

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 2871 / April 22, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13454

In the Matter of

HENNESSEE GROUP LLC and
CHARLES J. GRADANTE,

Respondents.

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

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Hennessee Group LLC (“Hennessee Group”) and Charles J. Gradante (“Gradante”) (together, “Respondents”).

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the “Offers”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-And-Desist Proceedings Pursuant to Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (the “Order”), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds¹ that:

A. **RESPONDENTS AND OTHER RELEVANT ENTITIES**

Respondents

Hennessee Group LLC is an investment adviser registered with the Commission pursuant to Section 203(a) of the Advisers Act, and is a New York limited liability company with its principal place of business in New York City. Hennessee Group is a hedge fund consultant that provides a range of hedge fund investment advisory services for its clients, which consist largely of qualified individual investors and family groups as well as foundations, endowments, and similar institutions. In 2005, Hennessee Group had approximately 100 clients and \$1.35 billion in client assets under management.

Charles J. Gradante ("Gradante"), age 63, resides in New York City. From 1997 through the present, Gradante has served as president, chief executive officer, chief investment officer, and a managing principal of Hennessee Group, which he co-founded with his spouse. At all relevant times, Gradante was a principal, agent, and control person of Hennessee Group and an investment adviser to Hennessee Group's clients. Gradante supervised all aspects of Hennessee Group's due diligence evaluation concerning the Bayou hedge funds and ultimately was responsible for Hennessee Group's decision to recommend investments in the funds to its clients.

Other Relevant Individuals and Entities

Bayou Fund LLC was a Stamford, Connecticut hedge fund formed in 1996 that was directed, managed, and controlled by an investment adviser, Bayou Management, LLC, that, in turn, was directed, managed, and controlled by Samuel Israel III, Daniel E. Marino, and, from 1996 through October 2001, James G. Marquez ("Marquez"). In January 2003, Bayou Management reorganized Bayou Fund into four successor funds: Bayou Superfund, LLC; Bayou Accredited Fund, LLC; Bayou Affiliates Fund, LLC; and Bayou No Leverage Fund, LLC. The successor funds are collectively referred to as the "Bayou Funds" and, for ease of reference, the Bayou Fund, the successor Bayou Funds, and Bayou Management, LLC are collectively referred to herein as "Bayou." Neither the Bayou Funds nor Bayou Management was registered with the Commission in any capacity.

Samuel Israel III ("Israel"), age 49, was the owner and managing member of Bayou Management from the time of its inception in 1996 until it ceased operation as a hedge fund in late 2005.

¹ The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

Daniel E. Marino (“Marino”), age 48, was the chief operating officer and chief financial officer of Bayou Management from the time of its inception in 1996 until it ceased operation as a hedge fund in late 2005.

B. SUMMARY

Hennessee Group is a hedge fund consultant and investment adviser that recommends hedge funds for client investment and monitors those investments on its clients’ behalf. In the course of soliciting clients, Hennessee Group, by and through its principal, Charles Gradante, made numerous representations concerning the quality and rigor of its due diligence process for evaluating hedge funds. Hennessee Group also routinely represented to clients and prospective clients that it would not recommend investments in hedge funds that did not satisfy all phases of its due diligence. Hennessee Group’s services in this regard were particularly important to its clients when, as was the case with Bayou, information regarding a fund’s trading strategies, solvency, and management was not publicly available. With regard to Bayou, Hennessee Group, at Gradante’s direction, did not perform several key elements of its advertised due diligence practices.

From February 2003 through August 2005, approximately forty clients of Hennessee Group invested a total of over \$56 million in the Bayou funds after receiving Hennessee Group’s recommendations. Most of those monies were lost and dissipated by Bayou’s principals, who defrauded their investors by fabricating Bayou’s performance in client account statements, periodic newsletters, and year-end financial statements that included a phony audit opinion fabricated by one of Bayou’s principals.

Hennessee Group and Gradante, in their capacities as investment advisers, owed fiduciary duties to their clients to perform the services that they represented they would provide and to disclose all material departures from the representations that they made to their clients. Despite their representations about their services, with regard to the Bayou Funds and the funds’ management, Hennessee Group and Gradante did not perform two of the five elements of the due diligence evaluation that they had represented to their clients they would undertake. In addition, Hennessee Group and Gradante failed to adequately respond to information that they received that suggested that the identity of Bayou’s outside auditor was in doubt and that there existed a potential conflict of interest between one of Bayou’s principals and its purported outside auditor.

