

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

1:07-cv-1198
Robert J. Jonker, U.S. District Judge

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION,

Plaintiff,

v.

DANIEL N. JONES AND
AZURE BAY MANAGEMENT, LLC

Defendants.

CIVIL ACTION
CASE NO.

COMPLAINT FOR PERMANENT INJUNCTIONS
AND OTHER EQUITABLE RELIEF

Plaintiff United States Securities and Exchange Commission (the "Commission") alleges
as follows:

SUMMARY

1. Investors in The Addington Fund LP ("Addington" or the "Fund"), a hedge fund, recently learned, on November 1, 2007, that for approximately the last two years the Fund suffered severe and undisclosed losses. Daniel N. Jones ("Jones"), portfolio manager and President of Addington, admitted to investors that he concealed from them losses that the Fund incurred sometime in 2005. For nearly two years, Jones prepared false statements and performance reports that he disseminated to the Fund's investors. Jones hid the true performance of the Fund, and instead of having a value of \$2.1 million, as Jones told investors, the Fund only has approximately \$200,000 remaining. Despite these losses, the Fund's general partner, Azure Bay Management, LLC ("Azure Bay"), through Jones, (collectively the "Defendants") continued to take fees of at least \$135,000 based on the Fund's false performance.

2. There is an imminent risk that investors will be further harmed. Jones caused Azure Bay to take \$16,500 in unfounded fees as recently as September 11, 2007, and has declared his intention to liquidate the Fund's remaining assets. Moreover, Jones is continuing to solicit funds, both for a new fund called The Addington Fund II ("Addington II") and for at least one other account that is under his management. Jones has proposed paying Addington investors back from fees generated from his management of this other account. Injunctive relief is required to preserve the remaining Addington assets, stop Jones and Azure Bay from taking further unfounded fees, halt Jones' solicitation of new funds, and ensure that remaining funds are returned to investors in a fair and orderly manner.

DEFENDANTS

3. Jones, age 42, is founder and President of Addington. Jones lives in Battle Creek, Michigan and conducts business from offices at 67 West Michigan Avenue, Suite 315, Battle Creek, Michigan, 49017. Jones manages Addington, which is an unregistered investment pool and a Delaware registered limited partnership.

4. Azure Bay is a Delaware limited liability corporation formed in 2001 and is based in Battle Creek, Michigan. Azure Bay is Addington's general partner and conducts business from offices at 67 West Michigan Avenue, Suite 315, Battle Creek, Michigan, 49017.

JURISDICTION AND VENUE

5. The Commission brings this action pursuant to the authority conferred on it by Section 20(b) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. § 77t(b)] and Section 209(d) of the Investment Advisers Act of 1940 (the "Advisers Act") [15 U.S.C. § 80b-9(d)].

6. The Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Section 214 of the Advisers Act [15 U.S.C. § 80b-14], and 28 U.S.C. §1331.

7. Venue is proper in this Court pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 214 of the Advisers Act [15 U.S.C. § 80b-14].

8. The acts, practices, and courses of business constituting the violations alleged herein occurred within the jurisdiction of the United States District Court for the Western District of Michigan and elsewhere.

9. Defendants, directly and indirectly, have made, and are making, use of the means and instrumentalities of interstate commerce and of the mails in connection with the acts, practices and courses of business alleged herein in the Western District of Michigan and elsewhere.

FACTS

The Addington Fund

10. In 2001, Jones started a private hedge fund called Addington. The Fund has 11 investors who contributed a total of \$1.5 million to the Fund.

11. Azure Bay is Addington's general partner. As the general partner, Azure Bay is responsible for investment decisions on behalf of the Fund and for the execution of the Fund's portfolio transactions.

12. Jones handles the day to day management of the Fund's investment portfolio for Azure Bay. Jones controls Azure Bay through his ownership of Azure Bay's parent company.

