

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

In the Matter of :
: INITIAL DECISION
MONTFORD AND COMPANY, INC. : April 20, 2012
D/B/A MONTFORD ASSOCIATES, and :
ERNEST V. MONTFORD, SR. :

APPEARANCES: W. Shawn Murnahan, M. Graham Loomis, and Michael J. Cates for the
Division of Enforcement, Securities and Exchange Commission

Bruce P. Brown and Jason F. Esteves for Respondents

BEFORE: Brenda P. Murray, Chief Administrative Law Judge

The Securities and Exchange Commission (Commission) issued its Order Instituting Administrative and Cease-and-Desist Proceedings (OIP) on September 7, 2011, pursuant to Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940 (Advisers Act). On November 9, 2011, the Commission denied Respondents' Suggestion for Interlocutory Review of a denial of their Motion to Dismiss Out-of-Time OIP. Montford and Company, Inc. d/b/a Montford Associates, Advisers Act Release No. 3311, 102 SEC Docket 48181.

At a hearing on November 7, 2011, I heard testimony from seven witnesses, including Respondent Ernest V. Montford, Sr. (Montford), and received thirty-three exhibits into evidence. The final brief was filed on January 25, 2012.¹

Issues

The issues in this proceeding are whether, in 2009 and 2010: (1) Respondents willfully violated Sections 206(1), 206(2), and 207 of the Advisers Act, 15 U.S.C. §§ 80b-6(1) and (2) and 80b-7; and (2) Montford aided and abetted and caused Montford and Company, Inc., d/b/a

¹ I will cite to the hearing transcript as "Tr. ___." I will cite to the Division of Enforcement's (Division) and Respondents' exhibits as "Div. Ex. ___ at ___." and "Resp. Ex. ___ at ___.", respectively. Both parties filed separate documents, Findings of Fact and Conclusions of Law ("Div. FF at ___." and "Resp. FF at ___.") and Post-Hearing Briefs ("Div. Br. at ___." and "Resp. Br. at ___."). The Division filed a Post-Hearing Reply Brief ("Div. Reply Br. at ___").

Montford Associates' (Montford Associates) violations of Section 204 of the Advisers Act, 15 U.S.C. § 80b-4, and Advisers Act Rule 204-1(a)(2), 17 C.F.R. § 275.204-1(a)(2). OIP at 4-5.

Findings of Fact

The findings and conclusions herein are based on the entire record. I applied preponderance of the evidence as the standard of proof. See Steadman v. SEC, 450 U.S. 91, 102 (1981). I have considered and rejected all arguments and proposed findings and conclusions that are inconsistent with this Initial Decision.

Respondents

Montford, age sixty-five, is a certified investment management analyst. Tr. 14, 19. He has passed various securities industry examinations - the Series 1, 4, 12, 24, 63, and 65, and the AMEX Put and Call exam, and has approximately forty years of securities industry experience: thirty years of association with major broker-dealer firms and twenty-three years as an investment adviser.² Tr. 15-19; Div. Ex. 2 at 3-4. In 1989, Montford founded Montford Associates, until March 30, 2012, a federally-registered investment adviser chartered in Georgia, with a principal place of business in Atlanta, Georgia.³ Tr. 15; Answer at 1. As its 100 percent owner, president, chief executive officer, and chief compliance officer, Montford has always controlled Montford Associates, and his actions can be attributed to the investment adviser.⁴ Tr. 14-15, 18, 169. In 2010, Montford Associates employed Montford, R. Brandon Burnette (Burnette), a senior research analyst, and Jeanne G. Heeley (Heeley), an investment analyst/office manager.⁵ Tr. 292.

Montford Associates did not manage its clients' assets. Tr. 38. In 2009-2010, it provided fee-based investment advisory services that included helping define investment objectives, advising on appropriate asset allocation, recommending investment managers, and monitoring and updating portfolio and manager performance. Tr. 19-20, 187, 218-21, 255-56, 265, 271; Div. Ex. 28 at 7. Montford personally met with clients once or twice per year, and participated in quarterly and other meetings by telephone. Tr. 187, 220, 255, 265, 272, 288. Montford Associates dealt with

² The examinations are as follows: Series 1, Registered Representative Examination; Series 4, Registered Options Principal; Series 12, NYSE Branch Manager; Series 24, General Securities Principal; Series 63, Uniform Securities Agent State Law; and Series 65, Uniform Investment Adviser Law.

³ On April 11, 2012, the Commission's Investment Adviser Public Disclosure website reported that Montford Associates Inc. "is NOT currently registered and is NOT filing reports with the SEC or any state."

⁴ The Advisers Act defines "control" as "the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company." 15 U.S.C. § 80b-2(12).

⁵ Burnette has a B.S. in Management from the Georgia Institute of Technology and a Masters in Business Management from Boston University. Heeley has a B.B.A. in Finance from Georgia State University. Div. Ex. 28, Sch. F.

businesses outside of Georgia and used the U.S. mails, internet, and other means of interstate commerce in its operations. OIP at 2; Answer at 1; Tr. 68-70, 99.

In 2009 and 2010, Montford Associates had gross revenues of approximately \$600,000 and \$830,000, respectively, approximately thirty clients, and \$800 million in assets under management (AUM). Tr. 20, 21. Its clients consisted of non-profit organizations with an average of about \$40 million under management, and were normally charged between eight and twenty basis points annually on AUM. Tr. 19-20. Clients included the Community Foundation for Northeast Georgia (Northeast Georgia Foundation), Fieldale Farms, the Georgia Ports Authority (GPA), the Holy Family Hospital of Bethesda Foundation (Holy Family Foundation), Piedmont College, the Resort Hotel Association or Resort Hotel Insurance Company (Resort Hotel), the Savannah Country Day School Foundation (Savannah Country Day), the Sea Island Companies Retirement Plan (Sea Island), St. Joseph's Candler Hospital system (St. Joseph's), and Tallulah Falls School Endowment.⁶ Tr. 34, 37-39, 253-54. Montford knew that the schools and charitable organizations that were his clients were managed by part-time volunteers who relied on his investment advice and valued stable and consistent investments. Tr. 21, 33, 43.

Commission Form ADV is the uniform form used by investment advisers to register with both the Commission and state securities authorities.⁷ In 2009 and the first half of 2010, the Form ADV consisted of two parts. Part I, which is available to the public on the Commission's website, requires information about the investment adviser's business, ownership, clients, employees, business practices, affiliations, and any disciplinary actions against the adviser or its employees. Part II requires investment advisers to prepare brochures containing information such as the types of advisory services offered, the adviser's fee schedule, conflicts of interest, and the educational and business background of management and key advisory personnel of the adviser. The brochure is the primary disclosure document that investment advisers provide to their clients.

Montford supervised preparation of the Form ADV that Montford Associates filed with the Commission on March 4, 2009 (March 2009 ADV). Tr. 24-26; Div. Ex. 28. The March 2009 ADV Part II represented that Montford Associates and related persons: (1) had no arrangement where it was paid cash by or received some economic benefit from a non-client in connection with giving advice to clients; (2) disclosed to clients and prospects all matters that reasonably could be expected to impair its ability to make unbiased and objective recommendations; and (3) did not accept any fees from investment managers or mutual funds. Tr. 25-26; Div. Ex. 28 at Item 13A, Sch. F.

Montford Associates filed a Form ADV Part II with the Commission on March 29, 2010, which Montford also approved, containing the same representations. Tr. 29-30; Div. Ex. 29 at Item 13A, Sch. F. Respondents did not amend the March 2009 ADV between its filing date and March

⁶ St. Joseph's had at least three separate accounts: Candler Depreciation Fund, Geechee Reinsurance, and Wachovia Defined Benefit Retirement Plan. Tr. 37; Div. Ex. 31.

⁷ The Commission adopted new rules on June 22, 2011, Advisers Act Release No. 3221, Rules Implementing Amendments to the Investment Advisers Act of 1940 (Corrected), and on July 28, 2010, Advisers Act Release No. 3060, Amendments to Form ADV.

29, 2010. Tr. 27. Since its founding, Montford Associates' Form ADV filings consistently represented that it did not accept any fees from investment managers or mutual funds. Tr. 26, 30.

