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SOAH DOCKET NO. 312-15-1229
SSB DOCKET NO. IC15-01

IN THE MATTER OF	§	
THE INVESTMENT ADVISER	§	
REGISTRATION OF	§	BEFORE THE STATE OFFICE
MOWERY CAPITAL MANAGEMENT, LLC	§	OF
AND THE INVESTMENT ADVISER	§	ADMINISTRATIVE HEARINGS
REPRESENTATIVE REGISTRATION	§	
OF FREDERICK EUGENE MOWERY	§	

STATE SECURITIES BOARD'S INITIAL CLOSING BRIEF

TO: THE HONORABLE ADMINISTRATIVE LAW JUDGES

COMES NOW, the staff of the State Securities Board to respectfully file this closing brief:

I. Introduction

Mowery Capital Management, LLC ("MCM") and Frederick Eugene Mowery ("Mowery")(collectively, "Respondents") are registered with the Securities Commissioner of Texas as an investment adviser and an investment adviser representative, respectively. This matter includes serious allegations of fraud and misleading conduct by Respondents, and seeks the revocation of Respondents' registrations with the Securities Commissioner and the assessment of administrative fines against Respondents. The hearing was held at the State Office of Administrative Hearings from March 9th through the 13th.

II. Overview of Allegations

On October 13, 2004, MCM and Mowery registered with the Securities Commissioner as an investment adviser and investment adviser representative, respectively. In connection with the investment advice provided by Respondents, clients incur two

costs: an annual investment advisory fee paid to Respondents and trading charges paid to the broker-dealer. Respondents selected the broker-dealer, Worth Financial Group, Inc. (formerly known as Promark Securities), used for trading in client accounts. Worth has been the broker-dealer for MCM clients since 2004. Respondents agreed with Worth that MCM clients trading costs would be $51 per equity trade. These costs are higher than other broker-dealers offering similar or more services than Worth. In recommending Worth, Respondents breached fiduciary duties owed to clients.

In 2007, MCM entered into an agreement with Worth, whereby Worth agreed to pay MCM for research and other services. This agreement presented a conflict of interest between MCM and its clients. Respondents did not disclose to clients the existence of this agreement with Worth or the conflict of interest that it presented. Respondents invoiced Worth pursuant to this agreement on a monthly basis. These invoices were often for tens of thousands of dollars on a monthly basis and have resulted in over $1,300,000 in payments from Worth to MCM. Yet, Respondents and Worth do not record the services purportedly rendered in connection with each invoice.

Investment advisers are required to provide clients a document that discusses key details about the investment advisers business and discloses conflicts of interest. Since March 2011, this document has been referred to as the Form ADV Part 2 or the "firm brochure." MCM's Part 2 failed to disclose the conflict of interest presented by the agreement with Worth. Furthermore, MCM's Part 2 contained misrepresentations about Mowery and MCM's business.

The staff of the Texas State Securities Board ("Staff") conducted an inspection of Respondents' office on April 9, 2014. The Staff first learned of MCM's agreement with Worth during this inspection and became concerned with the sizeable payments MCM was receiving for purportedly providing research and other services to Worth. Shortly after the Staff's inspection, Mowery created two documents purporting to be "research" written by Mowery. The contents of these documents were not written by Mowery, but were actually plagiarized material. As it turns out, plagiarism was not new to Mowery. Since at least 2006, MCM's website included a "Letter to Our Clients" that was falsely represented as being written by Mowery. In fact, the contents of the "Letter" were copied from an article written by a well-known commentator on the economy. Mowery took steps to cover up his misrepresentations, including lying under oath about how Mowery created the "Letter."

Finally, Respondents also submitted back-dated documents to the Staff. The Staff requested written records provided to clients disclosing MCM's payments of referral fees. Respondents had not provided clients with written disclosure of the referral payments at the time these clients entered into a relationship with MCM. Instead of informing the Staff of this fact, Respondents provided the Staff with four documents representing disclosure notices signed by clients. Respondents created the documents in April 2014, only days before submitting them to the Staff. Yet, two of the documents Respondents submitted to the Staff listed dates in 2005 and 2012.

To cover up the back-dating, Mowery used correction paper to conceal information on MCM's letterhead that would have made it obvious the documents submitted by Respondents were not created in 2005 or 2012.

In sum, Respondents have engaged in a pattern of unethical and fraudulent conduct involving significant breaches of duties owed to their clients along with efforts to mislead clients and the government.

III. Fiduciary Duties of Investment Advisers

A brief overview of the fiduciary principles applicable to investment advisers provides a useful lens to understand the significance of Respondents' actions.

A. Investment Advisers are Fiduciaries

Under Texas law, a fiduciary relationship arises when a party occupies a position of confidence toward another.[1] A "confidential relationship exists where one party is in fact accustomed to being guided by the judgement or advice of the other, or is justified in placing confidence in the belief that such person will act in its interest."[2] Respondents were provided broad discretions in managing client funds, including selecting the investments and the broker-dealer used to make the transactions. Respondents' clients have placed an enormous amount of trust and confidence in Respondents. The facts in this case clearly support finding that Respondents are fiduciaries to their investment advisory clients.

B. Duties Owed to Clients

Respondents owe clients various fiduciary duties, including: a duty of loyalty[3]; a duty of due care[4]; and a duty to disclose all relevant information[5].

The duty of loyalty recognizes the general principle that an agent must "act solely for the benefit of the principal."[6] Notably, the duty of loyalty encompasses numerous obligations. For example, an agent is prohibited from acting, on an undisclosed basis, "for persons whose interests conflict with those of the principal in matters in which the agent is employed."[7]

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[1] Miller-Rogaska, Inc. v. Bank One, 931 S.W.2d 655, 663 (Tex.App.1996).

[2] Thames v. Johnson, 614 S.W.2d 612, 614 (Tex.Civ.App.-Texarkana1981, no writ)

[3] Restatement (Third) of Agency §8.01, §8.06 (2006).

[4] Restatement (Third) of Agency §8.08 (2006).

[5] Restatement (Third) of Agency §8.11 (2006).

[6] Restatement (Third) of Agency §8.01, §8.06 (2006).

[7] Restatement (Third) of Agency §8.04, §8.06 (2006).

The duty of care requires a fiduciary to act with the standard care and with the standard skill for the functions the fiduciary is performing for the principal.[8] Furthermore, an agent has a duty to use reasonable effort to provide the principal with facts that the agent knows the facts are material to the agent's duties to the principal.[9]

All investment advisers, including those subject to state regulation, are subject to a fiduciary standard originating from the anti-fraud provisions of the Investment Advisers Act of 1940.[10] The seminal case on this subject is U.S. v. Capital Gains Research Bureau.[11] In *Capital Gains*, the U.S. Supreme Court stated that the Advisers Act "reflects a congressional recognition 'of the delicate fiduciary nature of an investment advisory relationship'."[12] The Court in *Capital Gains* discussed how courts have recognized various duties on fiduciaries, including "an affirmative duty of 'utmost good faith, and full and fair disclosure of all material facts'" and "an affirmative obligation 'to employ reasonable care to avoid misleading' his clients."[13] Although the present matter does not involve cited violations of the Investment Advisers Act of 1940, the fiduciary standard described in *Capital Gains* is very relevant because it applies to all investment advisers.

IV. Breach of Fiduciary Duties in Recommendation of Broker-Dealer

A. Background

On October 13 2004, MCM and Mowery registered with the Securities Commissioner as an investment adviser and investment adviser representative, respectively.[14] Because MCM is only an investment advisory firm, Respondents clients needed a broker-dealer for trading activity. Respondents recommended the brokerage used for trading in client accounts.[15] This firm is named Worth Financial Group, Inc. (formerly known as Promark Securities)[16] Worth is owned by Mowery's friend and former business associate, James Willard Clark. Respondents and Worth negotiated the trading costs that MCM clients would pay.

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[8] Restatement (Third) of Agency §8.08 (2006).

[9] Restatement (Third) of Agency §8.11 (2006).

[10] Investment Advisers Act of 1940, § 206, 15 U.S.C. § 80b-6(Laying out the prohibition on fraudulent conduct, Section 206 of the IA Act of 1940 starts, "It shall be unlawful for any investment adviser…").

[11] SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 84 S.Ct. 275, 11 L.Ed.2d 237 (1963).

[12] Id. at 282-283.

[13] Id. at 284

[14] Ex. SSB 112, Stipulated Facts 1, 5.

[15] Ex. SSB 112, Stipulated Fact 8.

[16] Tr. 845, lines 8-11.

During the hearing in this case, there was a lot of discussion about the cost of this trading activity. Yet, the Staff agrees with Respondents on one point – the SSB does not specifically mandate broker-dealer commission rates.

However, when an investment adviser selects the broker-dealer to be used for client accounts, Respondents must satisfy various fiduciary duties owed to their clients in connection with this selection. Mowery acknowledged Respondents' duty to determine which broker-dealer was appropriate for clients and their obligation to obtain "best execution" for the clients.[17] Respondents' clients trusted Mowery and MCM to take sufficient steps to make these determinations.[18]

Robert Brands, a current MCM client, said it best, "You know, I think you have to investigate as a buyer, and Fritz is a buyer of a service, has to investigate all the opportunities out there."[19] As the evidence shows, Respondents failed to meet this simple expectation.

B. Only Considered Worth for Broker-Dealer

Mowery testified that he considered two broker-dealers at the start of MCM: Worth and Oxford Financial Group.[20] However, after the Staff presented evidence that Oxford Financial Group was not even registered when MCM was started[21], Mowery was forced to admit that it was "probably true" he only considered Worth.[22]

Respondents' witnesses testified repeatedly that there are thousands of broker-dealers available.[23] Yet, Respondents never contemplated another broker-dealer before selecting Worth.

C. No Review of Worth's Business or Clark's Regulatory History

Prior to selecting Worth as the broker-dealer for MCM clients, Mowery knew that Worth was owned by his friend, Mr. Clark. However, Respondents did very little to understand much more about Worth's business or whether other broker-dealers would be better for MCM clients.

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[17] Tr. 93, lines 15-22.

[18] Tr. 851; 891

[19] Tr. 81, lines 16-18.

[20] Tr. 94, lines 15-20; 95, lines 3-6.

[21] SSB 114.

[22] Tr. 97, lines 5-6.

[23] Tr. 422; 945; 1059

Mowery did not review any records or conduct any research related to Worth.[24] The key reason for MCM's selection of Worth was Mr. Clark.[25] Yet, despite being aware that Mr. Clark had "some issues" with regulators, Mowery states that he did not gain an understanding of the specifics before choosing Worth.[26] Notably, Mr. Clark was required to withdraw his securities registrations by Arkansas regulators in connection with a transaction involving the sale of stock for an entity in which Mowery was also a Director.[27]

D. Respondents did not obtain "best execution"

A well-established component of an investment adviser's fiduciary duty is the obligation to obtain "best execution" of client trades.[28] Respondents incorrectly limit their best execution obligation to speed and price of trade execution.[29] As described below, an investments adviser's best execution obligation is much broader.

An investment adviser has to "execute securities transactions for clients in such a manner that the client's total cost or proceeds in each transaction is the most favorable under the circumstances."[30] The fact that Mowery only considered Worth supports finding that Respondents could not have determined if clients' "total cost or proceeds" were the "most favorable."

Clinton Edgar highlighted factors involved in a money manager's assessment of best execution, including: the ability of the broker-dealer to obtain the best price; the size and stability of the clearing firm and introducing broker; the types of investments available through the broker-dealer; trading capabilities of the broker-dealer; and trading costs.[31] Formal guidance issued by the U.S. Securities & Exchange Commission (SEC) reiterates that investment advisers "consider the full range and quality of a broker's services" and discusses factors similar to those mentioned by Mr. Edgar.[32] A closer examination of these various factors shows how Respondents' single-minded selection of Worth impacted the clients.

