients can "confirm and activate . . . trade communication." (Div. Ex. 205) However, the Procedural Agreement is silent on what NAV the trade communication will receive. In this regard, I credit the testimony of Bishop, who opined that a lawyer of ordinary skill and capacity "would not have recognized that the insertion of a time after 4:00 p.m. Eastern time in the draft procedural agreement could involve a violation of Rule 22c-1." (Resp. Ex. 514 at 5) Even if the Procedural Agreements are read in conjunction with the prospectuses or JBOC's Mutual Fund Manual, as the Division suggests, it is not clear that the Procedural Agreement contemplates a violation of Rule 22c-1. Rule 22c-1 is violated when a trade that was received after the NAV was established still receives that day's NAV. Because the Procedural Agreement is silent as to what NAV to use, it does not result in a per se violation of Rule 22c-1. It was not until someone other than Monson interpreted and implemented the Procedural Agreement that a violation occurred.

The Division cites several proceedings, both contested and settled, in support of its position. (Div. Post-Hearing Br. at 18-19.) Settled proceedings, however, have little, if any precedential value as no aspect of the case is ever litigated or presented to a decision maker acting judicially or quasi-judicially. Carl L. Shipley, 45 S.E.C. 589, 591-92 n.6 (1974). The contested proceedings upon which the Division relies are distinguishable from the instant proceeding.

In the contested proceedings, the "causing" respondent had some type of actual knowledge, or had received information, and failed to communicate it for a specific task he was asked to perform; or was a part of his general responsibilities or duties. See Erik W. Chan, 55

S.E.C. 715, 724-26, 734 (2002) (issuer's Secretary caused antifraud violations because he had personal/actual knowledge of misrepresentations and omissions in a private placement memorandum he was asked to review and comment on, but did nothing to correct it); Ira Weiss, 86 SEC Docket 2588 (Dec. 2, 2005) (respondent-counsel was hired specifically for the purpose of rendering an opinion and advice on the tax exempt status of bonds); McConville, 85 SEC Docket 3127 (June 30, 2005) (CFO and later corporate controller misled auditors despite knowing that the company had several problems with its internal accounting controls and financial statements).[22] In contrast, Monson had no actual knowledge of Rule 22c-1. He had no assigned duty or delegated responsibility for researching any possible legal implications of the trade times which were geared to the Fund/SERV requirements. Thus, the authorities the Division cites are unpersuasive.

Based on the specific circumstances described above, I find that the Division has failed to prove by a preponderance of the evidence that Monson knew, or should have known, that drafting the Procedural Agreement would contribute to JBOC's primary violations.

RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, I certify that the record includes the items set forth in the record index issued by the Secretary of the Commission on May 16, 2007.

ORDER

Based on the findings and conclusions set forth above:

IT IS ORDERED THAT this proceeding brought against SCOTT G. MONSON be, and it hereby is, DISMISSED.

[22] For the same reasons, the settled proceedings upon which the Division relies are distinguishable. See Craig M. Waggy, 88 SEC Docket 1237 (July 5, 2006) (respondent-CFO, who as part of his duties was responsible for company's books and records, received financial information that was contrary to the financial information provided in periodic reports filed with the Commission); Google, Inc., 84 SEC Docket 2452 (Jan. 13, 2005) (respondent-general counsel advised board of directors to approve a new stock option plan; but failed to inform the board of the ramifications of issuing options despite his knowledge of the underlying laws); John E. Isselmann, Jr., 83 SEC Docket 2905 (Sept. 23, 2004) (respondent-general counsel, who was involved in the review process of a company's quarterly report, failed to disclose written legal advice he received from outside counsel to a company's audit committee, board of directors, and auditor; and, caused the company to file materially false financial reports in a quarterly report filed with the Commission).

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice, 17 C.F.R. § 201.360. Pursuant to that rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111 of the Commission's Rules of Practice, 17 C.F.R. § 201.111. If a motion to correct manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or a motion to correct a manifest error of fact, or the Commission determines on its own initiative to review the Initial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

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Robert G. Mahony
Administrative Law Judge