UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3735 / December 12, 2013

INVESTMENT COMPANY ACT OF 1940
Release No. 30828 / December 12, 2013

ADMINISTRATIVE PROCEEDING
File No. 3-15643

In the Matter of **JOSEPH G. PARISH III and SCOTT H. SHANNON,** **Respondents.**	**ORDER INSTITUTING PUBLIC ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 203(f) AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940 AND SECTION 9(b) OF THE INVESTMENT COMPANY 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 that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(f) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act"), against Joseph G. Parish III ("Parish") and Scott H. Shannon ("Shannon," and together with Parish, "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(f), and 203(k) of the Investment Advisers Act of 1940 and Section 9(b) of the Investment Company 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 Respondents' Offers, the Commission finds[1] that:

A. Summary

1. This matter involves violations of the federal securities laws by Shannon and Parish in their role as investment managers for a collateralized debt obligation transaction ("CDO"). Shannon and Parish were the principals of NIR Capital Management, LLC ("NIR"), which, as the collateral manager of the CDO, was responsible for the independent selection, acquisition and monitoring of a portfolio of assets – the collateral – backing a series of securities issued to investors by a special-purpose vehicle (the "Issuer") named Norma CDO I Ltd. ("Norma").

2. Respondents nevertheless allowed the equity investor in Norma, a hedge fund firm consisting of Magnetar Capital LLC and its affiliates (together, "Magnetar"), to influence the selection of Norma's portfolio of collateral. Respondents knew that Magnetar sought to take short positions on CDO debt, in addition to its long investment in CDO equity. Respondents, therefore, should have realized that Magnetar's interests were not necessarily the same as those of potential investors in the debt tranches of Norma, whose investments depended solely on the CDO and its collateral performing well.

3. The Norma transaction was a $1.5 billion CDO that closed on March 1, 2007. The collateral for the transaction consisted of approximately 90% credit default swaps ("CDS") referencing residential mortgage backed securities ("RMBS").[2] Approximately 10% of the portfolio – the so-called "CDO bucket" – consisted of securities issued in other CDO transactions. The transaction was structured and marketed by subsidiaries of Merrill Lynch & Co., Inc. (collectively "Merrill"), which also lent their balance sheet to store, or "warehouse," collateral acquired for the CDO in the months leading up to the closing of the transaction.

4. As a result of Magnetar's influence, NIR ultimately incorporated into the portfolio collateral that Shannon sought to exclude, including significant exposure to RMBS that Magnetar and Merrill, not Respondents, had initially acquired and selected. Parish allowed

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[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.

[2] RMBS are bonds backed by pools of residential mortgage loans, in this case subprime loans.

Magnetar to influence the form of exposure to, or selection of, a substantial amount of CDO assets that ended up in Norma's portfolio and should have known that Shannon sought to exclude significant RMBS exposure.

5. In a Collateral Management Agreement with the Norma Issuer (NIR's client), NIR represented that, in performing its duties, it would:

> act in good faith and exercise reasonable care, using a degree of skill and attention no less than that which [NIR] exercises with respect to comparable assets that it manages for itself and . . . in a commercially reasonable manner consistent with accepted practices and procedures applied by reasonable and prudent institutional managers of national standing in connection with the management of assets [comparable to Norma's collateral].

6. NIR also represented that it would "follow its customary standards, policies and procedures in performing its duties" as collateral manager for Norma.

7. These representations were misleading because they did not disclose Magnetar's role in the process of collateral selection and because Respondents departed from the represented standard of care.

8. Merrill had arranged the Norma transaction at the impetus and behest of Magnetar, and Respondents knew that Magnetar picked NIR as the manager after Merrill proposed it for consideration. Both Merrill and Magnetar therefore were in a position to send NIR additional CDO business.

9. By March 2008 (a year after its closing), Norma had collapsed. Although Norma's investors lost more than $515 million, NIR received approximately $2 million in management fees, a portion of which flowed to Shannon and Parish individually.