13. Both the Fund's Private Placement Memorandum ("PPM") and the Limited Partnership Agreement provide Azure Bay with a management fee of 1% per year of each investor's capital balance, as of the first day of each month. This fee was subsequently increased by a later version of the PPM and an Amended and Restated Limited Partnership Agreement to 2% for any investor in the fund after September 8, 2006.

14. The PPM and Limited Partnership Agreement set forth a performance fee determined at year's end. The performance fee is 20% of any positive total return. A negative total return is carried forward to the following year, and reduces a subsequent year's performance fee allocation.

15. The performance fee is subject to a high water mark restriction. Azure Bay only receives performance fees when Addington's value is greater than its previous greatest value. If the Fund's value drops, Azure Bay must bring the Fund back above the previous greatest value before it can receive a performance fee.

16. Addington's largest investor is a Chicago-based investment adviser serving high net worth individuals and families (hereinafter referred to as "Investor A"). Investor A invested \$500,000 for a client in approximately July 2004, and invested \$150,000 on behalf of another client in approximately September 2005.

17. A principal of Investor A monitored its clients' investments in Addington and spoke to or met with Jones regularly to discuss the Fund's performance.

18. Investor A received regular communications from Jones about the Fund's performance. Jones provided Investor A with monthly performance reports, which disclosed, among other things, the investor's beginning and end portfolio value for the month.

19. Jones provided Investor A with monthly review and outlook statements that showed the current monthly and year-to-date performance, as compared against the S&P 500 and the Russell 3000 indexes. The monthly review and outlook statements also contained historical performance for the Fund broken down by month, quarter, and year.

20. Investor A received periodic emails from Jones that relayed information about the Fund's trading strategies, positions, and performance.

21. The monthly performance reports, the monthly review and outlook statements, and the periodic e-mails show the Fund performing well. Addington reported annual returns of 8.09% in 2005, 17.09% in 2006, and a year-to-date return of 18.02% through the third quarter of 2007.

22. The monthly review and outlook statements also showed that Addington's performance exceeded the S&P 500 and Russell 3000 indexes.

23. In Jones' periodic emails to Investor A, he summarized the Fund's performance, and generally showed positive returns for the fund in 2006 and 2007.

24. Azure Bay took fees for managing the Fund. Jones caused Azure Bay to collect at least \$94,273 in fees for 2007.

25. Investor A's clients paid \$19,561 in fees for 2005, \$41,854 in fees for 2006, and \$46,044 in fees for 2007.

The November 1, 2007 Meeting

26. Beginning in 2005, Jones approached a principal of Investor A with a new investment opportunity called Addington II. Jones advised this investor that Addington II would be nearly identical to Addington and Azure Bay would be the new fund's general partner. Jones supplied Investor A with Addington II promotional materials which touted the investment performance of the original Addington Fund for 2001-2005.

27. Jones and Investor A discussed Addington II throughout 2006 and much of 2007. During this time, Jones represented that Addington II would have the same performance as Addington and that Addington's historical returns had been positive, as specifically represented in the monthly performance reports, the monthly review and outlook statements, and the periodic emails.

28. Before making an investment, the principal of Investor A asked to meet Jones at Azure Bay's office to conduct an on-site review.

29. The meeting occurred on November 1, 2007. When the principal of Investor A asked for Addington's brokerage and account statements, Jones admitted that he had lost Addington's capital sometime in 2005 through bad trades. Jones admitted that all account and investor statements since that time were false.

30. During the November 1 meeting, Jones:

- a. Told the principal of Investor A that Addington's false returns were generated by a model portfolio and did not reflect the Fund's true performance;
- b. Gave the principal of Investor A Addington's September 2007 brokerage statement which shows that the Fund has \$201,778.72 in assets and that Jones withdrew \$16,500 on September 11, 2007; and
- c. Produced a brokerage statement for another fund he manages, which he represented to be a separately managed account with Addington. This account was valued at \$5.5 million as of September 28, 2007.

Jones' November 1 and 2, 2007 Emails

31. After the November 1 meeting, that same day Jones sent an email to all Addington investors. He admitted to losing Addington's capital and covering up Fund losses for the past two years. Investors were told that their monthly reports were false, tax statements could not be relied upon, and the Fund's performance to date was inaccurate.