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[24] Tr. 113, lines 19-23.

[25] Tr. 121, lines 16-18.

[26] Tr. 117, lines 15-16.

[27] Ex. SSB 85; Tr. 118-121.

[28] Securities Exchange Act Release No. 23170 (April 28, 1986); In the Matter of Kidder, Peabody & Co., Inc., SEC Rel. No. IA-232, 43 S.E.C. 911 (Oct. 19, 1968)

[29] Tr. 89-90

[30] Securities Exchange Act Release No. 23170 (April 28, 1986)

[31] Tr Page 579

[32] Securities Exchange Act Release No. 23170 (April 28, 1986)

i. Order Execution

Mowery incorrectly treats best execution as involving whether or not trades are getting done in a "timely manner" and whether you are getting the "best prices."[33] This type of data is reported publicly.[34] Yet, Mowery had not reviewed even this type of information prior to 2014. In fact, it was only after the Staff's investigation that Mowery reviewed this type of order execution information.[35] Previously, Mowery relied on Worth to make the best execution assessment.[36]

Because Respondents selected Worth as the broker-dealer for MCM client trades, three broker-dealers have been involved in trading execution for MCM clients: Worth, Maplewood Investment Advisors; and National Financial Services (NFS). NFS is the firm that has custody of the client funds and is also referred to as the clearing firm. NFS would not allow Worth to have a direct correspondent relationship with NFS because Worth did not have enough trading activity and it did not have enough of a clearing deposit.[37] This is why Worth had to enter into the "tri-party agreement" with Maplewood and NFS.[38]

Investment advisers do not have to use this sort of structure. In fact, current and former financial examiners, including a former industry consultant, testified about the fact that investment advisers more commonly use broker-dealers that are either "self-clearing" or are directly affiliated with the clearing firm.[39] Examples of these firms include, Charles Schwab, TD Ameritrade, and Fidelity.[40]

Mr. Edgar presented information, publicly available on the Internet, regarding order execution data for two self-clearing broker-dealers whose trading costs were less than what MCM clients incurred through Worth.[41] This data and Mr. Edgar's sworn testimony on this issue is extremely relevant because it evidences the fact that reported order

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[33] Tr. 89-90.

[34] Tr. 90, lines 4-9.

[35] Tr. 91, lines 15-17.

[36] Tr. 91, lines 18-21.

[37] Tr. 445, lines 15-25 ; 446, lines 4-9.

[38] Ex. SSB 15

[39] Tr. 59; 576

[40] Tr. 576

[41] Ex. SSB 90, SSB 94

execution at firms such as Schwab and TD Ameritrade is comparable to, if not slightly better than, NFS.[42]

ii. Financial Stability of the Broker-Dealers

Financial instability at Worth, Maplewood, or NFS could have a negative impact on the ability to trade efficiently in MCM client accounts. Yet, Mowery did not review the financial stability of any of these firms.

When questioned about how he assessed financial stability of custodian broker-dealers, Mowery acknowledged that he relied on Worth to select the custodian. [43] Furthermore, because Mowery did not review any records related to MCM,[44] Respondents could not make any assessments about the financial position of Worth.

Importantly, Schwab and TD Ameritrade – both of which provide lower trading costs than Worth – join NFS among the leading custodial and clearing firms in the country in terms of size and assets they custody.[45]

iii. Trading Capabilities

The trading capabilities available through a broker-dealer could affect trade execution. Examples relevant to this case include online trading capabilities and block-trading.

a. Online Trading Capabilities

Some broker-dealers offer investment advisers the ability to enter trades through online systems. This avoids any delay associated with calling a broker to place a trade.

Online trading has been available at broker-dealers for the entire time that MCM has been registered as an investment adviser. Staff members and Mr. Clark all testified about the availability of online trading at firms such as TD Ameritrade, Schwab, and Fidelity.[46] Mowery, on the other hand, is purportedly unaware of the fact that firms like discount brokerage firms like TD Ameritrade and Schwab allow investment advisers to trade online.[47]

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[42] Ex. SSB 90, 94; Tr. 589, 593, 602.

[43] Ex. SSB 111, pg. SSB-SOAH-4350-4351

[44] Tr. 113, lines 19-23.

[45] Tr. 602, lines 9-13.

[46] Tr. 461; 536; 578, lines 15-24

[47] Tr. 318, line 5-7

Until November 2014, Mowery had access to online trading through Worth on a system provided by NFS – called Streetscape.[48] Since November 2014, Mowery is forced to call Worth to place a trade. Mowery acknowledges that this additional step could impact the share price clients obtain.[49] Yet, Respondents continue to utilize Worth as the broker-dealer for their clients.

b. Block trading

Another important tool - "block trading" - allows an investment adviser to buy (or sell) a block of the same security, by placing a single order, and then allocate the shares amongst relevant clients at an average price. Without block trading, an investment adviser seeking to buy or sell the same security for multiple clients would have to enter the orders in a sequential manner. This could result in clients receiving different prices per share.

Respondents often recommended clients transact in the same security.[50] Accordingly, block trading is in the best interests of Respondents' clients.[51] Broker-dealers have offered block trading capabilities to investment advisers since the late 1990s/early 2000s.[52] Mowery was unaware of this fact.[53]

Respondents did not have block trading capability at Worth for equity trades until 2009.[54] Consequently, Respondents had to enter client trades on an account by account basis from the start of the Worth relationship to 2009.[55] For obvious reasons, this trade entry process takes longer than entering in a block order for shares that can be allocated later in the day. During that time period, clients are exposed to the risk of a change in prices. Furthermore, this trade entry process resulted in Respondents' clients paying more on a per share basis than others for transactions done in accordance with Respondents' practice.[56] Results like these would have been avoided if Respondents had utilized a broker-dealer that offered block trading for client accounts.

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[48] Tr. 110; 236

[49] Tr. 312-314

[50] Tr. 238, lines 9-12.

[51] Tr. 238, lines 5-8.

[52] Tr. 616, lines 23-25.

[53] Ex. SSB 111, Page 222, lines 15-17.

[54] Tr. 238, lines 13-20; Ex. SSB 111, Page 222, lines 12-14.

[55] Tr. 239, lines 10-14

[56] For examples, see Ex. SSB 155, 156.

Moreover, broker-dealers have offered the ability for investment advisers to allocate block transactions electronically since the early 2000s.[57] Respondents did not have this capability through Worth until 2014.[58] Mowery was unaware of how long electronic allocations have been available at other broker-dealers, but indicated it would be "news" to him if such capabilities were available since 2000.[59] This is another indication of how little Respondents did to understand the trading capabilities available at broker-dealers other than Worth.

iv. Value of Research

Worth did not provide research to MCM as part of the broker-dealer relationship.[60] Instead, MCM was purportedly providing research to Worth.

Mr. Edgar and Terria Heng offered evidence indicating the fact that other broker-dealers, including ones with lower trading costs, offer research to investment advisers.[61] Inexcusably, Mowery was not even aware of the fact that other broker-dealers would supply research to investment advisers.[62]

v. Product Availability

Based on the Staff's review of trading in MCM client accounts, the Staff confirmed that MCM clients could have accessed the same investments through many other broker-dealers, including those dealers costing much less on a per trade basis.[63]

The only product difference referenced by Respondents was Mowery's claim that he was sometimes able to obtain better prices for clients on bonds because Worth allowed him to shop multiple bond desks.[64] In concept this sounds like a good point. However, even theoretically, the amount of benefit this practice could pose to Respondents' clients is limited because bonds make up a relatively small portion of MCM's practice.[65]

In reality, Respondents did not offer any credible evidence that they in fact did obtain better bond prices for the clients. In fact, the only specific information on bond prices

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[57] Tr. 617, lines 1-4.

[58] Tr. 241. lines 13-18

[59] Tr. 240, lines 15-20.

[60] Ex. SSB 111, pg. 191, lines 15-16.

[61] Tr. 60, lines 1-7; 589, lines 18-22; Ex. SSB 90, pg. 3957.

[62] Tr. 234, lines 24-25; 235, lines 1-2.

[63] Tr. 581-582

[64] Tr. 124

[65] Ex. SSB 111, SSB-SOAH-4401, line 17

was raised by the Staff. This evidence indicates that Respondents were actually profiting in a MCM account on bond transactions with their clients – i.e., MCM was the one getting better prices than its clients.[66]

vi. Trading costs

Mowery negotiated the trading costs for MCM clients.[67] For the vast majority of the time period, clients were paying $51 per equity trade. But, Mowery did not review the trading costs at other BDs prior to selecting Worth.[68] Without such a review, how could Respondents have possibly understood if lower trading costs were available at broker-dealers offering similar services for MCM's clients?

The Staff presented testimony from current and former financial examiners who had worked on numerous examinations and investigations of investment advisers. In all, these Staff members have participated in over 170 examinations of investment advisers across Texas.[69] Additionally, one of the examiners provided consulting services to approximately 30 investment advisers before joining the Staff.[70] These witnesses offered sworn testimony confirming that state-registered investment advisers, including those similar to MCM, regularly obtain trading costs for clients between $7 and $16.99.[71] Even Mr. Clark confirmed that investment advisers can receive trading costs as low as $7.95.[72]

As noted previously, Mowery did not review costs at other broker-dealers prior to selecting Worth. Nevertheless, he claims to believe that MCM could not obtain those prices as an investment adviser.[73] In reference to a T.D. Ameritrade commission schedule, Mowery states, "as a professional, I would qualify under a broker-assisted trade."[74] A broker-assisted trade is one where the adviser places a call to the trade desk.[75] A broker-assisted trade is generally more expensive than the lowest cost trade advisers can obtain at certain broker-dealers. Mowery's claim that MCM would have to

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[66] Tr. 249-259

[67] Tr. 99-100

[68] Tr. 114, lines 21-25

[69] Tr. 51; 559; 645.

[70] Tr. 49-50.

[71] Tr. 63; 591

[72] Tr. 460, lines 10-13

[73] Tr. 318

[74] Tr. 318, lines 18-19.

[75] Tr. 460, lines 18-19.

rely on broker-assisted trades is used to justify his position that the costs at Worth are "comparable" to discount brokers.[76] Of course, this is another fiction generated by Mowery. As a "professional", Mowery likely knows, or at least reasonably should know, that investment advisers don't have to rely on broker-assisted trades.

Contrary to the evidence offered by many others, including Mr. Clark, Mowery states a belief that Respondents' clients could not obtain $9.99 trades at TD Ameritrade unless they trade their own accounts.[77] This is not true. Mowery does, or at least should, know better.

At best, Mowery's stated beliefs would be the result of Respondents' reckless abandonment of the standard of care Respondents owe clients.[78] More concerning is the fact that Respondents' have a motive to claim that the cost difference between Worth and other broker-dealers is minimal. If the cost is not much different, then Respondents' decision to use Worth would be easier to justify.

While the trading costs are not the only factor to consider in assessing best execution, they must be considered by an investment adviser in order to "execute securities transactions for clients in such a manner that the client's total cost or proceeds in each transaction is the most favorable under the circumstances". Respondents' claimed ignorance of the trading costs available for his clients at other broker-dealers does not excuse Respondents from satisfying their duty.

vii. Periodic and Systematic Review

Investment advisers should engage in the best execution evaluation "periodically and systematically."[79] Respondents appear to recognize this responsibility because MCM's Form ADV Part 2A states that MCM "reviews the execution of trades" and "trading fees" each quarter.[80] However, Respondents do not really engage in a periodic and systemic review of best execution. Respondents only mentioned Mowery's review of trading activity as his ongoing assessment of best execution.[81] This does not satisfy the investment adviser's obligation to determine if the "total costs or proceeds" of trading activity are the most favorable for clients.