B. Respondents

10. **Scott H. Shannon**, 50 and a resident of Charlotte, North Carolina, was one of NIR's two Managing Partners. By 2007, Shannon had 20 years of experience in structured and corporate finance. Shannon and his staff were primarily responsible for choosing Norma's RMBS assets.

11. **Joseph G. Parish III**, 57 and a resident of North Carolina, was NIR's other Managing Partner. By 2007, Parish had 28 years of experience in structured and corporate finance. Parish and his staff were primarily responsible for choosing Norma's CDO assets.

C. Other Relevant Entities

12. **NIR Capital Management, LLC** was an unregistered investment adviser based in Charlotte, North Carolina. During 2006 and 2007, NIR was the collateral manager for five

CDOs (totaling approximately $7.5 billion in assets under management), all arranged by Merrill. NIR was an affiliate of The NIR Group, LLC ("NIR Group"), which was formerly an investment management firm based in Roslyn, New York. Shannon and Parish ran all of NIR's day-to-day activities, including its investment-advisory function. Respondents were not involved in the activities of NIR Group other than their management of the assets of the CDOs.

13. **Merrill Lynch, Pierce, Fenner & Smith Incorporated**, the principal U.S. broker-dealer subsidiary of Merrill Lynch & Co., Inc., has been registered with the Commission since March 12, 1959. Merrill structured and marketed the Norma CDO and was one of the leading arrangers of CDOs between 2005 and 2008. On January 1, 2009, Merrill was acquired by Bank of America Corporation.

14. **Merrill Lynch International**, a Merrill affiliate incorporated under the laws of England, was the warehouse provider for Norma.

15. **Magnetar Capital LLC** is an asset manager headquartered in Evanston, Illinois. During 2006-2007 Magnetar was involved in creating a series of CDOs with various arranging banks and collateral managers. These CDOs were typically named after astronomical constellations, and so are sometimes known as "Constellation CDOs." At the time the RMBS and CDO assets were purchased, Magnetar had committed to purchasing $90 million worth of Norma's equity tranche. NIR was aware that Magnetar took $60 million in short positions on CDO assets into Norma's portfolio among the final pre-closing trades.[3] After the pre-close ramp was completed and without NIR's involvement, Merrill reduced the net cost of Magnetar's equity investment in Norma from $90 million to $39 million. Unknown to Respondents, Magnetar took an additional $20 million in short positions on CDO assets through Merrill into Norma's portfolio during the warehouse phase, and also took a short position on $5 million of securities issued by Norma itself.

16. **Norma CDO I Ltd.** was a special purpose vehicle incorporated in the Cayman Islands on December 7, 2006.

D. Facts

Background On CDOs and CDS

17. A CDO is a special purpose vehicle that issues debt to investors and uses the proceeds to invest in fixed income securities or loans. The CDO's debt is issued in different tranches that feature varying levels of risks and returns. The senior tranche is the highest rated, is first in the priority of repayment through what is called the CDO's waterfall and has the lowest risk of default. Because of the lower risk of default and the priority of repayment in the CDO's waterfall, the holders of the senior tranche have lower rates of return. The inverse is true for the lowest-rated tranche in the CDO. Typically, that tranche (usually referred to as "equity") is

[3] After Norma closed, Parish also allowed Magnetar to take an additional $8.9 million short position on a CDO that went into Norma's portfolio.

unrated, has the highest rate of return, is last in terms of the priority of repayment through the CDO's "waterfall" and has the highest risk of default.