As a result of the conduct described above, Hennessee Group and Gradante willfully violated Section 206(2) of the Advisers Act, which prohibits any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client, and Gradante caused Hennessee Group’s violations of Section 206(2) of the Advisers Act.

C. FACTS

Background – The Bayou Fraud

In 1996, Israel, Marino, and Marquez founded the Bayou Fund as a hedge fund or private investment pool. Israel and Marquez were Bayou's portfolio managers and Marino served as chief financial officer and chief operating officer. Marquez resigned from the Bayou entities in October 2001, and Israel and Marino continued to operate Bayou Fund and its four successor funds through 2005.

Bayou's purported investment strategy was day trading – buying and selling stocks throughout the day in an attempt to capture profits from market momentum. Israel represented to investors that he had developed a unique trading system and technical analysis that enabled him to trade profitably regardless of market conditions. Bayou also represented that, in order to maintain liquidity and minimize overnight exposure, virtually all of Bayou's securities positions were converted into cash at the close of each trading day.

Almost from its inception, the Bayou Fund lost money from trading. By 1997, Bayou devised and implemented a scheme to defraud investors and prospective investors by fabricating the fund's performance in monthly client account statements, periodic newsletters, and year-end financial statements. In 1998, realizing that the funds could not withstand an independent audit, Bayou's principals dismissed the funds' then-auditor, Grant Thornton LLP ("Grant Thornton"), and Marino fabricated "independent" audited financial statements and a phony auditor opinion letter. The bogus opinion letter was written on the stationery of a purported accounting firm named "Richmond-Fairfield Associates" ("Richmond-Fairfield"). From 1996 through mid-2005, Bayou attracted over \$400 million in investor capital by concealing trading losses and giving investors the misleading impression that the funds achieved modest and steady profits. The fraud unraveled in August 2005, after Bayou issued worthless redemption checks to certain investors from overdrawn bank accounts and began shutting down its operations.

Hennessee Group's Hedge Fund Consulting Services

Gradante managed Hennessee Group as an independent hedge fund consulting firm since its founding in 1997. Hennessee Group and its principals held themselves out as "Pioneers in Hedge Fund Consulting" with years of experience helping clients achieve "higher investment returns with lower risk" by recommending "a customized portfolio of hedge funds, properly diversified and managed." Hennessee Group's client relationships typically began with a meeting with the prospective client during which Gradante and others described Hennessee Group's services and provided a written presentation outlining its hedge fund evaluation and selection process and containing sample portfolios of hedge funds. If the prospective client wished to retain Hennessee Group, the parties executed an advisory agreement. Hennessee Group's advisory fee was one percent or less of the value of the assets that a client invested in hedge funds based on the firm's recommendation.

From 2002 through 2005 (the “relevant period”), Hennessee Group promoted its process for evaluating and selecting hedge funds as the “Five Level Due Diligence Process.” Hennessee Group represented to clients and prospective clients that it would not recommend investment in hedge funds that did not satisfactorily complete all five levels of its due diligence evaluation. As explained to clients and prospective clients, that process included:

- (i) a request for general information and data on “historical returns” from the hedge fund;
- (ii) a face-to-face initial interview with the fund manager that covered numerous topics such as the background of the fund manager, the fund’s “portfolio construction and attributes” and “risk management” principles, and the name and contact information of the fund’s outside audit firm;
- (iii) a detailed review and analysis of the fund’s investment portfolio, trading practices, and risk management discipline, generally based on prime brokerage reports sufficient to reflect the fund’s actual activity over a given period;
- (iv) an on-site visit to the fund’s offices to meet and interview key personnel such as the portfolio manager and head trader, examine the fund’s “technology and systems,” discuss the results of the Level III portfolio/trading analysis, and address any remaining issues from Hennessee Group’s earlier due diligence; and
- (v) a reference and background check on the fund’s manager, consisting primarily of “utiliz[ing] the principals’ contacts to verify [the] reputation of [the] portfolio manager,” and a “review of all audited financial statements,” as well as a review of the fund’s offering memorandum and “subscription documents.”

Hennessee Group’s marketing materials, its website, and its oral and written presentations described or referred to this “Five Level Due Diligence Process.” Hennessee Group routinely touted the excellence and rigor of the process.