Montford reviewed and signed the Form ADV Part I that Montford Associates filed with the Commission on May 8, 2009 (May 2009 ADV), and again on March 26, 2010, representing that Respondents did not: (1) recommend the purchase or sale of securities to advisory clients for which they had any other sales interest; or (2) buy or sell securities for themselves that they also recommended to advisory clients. Tr. 21, 23, 27-28; Div. Exs. 5 at 10-11, 23, and 59 at 10, 25. Respondents did not amend the May 2009 ADV between its filing date and March 26, 2010. Tr. 27.

Montford Associates' letterhead represented that the firm was an "Independent Investment Management Consultant to Corporations, Endowments, Foundations, and Charitable Institutions," and Montford claimed that status at the hearing. Tr. 31; Resp. Ex. 3. Montford Associates' promotional materials represented that it was "a source of independent investment advice for institutional investors." Answer at 2; Tr. 30-31. The company's website contained articles touting the benefits of an "independent" investment adviser, including one article entitled "Why Use an Independent Investment Advisor," which stated that "[t]he best investment advisors are *independent* – without affiliations to . . . money managers" and that "the *benefits* of having an impartial investment evaluator are several, but at the core of the concept is expert, experienced advice to the fiduciary without concern about conflicts of interest which occur with managers" Tr. 31-32; Div. Ex. 10 at 1-2. Another article on its website, "Montford Associates Offers Expert Independent Guidance," dated February 8, 2010, quotes Montford as saying that clients "need a strategy they can trust, because investments and monitoring of assets should be based on merit, not favoritism . . . or . . . undisclosed compensation." Tr. 33; Div. Ex. 11 at 1. Montford knew that these articles were posted on Montford Associates' website and that they were generally available to the public. Tr. 33-34.

SJK Investment Management, LLC

Montford met Stanley Kowalewski (Kowalewski), an investment manager, in 2002. Tr. 34. In late 2003, at Respondents' recommendation, four or five of Montford Associates' clients invested with Kowalewski, who was associated with Phoenix Partners, a firm he owned that offered fund of funds management. Tr. 34-35. When Kowalewski became associated with Columbia Partners, L.L.C. Investment Management (Columbia Partners) located in Chevy Chase, Maryland, in late 2004 or early 2005, these clients transferred their investments to Columbia Partners at Respondents' recommendation. Tr. 36-37; Resp. Ex. 2. By mid-2009, ten of Montford Associates' clients had followed its recommendation and invested a total of approximately \$50 million with Kowalewski at Columbia Partners. Tr. 37-39. These clients included the Fieldale Farms; GPA, Holy Family Foundation, Northeast Georgia Foundation; Piedmont College; Resort Hotel; Savannah Country Day; Sea Island; St. Joseph's; and Tallulah Falls School Endowment. Tr. 37-39.

According to Montford, Kowalewski called him in July 2009 and told him he was going to start SJK Investment Management, LLC (SJK), a registered investment adviser, 100 percent owned by Kowalewski, with a principal place of business in Greensboro, North Carolina. OIP at 2; Answer at 1; Tr. 43. On July 14, 2009, Montford received a letter from Columbia Partners, informing him that it could not reach a sale agreement with Kowalewski and was terminating his

employment on July 10, 2009, and liquidating the Columbia Partners Absolute Return Fund, Ltd., that Kowalewski managed.⁸ Tr. 47; Resp. Exs. 2, 4.

Montford knew that Montford Associates' clients would be uncomfortable moving their investments a third time to have Kowalewski manage their money. Tr. 43-44. Montford outlined for Kowalewski how to present his changed situation to Montford Associates' clients; he explained what these clients would be comfortable with and counseled Kowalewski on how to present his strategy to them. Tr. 48-53. Montford also told Kowalewski that he would assist him with the "administrative stuff" required to transfer Montford Associates' clients from Columbia Partners to SJK. Tr. 71. The arrangement was not memorialized in a written document. Tr. 73. Montford did not inform his clients that he assisted Kowalewski in this manner. Tr. 53.

Between July 10 and the middle of August 2009, Respondents met individually with nine or ten clients to discuss what they would do with Columbia Partners exiting the fund of funds business. Tr. 66-67. Respondents recommended that all Montford Associates' clients whose money was being managed by Kowalewski transfer their investments from Columbia Partners to SJK.⁹ Tr. 47-48. On July 23, 2009, Montford informed Columbia Partners that all Montford Associates' clients wanted their funds transferred to SJK and that the clients would provide the necessary documentation. Resp. Ex. 3.

Montford claims that Montford Associates worked to transfer the assets of ten of its clients from Columbia Partners to SJK from July 10 into September 2009. Tr. 68-69. Montford drafted letters that the ten clients sent, instructing Columbia Partners to transfer their assets to an SJK Absolute Return Fund.¹⁰ Tr. 149, 157-60; Resp. Exs. 3, 5, 11, 15. According to Montford, transferring client accounts from Columbia Partners to SJK "kind of defaulted" to Montford Associates, and it was an "administrative nightmare" because Columbia Partners was uncooperative and uninformed as to how to close a fund and SJK was not staffed "to pick up the ball." Tr. 55, 62, 67-71, 168. Heeley, the office manager, did not record the time she spent transferring client assets because she was unaware that Kowalewski was going to pay Montford Associates for the work. Tr. 73, 292, 294-95.

On August 30, 2009, Montford told Kowalewski that he would have to pay Montford Associates a fair amount for the administrative work it was doing to accomplish the transfer of accounts, and Kowalewski agreed to do so. Tr. 55-60. Montford believed this was appropriate because SJK and Columbia Partners caused the problem, Columbia Partners would likely not pay,

⁸ Columbia Partners postponed the date it closed the fund from August 31, 2009, to September 30, 2009. Tr. 70; Resp. Ex. 4.

⁹ Montford refers to SJK as operating a "hedge fund of funds" strategy that invested in registered securities, which was appropriate for risk averse conservative clients. Tr. 138-40.

¹⁰ One client, Piedmont College, did not transfer its funds to SJK, which did not impact the fee it paid Montford Associates. Tr. 161-62.

and SJK would benefit eventually. Tr. 71. According to Montford, this was the first time that Montford Associates had ever charged a fund manager for anything. Tr. 73, 176.

In October or November 2009, Kowalewski told Montford that he would pay Montford Associates \$130,000 at the end of 2009 or in 2010, and an additional amount after SJK finished its first year in business, for the services. Tr. 59-60, 93, 121. At Kowalewski's direction, on November 2, 2009, Montford Associates sent SJK an invoice for \$130,000 for "Consulting services for the SJK Investment Management LLC Launch July 15th – October 30, 2009." Tr. 89, 95; Div. Ex. 8. In an e-mail on November 10, 2009, Montford told Kowalewski, "I would like to have the project fee wired to our bank when you pay us." Div. Ex. 66. In the same e-mail chain, Montford advised Kowalewski that Montford Associates was advising a client, Fieldale Farms, "to give you another \$800,000." Tr. 95-96. Div. Ex. 66. Fieldale Farms invested \$1.5 million with SJK in June 2010, and Montford did not disclose to Fieldale Farms its payment arrangement with Kowalewski. Tr. 95-96, 108.

On November 30, 2009, at Kowalewski's direction, Montford Associates sent a second invoice for \$130,000, stating it was for a "Marketing and Syndication Fee for SJK Investment Management LLC Launch July 15th – November 30, 2009." Tr. 90-93; Div. Ex. 4 at cc 6. Kowalewski requested the changed description of services performed. Tr. 92-93. SJK paid Montford Associates \$130,000 on January 4, 2010. Answer at 3. Montford testified that he did not know how Kowalewski arrived at the \$130,000 amount. Tr. 94. Montford represented in a letter to a client on January 21, 2011, however, that the \$130,000 was a negotiated fee. Tr. 130; Div. Ex. 41. Kowalewski did not ask Montford to itemize his time or expenses. Tr. 178.

In October 2010, Kowalewski told Montford to send him an invoice for \$80,000, for a "Marketing and Syndication Fee for the SJK Investment Management LLC Launch," which Montford Associates did on November 1, 2010. Tr. 121-22, 127-28; Div. Ex. 17. Montford Associates received payment in November 2010. Tr. 123; Answer at 4. Montford understood that the payment was for the administrative work that Montford Associates did in 2009, for which it had received \$130,000, and he did not know how the amount was calculated. Tr. 121, 123. The \$210,000 Montford Associates received from SJK in 2010 was approximately twenty-five percent of its total revenue for that year. Answer at 2; Tr. 123.