18. A CDS is a type of derivative through which two parties transfer the risk of ownership of a particular reference obligation. The protection buyer ("short") of a CDS pays to purchase protection in the event of, *e.g.*, default, failure to pay interest, writedowns or substantial credit ratings downgrade of the reference obligation (collectively, "Credit Events"). The protection seller ("long") sells that protection and assumes the risk of a Credit Event on the reference obligation. In 2006, the protection buyer normally paid the protection seller a premium or spread as part of the CDS.[4] There are different types of reference obligations; the ones relevant here were RMBS or CDOs comprised of RMBS. In many respects, a CDS mimics the performance of the referenced asset. Thus, an investor can gain exposure to an asset by purchasing CDS that references the asset, instead of by purchasing the asset itself.

19. A CDO can be backed by bonds (a "cash CDO") or by CDS (a "synthetic CDO"). A CDO backed by both bonds and CDS is called a "hybrid CDO." Norma was a hybrid CDO. When fully ramped, Norma was comprised of approximately 95% synthetic assets.

20. Typically, a collateral manager would acquire synthetic collateral by sending out BWICs (or, bids wanted in competition) or responding to OWICs (or, offers wanted in competition) or broker/dealer axe sheets from the market ("axe" refers to a credit a broker/dealer has a particular interest in purchasing or selling). The winners of a BWIC process would be those counterparties who offered to pay the highest premiums to the CDO going long the asset. The inverse is true for an OWIC. The winner is the counterparty that agrees to accept the lowest premium for going long the referenced asset.

21. Because the acquisition of the collateral for a CDO takes time, a warehouse facility is normally opened at the arranging bank (here Merrill) for the benefit of the yet-to-be created CDO. A warehouse essentially is a designated account through which the bank finances the acquisition of collateral before the transaction closes. The bank purchases collateral upon the instruction of the collateral manager; the collateral is then placed in the warehouse facility for the benefit of the yet-to-be created CDO.

Roles Of NIR And Merrill

22. As collateral manager, NIR was the investment adviser for the Issuer, both selecting and managing a portfolio pursuant to a collateral management agreement with the Issuer.

23. In general, the collateral manager for a CDO determines which assets are appropriate for inclusion in a CDO's portfolio. A CDO transaction may or may not have a collateral manager. However, when a CDO is managed, the manager's independent selection of

[4] For example, a protection buyer may agree to pay a protection seller 150 basis points to purchase protection against default on a $10 million of a designated reference obligation, or $150,000 per annum, paid periodically.

assets is an important selling point to potential investors, and information about the collateral manager's selection process is included in marketing materials and the offering circulars by which the CDO's debt is sold.

24. Norma was structured and marketed by Merrill, which (as discussed) also acted as their warehouse lender.

Origin Of Norma

25. Norma came about because Magnetar, a prospective equity purchaser, approached Merrill in the spring of 2006 about arranging a series of CDOs that would meet certain of Magnetar's specifications so that Magnetar could purchase the equity in the resulting CDO. In industry parlance, this was a so-called "reverse inquiry" deal because it came about at the behest of an investor rather than an arranging bank or collateral manager. Magnetar approved NIR as the collateral manager for the Norma CDO after Merrill introduced NIR to Magnetar.

26. The equity piece of a CDO transaction was typically the hardest to sell and therefore the greatest impediment to closing a CDO. This was especially true by mid-2006 for CDOs linked to RMBS. Magnetar's willingness to buy the equity in a series of CDOs, including Norma, therefore gave it substantial leverage in these transactions.

27. Shannon and Parish understood that Magnetar was interested in "hedging" its investments in CDO equity with short positions on CDO debt. Respondents, therefore, should have realized that Magnetar's interests were not necessarily the same as those of potential investors in the debt tranches of Norma, whose investments depended solely on the CDO and its collateral performing well.

28. On or about August 17, 2006, NIR and Merrill entered into a warehouse agreement that, as is common with CDO warehouse agreements, gave NIR the responsibility to select and acquire collateral that, with Merrill's approval, would be warehoused at Merrill and ultimately included in the Issuer's portfolio at closing.

