

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5087 / December 21, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18950

<p>In the Matter of</p> <p style="text-align:center">Hedgeable, Inc.</p> <p>Respondent.</p>
--

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
PURSUANT TO SECTIONS 203(e) 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) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Hedgeable, Inc. (“Hedgeable” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) 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 it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

Summary

1. This matter involves a registered investment adviser—Hedgeable—that disseminated false and misleading marketing materials and performance data. Hedgeable operates a “robo-adviser”: an automated digital investment advisory program that is marketed to individuals, small business owners, trusts, corporations and partnerships through the fund's website, Hedgeable.com, as well as through social media platforms.

2. From at least 2016 until April 2017, Hedgeable posted on its website and social media platforms a “Robo-Index,” which purportedly allowed clients and prospective clients to compare the performance from 2014 and 2015 of two other robo-advisers—”Robo-Adviser 1” and “Robo-Adviser 2”—to the performance of Hedgeable's clients during the same period, which were aggregated in a “Hedgeable Composite.” The Robo-Index and Hedgeable Composite were misleading in several respects. First, the Hedgeable Composite only included a small subset—less than 4%—of the total number of Hedgeable clients during the 2014 and 2015 period. Second, Hedgeable's calculation methodology of the Robo-Index was incorrect, as it was not based on Robo-Adviser 1's or 2's actual trading models, but was instead an approximation of Robo-Adviser 1's or 2's performance based on information available from their websites. Third, even using its own methodologies, Hedgeable incorrectly calculated the annualized returns for both the Robo-Index and the Hedgeable Composite. Hedgeable failed to maintain sufficient documentation to substantiate the returns presented in the Robo-Index or the Hedgeable Composite. Hedgeable also posted misleading fact sheets on its website that overstated the returns of various Hedgeable ETFs, as compared to certain benchmarks of blended index returns.

3. Hedgeable's dissemination of false and misleading marketing materials and performance data was caused, in part, by its ineffective compliance program. Hedgeable's compliance policies and procedures did not require any officer of Hedgeable to review or approve marketing materials or performance data posted on Hedgeable's digital media platforms.

Respondent

4. Hedgeable is a Delaware corporation, with its principal place of business in New York, New York. Hedgeable has been registered with the Commission as an internet investment adviser since 2009. As of March 2018, Hedgeable reported assets under management of \$81 million. Hedgeable is winding down the investment advisory business. In its most recent form ADV, dated as of September 2018, Hedgeable reported that it no longer has assets under management, and is no longer eligible to be registered with the SEC.

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

Background

A. Hedgeable’s Advertising and Marketing Materials

5. Hedgeable created a *sui generis* “Robo-Index” to compare its performance to the performance of the two other, unaffiliated robo-advisers, Robo-Adviser 1 and Robo-Adviser 2. The Robo-Index was designed to compare a combination of Robo-Adviser 1 and 2’s average returns for 2014 and 2015 with actual returns by Hedgeable’s clients over the same period (the “Hedgeable Composite”). The two-year annualized rates of return were reported as follows:

<u>Robo-Index:</u> 2-Year Annualized Rate of Return (2014-2015)	<u>Hedgeable Composite:</u> 2-Year Annualized Rate of Return (2014-2015)
(0.53%)	4.2%

The comparisons were marketed on Hedgeable.com, as well as various social media platforms. However, there were several material issues with Hedgeable’s methodology in preparing the Robo-Index, and Hedgeable misstated and/or failed to disclose material facts relevant to its performance over the specified period.

6. First, in calculating the Hedgeable Composite returns for 2014 and 2015, Hedgeable included only 22 client accounts in 2014 and 38 client accounts in 2015, excluding 1,104 client accounts that were invested in 2014 and/or 2015. While Hedgeable disclosed that the Hedgeable Composite returns only included client accounts from the relevant period that were opened, funded, and invested for the full calendar year in 2014 and/or 2015, Hedgeable failed to disclose that, as a result of its methodology, the vast majority of its client accounts—over 96%—were not included in the Hedgeable Composite. The Hedgeable Composite returns thus reflect survivorship bias, as the small number of clients who maintained accounts for a full calendar year are likely to be clients who received higher-than-average returns as compared to Hedgeable’s total client base. By contrast, Hedgeable calculated the Robo-Index based on its analysis of the publicly-available information on Robo-Adviser 1 and 2’s websites. This was not an apples-to-apples comparison as Hedgeable was, in effect, comparing Hedgeable’s best returns against the returns Hedgeable believed were experienced by an average client of Robo-Adviser 1 and Robo-Adviser 2.