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[76] Tr. 317-318

[77] Tr. 302, lines 12-17

[78] Restatement (Third) of Agency §8.08 (2006)

[79] Securities Exchange Act Release No. 23170 (April 28, 1986)

[80] For example, SSB 2, Page SSB-SOAH-000028

[81] Tr. 322-323

viii. Conclusion

There is no doubt that best execution can be achieved without utilizing the lowest trading costs. There are a number of factors an investment adviser must consider in determining whether transaction executed for clients are being done under the most favorable total costs or proceeds. In selecting to route client trades through Worth, Respondents achieved essentially the same order execution quality that Respondents could have obtained from broker-dealers charging much less for trading fees. Moreover, these other broker-dealers – in addition to significantly lower costs - would have offered trading capabilities that have not always been available through Worth and research that Worth has never offered MCM.

The facts in this case prove by a preponderance of the evidence that Respondents breached their duty to achieve best execution for clients.

E. Breached Duty of Care

As discussed above, Respondents had the ability to obtain lower trading costs for their clients while achieving the same, or better order execution, and receiving additional benefits from the broker-dealer such as research and block-trading capabilities.

Respondents' clients have been led to believe that the higher costs at Worth are warranted because "you get what you pay for."[82] It was reasonable for clients to expect that Respondents had good cause to believe the higher costs for trading through Worth benefitted the clients. After all, they afforded Respondents a very high level of trust. Respondents, in turn, owed their clients a fiduciary duty to act with the standard care and with the standard skill for the functions the fiduciary is performing for the principal.[83]

Unfortunately, Mowery did not exercise due care in determining if the higher costs at Worth could provide services that presented value to Respondents' clients. As noted previously, Respondents did not even attempt to determine the costs at other broker-dealers before selecting Worth.[84] When pressed on this point, Mowery simply says, "I was comfortable with Worth, so I went with Worth."[85]

As detailed previously, Respondents also failed to understand key details about the services and execution capabilities at broker-dealers other than Worth. Respondents did not assess whether another broker-dealer could provide the same or more benefits to clients at lower trading costs; thus, Respondents could not have developed any

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[82] Tr. 837; 927; 988

[83] Restatement (Third) of Agency §8.08 (2006).

[84] Tr. 114, lines 10-25

[85] Id.

understanding as to whether or not the costs associated with Worth benefited their clients in reasonable proportion to the costs.

As Mr. Edgar's testimony confirmed, other broker-dealers could have executed transactions in the securities Respondents bought and sold in client accounts, could have obtained at least the same execution quality, and would have done so at a significantly lower trade costs. For the reasons stated above, Respondents breached the fiduciary duty of care they owed to clients in selecting Worth as the broker-dealer.

F. Section 28(e) Safe Harbor

Section 28(e) of the Securities Exchange Act of 1934 provides investment advisers a safe harbor to use client commissions to purchase "brokerage and research services" under certain circumstances.[86] The SEC has issued guidance interpreting Section 28(e), most recently in 2006.[87] Based on Mowery's stated reasons for using Worth, Respondents' selection of Worth at $51 per equity trade would not be protected by the Section 28(e) safe harbor.

Mowery says Respondents chose Worth for the following reasons:

- "I'd known Jim for a long period of time, and I felt like he was a high quality individual."[88]
- "I had access to, you know, a major wire house, NFS."[89]
- "It was going to work very efficiently for my firm."[90]
- Regarding "back office" functions such as cashiering, account paperwork, and transfers - "I was very comfortable that Jim could do this for me and take a lot of that work out of my office into his office so I didn't have to hire someone to do a lot of that stuff."[91]
- Worth helps to allocate block orders of bond and equities.[92]

Investment advisers, as fiduciaries, "are obligated to act in the best interests of their clients and cannot use client assets (including client commissions) to benefit

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[86] Securities Exchange Act of 1934, § 28(e), 15 U.S.C.A. § 78bb(e)(3)(C).

[87] Securities Exchange Act Release No. 54165 (July 18, 2006).

[88] Tr. 115

[89] Id.

[90] Id.

[91] Tr. 116

[92] Tr. 125, lines 4-8; 239-240

themselves, absent client consent."[93] Section 28(e) of the Exchange Act allows an investment adviser to not be found in breach of its fiduciary duties even if it chooses to pay a commission higher than what another broker-dealer would have charged to effect the same transaction. To benefit from the Section 28(e) safe harbor, the investment adviser must determine "in good faith that such amount of commission was reasonable in relation to the value of the brokerage and research services" provided by the selected broker-dealer.[94]

Respondents did not make a good faith determination that the commissions paid to Worth were reasonable in relation to the value of any additional brokerage or research services available through Worth.

First and foremost, Respondents cannot claim "good faith" if Respondents never made an assessment of what other broker-dealers would charge for trading in MCM client account before selecting Worth. Furthermore, Mowery's testimony that he believed MCM clients would have to pay at least $45 per trade at other broker-dealers has no credibility. A plethora of evidence confirmed that Respondents' could have traded the client accounts for significantly lower trading costs.[95] Mowery has absolutely no reason to not understand the commission structures available for clients of investment advisers. If Mowery genuinely doesn't understand that advisers can trade their clients' accounts for approximately 80% less than what Worth was charging, he is the only one to blame. His lack of interest in understanding what options were available for his clients is glaring.

In addition to his indifference before selecting Worth, Mowery is not even sure if he identified himself as an investment adviser during a recent communication with a broker-dealer purportedly during which he was interested in learning the commission costs at the dealer.[96] A person in Mowery's position acting in good faith would absolutely identify himself as an investment adviser.

Next, a number of the claimed benefits of using Worth did not add value compared to the services available for much lower commission costs. Specifically, clients were not going to get better execution trading through Worth because Respondents could have accessed NFS, or a broker-dealer with at least similar execution capabilities, for significantly lower costs.[97] Furthermore, Worth's assistance with allocations of equity block trades was only necessary because Worth did not offer MCM electronic allocation

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[93] Securities Exchange Act Release No. 54165 (July 18, 2006).

[94] Securities Exchange Act of 1934, § 28(e), 15 U.S.C.A. § 78bb(e)(3)(C).

[95] See Ex. SSB 89; 92. Also, testimony from Edgar and Clark

[96] Tr. 303, lines 7-10

[97] Tr. 539-540; 576

until 2014.[98] Respondents would not have needed Worth's assistance with these allocations at lower cost broker-dealers because many of them offered electronic allocation capabilities since early 2000s.[99]

Finally, a product or service believed to add value to justify the higher commission must be eligible "research" or "brokerage". Eligible "research" is mentioned in Sections 28(e)(3)(A) and (B)[100] and, thus must constitute "advice," "analyses," or "reports." Worth does not provide any of these to Respondents for the benefit of MCM clients. To be an eligible "brokerage" services for purposes of the Section 28(e) safe harbor, the service must involve effecting securities transactions or be "incidental thereto."[101] The SEC guidance describes specific post-trade services as being "incidental" to executing a transaction. [102] The only service listed in the SEC guidance and mentioned by Mowery as being available through Worth is the "electronic communication of allocation instructions." But, this can't justify higher commissions because Worth did not provide MCM this service until 2014 and other broker-dealers have offered it to investment advisers for many years – with lower commission costs.[103]

G. Breached Duty of Loyalty

Through early 2007, Worth and MCM were sharing offices and Worth was paying MCM for a portion of the office expenses.[104] In July 2007, MCM and Worth entered into the "Services Agreement."[105] From its inception, the Services Agreement contemplated payments from Worth to MCM for services MCM would provide Worth. As a result of these arrangements, Respondents had an interest in Worth's revenue.

The evidence indicates that Worth would not have been able to make very sizeable payments to MCM between 2007 and 2014 if Respondents clients were not trading through Worth at their established commission rate.[106] Mowery's claimed lack of understanding of Worth's revenue and financial situation is not believable. Not only are Mowery and Clark friends who speak very regularly, but Mowery also receives various

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[98] Tr. 241

[99] Tr. 616

[100] Securities Exchange Act of 1934, § 28(e), 15 U.S.C.A. § 78bb(e)(3)(C)

[101] Securities Exchange Act of 1934, § 28(e), 15 U.S.C.A. § 78bb(e)(3)(C); Securities Exchange Act Release No. 54165 (July 18, 2006).

[102] Securities Exchange Act Release No. 54165, 39 (July 18, 2006).

[103] Tr. 616

[104] Tr. 502, lines 11-19

[105] Ex. SSB 113

[106] Ex. SSB 152, 153

Worth financial records on a regular basis.[107] The Staff contends that Respondents placed their own interests over their clients when they caused MCM clients to pay $51 per equity trade to Worth. [108] This point is supported by the apparent absence of any effort to determine if another broker-dealer was more appropriate for Respondents' clients before selecting Worth.

Evidence presented at the hearing established that Mowery and Waring have held accounts at Worth also. Significantly, Mowery and Waring were often assessed commissions well below what MCM clients paid.[109] Waring referred to the fact that he was assessed only a $20 commission due to a "courtesy charge" for the owners of MCM.[110] Mowery paid even lower commissions on many trades – with almost 40% between $0-$1.[111] Respondents' clients were not aware of the reduced commissions.[112]

Respondents' client, Robert Lloyd, innocently identified why the reduced commissions for Respondents are concerning. Mr. Lloyd, a successful contractor, in relating common practices in his business stated, ""he's a big customer to them. He brings them lots of clients. So I don't – why would they not give him a better deal on his own stuff, you know, just because he's bringing them all this other business they make money off of."[113]

Unlike contractors and many other businesses, investment advisers are fiduciaries to their clients. In selecting the broker-dealer for clients, Respondents are serving as agents for the clients and should not acquire a material benefit through the use of this position.[114] The evidence put forth does not confirm that Respondents only received the commission reductions because they brought the MCM business to Worth. But given the Respondents one-tracked approach in selecting Worth, it doesn't matter if the benefit was given due to friendship or as an incentive – Respondents loyalty did not lay with the clients in selecting Worth as the broker-dealer.

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[107] Ex. SSB 63

[108] Restatement (Third) of Agency §8.01 (2006)

[109] Tr. 372 and Ex. SSB 154

[110] Tr. 372, lines 6-20

[111] Tr. 154

[112] For example – Tr. 700; 768, lines 5-12

[113] Tr. 934-935

[114] Restatement (Third) of Agency §8.02 (2006) (""An agent has a duty not to acquire a material benefit from a third party in connection with transactions conducted or other actions taken on behalf of the principal or otherwise through the agent's use of the agent's position.").

H. Contrasting Practices at Worth and Worth Asset Management

The record contains evidence of two investment advisers accounting for their fiduciary duties in selecting a broker-dealer. In sharp contrast to MCM's actions, Worth and Worth Asset Management ("Worth Asset") took some key steps to address clients' best interests.

Worth and Worth Asset give clients the option to choose between two arrangements – TD Ameritrade or Worth/NFS.[115] In doing so, the advisers will discuss with clients the perceived advantages and disadvantages of each firm.[116] Also notable is the reason that Worth began using TD Ameritrade in the first place. A predecessor to TD Ameritrade was known for its options capabilities and because Worth needed a more "robust options platform", Worth turned to that broker-dealer.[117] On the other end of the spectrum, Respondents do not give clients a choice – all clients use Worth for trading.

Furthermore, Worth's effort to find and use a third-party broker-dealer just because of a specific line of business shows a thoughtful approach in selecting a brokerage - an approach that is absent in Respondents' case.

Also very relevant is the difference in cost for Worth or Worth Asset clients to trade through Worth/NFS versus TD Ameritrade – it is $25 as opposed to $7.95 or $9.95.[118] Mr. Clark, in recognition of the fiduciary duties, keeps the cost for Worth advisory clients at $25, even if it means that Worth takes a loss on that trading activity.[119] Worth and Mr. Clark may or may not have other issues with their practices, but it appears that their approach to selecting a broker-dealer for clients is clearly more client-oriented than Respondents.