Assembly Of Norma's RMBS Portfolio

Magnetar And NIR Each Sourced Assets

29. During the summer of 2006, a representative of Magnetar ("Magnetar Representative") discussed with Respondents an investment product known as the ABX Index.[5]

[5] The ABX.HE was an index of RMBS names constructed by Markit Group Limited. The first ABX.HE Index was launched in January 2006. Dealers of subprime RMBS would select 20 different RMBS issued six months prior to the launch date with a new version of the index issued every six months. ABX.HE 2006-1 launched in January 2006 referencing 20 selected subprime RMBS issued in the second half of 2005. Each ABX.HE was actually five separate indices based on a tranche from each of the 20 subprime RMBS transactions related to the rating level of the tranche and then equally weighted in the index (*e.g.*, ABX.HE 2006-1 BBB contained the 20 "BBB" rated tranches from each of the selected subprime transactions).

The Magnetar Representative eventually asked that Respondents provide Magnetar a ranking of RMBS contained in the BBB rated ABX.HE 2006-1 and 2006-2 Indices (which will be referred to as the "2006 ABX Indices").

30. On August 16, 2006, Shannon, copying Parish, sent the Magnetar Representative an email attaching a "ranking" that divided the combined 40 bonds in the 2006 ABX Indices into what Shannon called "3 buckets based on our analysis of collateral, structure, performance, and issue/servicer."

31. In this email, Shannon described the buckets as follows (emphasis added):

> A) Top half: *these are the 20 bonds with the most appealing characteristics, and we would look to aggressively add these to the portfolio* assuming acceptable relative value. . . .
>
> B) Next 25%: *these 10 bonds are characterized by some weakness that would not disqualify them from purchase*, but would require some degree of enhanced premium for inclusion.
>
> C) Bottom 25%: *we would choose to stay away from these 10 bonds*, assuming that the market premium does not compensate for the heightened risk of default.

Respondents provided this analysis to the Magnetar Representative for informational purposes, not as a trading authorization.

32. On August 24, 2006, however, Parish emailed Shannon to say that a Merrill employee in the CDO group "left a voice message that the warehouse is open; she also noted that [Magnetar Representative] has done some index trades. Not sure what that means. . . . maybe he will ramp the deal for us." This last comment was a joke; as Parish (and Shannon) well knew, it was NIR's, not Magnetar's, job to "ramp" Norma, *i.e.*, to select and acquire collateral for the Norma warehouse.

33. However, as it turned out, in late August and early September 2006, the Magnetar Representative used the groupings in Shannon's "buckets" email to purchase $600 million worth of 2006 ABX Indices intended for Norma, which in effect caused Norma to take a long position on all 40 bonds on the 2006 ABX Indices at the BBB credit level. The Magnetar Representative subsequently caused Merrill to enter into separate CDS contracts by which Merrill took off-setting short positions on most or all of the 10 bonds that Shannon had put in the "bottom 25%" bucket.

34. The result intended by Magnetar and Merrill was for Norma to be long the 30 bonds in NIR's "top half" and "next 25%" groupings, and to have no net exposure to NIR's

"bottom 25%."[6] In total, Magnetar's purchases resulted in $472.5 million in long exposure (net the off-setting shorts) to the names on the 2006 ABX Indices, all intended for Norma.

35. Merrill never sent Respondents trade confirmations for the $600 million in long trades that the Magnetar Representative made, as required under the warehouse agreement. Thus Respondents, despite being the investment managers for Norma, were unaware of those trades. Consequently, beginning on August 17, 2006, Respondents set about independently assembling a portfolio for Norma.

36. As part of this process, among other things, Shannon and his team conducted credit analysis of potential collateral (over 2000 RMBS bonds), memorializing their results in continually updated lists of "acceptable" or "approved" RMBS bonds. Shannon primarily looked to and relied on the senior RMBS credit analyst at NIR ("Credit Analyst") to create the approved lists.