Hennessee Group had an Investment Committee, chaired by Gradante and comprised of the firm’s research staff, that met each month to review the status of each fund then undergoing the due diligence process and determine whether to proceed to the next level of evaluation of a particular fund. After recommending an investment in a hedge fund to its clients, Hennessee Group committed to monitor the fund for its clients on a monthly basis. Hennessee Group made monthly requests to funds for performance data, and conducted periodic meetings or conference calls with the fund manager to inquire about the manager’s current market views and concerns, the fund’s portfolio structure, the manager’s expectations for the fund, and any organizational changes.

Hennessee Group’s Recommendation of Bayou

In April 2002, a Hennessee Group client suggested that Hennessee Group review Bayou and several other funds with a view toward possibly recommending investments in Bayou to

Hennessee Group's clients. Hennessee Group contacted Bayou to initiate review and Bayou agreed to begin the process shortly thereafter. Hennessee Group began recommending Bayou to its clients in December 2002. Thereafter, Hennessee Group conducted ongoing monitoring of Bayou, which consisted of inquiries about the manager's current market views and concerns, the fund's portfolio structure, the manager's expectations for the fund, and any organizational changes, and continued recommending client investments in Bayou from January 2003 through July 2005, when Bayou announced that it would be liquidating the funds.

During the relevant period, Hennessee Group collected over \$500,000 in advisory fees for referring approximately forty clients to the Bayou Funds. By mid-2005, just prior to the public disclosure of Bayou's failure, Hennessee Group clients had placed over \$56 million in capital contributions into Bayou.

Hennessee Group Did Not Conduct a Due Diligence Evaluation of Bayou
Consistent With its Representations to Clients and Prospective Clients

With regard to Bayou, Hennessee Group, at Gradante's direction, failed to perform two elements of the due diligence evaluation that Hennessee Group had told its clients and prospective clients that it would do: (1) a portfolio/trading analysis; and (2) a verification of Bayou's relationship with its purported independent auditor. By not conducting the entire due diligence evaluation that it had advertised, and by failing to disclose to clients that its evaluation of Bayou deviated from its prior representations, Hennessee Group and Gradante rendered the prior representations about the due diligence process materially misleading and breached their fiduciary duties to Hennessee Group's clients.

A. Hennessee Group Did Not Conduct a Portfolio/Trading Analysis on
the Bayou Funds

Hennessee Group maintained detailed procedures on how the five levels of due diligence that were described in its marketing materials and website were to be conducted. Hennessee Group's evaluation purportedly included a detailed review and analysis of a fund's portfolio and trading records (also known as a "Level III review"). The promotional materials that Hennessee Group distributed to clients and prospective clients created the impression that the portfolio/trading analysis was Hennessee Group's specialty and a core element of its due diligence process, stating, for example, that investors "need to see more than just the returns; [they] should be able to understand how the returns were achieved and what factors affected them."

In order to conduct its portfolio/trading analysis, Hennessee Group sought prime brokerage reports either directly from a fund or from the fund's prime broker, consisting of a "portfolio snapshot" of a fund's investments at a given time and "trading activity reports" (also known as "realized and unrealized gain/loss reports"). Hennessee Group purportedly used the data in the reports to evaluate a manager's risk management discipline, hedging strategies, stop losses, distribution of returns by security, pricing of securities, and other trading practices. Although Hennessee Group often was unable to obtain such reports from funds, the firm failed to disclose to its clients that it did not conduct a portfolio/trading analysis under such circumstances.

In the fall of 2002, Bayou refused to provide Hennessee Group with the prime brokerage reports that Hennessee Group had requested. However, instead of insisting that Bayou provide the reports as a condition of potentially being recommended, Hennessee Group proceeded to the next phases of due diligence. Gradante decided that a portfolio/trading analysis was irrelevant for a day-trading fund like Bayou, which stated in marketing materials that it held securities positions for brief periods of time and converted positions to cash prior to each day's market closing.

As a result, Hennessee Group did not obtain or evaluate any quantitative information about Bayou's portfolio characteristics, investment and trading strategies, or risk management discipline. Instead of confirming Bayou's results and processes through an analysis of Bayou's historical trading data to determine whether the fund was, in fact, executing its purported "high-velocity" day-trading strategy and utilizing appropriate risk management techniques, Gradante and Hennessee Group relied entirely on Bayou's uncorroborated representations and purported rates of return that Bayou had provided during its initial information-gathering phases.

Hennessee Group never told the clients to whom it recommended Bayou that it had not conducted a portfolio/trading analysis on the funds. By failing to disclose this information in connection with its recommendation of Bayou, Hennessee Group left those clients with the misleading impression that it had conducted a portfolio, trading, and risk management evaluation of Bayou and that Bayou had satisfied Hennessee Group's purported standards. In so doing, Hennessee Group and Gradante breached their fiduciary duties to Hennessee Group's clients.