I. Breach of Fiduciary Duty is Fraud

Section 4.F of the Texas Securities Act explicitly lists certain definitions of "fraud" and "fraudulent practice." However, this section also states that nothing therein shall limit or diminish the full meaning of the terms "fraud," "fraudulent," or "fraudulent practice" as applied or accepted in courts of law or equity. [120] Pursuant to Texas common law, fraud can include both actual and constructive fraud.[121] Constructive fraud is the breach of a

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[115] Tr. 529, lines 12-16

[116] Id.

[117] Tr. 514, lines 2-10

[118] Tr. 556

[119] Tr. 556-557

[120] Tex. Rev. Civ. Stat. Ann. art. 581-4 (West 2010 & Supp. 2014).

[121] Archer v. Griffith, 390 S.W.2d 735, 740 (Tex. 1964).

legal duty which the law declares fraudulent.[122] Texas courts have recognized that the existence of a fiduciary relationship imputes to the relationship additional and higher duties.[123] A breach of these duties may constitute fraud.[124] It has been well established that investment advisers owe fiduciary duties to their clients.[125] Therefore, an investment adviser engages in a fraudulent practice when the adviser breaches a fiduciary duty it owes to its clients.[126]

J. Conclusion

The issue is not whether Worth could charge $51 per equity trade. Instead, the issue lay in Respondents actions, and inactions, in connection with selecting Worth as the broker-dealer for their clients. Every investment adviser that selects a broker-dealer for advisory clients is subject to having the decision reviewed for adherence to the adviser's fiduciary duties. Securities laws and fiduciary principles account for reasoned decision-making by well-intentioned advisers.

This case does not involve minor breaches of fiduciary duties nor an investment adviser that made a determination in good-faith. Unlike the vast majority of investment advisers in the state, Respondents were not acting in good-faith and severely breached the duty to seek best execution, the duty of care, and the duty of loyalty. Such significant breaches of fiduciary duties are fraudulent practices and should result in the strongest sanctions pursuant to Section 14.A(3) and 23-1 of the Texas Securities Act.

V. Failure to Disclose the Services Agreement

In 2006 and early 2007, Worth and MCM were sharing offices and Worth was paying MCM for a portion of the office expenses.[127] But around July 2007, Mowery was moving his office to McKinney[128], and thereby payments from Worth to MCM for office expenses would have appeared unjustified. In July 2007, MCM and Worth entered into the "Services Agreement."[129] From its inception, the Services Agreement contemplated

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[122] *Id.*

[123] Chien v. Chen, 759 S.W.2d 484, 495 (Tex. App. 1988).

[124] *Id. See also* In re Estate of Kuykendall, 206 S.W.3d 766, 770 (Tex. App. 2006).

[125] Capital Gains, 84 S.Ct. at 282-283.

[126] Cotton v. Weatherford Bancshares, Inc., 187 S,W,3d 687, 702 (Tex. App. 2006)("At common law, the term "fraud" means an act, omission, or concealment in breach of a legal duty, trust, or confidence justly imposed, when the breach causes injury to another or the taking of an undue and unconscientious advantage.")

[127] Tr. 502, lines 11-19

[128] Tr. 127, lines 7-11

[129] SSB 113

payments from Worth to MCM. The Services Agreement represented a conflict of interest that Respondents intentionally failed to disclose the Services Agreement to their clients.

A. The Services Agreement and Payments Present a Conflict of Interest

The Services Agreement and the corresponding payments represented a substantial conflict of interest between MCM and its clients because Worth's ability to pay MCM depended on Worth's revenues and trading in MCM client accounts generated at least a portion of that revenue. Mowery concedes that the Services Agreement represented a potential conflict that needed to be disclosed to clients.[130]

Mr. Clark testified that he would "budget" a percent of Worth's total revenue in determining the level of services Worth would purportedly obtain from MCM.[131] This suggests that the size of payments to MCM were likely to be affected by the amount of trading in MCM accounts because that trading was an important part of Worth's total revenue.

B. Respondents have a Duty to Disclose Conflicts of Interest

The *Capital Gains* Court stated that the Advisers Act indicates an "intent to eliminate, or at least to expose, all conflicts of interest which might incline an investment adviser – consciously or unconsciously – to render advice which was not disinterested."[132] Moreover, as fiduciaries, Respondents owed clients a duty to make "full and fair disclosure" of material facts.[133]

C. Respondents did not Disclose Conflicts of Interest to Clients

None of the current and former MCM clients who testified at the hearing stated an awareness of the Services Agreement. In fact, every client witness asked about knowledge of the Services Agreement denied having knowledge of it.[134] The clients' lack of knowledge of the Services Agreement and the conflict it presented was so apparent that Respondents' counsel stopped asking client witnesses if they were aware of the Services Agreement after three of Respondents' witnesses denied such knowledge.

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[130] Tr. 209, lines 23-25; 210, lines 1-5

[131] Tr. 473, lines 20-25; 500, lines 5-12

[132] SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 283, 84 S.Ct. 275, 11 L.Ed.2d 237 (1963).

[133] Id. at 284; Restatement (Third) of Agency §8.11 (2006).

[134] Tr. 360-361, 701-701, 764, 846, 887.

Respondents could only point to language in the Part 2 of the Form ADV.[135] It is important to note that the Part 2 was only used after March 31, 2011. Thus, Respondents have essentially conceded that they did not disclose the Services Agreement to clients between July 2007 and March 31, 2011.

The language in Part 2 referenced by Respondents describes elements of the Services Agreement, but omits the key piece of information – that the "corporate client" is actually Worth. In doing so, Respondents hid the conflict of interest raised by the Services Agreement behind an otherwise meaningless description of the services.

D. Respondents Intentionally Failed to Disclose the Services Agreement

Respondents' intention in not disclosing the Services Agreement is exemplified by Mowery's interaction with Walter Bradley in 2009. Mr. Bradley signed his agreement with MCM on April 27, 2009.[136] At that time, he was over 65 years old.[137] Mr. Bradley underlined language in the agreement that discussed payments from Worth to MCM.[138]

When Terria Heng first questioned Mowery about this language in May 2014, Mowery claimed that the language was not related to the Services Agreement and was only included in the event that MCM hired a registered representative.[139] Mowery further told Ms. Heng that he had provided the same explanation to Mr. Bradley prior to his signing the contract.[140]

Respondents' intention to not disclose the conflict of interest on the Part 2A language is also evident. In March 2011, and at all times since, Worth was the only entity with which MCM maintained a Services Agreement.[141] Yet, MCM never mentions Worth. Mowery was forced to admit that Respondents were the only ones that would know that "corporate client" was referencing Worth.[142] If MCM identified Worth as a "corporate client", the conflict of interest would have been apparent. Mowery acknowledged that the potential conflict would be different if the "corporate client" was an entity other than the client's broker-dealer Worth.[143]

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[135] Example Ex. SSB 2, page SSB-SOAH-000022 under "Advisory Services Agreement".

[136] Ex. SSB 113

[137] Ex, SSB 84, page SSB-SOAH-003896.

[138] Ex. SSB 113

[139] Tr. 56-57

[140] Tr. 58

[141] Tr. 425, lines 12-15

[142] Tr. 212, lines 15-18

[143] Tr. 212, lines 8-14

Instead, Mowery and Charles Waring testified that they chose to not list Worth specifically.[144] Mowery claims to have made this choice in the event that Worth changed its corporate name or other "corporate clients" entered into service agreements with MCM.[145] Mowery's explanation does not justify omitting a reference to Worth, especially because it was the only entity with which MCM actually had such an agreement and is the entity that would raise a conflict between MCM and its clients.

Moreover, Respondents' did not even generally describe the services agreements as presenting a potential conflict of interest. The term is completely absent. The only logical conclusion is that MCM and Mowery did not want the clients to know that the services agreement was with Worth and that it presented a conflict of interest.

E. The Conflict of Interest was a Material Fact

Whether or not an undisclosed fact is a "material fact" for purposes of Section 4.F of the Texas Securities Act depends on whether "there is a substantial likelihood that it would have assumed actual significance in the deliberations of a reasonable investor, in that it would have been viewed by the reasonable investor as significantly altering the total mix of available information."[146] This test aligns with the test for materiality under the federal securities laws.[147]

The conflict of interest raised by the Services Agreement was significant. MCM's ability to obtain payments under the Services Agreement depended on Worth's revenue. Worth's revenue included all trading costs earned by Worth, including those paid by Respondents' clients. Thus, there is a direct conflict between MCM and the clients. A reasonable investor would consider the existence of such a conflict significant to the investor's decision in selecting or remaining with an investment adviser.

In reviewing the "total mix" of information available to MCM clients, there was absolutely none informing them of the fact that Worth was paying money to MCM. Instead, clients were told, "Conflicts of Interest will be disclosed to the client in the unlikely event they should occur."[148] Clients trusted Respondents with the broker-dealer selection and expected that Respondents were placing the clients' interests ahead of their own. Clients would have known that Worth was the broker-dealer and reasonable investors would have known that the trading costs they pay go to Worth. Notably, MCM's Form ADV Part 2A is completely devoid of any reference to Worth by name even though Worth was: (1) the <u>only</u> broker-dealer selected for clients by Respondents; (2) the <u>only</u>

[144] Tr. 211, lines 19-22; 425, lines 18-22

[145] Tr. 212, lines 1-5

[146] Bridwell v. State, 804 S.W.2d 900, (Tex. Crim. App. 1991).

[147] Id. at 903-904.

[148] See "Firm Description" section on Form ADV Part 2A; For example, SSB 2, SSB-SOAH-000021.

"corporate client" with which MCM had a services agreement; and (3) a firm with which Mowery was registered in some capacity.[149]

The test for materiality does not require proof that a reasonable investor would have in fact acted differently with knowledge of the fact.[150] Nonetheless, evidence presented at the hearing confirmed that at least two clients would not have become MCM clients if made aware of the Services Agreement and the conflict it presented.[151]

There is little doubt a reasonable investor would have considered the existence of the conflict of interest as significantly altering the "total mix" of available information.

F. Conclusion

The definition of "fraud" under Section 4.F of the Texas Securities Act includes "an intentional failure to disclose a material fact." Respondents' failures to disclose the significant conflicts of interest presented by the Services Agreement and the sizeable payments to MCM from Worth constitute fraudulent business practices, fraud in connection with rendering investment advice

VI. Omissions & Misrepresentations on Form ADV Part 2

A. Background

The Form ADV is a uniform form used in connection with investment advisers registering with securities regulators. There are two parts to the Form ADV. Part 2 of the Form ADV is a disclosure document that investment advisers provide to their clients. Consistent with this purpose, since 2011, the Part 2 has required disclosures to be made in narrative form and be in "plain English." The Part 2 must also be filed with the appropriate securities regulator(s). Starting in 2011, Respondent MCM filed the Part 2 with securities regulators and provided the Part 2 to Respondents' investment advisory clients.[152]

As discussed below, the evidence presented at the hearing established that MCM's Part 2 failed to disclose material conflicts of interest and included misrepresentations of relevant facts.

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[149] Ex. SSB 112, Stipulated Fact 6 – Mowery was registered with Worth as an investment adviser representative between 2006 and November 2014, but MCM's Form ADV Part 2B never lists Worth under Mowery's "Business Experience." *For example, SSB 2, page SSB-SOAH-000032.*

[150] TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976).

[151] Tr. 360-361; 701, lines 15-21

[152] Ex. SSB 112, Stipulated Facts 21-26

B. Failure to Disclose Conflict of Interest

Item 12 of the Form ADV Part 2A requires investment advisers to disclose practices in connection with the recommendation of brokerages for client transactions. In general, investment advisers are required to disclose factors considered in connection with such recommendations and to disclose certain potential conflicts of interests between clients and the investment adviser.[153]

The Services Agreement and the corresponding payments from Worth represent a conflict of interest between MCM and its clients. This conflict is most pertinent in assessing MCM's recommendation of Worth as the broker-dealer for its clients. Yet, there is no mention of the conflict posed by the Services Agreement in Item 12 of the Form ADV Part 2A, nor in any other portion of the Part 2A.