Commission action against Kowalewski and SJK

On January 6, 2011, the Commission filed an emergency civil injunctive action, charging Kowalewski and SJK with securities fraud and obtaining a temporary restraining order and asset freeze. OIP at 2; Answer at 1. SEC v. Kowalewski, No. 1:11-cv-0056-TCB (N.D. Ga.). The Commission sought disgorgement of \$8.4 million, plus prejudgment interest, and penalties to be determined, possibly up to an additional \$67 million. On January 6, 2011, the Court entered an order temporarily restraining the defendants from violations of Section 17(a) of the Securities Act of 1933 (Securities Act), Section 10(b) of the Securities Exchange Act of 1940 (Exchange Act), Exchange Act Rule 10b-5, Sections 206(1), 206(2), and 206(4) of the Advisers Act, and Advisers Act Rule 206(4)-8, instituting an asset freeze, and ordering other relief. SEC Litigation

Release Nos. 21800, 22073 (Jan. 7 and Aug. 29, 2011). On February 2, 2011, the Court issued an Order Appointing Receiver and Continuing Asset Freeze.¹¹

Disclosure

Prior to January 6, 2011, Respondents did not disclose to clients or prospective clients in direct communications or in Montford Associates' Forms ADV that: (1) Montford and Kowalewski went on a three-day fishing trip to Montana in 2009, for which Kowalewski paid for the transportation, lodging, food, and guides;¹² (2) on August 30, 2009, Montford told Kowalewski that he would have to pay Montford Associates for the work it performed; (3) Montford invested \$235,000 of his retirement funds with SJK at the start of 2010, and SJK subsequently waived its management fee; and (4) Montford Associates received a total of \$210,000 from Kowalewski in 2010 - \$130,000 on January 4, 2010, and \$80,000 in November 2010. Tr. 60, 75-77, 103, 146, 214, 288-89; Div. Ex. 19. After each of these events, Respondents continued to recommend that clients invest additional funds with Kowalewski; they recommended that a client not withdraw its investment from SJK, without disclosing their financial dealings with him; and they did not update or revise Montford Associates Forms' ADV. Answer at 3-4; Tr. 8, 74, 105.

Recommendations to Clients

In the period 2009-2010, Montford Associates' clients invested over \$80 million with SJK at Respondents' recommendation. Answer at 4. According to Montford, SJK had about fifteen percent of the assets that Montford Associates' clients had under management. Tr. 140.

On October 15, 2009, Montford attended a meeting and recommended that client Piedmont College continue to invest with SJK because Kowalewski had made "a really good return for about three or four years." Tr. 103; Div. Ex. 68. On November 17, 2009, Montford e-mailed clients about the status of their investments with the SJK Absolute Return Fund of Funds and informed them that SJK was "taking care of the details in the transition," but did not mention that he had sent an invoice to Kowalewski on November 2, 2009, for consulting services. Tr. 98-100; Div. Ex. 15.

I. Sea Island and Resort Hotel

Respondents represented that Montford Associates was an independent investment adviser to Sea Island and Resort Hotel. James Barrow (Barrow), director of risk management for Sea Island, has been on the board of Resort Hotel since 1995. Tr. 251, 253. Sea Island began and is a member of Resort Hotel, an association of resort companies grouped for insurance purposes. Tr. 251-53. Sea Island's pension plan has been a Montford Associates' client since about 1994; it was valued at about \$32 million when it was taken over by the Pension Benefits Guarantee Corporation in October 2010. Tr. 252, 254. Resort Hotel first engaged Montford Associates in the late 1990s. Tr. 254. Barrow testified that Resort Hotel hired Montford mainly because he was independent. Tr.

¹¹ I take official notice of documents and rulings in Kowalewski. 17 C.F.R. § 201.323.

¹² On the fishing trip, Montford bought Kowalewski a fishing rod and jacket. Tr. 75.

256-57. He recalls that Montford made representations about being independent a couple of times, and it was understood that he was impartial and made recommendations based on what was good for his clients. Tr. 257. Sea Island's pension plan and Resort Hotel's assets were invested first with Kowalewski when he was with Phoenix Partners and Columbia Partners. Tr. 260. In June and July 2009, Montford recommended that Sea Island and Resort Hotel transfer their assets from Columbia Partners to SJK. Tr. 259-60.

On November 17, 2009, Montford participated in a Resort Hotel board discussion on whether it should hire an additional fund of funds manager or replace the existing fund of funds manager, SJK Absolute Return Fund, LLC. Tr. 97, 261-63; Div. Ex. 64. Montford did not disclose to the board of Resort Hotel that: (1) he had requested that Kowalewski pay Montford Associates on August 30, 2009, and in October or November, Kowalewski agreed to pay more than \$130,000; (2) he had billed SJK for \$130,000 on November 2, 2009; and (3) he had directed Kowalewski where to wire the payment on November 10, 2009. Tr. 59-60, 93, 97-98, 100, 121, 257, 261-63. Barrow believes that the board would have wanted to know this information and would consider it important in assessing Montford's impartiality. Tr. 257-58, 263-64. Barrow only cares that Montford received payment from an investment manager; he does not care why. Tr. 258.

On March 23, 2010, Kowalewski and Montford participated in an investment performance update at a Resort Hotel board meeting and discussed SJK, but neither mentioned to the board that Montford Associates had an agreement to receive funds from SJK. Tr. 263-65; Div. Ex. 65. Barrow's testimony is that such a disclosure would have made a difference to the board. Tr. 265-66.

II. St. Joseph's

St. Joseph's had been a Montford Associates' client since at least 2001 and was its biggest client, with about \$185 million invested.¹³ Tr. 171, 218. John Albert (Albert) was a member of St. Joseph's finance committee and chaired several committee meetings in 2009-2010.¹⁴ Tr. 217. Montford worked with St. Joseph's CFO to develop investment recommendations for the finance committee, which it considered and presented to the full board. Tr. 219, 226. Montford advised on strategy, gave advice on asset allocation when the portfolio needed rebalancing, provided quarterly reviews of investments, and personally attended meetings twice per year. Tr. 219-20. Albert testified that St. Joseph's made an initial investment with SJK in November 2009, and later, at Respondents' recommendation, St. Joseph's invested over \$7.4 million more with SJK in September 2010. Tr. 109-11, 222, 225-27, 250; Div. Ex. 31.

¹³ St. Joseph's paid eight basis points on assets under management in 2009 and nine basis points in 2010. Tr. 221. In 2010, the three St. Joseph accounts paid Montford Associates around \$146,000. Tr. 221. St. Joseph's initiated a civil action against Respondents in connection with these events, which resulted in a settlement. Tr. 171; Resp. FF at 12.

¹⁴ Albert retired from an executive position at the Union Camp Corporation. Tr. 215. He knew Montford, they belonged to the same church, and their children were friends. Tr. 218.

St. Joseph's considered it very significant that Montford was independent as he represented and that his investment recommendations were based exclusively on what was best for St. Joseph's. Tr. 220, 222-24. At no time did Montford disclose to St. Joseph's that he received money from, or had a business relationship with, SJK. Tr. 220-24, 227-28. Albert would have wanted to know this information because he considered the fact that Montford had an agreement to receive compensation from SJK a significant factor in questioning Montford's objectivity in recommending an investment. Tr. 225, 228. St. Joseph's became aware of Montford's compensation agreement with SJK from newspaper reports in January 2011 and when the Division contacted its CFO. Tr. 228-29. Albert considers it very significant that Montford received payments from an entity he recommended, regardless of the reason. Tr. 233. St. Joseph's terminated its business relationship with Montford Associates because it believed Montford committed a breach of trust. Tr. 229.

III. Savannah Country Day

Montford Associates became Savannah Country Day's trusted investment consultant in about 2004. Tr. 191, 213. With assets of between \$12 and \$14 million, Savannah Country Day paid Montford Associates a fee of between \$4,000 and \$5,000 quarterly; in 2009-2010, it paid Montford Associates about \$35,000. Tr. 187.