37. Using the approved lists, Shannon acquired assets in the marketplace. By November 9, 2006, NIR had caused the Norma warehouse to acquire $1.081 billion worth of synthetic RMBS collateral independently selected by Shannon and his team. $275 million of the synthetic RMBS collateral referenced 19 of the top 30 ABX names sent to Magnetar on August 16, 2006. Of that amount, only $150 million referenced bonds in the 2006 ABX Indices at the BBB credit level (and an additional $125 million referenced bonds in the 2006 ABX Indices at the BBB- credit level). This is in part because Shannon and his team did not find a number of bonds on the 2006 ABX Indices acceptable for purchase.

Shannon Accepted Magnetar's Purchases Despite Negative Credit Views

38. On or about November 9, 2006, Shannon and Parish learned from Merrill that Magnetar's trades were intended for Norma. Shannon and Parish were confused that a third party had purchased collateral for the portfolio.

39. As Norma's portfolio size was capped, it could not accommodate all of NIR's and Magnetar's trades.[7] Shannon attempted to determine which of the component parts of the Magnetar-acquired indices (meaning the individual names included in the 2006 ABX Indices) should stay in the portfolio and which should be eliminated by "shorting out" (*i.e.*, entering into offsetting trades on) the unwanted assets.

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[6] Magnetar did not fully offset all of the long exposure to the 10 bonds in the "bottom 25%," leaving $22.5 million in long exposure to four of the bonds. As discussed below, when Norma closed, this $22.5 million of exposure remained.

[7] Respondents and Merrill eventually came up with the solution to create a new CDO – known as Fourth Street Funding, Ltd. ("Fourth Street") – to house the excess collateral. To "accommodate" Magnetar's purchases, Respondents and Merrill moved $260 million in RMBS collateral that NIR actually selected for Norma from that warehouse into a later-created Fourth Street warehouse.

40. Starting on November 13, 2006, Shannon categorized (in a spreadsheet that Parish sent to Merrill, copying Shannon, on that same day) $82.5 million of Magnetar's index purchases as "short." On that same day, Shannon wrote to the Credit Analyst:

> This is a long story which I'll fill you in on later, but I need to get your confirmation that the "Long" index names [*i.e.*, bonds] I listed below are OK for us to invest, while the "Short" are deals we want to stay away from . . . . The short story is that we have the opportunity to pull in names from the index to fill out our ramp (part of Magnetar hedging strategy), and I created the list below based on what we had already invested in, plus names on the Approved List that we didn't hit due to tight spread levels. Concentrations are not an issue, at least in this preliminary view. Please let me know if you would change any of these. Pretty timely.

41. On November 16, 2006, Shannon wrote Parish, "Do you want to give [Merrill] an indication of which names we would want to short?", to which Parish responded, "[Merrill] told [u]s to work it through [Magnetar]. We should compile a list of required short positions . . . ." On November 17, 2006, Shannon wrote to the Credit Analyst, "I created the attached based on what you gave me last night. Just would like you to confirm this is accurate prior to forwarding to Merrill." In the attached spreadsheet, Shannon now identified $127.5 million in Magnetar's index purchases (including the $82.5 million from the November 13 list) as "short." Later that day, Shannon sent the same spreadsheet to Parish: "See attached for listing of long, shorts."

42. On November 21, 2006, Shannon, copying Parish, sent Merrill a "portfolio report . . . to reconcile the long/short Index positions." The report classified the forty RMBS underlying Magnetar's ABX purchases as either "long," "fence," or "nuetral" [sic]. The "neutral" [sic] category consisted of $67.5 million of exposure (including the $22.5 million discussed in paragraph 48 below) that Shannon wanted to neutralize by shorting. The "fence" category consisted of an additional $90 million of exposure that Shannon was on the fence about ($60 million of which Shannon previously marked as "short" on November 17).