B. Hennessee Group Failed to Verify Bayou's Relationship with its Independent Auditor

Hennessee Group told many of the clients to whom it recommended an investment in Bayou, that as part of its review of a fund's audited financial statements, Hennessee Group verified the fund's relationship with its purported independent auditor and that the audit firm had actually conducted the audit. Hennessee Group's staff frequently made this representation to prospective clients. In reality, Hennessee Group's "Verify Auditor" procedure consisted only of confirming that a fund's financial statements contained an unqualified audit opinion letter.

In mid-2002, Bayou provided Hennessee Group with copies of its three most-recent annual financial statements, for fiscal years 1999 through 2001. Those financial statements were presented on Richmond-Fairfield stationery and included unqualified audit opinions purportedly issued by Richmond-Fairfield, but in fact were drafted by Marino and signed by him in the firm's name. Bayou also told Hennessee Group numerous times during the due diligence process that the funds had "outgrown" Richmond-Fairfield and had selected another accounting firm, Hertz, Herson & Co., LLP ("Hertz Herson"), to serve as its new auditor beginning with the 2002 annual audit. However, despite having represented to prospective clients that it verified a fund's audit relationship, Hennessee Group took no steps during the initial evaluation to contact either Hertz Herson, which was an actual accounting firm, or Richmond-Fairfield to confirm whether either had an audit relationship with Bayou.

Auditor verification was particularly warranted with regard to Bayou. Hennessee Group had no prior dealings with and was unfamiliar with Richmond-Fairfield and Hertz Herson. Of the approximately 150 hedge funds that Hennessee Group monitored on behalf of its clients, none other than Bayou had ever used Hertz Herson or Richmond-Fairfield as its outside auditor.

Hennessee Group Disregarded Red Flags
During its Due Diligence Review and Subsequent Monitoring of Bayou

Hennessee Group also failed to adequately investigate and reconcile certain negative and contradictory information about Bayou that Hennessee Group had a duty to investigate by virtue of its representations to its clients that it would conduct on-going monitoring of the clients' investments.

Although Hennessee Group reviewed audited financial statements of the Bayou funds, Hennessee Group failed to reconcile Bayou's conflicting claims about its auditor's identity, and accepted without the requisite skepticism or searching inquiry Bayou's claim that it had changed outside auditors several times. During the due diligence process, Bayou provided Hennessee Group with several contradictory responses regarding the identity of its auditor. In June 2002, Bayou informed Hennessee Group that its auditor was Grant Thornton. During the fall of 2002, Bayou gave Hennessee Group three different marketing documents, two identifying Hertz Herson as Bayou Fund's auditor, and the third identifying Grant Thornton as Bayou Fund's auditor. In fact, Grant Thornton had not audited Bayou since fiscal year 1997, and Hertz Herson had never been retained to audit the hedge fund.

In September 2002, Israel and Marino told Gradante that, while Bayou's original auditor had been Grant Thornton, "bad service" had prompted Bayou to switch to the "more client friendly" Richmond-Fairfield in 1999. At that time, Israel and Marino also told Gradante that Bayou had "outgrown" Richmond-Fairfield and had selected Hertz Herson to be its new auditor. Marino later provided Hennessee Group with the name of the purported engagement partner at Hertz Herson.

Hennessee Group did not attempt to investigate this inconsistent information to determine whether Hertz Herson had in fact been retained to conduct the audit of Bayou Fund for 2002. In fact, Hertz Herson had not been retained to conduct the 2002 audit of the Bayou Fund. In addition, Hennessee Group also failed to contact Richmond-Fairfield or Grant Thornton to verify those past relationships and obtain their perspectives on whether and why Bayou had terminated them.

In the spring of 2003, after Hennessee Group had already begun recommending investments in Bayou, Bayou sent Hennessee Group two marketing documents that identified Hertz Herson as Bayou's auditor. One of those documents further stated, "In 2002, *Hertz Herson conducted a first time audit* for the Bayou Fund LLC. Previous auditor for the Bayou Fund LLC was Richmond Fairfield." (Emphasis added.) As noted above, Bayou previously had told Hennessee Group during the due diligence process in 2002 that it had outgrown Richmond-Fairfield and retained Hertz Herson as its new auditor.