In mid-2009, Will Monroe (Monroe) became Chair of the Savannah Country Day's Endowment Committee.¹⁵ Tr. 184-85. Independence and conflicts of interest were important considerations for Monroe and other Savannah Country Day committee members. Tr. 188-89. In an e-mail on September 28, 2009, Montford responded to some questions Monroe raised about Kowalewski, but Montford did not mention, either in the e-mail or in conversations, that he had asked Kowalewski to pay Montford Associates for administrative services and was awaiting payment. Tr. 194; Div. Ex. 35. In April 2010, Savannah Country Day voted to terminate SJK as one of its investment managers. Tr. 113-14, 196; Div. Ex. 24. Montford objected vigorously and in September 2010, Savannah Country Day followed Montford's recommendation and did not withdraw its investments from SJK.¹⁶ Tr. 114-20, 196-99, 208-09, 212, 214; Div. Ex. 25. Montford did not disclose in any discussions with Savannah Country Day that Montford Associates had received funds from SJK. Tr. 114, 214. In fact, according to Monroe, Montford represented in September 2010, more than once, that fees from consulting clients were his only income and that he was not paid by any investment manager. Tr. 188, 199. Montford's statement is reflected in the minutes of the September 23, 2010, Savannah Country Day Endowment Committee meeting. Tr. 201; Div. Ex. 57 at 0860.

Savannah Country Day terminated its relationship with Montford Associates when it learned from the school's attorney in January 2011 that Respondents had received payments from Kowalewski. Tr. 202; Div. Ex. 41. Monroe testified that he would not consider Montford to be an independent consultant if he received payments from Kowalewski for any reason. Tr. 201-04.

¹⁵ Monroe retired on December 31, 2005, after a twenty-five-year career with Smith Barney. Tr. 184.

¹⁶ Some members of Savannah Country Day questioned Montford's investment advice. Tr. 204-07.

After the termination, Montford wrote to the Chairman of the Board of Savannah Country Day stating that the \$130,000 was a negotiated fee and that the “big loser in this is Savannah Country Day.” Tr. 131; Div. Ex. 41.

IV. Tallulah Falls School Endowment

Tallulah Falls School Endowment became a Montford Associates client in 2008. Tr. 106. At Respondents’ recommendation, Tallulah Falls School Endowment invested with Kowalewski over a two-year period, beginning when he was at Columbia Partners. Tr. 106-07. In 2010, Tallulah Falls School Endowment invested an additional \$1 million with SJK at Respondents’ recommendation. Tr. 107.

V. GPA

Montford represented to GPA that he was an independent investment adviser, which was very important to GPA’s board and finance committee for making investment decisions about its employee pension plan’s assets. Tr. 270-71. Marie Roberts (Roberts), GPA’s chief financial officer, testified that GPA hired Montford Associates in 1992 to provide advice on the equity portion of its employee pension plan, and in the period 2009-2010, a majority of the plan’s approximately \$100 million in assets were invested using Montford’s advice. Tr. 269, 270-71, 279.

GPA had about ten percent of its employee pension plan assets invested with Kowalewski at Columbia Partners in 2009. Tr. 271. On July 7, 2009, Montford e-mailed Roberts, recommending that GPA transfer the employee pension plan assets at Columbia Partners to SJK, and Montford subsequently recommended this to GPA’s finance committee. Tr. 273; Div. Ex. 49. GPA’s board followed Montford’s recommendation. Tr. 274. GPA paid Montford Associates a fee of about \$109,000 in 2009. Tr. 271. GPA did not know in 2009 and 2010 that Montford had made an arrangement with Kowalewski to receive a fee. Tr. 274. GPA would have wanted to know this information to assess whether Montford’s recommendations were impartial and not tied to “anything financial.” Tr. 274.

In January 2011, Roberts read in the newspaper that Montford had received a fee from Kowalewski. Tr. 274-75. Later, in January 2011, Montford confirmed to Roberts and the GPA finance committee that Kowalewski paid him \$130,000 for help setting up SJK. Tr. 275-76. Montford did not disclose the additional payment of \$80,000. Tr. 276. GPA terminated Montford Associates mainly over the issue of independence and failure to disclosing taking payments from SJK. Tr. 283.

VI. Northeast Georgia Foundation

The Northeast Georgia Foundation is a non-profit philanthropic foundation with an investment portfolio of about \$15 million. Tr. 285-86. Montford Associates began advising the Northeast Georgia Foundation’s investment committee in 2006 and was still doing so at the time of the hearing. Tr. 287. Bill Short, president of Fiber Tech, Inc., and the Northeast Georgia Foundation’s vice president and investment committee chairman, testified that Montford and Montford Associates’ materials represented that they were independent, which was an important

consideration. Tr. 287-88. In 2009, the Northeast Georgia Foundation followed Montford's recommendation and invested with SJK. Tr. 285-86, 287-88. Montford did not disclose his agreement with Kowalewski to receive a fee or that Kowalewski paid Montford Associates \$210,000, in 2009 through 2010. Tr. 288-89.

Arguments

The Division

The Division maintains that Respondents' arguments are overwhelmed by the facts that in 2009, Kowalewski agreed to pay them an amount at their request, and they accepted a total of \$210,000 from SJK in 2010, when they were asserting in ADV filings and public statements that they received no benefits from non-clients in connection with giving advice to clients, did not accept any fees from investment managers, and provided independent investment advice. Div. Br. 1-3, 5-6, 12-19. The Division points to evidence to support its position that Kowalewski paid Respondents to recommend SJK to clients and not, as Montford claimed, simply for administrative services. Div. Br. at 6-11. The Division cites examples to support its position that Montford was not forthcoming and truthful in disclosing information to the Division or to his clients during the investigation and after it was concluded. Div. Br. at 19-20. The Division rejects Montford's contention that he has tried to assist the government's investigation, citing his initial failure to turn over the invoice Montford Associates sent to SJK, dated November 1, 2010, in response to a subpoena he received on December 9, 2010. Tr. 127-28; Div. Br. at 36-37.

In its Reply Brief, the Division challenges Respondents' position on violations of Sections 206 and 207 of the Advisers Act and Respondents' reading of the applicable case law. Div. Reply Br. at 6-13.

Respondents

Almost one-third of Respondents' Brief urges reconsideration of my ruling denying dismissal of the proceeding because of a claimed violation of Section 4E of the Exchange Act. Respondents argue that their motion to dismiss should have been granted because there is no evidence that the Director of Enforcement ever determined that this proceeding was sufficiently complex such that a determination to file an action could not have been completed within 180 days. Resp. Br. at 2-7.

Respondents believe there were no violations of Section 206 of the Advisers Act because Montford Associates was an independent adviser and the payments it received from SJK were not "fees." Tr. 167-68, Resp. FF at 9-10; Resp. Br. at 7-10. Montford insists that \$210,000 was the reasonable value of the services Montford Associates provided to SJK so that the concept of unjust enrichment is totally inapplicable to this situation. Tr. 156-57; Resp. FF at 10.

Montford claims it never occurred to him to inform Montford Associates' clients that Montford Associates was charging SJK because he only asked for payment when he realized how much time and effort Montford Associates' small office had spent in July and was still spending in August to assist SJK. Tr. 57-58, 74, 167-68.

Montford points out that Montford Associates' client fees were based on AUM and were not related to whether clients accepted recommendations to invest with Kowalewski. Tr. 162-63. Respondents claim that there is no evidence that the advice to invest in SJK resulted in financial benefit to them and that the Division failed to meet its burden "[o]n the most important factual issue in the case – whether Montford had a financial incentive to steer clients to SJK." Resp. Br. at 8.

Respondents argue that they did not violate Section 207 of the Advisers Act "because the [e]conomic [b]enefits [r]eceived from SJK were not 'in connection with giving advice to clients.'" Resp. Br. at 11. Montford testified that he did not meet with clients prior to August 30, 2009, to encourage them to invest with SJK and that he recommended SJK later.¹⁷ Tr. 62. Montford is adamant that Montford Associates' recommendation of Kowalewski had nothing to do with payments from SJK. Tr. 65, 73. Montford denies that Kowalewski paid him the \$210,000 fee for recommending that clients invest with SJK. Tr. 61-62, 65. Heeley is sure that Kowalewski's payments were not contingent on Montford moving clients into SJK. Tr. 292-93.