43. By late November 2006, Shannon accepted the collateral Magnetar had selected. On November 28, 2006, Shannon, without copying Parish, wrote to the Credit Analyst (emphasis added): "Long story short, it looks like the plan had always been to include the 30 names in the index that we said were acceptable, and not include the bottom 10. *This will pick up some bonds that we would not otherwise have bought based on recent performance, but they will be in the portfolio*."

44. Shannon continued:

> Magnetar bought all the names in the index, so we have excess concentrations in a number of names that would either stay in the

> deal, or seed a new mez[zanine] deal[8] . . . . Communication between us, Magnetar, and Merrill [has] not been very effective . . . .

45. Shannon followed up in a December 3, 2006 email, again without copying Parish, to the Credit Analyst (emphasis added):

> Perhaps you could . . . *let me know the deals [i.e., RMBS bonds] in norma that we should be prepared to defend based on recent performance* . . . .
>
> As I believe I mentioned last week, the final portfolio includes a number of index trades we did not execute, as we are long the 30 names we initially indicated to Magnetar were acceptable. *This leaves us with several names we probably would not want* such as rasc deal and mabs deal, but we also picked up a number of good ones such as ramp EFc and ffml.

46. In total, in November 2006 NIR ultimately incorporated into the portfolio at least $67.5 million, and as much as $157.5 million, in collateral that Shannon had sought to exclude.

47. In December 2006, NIR and Merrill entered into a warehouse agreement for Fourth Street, the new CDO that would house the excess collateral resulting from Magnetar's competing purchases. In January 2007, Respondents and Merrill moved $260 million worth of synthetic RMBS assets and $28 million of CDO assets that Respondents had independently selected for Norma months earlier from the Norma warehouse into the Fourth Street warehouse.

Norma Closed With RMBS Assets Shannon Did Not Want

48. As the March 1, 2007 closing date for Norma approached, Shannon continued to try to exclude certain bonds from the portfolio, including the $22.5 million in long exposure that Magnetar did not fully short out from the August 2006 "bottom 25%" bucket. For example, on February 23, 2007, Shannon, copying Parish, sent an email to Merrill employees with the subject heading "Non-inclusion of several bonds into Norma." Seeking to have Merrill at least eliminate Norma's remaining $22.5 million exposure to four bonds that NIR initially ranked at the bottom, Shannon noted in pertinent part: "we don't want to be long these bonds."

49. After Merrill relayed Shannon's concerns to Magnetar, the Magnetar Representative responded to both Merrill and Parish, "As we discussed, think we should close the deal [with the $22.5 million], then see what combo of stuff we can trade . . . and those names we need to hedge. Some of those will be super difficult to trade right now."[9] The $22.5 million

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[8] The new transaction was Fourth Street. *See* footnote 7 above.

[9] A day later, Shannon noted in an email to the Credit Analyst: "We really don't want to be long those 22.5mm bonds, but if we short now without corresponding purchase of additional bonds at wider spreads, we would

– along with the other Magnetar purchases that Shannon had sought to short out – was in Norma's closing portfolio.

Assembly Of Norma's CDO Bucket

50. Parish allowed Magnetar to be involved in the form and selection of CDO assets acquired for Norma. As a result, Parish knew that Magnetar was the short counterparty for much of Norma's synthetic exposure to CDO securities (and, unknown to Respondents, Magnetar was the short counterparty on nearly all of that synthetic exposure through Merrill).

51. Parish began work on Norma's $150 million "CDO bucket" in mid-September 2006. Before purchasing any CDO securities, Parish reached out to the Magnetar Representative on September 18, 2006: "not sure if you consider exposure to your CDOs [i.e. Constellation CDOs] to be redundant or not. Let me know either way." The Magnetar Representative responded: "I actually prefer to have my CDOs in the portfolio. Whether or not you buy the cash, I will do CDS [that is, be the short counterparty] with you in whatever size you need."