Respondents' point to language in Item 2 of the Form ADV Part 2A as describing the Services Agreement. [154] The words in Item 2 of the Form ADV Part 2A describe the services associated with the Services Agreement. However, they intentionally do not disclose the material conflict of interest posed by the Services Agreement.[155]

C. Misrepresentation regarding Receipt of Trading Fees

Since 2011, Respondent MCM's Form ADV Part 2A has included the following representation under the "Brokerage Practices" section: "[Respondent MCM] does not receive any portion of the trading fees."[156] Contrary to this statement, evidence presented at the hearing showed the following:

1) Worth only paid MCM after it received a payment that included the MCM based trading fees[157]; and

2) In many months, Worth could not have paid the amount invoiced by MCM without MCM clients trading at Worth[158].

First, Worth could not directly pay MCM or Mowery any portion of the trading fees/commissions because of legal restrictions.[159] Exhibit SSB 152 illustrates the connection between the trading fees paid by MCM clients and the payments from Worth

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[153] Ex. SSB 112 Stipulated Fact 27

[154] Tr. 210, lines 13-19

[155] For detailed discussion, see Section V, *supra*.

[156] Ex. 112, Stipulated Fact 28

[157] Tr. 656, lines 1-15

[158] Ex. SSB 152, 153; Tr.65-668

[159] Tr. 57, lines 15-19; 84, lines 21-24

to MCM. As Andrew Dick testified, the only variable in the analysis presented in Exhibits SSB 152 and 153 is the removal of MCM trading related income to Worth.[160] Without the trading fees paid by MCM clients to Worth, Worth could not have made the services payment it made to MCM in many months.[161] In fact, the payments to MCM were sometimes so sizeable that Worth would have had to cut other expenses in addition to not paying MCM if MCM clients were not trading through Worth.[162] The evidence is clear – MCM was receiving a portion of the trading fees when it accepted the sizeable payments under the Services Agreement.

The Staff has met its burden to establish by a preponderance of the evidence that Respondents misrepresented a relevant fact by stating the MCM "does not share in the trading fees." Respondents knew MCM was receiving payments, often for tens of thousands of dollars, from Worth on a monthly basis. Respondents knew that part of Worth's revenue used to pay MCM included the trading fees paid by MCM clients. MCM was only billing for the services payment after Worth received the payment from Maplewood.

D. "Discount Broker"

Respondent MCM's Form ADV Part 2A includes a section titled "Asset Management". This section has included the following representation: "Assets are invested primarily in exchange listed securities and exchange-traded funds, usually through discount brokers or fund companies." (emphasis added) At all relevant times, MCM used Worth as the broker through which client assets were invested. Worth is not a discount broker.

Although there is not a formal definition of the term "discount broker", it is generally understood to involve a certain type of cost structure. One that is much different than what Worth charges MCM clients. This common understanding of the term would have been known to MCM and Mowery. Notably, Respondents' counsel and client witnesses regularly associated the term discount broker with a certain type of firm distinguishable from the MCM/Worth arrangement.[163]

Even Mr. Clark, the majority owner and President of Worth, could not recall if he had ever referred to Worth as a discount broker and would not refer to Worth as a discount broker in his testimony.[164]

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[160] Tr. 665

[161] Ex. SSB 152; Tr. 665

[162] Ex. SSB 152; Tr. 666

[163] Tr. 17; 76; 829; 1040-1041; 1062

[164] Tr. 466-467

Respondents' attempt to claim that they view Worth as a discount broker is undermined further by their own words. In 2004, Worth (f/k/a Promark) was the broker-dealer for MCM clients. As Mowery acknowledged, the business model was the same between Promark and Worth.[165] Yet, MCM's Form ADV Part II from 2004 stated that "clients may pay more than discount brokers but less than full retail."[166]

Mowery's explanation of this language from the 2004 Part II confirms his understanding that clients would generally associate the term "discount broker" with a certain type of broker-dealer and cost structure.[167] This is relevant because Black's Law Dictionary defines "material misrepresentation", in part, as a "false statement to which a reasonable person would attach importance in deciding how to act in the transaction in question or to which the maker knows or has reason to know that the recipient attaches some importance."[168]

E. Bankruptcy

Mowery filed a bankruptcy petition in September 2005.[169] From March 31, 2011 to May 15, 2014, MCM's Form ADV Part 2B included a representation that Mowery had not filed a bankruptcy petition.[170] Multiple clients spoke to the relevancy of this information.[171] Of all the clients, Keith Nickles stated it best when he displayed an understanding that "rough times" happen, but knowledge of the bankruptcy would have caused him to obtain sufficient details about the bankruptcy to make an informed decision.[172]

Both Mowery and Waring were involved in preparing and reviewing MCM's Form ADV Part 2. Although Respondents' claim that the misrepresentation related to the bankruptcy was just an "error", the evidence indicates otherwise. Between 2011 and May 2014, MCM amended the Form ADV Part 2 multiple times.[173] Each of these times, Mowry and Waring reviewed the Part 2.[174] Despite multiple amendments and reviews,

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[165] Tr, 215

[166] Ex. SSB 115, pg. SSB-SOAH-5010

[167] Tr. 218

[168] Black's Law Dictionary.

[169] Ex. SSB 112, Stipulated Fact 31

[170] Tr. 232

[171] Tr. 358; 703

[172] Tr. 703

[173] Tr. 232

[174] Tr. 233; 426, lines 1-12

Respondents claim they did not notice this misrepresentation until after the staff of the State Securities Board initiated its investigation of MCM. This is hardly a coincidence.

Motive, past conduct, and related wrongful acts are factors to be considered when discerning whether certain conduct is fraudulent in nature.[175] MCM had a motive to misrepresent Mowery's bankruptcy history. Potential and existing clients would logically be more likely concerned with Respondents' money management capabilities. While not all persons would have altered their decisions based on the disclosure, some clearly would have.[176] Ultimately, disclosure of the bankruptcy would have increased the chances that certain persons would not have become clients of MCM.

Respondents' failure to disclose the bankruptcy was not limited to the Form ADV Part 2. Mowery's bankruptcy was not disclosed on his "Form U4" either.[177] Exhibit SSB 10 presents the filing history associated with Mowery's Form U4. Between 2005 and May 2014, Mowery files seven (7) amendments to his Form U4 without disclosing the 2005 bankruptcy.[178]

F. ADV Part 2 Filed with Securities Commissioner

In order to obtain registration as an investment adviser, a firm must submit various documents necessary to determine the business repute and qualifications of the investment adviser and its representatives. Oscar Gonzalez, the Assistant Director of the Registration Division for the SSB, described the types of documents reviewed during this process, including: Form ADV Parts 1 and 2; Secretary of State filings; a certified or audited balance sheet; the Form U4 for representatives; and the investment advisory agreements.[179]

To that end, in June 2012 MCM submitted, via email, a Form ADV Part 2 (a/k/a "firm brochure") in connection with its application for registration as an investment adviser.[180] In this email, MCM inaccurately identified the Part 2 attached to the email as the one that was filed on the IARD system.[181]Despite Waring's inaccurate statement to Mr. Gonzalez, both the version emailed by MCM and the version of the Form ADV Part 2 that was actually on file with the Securities Commissioner contained the

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[175] Cotton v. Weatherford Bancshares, Inc. 187 S.W. 3rd 687, 707 (Tex. App. – Fort Worth 2006, pet. denied.)

[176] Tr. 358-359; 702-703

[177] Ex. SSB 11

[178] Ex. SSB 10

[179] Tr. 718

[180] Ex. MCM 31

[181] Ex. MCM 31; Tr. 742-743

misrepresentations described above related to "discount brokers"; MCM's receipt of a portion of the trading fees; and Mowery's bankruptcy.[182]

VII. Misrepresenting Writings as Own

Evidence presented at the hearing confirmed that Mowery represented writings as his own despite the fact the materials were originally written by someone else. The Staff uncovered multiple examples of Mowery engaging in this conduct. As described below, Mowery does not recognize the conduct as wrongful and instead repeatedly attempted to justify his actions.

A. "Letter to Our Clients" from MCM website

After Respondents formed MCM in 2004, Mowery placed a "Letter to Our Clients" on the MCM public website.[183] The vast majority of the "Letter" was actually copied verbatim from an article written by Larry Kudlow in 1999.[184] Mowery did not attribute the writing to Mr. Kudlow. Instead, at the end of the "Letter", after adding, "As always, thank you for your business", Mowery wrote "Sincerely, F.E. Mowery, Fritz Mowery, President." In doing so, it is apparent that Mowery was representing to anyone reading the "Letter", including prospective and existing clients, that he had authored the contents. Of course, this was a misrepresentation.

To ensure this misrepresentation was not obviously noted, Mowery was careful to amend specific portions of the article. Specifically, the original article, included a sentence starting with, "I can put it no better than my friend and mentor, Arthur Laffer…"[185] Mowery amended the start of this sentence to state, "I can put it not better than one of the greatest economists of our time, Arthur Laffer…" [186]

Mr. Kudlow has been a Chief Economist at various financial institutions and is a well-known commentator on the economy.[187] Mowery has not been either. The article Mr. Kudlow wrote is very well-written in style and substance and conveys his deep understanding of economic history and trends. Mowery's motive in copying Mr. Kudlow's article without attribution is simple to understand – anyone reading the article would be led to believe that Mowery possesses an equally high level of understanding and ability to comment on the economy. An investment adviser's understanding of the economy would be a relevant fact in an investor's selection of an investment adviser.

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[182] Ex. SSB 2; Ex. MCM 31

[183] Ex. SSB 100

[184] Ex. SSB 101

[185] Ex. SSB 101

[186] Ex. SSB 100

[187] Tr. 346-347

These realities explain why Respondents maintained the "Letter" on MCM's website from at least 2006 to October 2014.[188]

B. "Research" for Worth

On April 9, 2014, the Staff conducted an inspection of MCM's offices.[189] One of the issues noted during the inspection was the Services Agreement and the size of the payments from Worth.[190] As the Staff began to scrutinize the research and other services purportedly provided by MCM, Mowery again created documents representing him as the original author even though the content was originally written by others.

On April 30, 2014, Mowery sent a document titled "The Interest Rate Trap" via email to Mr. Clark.[191] This document included a discussion about the interest rate environment and presents opinions as to its future impact on the stock market.

In the body of the email, Mowery wrote, "My research on intersts rates and where to invest." (sic in original) Furthermore, at the end of the document Mowery included, "Sincerely, Fritz Mowery."[192] Unfortunately, Mowery was once again being insincere because he had copied the majority of an article originally written by Zacks Investment Management.[193]

The Zacks article was written by Mitch Zacks, who is highly educated, writes extensively, and has published two books on investment strategies.[194] In addition to presenting his research based opinion in the article, Mr. Zacks prepared a table of data on the ten-year Treasury yield. Mowery copied all of this and included it in the document that supposedly presented his "research on interest rates." The truth is his document was basically a cut-and-paste from the Zacks article.

Less than two weeks later, on May 12, 2014, Mowery sent Mr. Clark another document over email, this one titled "A Better Safe Haven than Gold."[195] This document was copied almost entirely from an article, bearing the same title, published on the Vanguard

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[188] Ex. SSB 112, Stipulated Fact 35

[189] Tr. 647

[190] Tr. 648-650

[191] Ex. SSB 112, Stipulated Fact 33

[192] Ex. SSB 96

[193] Ex. SSB 97; Tr. 157

[194] Ex. SSB 97

[195] Ex. SSB 112, Stipulated Fact 34; Ex. SSB 98

website.[196] Notably, the material on Vanguard's website appears subject to copyright protection. (SSB 99 – pg with copyright symbol)[197]

Mowery attempts to claim that he did attribute the writing to Vanguard based on the fact that he also copied the footnotes from the original Vanguard article. (1.165) But, this is nothing more than reflection of the fact that Mowery copied the entire Vanguard article. Mowery intended for the regulators and others who read the May 12, 2014 email and document to believe that he had authored the material. At the end of the document, but above the footnotes, he lists "Fritz Mowery, President Mowery Capital Management."