According to Montford, Kowalewski was the most exceptional hedge fund of funds manager that Montford Associates' clients ever used and Montford recommended Kowalewski consistently to clients over a long period. Tr. 65, 140-42. Montford claims that from 2003 through 2010, SJK's fund of funds had an extraordinarily good average return of about eight percent per year, while the return for the conservative fund of funds index was about three percent, and the stock market was about four percent. Tr. 144-45. Specifically, he notes that GPA's return on its SJK investment as of December 31, 2010, was 10.5% per year "Trailing 5-Years," when the benchmark had a five-year trailing index of 1.7% per year. Tr. 280-81; Div. Ex. 56 at 070.

Montford insists that SJK's returns were honest gains because SJK was audited annually and moneys were accounted for when transferred from Columbia Partners in 2009. Tr. 145. This testimony is disputed by Monroe's testimony that Savannah Country Day lost money on its investments with Kowalewski through 2009 and that when SJK was liquidated, Savannah Country Day did not receive the amount indicated on its account statements. Tr. 208, 211.

Findings and Conclusions

Motion to Dismiss

On October 5, 2011, I denied Respondents' motion to dismiss "based on e-mails from Division staff in Atlanta to the Division Director, and physical evidence showing notice to the Commission Chairman that the Director intended to grant the 180-day extension." Montford and Company, Inc., Order Following Pre-hearing Conference. I denied Respondents' Application for Interlocutory Review on October 18, 2011. Montford and Company, Inc., Administrative Proceedings Rulings Release No. 684. The Commission issued an Order Denying Suggestion for Interlocutory Review on November 9, 2011. Montford and Company, Inc., Advisers Act Release No. 3311 ("[T]he law judge implicitly found that the Division Director had made the required

¹⁷ The Division's position is that Montford admitted in his investigative testimony on December 17, 2010, that recommending SJK to clients was a service he provided for the \$130,000. Tr. 60-62.

complexity determination, noting that the Division had asserted that ‘the Division Director is not required to articulate or memorialize the reason for deciding that an investigation is sufficiently complex.’”).

As an initial matter, I deny reconsideration of Respondents’ motion to dismiss. Section 4E of the Exchange Act provides that:

- (1) *In General.* Not later than 180 days after the date on which Commission staff provide a written Wells notification to any person, the Commission staff shall either file an action against such person or provide notice to the Director of the Division of Enforcement of its intent to not file an action.
- (2) *Exceptions for Certain Complex Actions.* . . . if the Director of the Division of Enforcement . . . determines that a particular enforcement investigation is sufficiently complex such that a determination regarding the filing of an action against a person cannot be completed within the deadline specified . . . the Director of the Division of Enforcement . . . may, after providing notice to the Chairman of the Commission, extend such deadline as needed for one additional 180-day period.

Exchange Act Section 4E does not: (1) require that the Director of the Division of Enforcement make public his/her determination that the complex nature of the investigation precludes initiating an action within 180 days of the Wells submission; or (2) provide for challenging that judgment. Rather, Section 4E requires that the Director of the Division of Enforcement take certain actions where he/she makes such a determination. Here, the Director extended the deadline, so one can deduce that he/she made the determination, which the Commission affirmed when it directed that an Initial Decision be issued within 300 days of service of the OIP, the time period for the most complex administrative proceedings.

Respondents Willfully Violated Sections 206(1) and 206(2) of the Advisers Act¹⁸

Section 206 of the Advisers Act prohibits any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, from: (1) employing any device, scheme, or artifice to defraud any client or prospective client; and (2) engaging in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.

Scienter is required for a violation of Section 206(1), but not for a violation of Section 206(2), where negligence will suffice. SEC v. Steadman, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992); SEC v. Moran, 922 F. Supp. 867, 896-97 (S.D.N.Y. 1996). Scienter is defined as a mental state consisting of an intent to deceive, manipulate, or defraud. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194 n.12 (1976). Reckless conduct satisfies the scienter requirement. Vernazza v. SEC, 327 F.3d at 860; SEC v. Blavin, 760 F.2d 706, 711-12 (6th Cir. 1985). With respect to the antifraud

¹⁸ The OIP uses the term willful, which generally means no more than the person knows what he is doing, but Sections 206(1) and 206(2) of the Advisers Act do not specify willfulness. Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000).

provisions of the Exchange Act, recklessness has been described as an extreme departure from the standards of ordinary care, which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it. See Sundstrand Corp. v. Sun Chem. Corp., 553 F.2d 1033, 1045 (7th Cir. 1977), cert. denied, 434 U.S. 875 (1977).

The fraud toward clients that Section 206 prohibits may involve affirmative misrepresentations or nondisclosure of facts, and the nature and extent of disclosure depends on the circumstances and the reasonable expectations of the parties. 2 Tamara Frankel & Ann Taylor Schwing, The Regulation of Money Managers, 13-17 (2d ed. Supp. 2007). An omitted fact is material if there is a substantial likelihood that a reasonable investor would consider it important in deciding the matter before him. TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). A finding that Montford's undisclosed dealings with Kowalewski were material information is supported by the testimony of every client witness – each expected that Montford would have disclosed this information. See SEC v. Capital Gains Research, 375 U.S. 180, 201 (1963) (an investment adviser must fully and fairly reveal his personal interests in his recommendations to his clients); Vernazza v. SEC, 327 F.3d 851, 859 (9th Cir. 2003) (“It is indisputable that potential conflicts of interest are ‘material’ facts with respect to clients and the Commission.”); Steadman v. SEC, 603 F.2d 1126, 1130 (5th Cir. 1979) aff’d on other grounds, 450 U.S. 91 (1981) (potential conflicts of interest can be material facts with respect to clients and the Commission).

The leading case on the duties of an investment adviser is Capital Gains Research, which held:

The Investment Advisers Act of 1940 thus reflects a congressional recognition ‘of the delicate fiduciary nature of an investment advisory relationship,’ as well as a congressional intent to eliminate, or at least to expose, all conflicts of interest which might incline a[n] investment adviser-consciously or unconsciously-to render advice which was not disinterested.

Courts have imposed on a fiduciary an affirmative duty of ‘utmost good faith, and full and fair disclosure of all material facts,’ as well as an affirmative obligation ‘to employ reasonable care to avoid misleading’ his clients.

Failure to disclose material facts must be deemed fraud or deceit within its intended meaning, for, as the experience of the 1920’s and 1930’s amply reveals, the darkness and ignorance of commercial secrecy are the conditions upon which predatory practices best thrive.

The statute, in recognition of the adviser’s fiduciary relationship to his clients, requires that his advice be disinterested. To ensure this it empowers the courts to require disclosure of material facts.

Capital Gains Research, 375 U.S. at 191-92, 194, 200, 201 (footnotes excluded),

A conflict of interest is a “real or seeming incompatibility between one’s private interests and one’s public or fiduciary duties.” Black’s Law Dictionary 295 (7th ed. 1999). Respondents had a conflict of interest because while representing that they provided independent investment advice, they recommended an investment manager with whom they had undisclosed dealings that benefited both them and the investment manager. Montford requested compensation from Kowalewski, an investment manager Respondents recommended, that resulted in \$210,000 in undisclosed payments to Respondents. The incompatibility or conflict between these payments and Respondents’ other undisclosed dealings with Kowalewski and the fiduciary duty Montford Associates owed its clients placed Respondents in a conflicted position. The fact that Respondents, who represented themselves as independent, did not disclose their dealings with Kowalewski while recommending Kowalewski to their clients were conflicts of interest in violation of Sections 206(1) and (2) of the Advisers Act.

Independence has always been an essential requisite for an investment adviser. Montford, who earned multiple securities licenses and had considerable experience running a successful investment adviser, knew, should have known, or acted recklessly in representing Montford Associates as an independent investment adviser to the public and in Forms ADV when he was requesting that Kowalewski pay Montford Associates a fee, having Montford Associates send Kowalewski invoices, accepting Kowalewski’s wire transfers, and accepting other benefits from Kowalewski. Respondents’ undisclosed actions come within the definition of schemes or artifice to defraud and transactions, practices, or course of business which operated as a fraud or deceit upon clients or prospective clients.