32. Jones admitted that these errors were his fault and that he had continued managing the Fund in an effort to recover Addington's losses.

33. Jones sent a second email on November 2, 2007 to Fund investors. In this email, Jones promised to repay investors in full within 3 to 5 years. Jones said he is moving towards liquidating the Fund's remaining assets and proposed using performance fees earned on a separately managed account with Addington to repay Fund investors. He claimed this other account generated a performance fee of over \$60,000 for one quarter, and that the amount under management in the account would likely increase.

34. In the November 2 email, Jones told investors that the fees generated from the management of these assets would allow him to repay Addington investors in 3 to 5 years after allowing for overhead expenses, including paying Jones' salary.

Misrepresentation of Material Fact and Breach of Fiduciary Duty

35. From at least January 2006 to October 2007, Jones and Azure Bay, in connection with the offer and sale of limited partnership interests in Addington II, made material misrepresentations to Investor A. Jones advised Investor A, a prospective investor in Addington II, that Addington II would perform as well as Addington. The Addington performance figures, however, were false and misleading. Instead of making the gains that Jones represented to Investor A, Addington suffered significant and undisclosed losses in 2005.

36. The misrepresentation of Addington's performance was material because it pertains to the anticipated performance of Addington II and serves as a basis for a reasonable investor to assess the merits of an investment in Addington II. Jones made the misrepresentations knowingly or recklessly because he knew the true performance of the Fund and knew that he had been hiding significant losses.

37. From at least January 2006 to October 2007, Jones and Azure Bay took fees to which they were not entitled, and which were computed based on the falsely inflated value of the Fund. The fees were material. A reasonable investor would consider it important that its investment adviser was taking fees in excess of those allowed, thereby misappropriating the Fund's assets. Jones and Azure Bay knew or were reckless in not knowing that they took fees to which they were not entitled.

The Threat of Ongoing Use and Solicitation

38. There is a reasonable likelihood that Jones and Azure Bay will engage in future violations of the securities laws.

39. Addington has approximately \$200,000 in remaining capital. The Defendants recently withdrew \$16,500 in supposed fees from Addington. Jones and Azure Bay continue to have trading authority over the Addington account, and have plans to liquidate the Fund's remaining assets.

40. Jones continues to have management authority over a separate account that has approximately \$5.5 million. On information and belief, Jones is soliciting additional funds for that account so that he can use the fees generated by the management of that account to repay Addington investors. Jones is likely to be fraudulently soliciting those funds, having neglected to disclose his fraud in connection with Addington.

COUNT I

Violations of Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)]

41. Paragraphs 1 through 40 are realleged and incorporated by reference.

42. At the times alleged in this Complaint, Defendants, in the offer and sale of securities in the form of limited partnership interests in Addington II, by the use of the means and instruments of transportation and communication in interstate commerce and by the use of the mails, directly and indirectly, have employed and are employing devices, schemes and artifices to defraud, all as more fully described above.

43. In the offer and sale of securities described above and as part of the scheme to defraud, Defendants have made and are making false and misleading statements of material fact or have omitted and are omitting to state material facts necessary in order to make the statements

made, in light of the circumstances under which they were made, not misleading to investors and prospective investors regarding, among other things, the performance of Addington.

44. Defendants knew or were reckless in not knowing that the statements described herein were materially false and misleading.

45. By reason of the activities described herein, Defendants have violated and are violating Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)].

COUNT II

Violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and (3)]

48. Paragraphs 1 through 40 are realleged and incorporated by reference.

49. At the times alleged in this Complaint, Defendants, in the offer and sale of securities, by the use of the means and instruments of transportation and communication in interstate commerce and by the use of the mails, directly and indirectly, obtained money or property by means of an untrue statement of a material fact or an omission to state a material fact necessary in order to make statements made, in the light of the circumstances under which they were made, not misleading, as more fully described above.