52. On November 27, 2006, Parish, copying Shannon, sent the Magnetar Representative a summary of securities acquired or pending for Norma's CDO bucket (totaling $118 million). The Magnetar Representative responded to Parish and Shannon, copying several Merrill employees:

> First of all, I'm starting to feel like I'm not seeing any of the trade approval requests. I should be on the regular distribution list for those, resi [RMBS], CDO or anything else (especially anything else!), as I'm sure has been discussed.
>
> Second, I definitely want to approve any CDO's that go in the deal, don't recall approving any, so I assume "Approved" means only that NIR has internally approved the credit.
>
> For [the three *non*-Constellation CDOs that NIR had acquired in cash form], I only want them in the deal if I'm buying the protection [*i.e.*, if Magnetar can short them synthetically], absolutely do NOT want any of those three bonds in the deal as cash bonds.

53. In a further email to Parish, the Magnetar Representative continued to assert his "rights": "just wanted to put my foot down with ML on stuff going in warehouse without my approval. Technically, I have approval rights on resi [RMBS], but on CDO's it has always been very clear that I want to be involved from the beginning." Parish and the Magnetar

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be in violation of [a] test [referring to a credit rating agency-imposed hedge test]." Shannon also referred to one of these RMBS bonds as a "real stinker."

Representative agreed to a telephone call, with Parish noting: "We can review the portfolio and get clear on any mixed signals."

54. After this, Parish accommodated Magnetar's preferences. In particular, in November 2006, Parish and Magnetar jointly worked with Merrill on the CDO bucket and made the following changes:

- removed one $7.5 million non-Constellation CDO that NIR had acquired in cash form;
- changed the form of two non-Constellation CDOs from cash to synthetic form (with Magnetar as the short counterparty),[10] which increased the size of the CDO bucket by $9.5 million; and
- cancelled an order for a cash Constellation CDO and replaced it with a new order for the same CDO in synthetic form (with Magnetar as the short counterparty) for the same amount.

55. In December 2006, NIR acquired exposure to two additional CDOs. One was a Constellation CDO in synthetic form (again, with Magnetar as the short counterparty) and one was a non-Constellation cash CDO that the Magnetar Representative approved for consideration.

56. When fully ramped prior to closing, Norma had six cash CDO positions totaling $57.5 million (five of which were bonds from other Constellation CDOs), and seven synthetic CDO positions totaling $85 million (five of which were on other Constellation CDOs). Known to Parish, Magnetar was the short counterparty on four of the synthetic positions, meaning that Magnetar had a $60 million short position opposite Norma's CDO assets. (Unknown to Respondents, Magnetar took an additional $20 million in short positions on CDO assets through Merrill into Norma's portfolio.) After Norma closed, Parish also allowed Magnetar to take an additional $8.9 million short position on a CDO that went into Norma's portfolio.

57. Magnetar's undisclosed involvement in the assembly of the CDO bucket disadvantaged Norma and its investors. The synthetic CDO securities that Magnetar demanded in place of cash CDO securities had an "implied writedown" feature that obligated Norma, as the long counterparty, to pay the short counterparty when certain contractually specified events short of default occurred. This feature caused Norma to suffer losses more quickly than it would have if it owned the CDO securities in cash form.

[10] Parish at one point asked the Magnetar Representative if he would be "opposed" to NIR bringing back a cash component to one of the CDO securities and the Magnetar Representative responded, "Afraid so, [that CDO] in particular I don't want the cash in there."

Shannon And Parish Misled Their Advisory Client, The Issuer

58. Shannon and Parish each received $116,553 out of NIR's $2.2 million management fee for Norma. NIR's client, the Issuer, however, knew nothing about Magnetar's involvement in collateral selection or about Respondents' compromised decision-making.