Respondents’ defense that they did not intend to deceive is unpersuasive because intent is not required for a violation. See Capital Gains Research, 375 U.S. at 200. Respondents offered no plausible excuses for their flagrant violations. Resp. Br. at 7-10. When asked at the hearing whether he would ever take money from an investment manager without disclosing the fact, Montford testified, “Of course not No, it was a one-off, something I’ll live to regret all my life.” Tr. 176.

Montford is directly liable because he was acting as an unregistered investment adviser as well as a person associated with Montford Associates. See John J. Kenny, Securities Act Release No. 8234 (May 14, 2003), 56 S.E.C 448, 485 n.54 aff’d, 87 Fed. Appx. 608 (8th Cir. 2004) (unpublished) (“An associated person may be charged as a primary violator under Section 206 where the activities of the associated person cause him or her to meet the broad definition of ‘investment adviser.’”).

Respondents Willfully Violated Section 207 of the Advisers Act

Section 207 of the Advisers Act prohibits willfully making any untrue statement of a material fact in any registration application or report filed with the Commission under Sections 203 or 204, or willfully omitting to state in any such application or report any material fact which is required to be stated.

Respondents willfully violated Section 207 of the Advisers Act because Montford Associates made materially false representations in its Form ADV filed in 2010: Form ADV Part I on March 26, 2010, and Part II on March 29, 2010, which Montford approved. In Part II, Montford

Associates represented that it did not receive any economic benefit from non-clients in connection with giving advice to clients; it would disclose matters that could impact its ability to render objective advice; and it did not accept fees from investment managers. These were materially false representations.

In Part I, Montford Associates represented that Respondents did not recommend sales where they had an interest and did not buy or sell securities for themselves that they recommended. These were materially false representations because in 2009, Montford accepted substantial gifts from Kowalewski and took actions to assist Kowalewski that indicated he had an interest in Kowalewski's success, and Montford bought securities that he recommended early in 2010, when he invested his retirement funds with SJK, which subsequently waived the management fee.¹⁹

Respondents' defense that the representations were accurate because the economic benefits they received were not in connection with giving advice to clients is unpersuasive. Resp. Br. at 11.

Montford Associates Violated Section 204 of the Advisers Act and Advisers Act Rule 204-1(a)(2) and Montford Aided and Abetted and Caused the Violations

Taken together, Section 204 of the Advisers Act, Advisers Act Rule 204-1(a)(2), and instructions on the Form ADV require investment advisers that use the mails or any means or instrumentality of interstate commerce in connection with their business to update their Form ADV annually, and to amend Part II of the Form ADV promptly, if information therein becomes materially inaccurate.

Montford Associates, which employed the mails and the means of interstate commerce in conducting its investment adviser business, violated Section 204 of the Advisers Act and Advisers Act Rule 204-1(a)(2) because it failed to correct the representations in its 2009 Form ADV filing Part II when Montford began improper activities with Kowalewski. The Division claims that this occurred in August 2009 after Montford Associates agreed to receive fees from SJK; Montford, however, claims the agreement occurred in October or November 2009. In any event, Respondents did not correct the statements in Montford Associates' March 2009 ADV Part II when they became materially inaccurate in the period between March 4, 2009 and March 29, 2010. Thus, Montford Associates violated Section 204 of the Advisers Act and Advisers Act Rule 204-1(a)(2) when Montford Associates failed to update with accurate material information its Form ADV Part II filed on March 29, 2010.

"The general requirements for establishing aiding and abetting liability are well settled in this Circuit. Plaintiffs must prove (1) a securities law violation by a primary wrongdoer, (2) knowledge of the violation by the person sought to be charged, and (3) proof that the person sought to be charged substantially assisted in the primary wrongdoing." *Armstrong v. McAlpin*, 699 F.2d 79, 91 (2nd Cir. 1983), citing *IIT, An International Investment Trust v. Cornfeld*, 619 F.2d 909, 922 (2nd Cir. 1980). Montford aided and abetted Montford Associates' primary violations of Advisers Act Section 204 and Advisers Act Rule 204-1(a)(2) because he knew, or was reckless in not

¹⁹ The Division does not claim that Respondents violated Advisers Act Section 207 with respect to the Form ADV Part I filed on March 26, 2010. Div. Br. 28-29.

knowing, that Montford Associates was in violation with respect to its Form ADV filings and, as the person in control of Montford Associates who supervised the filings, he provided substantial assistance in Montford Associates' commission of the violations.

Public Interest

Arguments

The Division requests that Respondents be ordered to: (1) cease and desist from committing or causing violations, and any future violations, of Sections 204, 206(1), 206(2), and 207 of the Advisers Act and Advisers Act Rule 204-1(a)(2); (2) disgorge \$210,000 and pay prejudgment interest in the amount of \$7,907.98; and (3) each pay a civil penalty of \$25,000. The Division further requests that Montford be barred from associating with any investment adviser. Div. Br. at 32, 33, 35, 37.

Respondents contend that no relief is proper, but if it should be considered, then the following factors are relevant: Montford has a long and spotless record in the securities industry, and any violation was isolated;²⁰ Montford did not intend to cause harm; he has lost his business and the retirement funds he invested with Kowalewski; and he has paid \$40,000 to one client and incurred well over \$100,000 in legal fees. Resp. Br. at 11-12.

Respondents argue that a cease-and-desist order is unnecessary, unwarranted, and unlawful in the 11th Circuit, citing SEC v. Smyth, 420 F.3d 1225 (11th Cir. 2005) and Burton v. City of Belle Glade, 178 F.3d 1175, 2000 (11th Cir. 1999), and that an injunction to obey the law would violate Rule 65 of the Federal Rules of Civil Procedure. Resp. Br. at 12-14. Finally, Respondents maintain that the financial losses they have endured negate the need for a civil penalty. Resp. Br. at 16.

Sanctions Pursuant to Sections 203(e) and 203(f) of the Advisers Act

Sections 203(e) and 203(f) of the Advisers Act requires the Commission to revoke the registration of and impose certain sanctions on an investment adviser or associated person, after notice and opportunity for hearing, where it is in the public interest and the adviser or associated person has willfully made or caused to be made a materially false or misleading statement, or omitted material information, in a report required to be filed with the Commission. The criteria most often used to assess the public interest are the egregiousness of a person's actions, the isolated or recurring nature of the violations, the degree of scienter involved, the sincerity of a person's

²⁰ Respondents claim that "Montford has never been cited for any violation of the law no matter how minor or trivial. Tr. 138." Resp. FF at 2. The Division notes that Respondents' claim is in error because Montford was named in a customer suit, while associated with a broker-dealer, that was settled out of court for \$30,000 in 1984. Div. Ex. 2 at 8; Div. Reply Br. at 13.

assurances against further violations, a person's recognition of wrongdoing, opportunities to commit future violations, and deterrence.²¹

I. Egregiousness

Respondents' conduct was egregious because they blatantly violated a basic premise of an investment adviser's role accepted for almost fifty years, which is that the adviser owes to its clients the fiduciary duty of being independent. See Capital Gains Research, 375 U.S. at 201 ("The statute, in recognition of the adviser's fiduciary relationship to his clients, requires that his advice be disinterested."). For over a year and a half, Montford failed to disclose to clients and prospective clients a beneficial relationship he and Montford Associates had with an investment manager they recommended.

Respondents advised clients to retain Kowalewski without disclosing that Montford had requested money from Kowalewski, he had sent Kowalewski multiple invoices, he had accepted Kowalewski's wire transfers, and Kowalewski paid for a fishing trip out west and waived the management fee for handling Montford's retirement account. Montford did not simply recommend Kowalewski to clients; in one instance he lobbied for him so strongly that Savannah Country Day changed its position and retained him. Taking chutzpah to new heights, Montford cited the fiduciary duty he owed Savannah Country Day as the reason he objected to terminating Kowalewski. Div. Ex. 24.

II. Isolated or recurring nature of the violations

Respondents' violations were recurring and occurred repeatedly from at least August 2009 through the end of 2010. Several witnesses testified that they only learned of the violations because of the Commission's 2010 investigation in connection with Kowalewski that became public in January 2011.