50. At the times alleged in this Complaint, Defendants, in the offer and sale of securities, by the use of the means and instruments of transportation and communication in interstate commerce and by the use of the mails, directly and indirectly, engaged in transactions, practices and courses of business which operated or would have operated as a fraud and deceit upon purchasers, as more fully described above.

51. By reason of the activities described herein, Defendants have violated and are violating Sections 17(a)(2), and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(2) and (3)].

COUNT III

Violations of Section 206(1) and (2) of the Investment Advisers Act of 1940 [15 U.S.C. § 80b-6(1) and (2)]

52. Paragraphs 1 through 40 are realleged and incorporated by reference.

53. At all times alleged in the Complaint, each of the Defendants was an investment adviser as defined under the Investment Advisers Act of 1940. The Defendants manage the investments of the Fund in exchange for compensation in the form of performance and management fees.

54. Each of the Defendants, while acting as an investment adviser, by the use of the means and instrumentalities of interstate commerce and of the mails, directly and indirectly, has employed and is employing devices, schemes and artifices to defraud its client, the Fund; and has engaged and is engaging in transactions, practices, and courses of business which operate as a fraud or deceit upon its client, the Fund.

55. By reason of the activities described herein, the Defendants have violated and are violating Sections 206(1) and (2) of the Investment Advisers Act of 1940 [15 U.S.C. § 80b-6].

PRAYER FOR RELIEF

WHEREFORE, the Commission requests that the Court:

I.

Find that Defendants committed the violations alleged above.

II.

Grant a Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, restraining and enjoining Defendants Jones and Azure Bay, their officers, agents, servants, employees, attorneys and those persons in active concert or participation with them who receive actual notice of the Permanent Injunction, by personal service or otherwise, and each of them, from, directly or indirectly, engaging in the acts, practices or courses of business described above, or in conduct of similar purport and object, in violation of Sections 17(a)(1), 17(a)(2) and 17(a)(3) of the Securities Act [15 U.S.C. §§ 77q(a)(1), q(a)(2) and q(a)(3)], and Sections 206(1) and (2) of the Advisers Act [15 U.S.C. § 80b-6(1) and (2)].

III.

Grant an Order requiring Defendants Jones and Azure Bay to disgorge all profits or proceeds that they have received as a result of the acts and courses of conduct complained of herein, with prejudgment interest.

IV.

Grant an Order prohibiting Defendants Jones and Azure Bay, their officers, agents, servants, employees, attorneys, and those persons in active concert or participation with them who receive actual notice of the Order of Permanent Injunction by personal service or otherwise, and each of them, from directly or indirectly,

A. transferring, selling, assigning, pledging, dissipating, concealing or otherwise disposing of in any manner, any funds, assets, accounts, or other property belonging to, or in the possession, custody or control of the Defendants Jones and Azure Bay, wherever located,

B. transferring, selling, assigning, pledging, dissipating, concealing or otherwise disposing of in any manner, any funds, assets, accounts, or other property belonging to, or in the possession, custody or control of Addington, wherever located,

C. destroying, mutilating, concealing, altering or disposing of in any manner, any of the books, records, documents, correspondence, brochures, manuals, obligations or other property (including records contained on any computer or computer diskette) pertaining to the Fund and Azure Bay, wherever located.

V.

Grant an Order directing the Defendants to pay civil fines and/or penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. §77t(d)] and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9(e)].

VI.

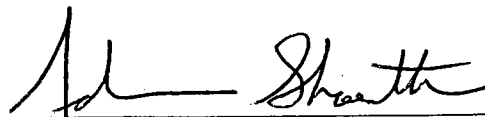
Retain jurisdiction of this action in accordance with the principals of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees that may be entered or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VII.

Grant Orders for such further relief as the Court may deem appropriate.

Dated: November 29, 2007

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Linda Ieleja Gerstman". The signature is written in a cursive style with a horizontal line underneath.

Linda Ieleja Gerstman (IL ID # 6204334)

Andrew Shoenthal (IL ID # 6279795)

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