Although Mowery copied most of the article word-for-word, his amendment to one sentence from the Vanguard article highlights Mowery diligence towards misrepresenting the authorship of the documents he emailed to Worth. Here is a comparison of the change he made:

Vanguard article	*Mowery's May 12, 2014 document*
"Even as interest rates rise, what ultimately matters most for risk-averse clients is the return of their *total* portfolio. Over the long term, **Vanguard** expects bonds to continue to reduce the risk of loss for balanced investors." (SSB 99)	"Even as interest rates rise, what ultimately matters most for risk-averse clients is the return of their *total* portfolio. Over the long term, **Mowery Capital Management** expects bonds to continue to reduce the risk of loss for balanced investors." (SSB 98)

Mowery testified that Mr. Clark did not care whether or not Mowery had authored the material.[198] That may or may not be true, but is irrelevant to the allegation in this case. Yet, Mr. Clark never testified that the authorship of these articles was irrelevant to him. Furthermore, it was not just the SSB that was asking questions about the Services Agreement. As Mr. Clark acknowledged, the Financial Regulatory Authority (FINRA), which regulates broker-dealers like Worth, was also looking into the payments from Worth to MCM.[199]

Mowery needed to convince regulators that MCM was actually providing research to Worth. Mowery acknowledged that MCM was unable to produce any written research when it was sought by the Staff.[200] Mowery claims that at least part of the reason he wasn't able to provide written evidence of the research to the Staff was because he

[196] Ex. SSB 99; Tr. 162

[197] Ex. SSB 99, pg. SSB-SOAH-004039

[198] Tr. 165

[199] Tr. 544

[200] Tr. 171

overwrites the files associated with written research.[201] It is unclear why Mowery would need to overwrite files -- if he had actually generated written research.

On the contrary, it is clear that Respondents did not present any evidence at the hearing of written research generated by Mowery before the Staff's investigation started in April 2014. The existence of research generated by Mowery for Worth was extremely relevant in connection with Worth's payments to MCM. These facts highlight why Mowery created the subject documents in a manner that misrepresented his role in authoring them.

C. Mowery's Testimony

Mowery's statements about the purposes for these writings and his vapid attempts to rationalize his conduct highlight both his intent to deceive and the likelihood that he would continue to engage in misrepresentations.

Mowery claimed to have drafted the "Letter" based on notes he took at a conference where Mr. Kudlow spoke and then posted the "Letter" to his website because he wanted his clients to have this information.[202] If that was Mowery's goal, he could have achieved it by sharing a copy of the article or conveyed the same information and attribute the work to Mr. Kudlow. That is not what he wanted to do – he intended to create the impression that he authored the contents of the "Letter".

With respect to the "research" documents, Mowery admitted at the hearing that Mr. Clark had not requested research on either subject at the time Mowery sent the documents.[203] The fact that he sent two such documents on an unsolicited basis and shortly after the SSB investigation was initiated, must be contrasted with the fact that Respondents could not offer any similar material for times prior to the SSB investigation. Mowery claims his goal in taking the original material and placing it on a document with his name was to convey that he supported the stated position.[204] This explanation is illogical.

With respect to the Vanguard article, Mowery implies that it was necessary for him to put the contents of the original article under his name because they would not have "carried as much weight" without him doing so.[205] Vanguard, of course, is one of the largest money managers in the world, with trillions of dollars under its management. The only thing that makes sense is that Mowery wanted to convince someone that he was

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[201] Id.

[202] Ex. SSB 111, pg. SSB-SOAH-004456

[203] Tr. 156-157; 163

[204] Tr. 166; 167, lines 5-7

[205] Tr. 167

putting in the effort to write original research articles when all he was actually doing was passing along one written by another person.

Mowery's apparent apathy towards the inappropriateness of his conduct is even more concerning than his attempts to indicate an innocent motive. Instead of accepting responsibility for copying the work of others verbatim and without attribution, Mowery says, "I see no harm and I don't think it is inappropriate."[206] Even with the prospect that he had taken copyrighted material and put his name on it, Mowery responds, "I felt it was fair use to use this to send to Mr. Clark, because I had this opinion." Contrast this statement with Mowery's support for the payments under the services agreement, "…I would be selling my research which is my intellectual property…"[207] Mowery's attitude suggests that he would continue to misrepresent the work of others as his own.

D. Misrepresentations are Fraudulent

In connection with each of the three writings referenced above, Respondent Mowery misrepresented the work of others as his own. The definition of "misrepresentation" in Black's Law Dictionary includes, "The act or an instance of making a false or misleading assertion about something, usu. with the intent to deceive. The word denotes not just written or spoken words but also any other conduct that amounts to a false assertion."

Mowery made sure to include a signature line with his name in connection with each of the writings, yet he never mentions the original authors' names. Furthermore, he modified specific portions of each article to further the assertion that he originally authored the material. The misrepresentations associated with these writings were all connected directly to Respondents' investment advisory business.

The definition of "fraud" under the Texas Securities Act includes "misrepresentations, in any manner, of a relevant fact."[208] The evidence supports finding that Respondent Mowery engaged in fraudulent business practices. Pursuant to Section 14.A(3) of the Texas Securities Act, finding that an investment adviser representative engaged in a fraudulent business practice constitutes a basis for revocation of the investment adviser representative's registration with the Securities Commissioner.

VIII. Misrepresentations during Investigation

Respondent Mowery's misleading conduct was not limited to his clients. As described below, Mowery began taking steps to mislead the Staff from the early stages of its investigation.

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[206] Ex. SSB 111, pg. SSB-SOAH-004439

[207] Tr. 178, lines 8-10

[208] Section 4.F of the Texas Securities Act

A. Back-dated Documents Submitted to the Staff

i. Background

At times between 2004 and 2012, MCM compensated an individual (the "Solicitor") in connection with clients that the solicitor referred to MCM. MCM had agreed to pay the Solicitor 30% of the fees collected by MCM from the above-referenced clients.

On April 18, 2014, the Staff was contacted by counsel for the Respondents and for the Solicitor.[209] The Staff's main concern was whether or not the solicitor relationship had been disclosed to the clients at the time they entered into an advisory relationship with MCM.[210] At a meeting on April 22, 2014, the Staff requested any written records disclosing the relationship to clients.[211]

On April 25, 2014, among other records, Respondents submitted documents representing disclosure notices (the "Notices") provided to clients referred to Respondent MCM by the Solicitor.[212] Respondents submitted four of these Notices to the Staff.[213] Two of the notices were dated and the other two were not dated. All of the Notices were signed in April 2014. But, the two Notices that listed dates bore the dates December 12, 2005 and June 14, 2012.[214] These dates are significant because they are the same dates that the respective clients signed their investment advisory agreements with Respondent MCM.[215]

In submitting the Notices, Mowery did not inform the Staff that all four of the Notices were created and signed in 2014.[216] In a follow-up request, during which the Staff sought information about the undated Notices, the Staff made it clear to Respondents that it appeared the two dated notices were signed on the listed dates.[217] Respondent Mowery submitted a signed statement informing the Staff that the undated Notices were signed in April 2014, but did not state that the dated Notices were also signed in April 2014.[218]

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[209] Tr. 561, lines 17-19

[210] Tr. 562, lines 13-18

[211] Tr. 563

[212] Ex. 112, Stipulated Fact 38

[213] Ex. SSB 70; 74; 76;78

[214] Ex. SSB 70; 76

[215] Ex. SSB 69; 75

[216] Tr. 283; 287

[217] Tr. 564, lines 8-19; Ex. SSB 79

[218] Ex. SSB 79; Tr. 566-567

In order to mask the back-dating, Mowery used correction-paper to cover-up the two addresses listed on the bottom of MCM's current letterhead.[219] The addresses included one in Dallas and one in McKinney.[220] The McKinney address did not exist in 2005.[221] Furthermore, Respondents did not maintain offices at the listed McKinney address in 2012.[222] Accordingly, if Mowery did not hide the addresses on the signed Notices, it would have been obvious that the dated Notices were not signed in 2005 or 2012.

ii. Staff Discovered Back-Dating

The Staff eventually uncovered the back-dating and informed Respondents' counsel. At that point, Respondents requested the opportunity to meet with the Staff. (3.569) At the meeting, Mowery provided an explanation for why he used correction paper to remove the addresses from the Notices. Mowery said that he removed the Dallas address because it was his old address, which is why he felt the need to remove it from the document.[223] Of course, this could not explain why he covered up the McKinney address. For that, Mowery claimed that he removed his current address because he didn't want the document to appear "off balance". [224] Yet another illogical explanation, which is why the Staff did not believe Mowery was genuine in his remorse or acceptance of responsibility for his actions.[225]

iii. Respondents had Motive to Mislead Staff

The only logical explanation for Mowery's actions is that he intended for the Staff to believe Respondents disclosed the solicitor relationship in writing to those two clients in 2005 and 2012 -- at the time they entered into their investment agreements. The truth is Respondents had not timely disclosed the referral payments to most of the clients. The Solicitor referred six clients to MCM. Five of these six clients testified at the hearing. None recalled receiving a written disclosure at the time they entered into the relationship with MCM.

The dated Notices were signed by Steven Ross and Richard & Drew Allen. Mowery has now admitted that the Notice was signed by Mr. Ross in 2014, after the SSB investigation.[226] Mowery also now admits he wrote December 12, 2005 on the Ross

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[219] Tr. 569-570

[220] SSB 80

[221] Tr. 568

[222] Tr. 569

[223] Tr. 570, lines 9-13

[224] Tr. 570, lines 14-24

[225] Tr. 23

[226] Tr. 282

Notice. Mr. Ross did not testify at the hearing so there is no evidence that he was notified before 2014 of the payments to the Solicitor.

Mr. Allen testified that he signed the Notice in 2014 and that he chose to date the document to June 14, 2012 because he recalled the arrangement and Mowery told him that the letter was missing from his file.[227] Mr. Allen testified earlier that he could not recall exactly how he became aware of the relationship – so it doesn't appear that Mr. Allen recalls receiving a version of the Notice in 2012.[228] Mowery told Allen that MCM was updating the files and that a document purportedly similar to the Notice was missing.[229] (4.881) But, Mowery admitted at the hearing that it was not his practice to provide this written disclosure to his clients.[230]

So, then why would Mowery tell Mr. Allen that the notice was missing from the file? It is because Mowery was anticipating having to submit these documents to the Staff. Of course, Mowery did not tell Mr. Allen this fact. Mr. Allen was not aware that Mowery was producing the Notice to the Staff[231] or that anyone would be led to think that the Notice was actually signed in 2012.[232]

As stated previously, a "misrepresentation" includes, "not just written or spoken words but also any other conduct that amounts to a false assertion."[233] By submitting the back-dated Notices to the Staff, Respondents misrepresented when Mr. Ross and the Allens signed the Notices disclosing the payments to the Solicitor. Black's Law Dictionary further defines "material misrepresentation".[234] Respondents' misrepresentations related to the Notice were clearly likely to induce the Staff to believe that the Notices were provided to Mr. Ross and the Allens in a timely manner. As Clint Edgar testified, the Staff's "main concern" was determining whether or not the solicitor relationship was disclosed to clients at the time they entered into the advisory relationship with MCM.[235]

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[227] Tr. 880-881

[228] Tr. 878

[229] Tr. 881

[230] Tr. 284, 14-18

[231] Tr. 881, lines 4-8

[232] Tr. 882, lines 10-13

[233] Black's Law Dictionary

[234] **1.** *Contracts.* A false statement that is likely to induce a reasonable person to assent or that the maker knows is likely to induce the recipient to assent. **2.** *Torts.* A false statement to which a reasonable person would attach importance in deciding how to act in the transaction in question or to which the maker knows or has reason to know that the recipient attaches some importance.