III. The degree of scienter involved, the sincerity of a person's assurances against further violations, and recognition of wrongdoing

As noted, Montford knew, or was reckless in not knowing, that his actions were illegal. The evidence is that he had a high degree of scienter, any remorse is only because of the results to him personally and professionally, and he does not acknowledge wrongdoing. Montford has stated that he will not commit further violations, but he has not acknowledged that what he did was wrong. He persists in claiming that he did nothing wrong because what he received from Kowalewski were not "fees." Resp. Reply Br. at 7. I take particular note of Montford's January 21, 2011, communication to Savannah Country Day, where he states that he understands Montford Associates was terminated because it charged SJK a business consulting fee in 2009 and laments that he never had an opportunity to explain the facts about the fee to the board. Finally, Montford's description of

²¹ Steadman, 603 F.2d at 1140; see also Joseph J. Barbato, Securities Act Release No. 7638 (Feb. 10, 1999), 53 S.E.C. 1259, 1281 n.31; Donald T. Sheldon, 51 S.E.C. 59, 86 (1992); McCarthy v. SEC, 406 F.3d 179, 189 (2d Cir. 2005).

himself as a victim of Kowalewski's illegal behavior, as well as his testimony and demeanor, cause me to conclude that he believes, in spite of the statutory and regulatory provisions, that he was an independent adviser. Tr. 31.

The record contains several instances that raise questions about Montford's credibility. He initially failed to produce a copy of an invoice for \$80,000, dated November 1, 2010, that he submitted to Kowalewski, in response to a Commission subpoena dated December 9, 2010. Tr. 127-28. In his January 21, 2011, e-mail to Savannah Country Day, referenced immediately above, Montford fails to mention that he received \$80,000 from Kowalewski in November 2010, and maintains that the \$130,000 was a negotiated fee with Kowalewski, yet he testified the payment was non-negotiated. Tr. 130; Div. Ex. 41. In addition, Montford testified that the \$130,000 from Kowalewski was not for recommending Kowalewski, but in his investigative testimony, he said it was fair to say that the services he provided in connection with the \$130,000 included meeting with seven or eight clients on behalf of SJK from June through November 2009 and recommending they continue to invest with SJK. Tr. 62-74.

IV. Opportunities to commit future violations and deterrence

Montford's continued participation in the securities industry would allow him an opportunity for future violations. Deterrence is also recognized as a valid reason for imposing a sanction. See Johnson v. SEC, 87 F.3d 484, 491 (D.C. Cir. 1996); Steven Altman, Exchange Act Release No. 63306 (Nov. 10, 2010), 99 SEC Docket 34405, 34435 petition for review denied, 666 F.3d 1322 (D.C. Cir. 2011); Paul David Pack, Exchange Act Release No. 34660, (Sept. 13, 1994), 51 S.E.C. 1279, 1283; Richard C. Spangler, Inc., 46 S.E.C. 238, 254 n.67 (1976); Arthur Lipper Corp., 46 S.E.C. 78, 100 (1975) ("If these proceeding are to be truly remedial, they must have a deterrent effect on other investment company managers who may be tempted to enrich themselves at the expense of their beneficiaries.").

All the reasons set forth above, particularly Montford's refusal to accept that his conduct was illegal, indicate a high probability that if allowed an opportunity, he would likely commit future violations. For these reasons and to deter others from similar illegal conduct, it is in the public interest to bar Montford from association to the extent allowed by Section 203(f) of the Advisers Act.

Cease-and-Desist Order Pursuant to Sections 203(k) of the Advisers Act

Section 203(k) of the Advisers Act empowers the Commission to order a person who has been found, after notice and hearing, to have violated the Advisers Act, or to have caused the violation, to cease and desist from committing or causing such violations and any future violations.

The factors for considering whether a cease-and-desist order is warranted are very similar to the Steadman factors, with added emphasis on the possibility of future violations. KPMG Peat Marwick, LLP, Exchange Act Release No. 43862 (Jan. 19, 2001), 54 S.E.C. 1135, 1185, petition denied, 289 F.3d 109 (D.C. Cir. 2002). Respondents' argument that the Commission has no authority to impose a cease-and-desist order in the 11th Circuit is invalid. See SEC v. Carriba Air, Inc., 681 F.2d 1318, 1321 (11th Cir. 1982); SEC v. Ginsburg, 362 F.3d 1292, 1305 (11th Cir. 2004).

See also SEC v. Rivers, 272 F.R.D. 607, 609 (M.D. Fla. 2011); SEC v. Huff, 758 F. Supp. 2d 1288, 1354-55 (S.D. Fla. 2010).

For all the reasons previously stated, especially Montford's failure to acknowledge his illegal acts, I find that a cease-and-desist order against Respondents is appropriate to eliminate the high probability that if given the opportunity, they will commit or cause future violations of Sections 204, 206(1), 206(2), and 207 of the Adviser Act and Advisers Act Rule 204-1(a)(2).

Disgorgement

Advisers Act Section 203(j) authorizes disgorgement and reasonable interest in any proceeding in which the Commission may impose a penalty; this proceeding was instituted pursuant to Advisers Act Sections 203(e) and 203(f), which allow imposition of a penalty. The proceeding was also instituted pursuant to Advisers Act Section 203(k)(5), which authorizes disgorgement and reasonable interest in any cease-and-desist proceeding under Section 203(k)(1). This is a cease-and-desist proceeding.²²

Disgorgement of illegal gains is an equitable remedy designed to deprive the wrongdoer of his unjust enrichment and thereby deter him and others from violating the securities laws. SEC v. First Pacific Bancorp., 142 F.3d 1186, 1191-92 (9th Cir. 1998), cert. denied, 525 U.S. 1121 (1999). "The primary purpose of disgorgement orders is to deter violations of the securities laws by depriving violators of their ill gotten gains." SEC v. Fischbach Corp., 133 F.3d 170, 175 (2d. Cir. 1997); see also SEC v. First Jersey Securities, Inc., 101 F.3d 1450, 1474 (2d. Cir. 1996) ("The deterrent effect of an SEC enforcement action would be greatly undermined if securities law violators were not required to disgorge illicit profits.").

The Division recommends \$210,000 as the disgorgement amount and calculates \$7,907.98 as prejudgment interest for the period beginning April 1, 2010, the first day of the month following the March 29, 2010, adoption of Montford Associates' Form ADV Part II that retained the language "[w]e do not accept any fees from investment managers," to the date of the hearing, November 7, 2010, citing SEC v. First City Financial Corp. Ltd., 890 F.2d 1215, 1231 (D.C. Cir. 1989). Div. Br. at 32-33, Ex. A.

Respondents maintain that disgorgement is inappropriate because: Montford was a victim of Kowalewski; the Division has not shown a relationship between its disgorgement amount and the damage caused by Montford's failure to disclose the payments to his clients; there has been no unjust enrichment; disgorgement will not protect the public; and the disgorgement amount is not profit but the gross amount Montford Associates received. Resp. Br. at 15-16.

Respondents' position that disgorgement is inappropriate because Montford Associates earned \$210,000 for administrative work performed for Kowalewski is unreasonable on its face. The administrative task of transferring the customer accounts was not Respondents' responsibility;

²² The OIP cites Sections 203(e) and 203(k) of the Advisers Act as authority for ordering Montford Associates to pay disgorgement, and Advisers Act Sections 203(f) and 203(k) as authority for ordering disgorgement from Montford. OIP at 5.

it appears they volunteered to do it to assist Kowalewski. The time and effort required to complete the “paperwork” to move ten customer accounts from an investment manager located in Maryland to an investment manager located in North Carolina could not possibly cost almost a quarter of a million dollars. In fact, Montford testified he would have been satisfied with \$130,000. Tr. 121. Respondents did not produce any time sheets, letters, records of meetings, calculations, analyses, or records that would show they put forth the time and effort to earn \$130,000 or \$210,000. The \$210,000 has all the indicia of ill-gotten gains or unjust enrichment.

Respondents did not cite any support for their claim that any disgorgement amount should be reduced by \$40,000, the amount they paid to St. Joseph’s in settlement of a civil suit. Tr. 171; Resp. Br. 15-16. Ill-gotten gains and settlement of a lawsuit based on undefined civil claims are two unrelated subjects.

Respondents’ misconduct unjustly enriched them by at least \$210,000. The record shows that several clients would not have retained Montford Associates if they had known of its dealings with Kowalewski in 2009 and 2010. St. Joseph’s paid a management fee of \$146,000 in 2010; GPA paid \$109,000 in 2009, and Savannah Country Day paid \$35,000 in 2009 and 2010. These clients left Montford Associates when they learned the information that Respondents failed to disclose.²³ Based on this evidence, Respondents’ ill-gotten gains, or funds illegally obtained by Montford Associates and Montford, could reasonably be considered to total at least \$500,000.