Shortly thereafter, in May of 2003, Hennessee Group received a copy of Bayou Fund's audited financial statements for fiscal year 2002, presented on Richmond-Fairfield stationery, which included an audit opinion from Richmond-Fairfield, rather than Hertz Herson. Gradante and a Hennessee Group research analyst both reviewed Bayou's audit report as part of the firm's routine monitoring process, and noted the discrepancy in the information that Bayou had provided concerning the identity of its outside auditor, but made no effort to inquire into Bayou's prior representations about having retained Hertz Herson.

The following year, in June 2004, Hennessee Group received a copy of the Bayou Funds' audited financial statements for fiscal year 2003, which again purportedly had been prepared and certified by Richmond-Fairfield, not Hertz Herson. Despite this, Hennessee Group and Gradante took no action to investigate this inconsistency in Bayou's representations regarding its auditor, and relied solely on an explanation from Bayou.

In late April 2005, Marino told Hennessee Group that "[t]he audit for 2004 was recently completed by Hertz Herson and he anticipates it being sent out in the next week or two." However, Hennessee Group did not actually receive Bayou's fiscal year 2004 audit until mid-July 2005. As with the 2002 and 2003 audits, Bayou's 2004 audit purportedly had been conducted and certified by Richmond-Fairfield, instead of Hertz Herson. One week after Hennessee Group received the 2004 audit report, Bayou announced that it was liquidating the funds. Hennessee Group and Gradante did not disclose to any of their clients the contradictory information that Bayou had provided over several years concerning the identity of its auditor.

Hennessee Group and Gradante Failed to Investigate a Rumor
That Marino was Affiliated With Bayou's Outside Auditing Firm

Hennessee Group also failed to investigate a rumor concerning Marino's connection to Richmond-Fairfield. On Friday, January 14, 2005, a client of Hennessee Group who had invested in Bayou sent an email to Hennessee Group stating:

I am told the head of back office for Bayou is also a principal in the firm that does their annual audit; also that there have been discrepancies in K-1's put out by Bayou. Seems like a lot of smoke. For a 12 to 15% return fully taxed at ordinary rates, I'm thinking I shouldn't take a chance on another implosion. When will your next due diligence take place on Bayou and will it cover such things as the fact it appears the head of back office (Marino or some name like that) is auditing himself by being a principal of the outside audit firm?

On January 19, four days after Hennessee Group received the investor's email, Gradante sent an email to Israel and Marino titled "RUMOR WITH POTENTIALLY DAMAGING IMPACT ON BAYOU" that stated:

A CLIENT of hennessee and bayou has heard that dan marino is a principal or has an economic interest in your accounting firm.....i know you guys are always doing the right thing so i wouldn't be surprised if this is a stretch of

the truth....can you go on the record for me so i can help us all “NIP THIS IN THE BUD.”²

Marino called Gradante in response to the email and told Gradante that, before joining Bayou in 1999, he had been associated with Bayou’s audit firm, but that he had severed all ties with the audit firm when he joined Bayou. Gradante accepted Marino’s explanation and requested that Marino put a statement of denial in an email or letter. Marino agreed to provide an email by January 21 that would give “a full explanation” of his resume and background.

On January 25, 2005, Marino sent an email to Gradante in which he represented that from 1991 through 1998, Marino operated his own accounting practice at a firm known as “Marino & Group, CPA”; in 1997, Marino began providing accounting and tax advice for the Bayou entities; in 1998, Marino began performing audit work for the Bayou Fund; and in January 1999, Marino sold his share of the accounting firm and accepted Israel’s offer to join Bayou full time to manage operations and the back office, and had served as Bayou’s chief financial officer and chief operating officer since that time.

Marino’s assertions in the email, however, conflicted with information that Bayou had provided to Hennessee Group during the previous three years. For example, at least two Bayou marketing documents provided to Hennessee Group in early 2003 contained biographical information about Marino that stated, “*In 1996, Mr. Marino joined Mr. Israel as part of the original management team at Bayou as CFO and COO, and has performed these functions for Bayou since its inception.*” (Emphasis added.) These earlier disclosures directly contradicted Marino’s assertion in the email to Gradante that he had joined Israel at Bayou in January 1999 as chief financial officer and chief operating officer. In addition, at that time, Hennessee Group’s due diligence file and materials on Bayou already contained several statements from Marino that Bayou had switched auditors from Grant Thornton to “a more client friendly” Richmond-Fairfield in 1999, which directly conflicted with Marino’s claim in the email that “Marino & Group, CPA” had begun performing audit work for Bayou in 1998.