7. Second, Hedgeable’s calculation methodology for the Robo-Index was incorrect, as it failed to approximate the actual expected returns for an average client of Robo-Adviser 1 or 2. Hedgeable did not have access to actual performance data for Robo-Adviser 1 or 2’s models. Hedgeable developed the Robo-Index using its own estimation of Robo-Adviser 1 and 2’s theoretical trading models, based upon information available from the Robo-Adviser 1 and 2 websites in the companies’ account-opening processes. To obtain access to model portfolio holding weights as of year end, Hedgeable went through the process of creating accounts at Robo-Adviser 1 and 2 through their websites. However, Hedgeable failed to actually approximate the returns from Robo-Adviser 1 and 2’s actual models. For example, in developing the Robo-Index, Hedgeable failed to adjust its theoretical model to match changes made by Robo-Adviser 2 to the weights assigned to its various risk categories. Accordingly, Hedgeable’s theoretical model for the

Robo-Index was based upon incorrectly weighted risk categories, and thus could not accurately calculate Robo-Adviser 2's expected returns. Hedgeable also incorrectly assumed that Robo-Adviser 2 rebalanced its portfolios to its model weights on a quarterly basis instead of maintaining its portfolios at adjusted weights for multiple quarters. As a result, the Robo-Index did not accurately reflect expected returns using Robo-Adviser 2's actual models.

8. Third, Hedgeable erroneously published a comparison of the two-year annualized returns from 2014 and 2015 for the Robo-Index and Hedgeable Composite, when in fact the numbers published on its website reflected cumulative returns. Specifically, Hedgeable indicated on its website that the annualized Robo-Index return for 2014 and 2015 was -.53%. The annualized Robo-Index return for this period was actually -.266%. Similarly, Hedgeable disclosed that its annualized return for 2014 and 2015 for the Hedgeable Composite was 4.2%. In fact, 4.2% was a cumulative return. The annualized Hedgeable Composite return was actually 2.07%.

Failure to Maintain Required Documentation Relating to Performance Reporting

9. In addition, Hedgeable failed to maintain sufficient documentation to substantiate the returns presented in the Robo-Index and the Hedgeable Composite. Hedgeable did not have access to, and therefore did not maintain independent documentation from, Robo-Adviser 1 or 2 to substantiate Robo-Adviser 1 or 2's portfolio holdings for 2014 and 2015. Hedgeable was unable to provide supporting documentation for the returns of its Robo-Index. Similarly, Hedgeable was unable to produce data to substantiate the performance returns of clients in the Hedgeable Composite.

Misleading Disclosures in Hedgeable Fact Sheets

10. Hedgeable posted fact sheets on its website for its various model portfolio strategies. The gross performance returns for the model portfolios ("Model Portfolio Returns") consisted of back-tested returns for the periods prior to the inception of the strategies, and live returns when the models were being managed live by Hedgeable. The Model Portfolio Returns are compared to benchmark returns, which are mostly blended index returns calculated by Hedgeable ("Benchmark Returns").

11. The fact sheets from Hedgeable.com contained at least three materially misleading disclosures that gave the impression that Hedgeable's strategies outperformed the benchmarks by a greater margin than they did in reality. First, Hedgeable failed to update the annual benchmark returns in the fact sheets for certain years, which made it appear as though the model portfolio outperformed its benchmark for earlier years to a much greater extent than it actually did. Second, Hedgeable erroneously calculated at least three ETF Benchmark Returns, which turned out to be higher when the proper calculations were applied. Finally, Hedgeable improperly calculated Model Portfolio Returns for several ETFs, which caused Hedgeable to inflate the Model Portfolio Returns for several ETFs on their respective fact sheets.