[235] Tr, 562

Therefore, the Staff requested that Respondents' submit any documents disclosing this relationship. [236]

iv. Conclusion

The evidence supports finding Respondents engaged in a material misrepresentation in connection with information deemed necessary to determine the business repute and qualifications of an investment adviser representative. Pursuant to 14.(A)(7) of the Texas Securities Act, Respondents registrations with the Securities Commissioner may be revoked.

B. *Testimony Provided to the SSB*

On November 13, 2014, Mowery provided sworn testimony to the Staff.[237] During the testimony, the Staff collected information necessary to determine Mowery and MCM's business repute and qualifications.[238]

The Staff asked Mowery to describe the origin of the "Letter to Clients" that was on MCM's website. Mowery swore, repeatedly, that he prepared the "Letter" based on notes he took at a seminar presented by Larry Kudlow. Specifically, Mowery stated:

- "He's a really good speaker and I was taking notes as fast as I could. And I left the seminar and went right to my office and typed this up."[239] (SSB 111 – 296)
- "I created it from his speech." (SSB 111 – 296)
- "And he had a PowerPoint too." (SSB 111 -298)
- That he copied the PowerPoints as closely as he could. (SSB 111 – 298)

He further represented under oath that he did not copy anything written by Mr. Kudlow in preparing the "Letter." Mowery said:

- "No. No, I haven't" in response to the Staff's inquiry as to whether Mowery had ever read anything written by Kudlow.
- "I copied it as closely as word for word as I could take. Okay? From notes that I had."[240]

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[236] Tr. 563

[237] Ex. SSB 111

[238] Id.

[239] Id. at SSB-SOAH-004456

[240] Id. at SSB-SOAH-004457

- "I don't remember having anything in writing from Mr. Kudlow. I wrote it from my notes as closely as I could."[241]

None of these statements was the truth. As described previously, the "Letter" on MCM's website is almost an exact copy of an article written by Larry Kudlow in December 1999. Based on this fact, common sense suggests that Mowery's sworn testimony that he created the "Letter" based on a speech is false.

In his testimony at the hearing, Mowery attempts to back-track and claim that he testified less definitively about the source of the contents of the "Letter."[242] This also is not true. Notably, at the hearing Mowery again testified that he attended the seminar at a hotel in the Dallas area.[243]

The testimony provided by Susan Varga at the hearing further undermines Mowery's story. Ms. Varga is Mr. Kudlow's Chief Operating Officer and has worked for him since 1997.[244] She stated that Mr. Kudlow has given one speech in Dallas – in 1999 at the Federal Reserve Bank of Dallas.[245] Given the security required at such banks, it is hard to imagine Mowery would have confused it with a hotel. Nonetheless, even if Mowery did attend the Kudlow speech in 1999, Mr. Kudlow did not read from the article that Mowery copied.[246]

The defense is likely to argue that Mowery's statements at his November 2014 testimony were not false in a material way because Mowery testified that the source was Mr. Kudlow. Such an argument is unconvincing.

As the statements listed above show, Mowery testified very definitively about the source of the contents of the "Letter" – his notes from a speech by Mr. Kudlow. The Staff's questions made clear that the Staff wanted to know if Mowery copied a writing or obtained elsewhere the information used to create the "Letter". Finally, copying a previously written article is materially different than creating a piece of writing based on a speech. The former requires little effort and takes entirely from another person's thoughts and skill. Creating a new writing based on a speech suggests, if not requires, that the writer apply their own filter on relevant issues and apply their own communication skills. The former is recognized a clear ethical breach, the latter is not.

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[241] Id. at SSB-SOAH-004460

[242] Tr. 294

[243] Tr. 293

[244] Tr. 346

[245] Tr. 350

[246] Id.

The Staff took Mowery's sworn testimony during the course of its investigation and informed Mowery of his rights and reminded him that his testimony was subject to the state's perjury laws.[247] Mowery told a very definitive and unwavering story filled with untruths. Mowery had reason to know that the Staff attached importance to the difference between notes from a speech and copying a previous writing. If nothing else, the specificity of the Staff's questions on this point made clear the Staff's focus. Therefore, the evidence supports finding Mowery engaged in a material misrepresentation in connection with information deemed necessary to determine the business repute and qualifications of an investment adviser representative.

Pursuant to Section 14.A(7) of the Securities Act, Respondents' material misrepresentations in submitting the back-dated Notices and providing false testimony constitute bases for the revocation of Respondents' registrations with the Securities Commissioner.

IX. Witness Credibility

Witness credibility is a matter within the exclusive purview of the Administrative Law Judges. Because the record in this matter is replete with examples of misleading and untrue statements by witnesses affiliated with Respondents, the Staff highlights the following for the ALJs consideration as they weigh the evidence and statements offered.

A. Fritz Mowery

Obviously, a number of allegations in this matter relate to Mowery's truthfulness. The evidence presented with respect to those allegations supports finding Mowery uncredible. Throughout this brief, the Staff has highlighted misstatements made by Mowery under oath. Additional indications of Mowery's disingenuous responses at the hearing, include, among others, the following:

1) Mowery testified that he contacted TD Ameritrade in 2014 to understand the trading costs at TD Ameritrade.[248] In connection with this communication, Mowery testified that he requested a commission schedule, which he received and was exhibited as MCM 9.[249] Evidence offered by the Staff contradicted Mowery's claim that TD Ameritrade sent him the document labeled MCM 9 in 2014 because that document had actually been superseded by TD Ameritrade in 2012.[250]

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[247] SSB 111

[248] Tr. 299-301

[249] Id.

[250] Tr. 584

2) Mowery testified that he had not received any financial or pecuniary gain for placing an investor in a real estate investment.[251] David Goettsche described, very credibly, about Mowery's actions in connection with Mr. Goettsche investing in a real estate investment where Mowery "was to receive 10% ownership off of [the Goettsches] investments."[252]

3) Streetscape is the NFS on-line trading system that Mowery used in trading through Worth.[253] At the March hearing, Mowery first stated that he last accessed Streetscape "maybe a couple weeks ago...recently".[254] Later, after the Staff points out that his access to Streetscape was terminated in November 2014[255], Mowery amends his description of accessing Streetscape. He now says he accesses Streetscape through Mr. Clark,[256] and denies using Mr. Clark's log-on information.[257] But, the next day, Mowery says he could use Mr. Clark's log-on to enter a trade if Mr. Clark was not available.[258] His answers shifted based on the focus of the Staff's questioning.

4) In July 2014, the 2007 Services Agreement was replaced with one that called for fixed payments from Worth of $4,000 monthly.[259] This change resulted in a significant reduction in the size of payments from Worth to MCM.[260] Just days after the modification to the Services Agreement, MCM's office rent is reduced by 50%[261] and Worth Asset Management begins to pay the other 50% directly to the landlord.[262] Mowery claims that Worth Asset Management was paying this portion

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[251] Tr. 140-141

[252] Tr. 636

[253] Tr. 110, lines 1-4.

[254] Tr. 110-111

[255] Tr. 236

[256] Id. at line 21

[257] Tr. 237

[258] Tr. 311-312.

[259] Ex. SSB 14

[260] Tr. 191, lines 16-19

[261] Tr. 191, lines 20-24

[262] Tr. 191-193

because it was sharing an office with MCM.[263] This assertion is undermined by Mr. Clark, who twice denies sharing an office with MCM in 2014.[264]

B. James Clark

1) Mr. Clark sponsored MCM 10 into the record. The data and calculations on MCM 10, Mr. Clark said, showed that there was not a correlation between the payments Worth made to MCM and the amount of commissions generated by MCM clients.[265] When the Staff pointed out the numerous inaccuracies with the data included on MCM 10, Mr. Clark attempted to distance himself from the document. [266]

2) Mr. Clark testifies inaccurately about the commission costs at TD Ameritrade.[267] The context in which he misstates the costs is relevant because it is during a line of questioning from Respondents' counsel about how the number of shares traded can increase the trading costs.[268] Mr. Clark testifies that clients would have to pay an extra cost above $16.99 for every share.[269] This was not a true statement because clients could buy up to 1000 shares for the $16.99.[270] Mr. Clark would have known this because his firms has clients trading at TD Ameritrade. Yet, the Staff was forced to clear up the record on re-direct.[271]

X. Sanctions

A. Revocation of Registrations

As detailed above, the Staff has established by a preponderance of the evidence that numerous bases exist for the revocation of Respondents' registrations. The Staff does not seek the revocation of Respondents' registrations lightly, but believes very strongly that such a sanction is consistent with existing precedent and is in the best interest of the investing public.

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[263] Tr. 192

[264] Tr. 471-472; Tr. 502

[265] Tr. 505-506

[266] Tr. 550-556

[267] Tr. 536-537

[268] Id.

[269] Id.

[270] MCM 9

[271] Tr. 538-539

i. Consistency

Respondents' actions are not technical violations of administrative regulations. Instead, Respondents engaged in a pattern of deceit and fraud. Respondents' violations are of the nature that have consistently resulted in the severest of sanctions against registered securities professionals.

In 2003, Robert Kurtis Mauss was the subject of an action revoking his registration because he sold certain securities without the proper registrations and because he failed to disclose his involvement in selling those securities in filings with the Securities Commissioner and to his employer.[272]

In 2007, the registrations of Leland Alan Dykes and One Financial Securities, Ltd. were revoked based on the fact that Dykes and One Financial failed to furnish information requested by the Staff and failed to report accurate information on filings with the Securities Commissioner.[273] Respondents conduct is similar in that both matters involve measures that impede a government investigation and involve false filings. But the present matter is much more significant because of the extent of the fraudulent actions and because it also involves fraud on clients.

In 2012, Dale Lewis Stringer was found to have engaged in fraudulent business practices because sold investments to some persons that did not meet the minimum qualifications for the investments.[274] Stringer instructed clients to designate themselves as "accredited", when he knew they were not. Furthermore, Stringer failed to disclose to these investors that they did not actually qualify for these investments. His registration as an investment adviser representative was revoked. It should be noted that the action against Stringer does not indicate that he failed to disclose facts to investment advisory clients. Respondents' fraudulent conduct, on the other hand, impacted advisory clients, to whom Respondents owed the highest of duties.

The SSB has consistently sought the strongest of sanctions against registered individuals that engage in fraudulent representations in filings with the Securities Commissioner or in connection with investigations by the Staff. Often these matters result in default actions after the individual and/or entity fail to appear in the contested case.[275] Nonetheless, those matters illustrate that fraudulent conduct during the course

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[272] In the Matter of the Agent Registration of Robert Kurtis Mauss, Order No. CDO/REV-1518

[273] In the Matter of the Dealer Registration of One Financial Securities, Ltd., Order No. IC07-REV-18

[274] In the Matter of the Investment Adviser Representative Registration of Dale Lewis Stringer, Order No. IC12-REV-12.

[275] For example, In the Matter of the Agent Registration of Christopher Anthony Corso Sr. (Order No. IC07-REV/FIN-05); In the Matter of the Investment Adviser Registration of Duncan Private Wealth Management and the Investment Adviser Representative Registration of Donovon Colin Duncan (Order NO. IC12-REV-18); In the Matter of the Investment Adviser Registration of Warren Financial Services, LLC and the Investment Adviser Representative Registration of Kenneth Wayne Graves (Order No. IC14-

of an investigation regularly results in the loss of a person losing their license with the Securities Commissioner.

ii. Likelihood that would engage in further violations

Mowery hopes to convince your Honors that he has accepted responsibility for his conduct and that he did not intend to engage in the fraudulent acts. The evidence in this matter suggests otherwise. Saying one has accepted responsibility is very different than actually accepting it.