Gradante read Marino’s email shortly after it was received. Although Hennessee Group had information in its files that directly contradicted Marino’s explanation, the firm made no effort to verify the assertions Marino made in his email. Gradante took no other steps to verify Marino’s claims, such as contacting Richmond-Fairfield or conducting internet and/or public records searches on Richmond-Fairfield or Marino. In fact, Marino was listed as Richmond-Fairfield’s registered agent in New York State public records. Publicly-available state accountancy board records disclosed that Richmond Fairfield had been registered with New York State in October 2000 under Marino’s name and personal address.

Shortly thereafter, Gradante told the investor that the rumor was false and that Marino had provided a full explanation.

² At some point, Hennessee Group received information suggesting that the source of the rumor may have been an individual affiliated with a rival hedge fund consulting group that had advised its clients to withdraw all of their money from Bayou.

D. VIOLATIONS

Hennessee Group and Gradante, in their capacities as investment advisers, owed fiduciary duties to their clients to not misrepresent the services that they were providing and to disclose all material departures from the representations that they made to their clients. With regard to the Bayou Funds and the funds' management, Hennessee Group and Gradante failed to conduct two of the five elements of the due diligence review that they had represented to their clients they would undertake. In addition, Hennessee Group and Gradante failed to adequately respond to information that they received that suggested that the identity of Bayou's outside auditor was in doubt and that there existed a potential conflict of interest between one of Bayou's principals and the purported outside auditor of Bayou. Hennessee Group and Gradante breached their fiduciary duties to their investment advisory clients.

As a result of the conduct described above, Hennessee Group and Gradante willfully violated Section 206(2) of the Advisers Act, which prohibits any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client, and Gradante caused Hennessee Group's violations of Section 206(2) of the Advisers Act. Scierer is not a required element of Section 206(2); negligence suffices for liability. *See SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963); *SEC v. Steadman*, 967 F.2d 636, 643 (D.C. Cir. 1992). An investment adviser is accountable for the actions of its principals. *See SEC v. Manor Nursing Ctrs. Inc.*, 458 F.2d 1082, 1089 n.3, 1096-97 nn.16-18 (2d Cir. 1972) (company's scierer imputed from individuals who control it).

E. UNDERTAKINGS

Respondents have undertaken to:

1. Adopt policies and procedures to ensure adequate oral and written disclosures to clients and prospective clients regarding Hennessee Group's process for evaluating, selecting, and monitoring hedge funds, and maintain a written manual setting forth such policies and procedures.
2. Within thirty (30) days of the issuance of this Order, mail a copy of this Order, together with a cover letter in a form not unacceptable to the Commission staff, to each of Hennessee Group's existing clients. Respondents shall also provide a copy of this Order to any new client that engages Hennessee Group or Gradante within two (2) years of the date of this order.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondents' Offers.

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

- A. Respondents Hennessee Group and Gradante be, and hereby are, censured.
- B. Respondents Hennessee Group and Gradante cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act.
- C. Respondents shall comply with the undertakings enumerated in Section III.E., above.
- D. IT IS FURTHER ORDERED that Respondents Hennessee Group and Gradante shall, within three hundred sixty-five (365) days of the entry of this Order, jointly and severally pay disgorgement of \$549,076.00³ and prejudgment interest of \$165,568.12 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice Section 600. Payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Hennessee Group or Gradante as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Yuri B. Zelinsky, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549.
- E. IT IS FURTHER ORDERED that Respondents Hennessee Group and Gradante shall, within thirty (30) days of the entry of this Order, jointly and severally pay a civil money penalty in the amount of \$100,000.00 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. Section 3717. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Hennessee Group or Gradante as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Yuri B. Zelinsky, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549.
- F. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, a Fair Fund is created for the disgorgement, interest, and penalties referenced in Sections IV.D and E above (the "Distribution Fund"). Regardless of whether any such Fair Fund distribution is made, amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondents agree that they shall not, after offset or reduction in any Related Investor Action based on Respondents' payment of disgorgement in this action, argue that they are

³ The disgorgement amount takes into consideration payments that Hennessee Group previously has made to certain of its clients.

entitled to, nor shall they further benefit by offset or reduction of any part of a Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondents agree that they shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the United States Treasury or to a Fair Fund, as the Commission directs. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondents by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

G. Respondents shall cooperate with the Distribution Fund Administrator, including upon request, providing any documents, records, and information as are necessary for the Distribution Fund Administrator to carry out his duties.

By the Commission.

Elizabeth M. Murphy
Secretary