Rule 600(a) of the Commission’s Rules of Practice provides that:

The disgorgement order shall specify each violation that forms the basis for the disgorgement ordered; the date which, for purposes of calculating disgorgement, each such violation was deemed to have occurred; the amount to be disgorged for each such violation; and the total sum to be disgorged. Prejudgment interest shall be due from the first day of the month following each such violation through the last day of the month preceding the month in which payment of disgorgement is made. The order shall state the amount of prejudgment interest owed as of the date of the disgorgement order and that interest shall continue to accrue on all funds owed until they are paid. 17 C.F.R. § 201.600(a).

On the evidence in this record, it is impossible to fashion a disgorgement order with the specificity that Rule of Practice 600 envisions. Respondents’ violations occurred:

- (1) On August 30, 2009, when Montford told Kowalewski he would have to pay Montford Associates, Kowalewski agreed to do so, and Respondents did not inform their clients or amend their Form ADV;
- (2) in October or November 2009, when Kowalewski told Montford he would pay \$130,000 at the end of 2009 or early 2010 and Respondents did not inform their clients or amend their Form ADV;

²³ Prior to these events, Montford Associates had thirty clients, and on November 7, 2011, it had seven. Tr. 20, 169.

- (3) on November 2, 2009, when Montford Associates invoiced SJK for \$130,000 or November 30, 2009, when it sent SJK a second invoice for the same amount and Respondents did not inform their clients or amend their Form ADV;
- (4) in October or November 2009, when Kowalewski told Montford he would pay more than \$130,000 after SJK finished its first year in business and Respondents did not inform their clients or amend their Form ADV;
- (5) on January 4, 2010, when SJK paid the invoice for \$130,000 and Respondents did not inform their clients or amend their Form ADV; and
- (6) on November 1, 2010, when Montford Associates sent SJK an invoice for \$80,000 and in November 2010, when Montford Associates received \$80,000 from SJK and Respondents did not inform their clients or amend their Form ADV.

SEC v. Patel, 61 F.3d 137, 140 (2d Cir. 1995) and SEC v. First City Fin. Corp., 890 F.2d 1215, 1232 (D.C. Cir. 1989) stand for the proposition that courts, and presumably administrative agencies, have discretion in making a disgorgement calculation that need only be a reasonable approximation of profits causally connected to the violations. See also SEC v. Calvo, 378 F.3d 1211, 1217 (11th Cir. 2004). On this evidence, a reasonable amount is the following: (1) \$130,000, with prejudgment interest from February 1, 2010, the first day of the month following receipt of the funds and the non-disclosure to clients and failure to amend Montford Associates' Form ADV and (2) \$80,000, with prejudgment interest from December 1, 2010, the first day of the month following receipt of the funds and the non-disclosure to clients and failure to amend Montford Associates' Form ADV.²⁴ Prejudgment interest shall be calculated at the rate of interest established under Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. § 6621(a)(2), shall be compounded quarterly, and shall run through the last day of the month preceding the month in which payment is made. 17 C.F.R. § 201.600(a), (b).

Respondents have not shown a financial inability to pay. Terry T. Steen, Exchange Act Release No. 40055 (June 2, 1998), 67 SEC Docket 0837, 0847-48 (“[A] respondent who fails to introduce material evidence of inability to pay before the law judge has waived this issue.”).

Civil Penalties Pursuant to Section 203(i)

Section 203(i) of the Advisers Act authorizes the Commission, in any proceeding instituted pursuant to Sections 203(e), (f), or (k), to impose a civil penalty after notice and hearing if it finds a penalty is in the public interest and the person has willfully violated or willfully aided and abetted a violation of the Advisers Act. Advisers Act Section 203(i)(2) specifies that civil monetary penalties can be issued for each act or omission in violation of the federal securities laws. Section 203(i)(3) states that in determining whether a penalty is in the public interest, consideration may be given to: (a) whether the violations involved fraud, deceit, manipulation, or deliberate disregard of a

²⁴ I do not have substantial disagreement with the Division's position on disgorgement, but prefer my approach because it adheres closer to the dates of the respective violations.

regulatory requirement; (b) the resulting harm caused to others from the acts or omissions; (c) the extent of unjust enrichment considering any restitution paid to persons injured by the behavior; and (d) any past violations. 15 U.S.C. § 80b-3(i)(3). There are three tiers of maximum penalties for violations that occurred after March 3, 2009. 17 C.F.R. § 201.1004. The Third Tier is applicable if the conduct involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement and resulted in substantial loss or significant risk of substantial loss to other persons or substantial pecuniary gain to the person committing the violation. The maximum amount for each act or omission at the Third Tier is \$150,000 for a natural person and \$725,000 for any other person.

Respondents demonstrated a high level of deceit and reckless disregard of basic regulatory requirements in their dealings with clients, all non-profits that paid significant sums for what they believed was independent, investment management advice. On this record, it is in the public interest to assess a Tier Three civil penalty of \$500,000 on Montford Associates and \$150,000 on Montford. These amounts are considerably more than the Division recommended, but they are warranted given Respondents' brazen conduct toward their non-profit clients and should serve to deter other fiduciaries from similar self-serving conduct.

Fair Fund

Pursuant to Rule 1100 of the Commission's Rules of Practice, 17 C.F.R. § 201.1100, I will require that the amount of disgorgement and civil money penalties be used to create a Fair Fund for the benefit of Montford Associates' clients harmed by the violations.

Record Certification

Pursuant to Rule 351(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.351(b), I certify that the record includes the items set forth in the Record Index issued by the Secretary of the Commission on February 23, 2012.

Order

I ORDER that, pursuant to Section 203(f) of the Investment Advisers Act of 1940, Ernest V. Montford, Sr., is barred from association with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization.

I ORDER FURTHER that, pursuant to Section 203(k) of the Investment Advisers Act of 1940, Montford and Company, Inc., d/b/a Montford Associates, and Ernest V. Montford, Sr., shall cease and desist from committing or causing any violations, and any future violations, of Sections 204, 206(1), 206(2), and 207 of the Advisers Act and Advisers Act Rule 204-1(a)(2).

I ORDER FURTHER that, pursuant to Section 203(k) of the Investment Advisers Act of 1940, Montford and Company, Inc., d/b/a Montford Associates, and Ernest V. Montford, Sr., shall disgorge \$130,000, with prejudgment interest from February 1, 2010, and shall disgorge \$80,000, with prejudgment interest from December 1, 2010. Prejudgment interest shall be calculated at the rate of interest established under Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. §

6621(a)(2), shall be compounded quarterly, and shall run through the last day of the month preceding the month in which payment is made.

I ORDER FURTHER that, pursuant to Section 203(i) of the Investment Advisers Act of 1940, Montford and Company, Inc., d/b/a Montford Associates, shall pay a civil penalty of \$500,000 and Ernest V. Montford, Sr., shall pay a civil penalty of \$150,000.

I ORDER FURTHER, pursuant to Rule 1100 of the Commission's Rules of Practice, 17 C.F.R. § 201.1100, the creation of a Fair Fund and that the amount of disgorgement and civil money penalties collected be placed in this Fair Fund and used for the benefit of the Montford and Company, Inc., d/b/a Montford Associates' clients harmed by the violations found in this Initial Decision.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice. See 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. See 17 C.F.R. § 201.111. If a motion to correct a 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 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 motion to correct 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 occurs, the Initial Decision shall not become final as to that party.

Payment of the amounts to be disgorged and the civil money penalties shall be: (i) made by United States postal money order, certified check, bank cashier's check, or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) mailed or delivered by hand to the Office of Financial Management, Securities and Exchange Commission, 100 F Street NE, Mail Stop 6042, Washington, DC 20549; and (iv) submitted under cover letter that identifies the respondents and the file number of this proceeding. A copy of the cover letter and check shall be sent to W. Shawn Murnahan, Division of Enforcement, Securities and Exchange Commission, 950 East Paces Ferry Road, N.E., Suite 900, Atlanta, Georgia 30326-1382.

Brenda P. Murray
Chief Administrative Law Judge