12. The disclosure of inaccurately low Benchmark Returns and inaccurately high Model Portfolio Returns on the fact sheets gave the impression that Hedgeable's strategies outperformed the benchmarks by a materially greater margin than they did in reality.

B. Hedgeable's Compliance Failures

13. The dissemination of misleading marketing materials and performance data was caused, in part, by Hedgeable's failure to adopt and implement an adequate compliance program.

14. Since 2009, Hedgeable has maintained a written Compliance Policies and Procedures Manual. However, those policies and procedures were not reasonably designed to prevent Hedgeable's violations of the Advisers Act and rules thereunder. Specifically, from 2009 to October 2017, Hedgeable had no written policies and procedures regarding the review and approval of advertisements and promotional material posted on Hedgeable's digital media (website, blog, social media, etc.). Hedgeable's CCO during the relevant period was not aware that Hedgeable's social media postings were considered marketing materials under the Advisers Act, and accordingly, did not review Hedgeable's social media postings.

15. Hedgeable's policies and procedures required Hedgeable employees to "obtain approval from the CCO before [sending] any written communications to investors or prospective investors." However, this language was not broad enough to require the review of marketing and promotional materials posted on Hedgeable's digital media, which was the core of Hedgeable's business. In October 2017, Hedgeable amended its policies and procedures to specifically require that all advertisements and promotional materials, including those posted on Hedgeable's digital media, be reviewed by the CCO, a designee of the CCO, or another officer if the materials were prepared by the CCO.

Violations

16. As a result of the conduct described above, Hedgeable willfully² violated Section 206(2) of the Advisers Act, which prohibits an investment adviser from engaging in "any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." A violation of Section 206(2) of the Advisers Act does not require proof of scienter but, rather, "may rest on a finding of simple negligence." *SEC v. Steadman*, 967 F.2d 636, 643 n. 5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963)).

17. As a result of the conduct described above, Hedgeable willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) thereunder, which prohibit any registered investment adviser from, directly or indirectly, publishing, circulating, or distributing an advertisement which contains any untrue statement of material fact, or which is otherwise false or misleading. A showing of negligence is also sufficient to establish a violation of Section 206(4) of the Advisers Act and the rules thereunder. *Steadman*, 967 F.2d at 647.

² A willful violation of the securities laws means merely "that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "also be aware that he is in violation one of the Rules or Acts." *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

18. As a result of the conduct described above, Hedgeable willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require that registered advisers adopt and implement written policies and procedures reasonably designed to prevent violations by the adviser and its supervised persons of the Advisers Act and the rules thereunder.

19. As a result of the conduct described above, Hedgeable willfully violated Section 204(a) of the Advisers Act and Rule 204-2(a)(16) thereunder. Section 204 of the Advisers Act requires investment advisers to make and keep certain records as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors. Rule 204-2 under the Advisers Act requires investment advisers registered or required to be registered to make and keep true, accurate, and current books and records related to their investment advisory business, including all accounts, books, internal working papers, and any other records or documents that are necessary to form the basis for or demonstrate the calculation of the performance or rate of return of any or all managed accounts or securities recommendations in any notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication that the investment adviser circulates or distributes, directly or indirectly, to 10 or more persons.

IV.

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

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

A. Respondent cease and desist from committing or causing any violations and any future violations of Sections 204, 206(2), and 206(4) of the Advisers Act and Rules 204-2, 206(4)-1, and 206(4)-7 promulgated thereunder.

B. Respondent is censured.

C. Respondent shall pay a civil money penalty of \$80,000, payable as follows: \$40,000 within thirty (30) days of entry of this Order and \$40,000 within ninety (90) days of the entry of this Order, made payable to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If any payment is not made by the date the payment is required by this Order, the entire outstanding balance, plus any additional interest accrued pursuant to pursuant to 31 U.S.C. 3717, shall be due and payable immediately, without further application.

Payment must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or

- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Hedgeable as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to C. Dabney O'Riordan, Associate Director, Division of Enforcement, Securities and Exchange Commission, Los Angeles Regional Office, 444 South Flower Street, Suite 900, Los Angeles, CA 90071.

D. 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, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of 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, Respondent agrees that it 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 Securities and Exchange Commission. 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 Respondent 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.

By the Commission.

Brent J. Fields
Secretary