In assessing whether or not Respondents' registration should be revoked, a key fact is that Respondents' fraudulent actions have been ongoing for many years. From the inception of MCM in 2004, Respondents breached their duties in selecting Worth for client transactions. Mowery first misrepresented his authorship of the "Letter" as early as 2006. Starting in 2007, Respondents failed to disclose to clients a major conflict of interest with clients. Since at least 2011, Respondents have provided clients with a disclosure document that omits material information and misrepresents other relevant facts. Then in 2014, Respondents made material misrepresentations to the Staff during the course of its investigation. The duration – and variety – of fraudulent actions by the Respondents indicates that Respondents are not likely to cease engaging in fraud.

Respondents seek to highlight their efforts to correct violations. But, even this regard, it is notable that Respondents have a pattern of limiting their corrective actions to the bare minimum. As a result, these corrective steps do not appear genuine. Take for example Respondents disclosure of the solicitor relationship to the Goettsches in 2006. In June 2006, the Goettsches and their lawyer meet with Mowery regarding a real estate investment. [276] Less than a month later, Mowery sends the Goettsches a letter disclosing, for the first time, the payments to the Solicitor.[277] Notably, there is no evidence that Respondents took steps to disclose the solicitor relationship in writing to Mr. Ross – who had been solicited in 2005. Nor do Respondents implement a practice of ensuring that written disclosure of the solicitor relationship is provided to clients in the future.

A starker example is found in Respondents' modification of the Services Agreement in July 2014. Respondents were aware of the Staff's concerns with the payments from Worth. MCM and Worth modified the agreement to reflect a fixed payment formula and a significant reduction in the amount of money Worth would pay MCM. On its face, this measure seems like an attempt to improve business practices. Yet, what the agreement doesn't reflect is the fact that immediately upon modification of the Services

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REV-05); and In the Matter of the Agent and Investment Adviser Representative Registrations of Lloyd James Chappell (Order No. IC14-REV-01).

[276] Tr. 622

[277] Tr. 625

Agreement, Worth starts to pay 50% of MCM's rent and directs the payments to MCM's landlord.[278]

Mowery's statements and actions throughout the Staff's investigation and at the hearing suggest that he will continue to engage in fraudulent conduct. He should not be able to do so while continuing to hold a license issued by the Securities Commissioner.

iii. Investing Public's Confidence

Securities regulation should both protect investors and promote capital formation. These two objectives are not mutually exclusive. When regulators are successful at identifying inappropriate conduct, preventing undisclosed conflicts of interest, and barring bad-actors, current investors are protected and the future investors are less worried about putting their hard-earned money into the marketplace.

Market confidence is not hurt only by persons who engage in Ponzi schemes or theft of funds. It is also hurt when financial professionals, especially those afforded the highest levels of trust – like Respondents, engage in deceptive conduct that abuses the confidence investors place in them. Mr. Nickles testimony stands out in this regard. Based on his experience with Respondents, Mr. Nickles has refused to retain another investment adviser.[279]

For all of the reasons stated above, the Staff respectfully prays that the Honorable ALJs recommend the Securities Commissioner revoke Respondents' registrations.

B. Administrative Penalty

i. Legal Authority

Section 23-1 of the Texas Securities Act[280] states in part:

A. After giving notice and opportunity for a hearing, the Commissioner may ... issue an order which assesses an administrative fine against any person ... found to have:

(1) engaged in fraud or a fraudulent practice in connection with:

(B) the rendering of services as an investment adviser or investment adviser representative;

Pursuant to Section 23-1.A(1)(B) of the Texas Securities Act, the aforementioned fraud in connection with the rendering of services as an investment adviser or investment

[278] See generally Tr. 188-193

[279] Tr. 704

[280] The Securities Act, Tex. Rev. Civ. Stat. Ann. arts. 581-1 to 581-43 (West 2010 & Supp. 2014)

adviser representative constitute bases for the assessment of an administrative fine against Respondents.

Pursuant to Section 23-1.B(1) of the Texas Securities Act, the Respondents may be assessed an administrative fine in an amount that is the greater of $20,000 per violation or the gross amount of any economic benefit gained as a result of the fraudulent acts or practices for which the fine is assessed.

In addition to the amount of an administrative fine authorized pursuant to Section 23-1.B(1), pursuant to Section 23-1.B(2) of the Texas Securities Act, Respondents may be assessed an additional $250,000 in administrative fines because of the fraudulent acts or practices committed against a person 65 years of age or older.

Section 106.1 of the Rules and Regulations of the State Securities Board[281] identifies the following criteria to be considered in assessing an administrative penalty:

(1) The seriousness, nature, circumstance, extent, and persistence of the conduct constituting the violation;

(2) The harm to other persons resulting either directly or indirectly from the violation;

(3) Cooperation by the person or company in any inquiry conducted by the State Securities Board concerning the violation, efforts to prevent future occurrences of the violation, and efforts to mitigate the harm caused by the violation, including any restitution made to other persons injured by the acts of the person or company;

(4) The history of previous violations by the person or company;

(5) The need to deter the person, company or others from committing such violations in the future; and

(6) Such other matters as justice may require.

ii. Permissible penalty amount under Section 23-1

Pursuant to Section 23-1.(B)(1) of the Texas Securities Act, Respondents may be fined up to $1,337,580 because that is the amount of money MCM received as a result of the Services Agreement.[282] Respondents' fraudulent failures to disclose the conflict of interest created by the Services Agreement is at the center of this matter. Not only was it a significant conflict of interest, but it likely served as an actual incentive for Respondents to continue breaching their duties of care, loyalty and best execution.

[281] Rules and Regulations of the State Securities Board, 7 Tex. Admin. Code Chapter 101 (Supp. 2014)

[282] hT, Page 687

Furthermore, pursuant to Section 23-1.(B)(2) of the Texas Securities Act, an additional $250,000 fine may be assessed because the fraudulent acts in this case were committed against persons over the age of 65. Beginning in 2011, MCM provided the Part 2 of the Form ADV to its investment advisory clients.[283] MCM's client list confirms that between 2011 and November 2014 multiple clients of MCM were over the age of 65.[284] As a result, the Form ADV Part 2s with the above described misrepresentations and omissions were provided to multiple persons over the age of 65. Furthermore at all times since 2011, MCM has had clients over the age of 65. Accordingly, these clients were subject to Respondents' fraudulent omissions related to the Services Agreement and Respondents' fraudulent breaches of fiduciary duties owed to these clients.

Therefore, the maximum amount of penalty that can be assessed in this matter is $1,587,580.00, which amounts to an average of $226,797.14 per year for the 7 years between July 2007 and July 2014.[285]

iii. Application of §106.1 Criteria and Staff Request

As a preliminary matter, the Staff offers that the most important sanction in this matter is the revocation of Respondents' registrations. That said, a financial penalty in addition to the revocation of Respondents' registrations is clearly warranted because Respondents obtained a financial gain through fraudulent conduct and caused investors financial harm too.

Respondents' fraudulent practices in rendering investment advisory services extend back many years and involve serious abuses of the trust clients afforded Mowery and MCM. The willful nature of Respondents' failures to disclose material conflicts of interest is readily apparent throughout the evidence in this case. While Respondents breach of their duty to obtain best execution is serious, their abrogation of the responsibility to act with due care and loyalty towards their client is especially serious.

The fraudulent practices resulted in harm to Respondents' clients. They all paid higher trading costs than they would have if Respondents had acted in good faith and with loyalty to the clients. Instead, Respondents didn't even attempt to determine if clients could save money – and thereby improve performance in their portfolios – at a broker-dealer other than Worth.

Clients called to the hearing by Respondents exhibited the highest level of trust and loyalty. Most should be commended for these fine qualities. Almost all of the clients

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[283] Ex. 112, Stipulated Fact 26

[284] Ex. SSB 84 indicates that at least the following MCM clients were over 65 years of age between 2011 and November 2014: Jerry Yoes; Michael McNeil; Richard "Tex" Brown; David Ross; Ellen Pluta; Randall & Donna Mickan; Walter Bradley; Robert Beaton; Frances Russell; Mary Ann Gardner; Gene Getz; and James Henry.

[285] The period during which the original Services Agreement was effective.

mentioned that performance in their portfolios was there priority. While there was no documented proof that Respondents have rendered strong performance for clients, it is unmistakable that this performance would have been improved if trading costs were lower. Again, significantly lower trading costs were available for Respondents' clients and would have resulted in the same if not better trade execution and services from the broker-dealer. Respondents cannot convincingly argue this point. They did not even conduct such an assessment in selecting Worth and offered no credible evidence to show Worth was necessary to achieve the performance in client account.

Without belaboring the point, Respondents actions during the course of the investigation only fit the very loosest definition of cooperation. To be fair, Respondents attended investigative testimonies and responded to requests for information. However, in each of these measures, Respondents took active steps to mislead the Staff.

Respondents do not have any prior regulatory violations. While they should get credit for this fact, the seriousness and duration of the fraudulent conduct cuts strongly against granting much credit on this point.

Finally, there is a very significant need to deter Respondents and others in positions similar to Respondents. As a result of the broad discretion and trust investors give investment advisers, these fiduciaries have the ability to conduct serious frauds over extended periods of time. If the only sanction that front-line securities regulators could effect was revoking the fraudster's license, unethical investment advisers would be further incentivized to enjoy the benefits of a potentially long-running fraud at the expense of individual investors and the investing public's confidence.

Therefore, the Staff respectfully requests that the Honorable ALJs in this matter recommend that the Securities Commissioner assess an administrative fine of $450,000 in addition to a revocation of Respondents' registrations. This amount corresponds to the fact that Respondents returned to state registration in June 2012 and the Services Agreement was in effect for two years after that point - $450,000 approximately equals two years of the average annual benefit to Respondents described above.[286]

[286] See *supra Section X.B(2)*

XI. Assessment of Hearing Costs

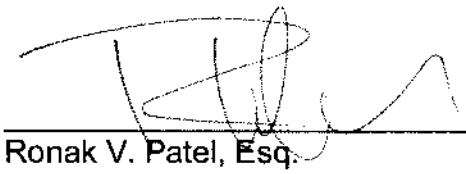
Section 105.13 of the Rules and Regulations of the State Securities Board provides that the Securities Commissioner may assess the costs associated with a written transcription of the hearing to one or more parties.[287] The law clearly provides that Respondents pay this significant cost, and equity demands it for the following reasons:

1) Respondents engaged in myriad fraudulent acts that had to be addressed by the Staff through a lengthy administrative hearing. The Staff understands that Respondent too incurred costs in defending themselves, but the Respondents violations were willful unlike the Staff's obligation to bring this action.

2) Mowery and Mr. Clark were called as witnesses by the Staff, but both witnesses had aligned with the Respondents. Obtaining their testimony during the hearing required extensive time and effort. Of course, the Staff wanted to elicit significant amounts of information from each. However, Mowery and Clark provided false and/or evasive answers throughout their testimonies. This required the Staff to spend extra time ensuring the record was as clear as possible – sometimes unsuccessfully.

3) Respondents called 11 client witnesses that each offered almost the same testimony. The Staff is glad they were each afforded the opportunity to present their opinions and support for their personal friend. However, this process added significant time to the record.

Therefore, the Staff respectfully requests that the Honorable ALJs in this matter recommend that the Securities Commissioner assess all of the hearing costs to Respondents.



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[287] Rules and Regulations of the State Securities Board, 7 Tex. Admin. Code Chapter 101 (Supp. 2014)

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been to Respondents' counsel via email, and to the Securities Commissioner's Representative by hand-delivery, done on this, the 24th day of April, 2015.

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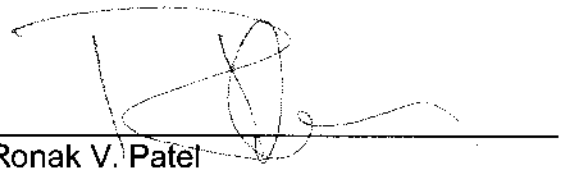

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