59. In the Collateral Management Agreement for Norma (which Shannon signed on behalf of NIR), NIR represented to the Issuer that all collateral purchased for the Issuer on or before the closing date "satisf[ied] all of the terms and conditions applicable to such purchases as set forth" in the Collateral Management Agreement. And in the Collateral Management Agreement, NIR undertook to:

> act in good faith and exercise reasonable care, using a degree of skill and attention no less than that which [NIR] exercises with respect to comparable assets that it manages for itself and, without limiting the foregoing, in a commercially reasonable manner consistent with accepted practices and procedures applied by reasonable and prudent institutional managers of national standing in connection with the management of assets of the nature and character of [Norma's collateral] . . . . To the extent not inconsistent with the foregoing, [NIR] shall follow its customary standards, policies and procedures in performing its duties [as Collateral Manager].

60. These representations were materially false or misleading in that Respondents departed from the required level of care and from NIR's customary standards, policies and procedures when Respondents allowed Norma to acquire assets that Magnetar, not NIR, had initially chosen and that Shannon would have preferred to exclude from the portfolio.

E. Violations

61. As a result of the negligent conduct described above, Respondent Parish willfully[11] violated Section 206(2) of the Advisers Act, which prohibits "engag[ing] in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client."[12]

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[11] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing. It does not mean that, in addition, he must suppose that he is breaking the law.'" *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 violating one of the Rules or Acts.'" *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

[12] Unlike Section 206(1) of the Advisers Act which requires proof of scienter, Section 206(2) of the Advisers Act 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, 194-95 (1963).) *See also SEC v. Wash. Inv. Network*, 475 F.2d 392, 396 (D.C. Cir. 2007).

62. As a result of the conduct described above (which at a minimum was reckless), Respondent Shannon willfully violated Sections 206(1) and 206(2) of the Advisers Act. Section 206(1) of the Advisers Act prohibits "employ[ing] any device, scheme, or artifice to defraud any client or prospective client."

F. Undertakings

63. Respondents have undertaken to dissolve NIR Capital Management, LLC within seventy-five (75) days upon the issuance of this Order. Within ten (10) days of such action, Respondents shall certify to the staff that NIR Capital Management, LLC has been dissolved.

64. In determining whether to accept this Offer, the Commission has considered these undertakings.

IV.

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

Accordingly, pursuant to Sections 203(f), 203(k), 203(i), and 203(j) of the Advisers Act and Sections 9(b), 9(d), and 9(e) of the Investment Company Act, it is hereby ORDERED that:

A. Respondent Shannon cease and desist from committing or causing any violations and any future violations of Sections 206(1) and (2) of the Advisers Act, and Respondent Parish cease and desist from committing or causing any violations and future violations of Section 206(2) of the Advisers Act.

B. Respondent Shannon be, and hereby is:

barred from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization; and

prohibited from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter;

with the right to apply for reentry after two (2) years to the appropriate self-regulatory organization, or if there is none, to the Commission.

C. Any reapplication for association by Respondent Shannon will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered

against Respondent Shannon, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

D. Respondent Parish be, and hereby is:

suspended from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization for a period of 12 months, effective on January 1, 2014; and

prohibited from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter for a period of 12 months, effective on January 1, 2014.

E. Respondent Shannon shall, within ten (10) business days of the entry of this Order, pay disgorgement of $116,553 and prejudgment interest of $24,109 and a civil money penalty in the amount of $116,553 (for a total payment of $257,215) to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 and 31 U.S.C. § 3717.

Respondent Parish shall, within ten (10) business days of the entry of this Order, pay disgorgement of $116,553 and prejudgment interest of $24,109 and a civil money penalty in the amount of $75,000 (for a total payment of $215,662) to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 and 31 U.S.C. § 3717.

Payment must be made in one of the following ways:

(1) 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

(2) 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 Shannon and Parish as Respondents 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 Andrew M. Calamari, Director, New York Regional Office, Securities and Exchange Commission, 3 World Financial Center Suite 400, New York, NY 10281.

By the Commission.

Elizabeth M. Murphy
Secretary