SECURITIES AND EXCHANGE COMMISSION

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Unless otherwise noted, each of the following individual Members of the Commission voted affirmatively upon each action of the Commission shown in the file:

CHRISTOPHER COX, CHAIRMAN

PAUL S. ATKINS, COMMISSIONER

ROEL C. CAMPOS, COMMISSIONER

ANNETTE L. NAZARETH, COMMISSIONER

KATHLEEN L. CASEY, COMMISSIONER

33 Documents

Commissioner Nazareth
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55688 / May 1, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12623

In the Matter of **Shoreland Trading, LLC,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Shoreland Trading, LLC ("Shoreland" 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, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

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

1. Shoreland is a broker-dealer registered with the Commission.

Document 1 of 33

2. On February 6, 2007, a judgment was entered by consent against Shoreland, permanently enjoining it from future violations of Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in the civil action entitled Securities and Exchange Commission v. K.L. Group, LLC, et al., Civil Action Number 05-80186-Civ-RYSKAMP/VITUNAC in the United States District Court for the Southern District of Florida.

3. The Commission's complaint in the civil action alleged that Shoreland and other defendants fraudulently overstated the value of investors' accounts and the profitability of their trades, while concealing trading losses.

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, it is hereby ORDERED:

Pursuant to Section 15(b) of the Exchange Act, Respondent Shoreland's registration with the Commission be, and hereby is, revoked.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

Chairman Cox
Not Participating

SECURITIES EXCHANGE ACT OF 1934
Release No. 55696 / May 2, 2007

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2605 / May 2, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12627

In the Matter of **Terry M. Phillips,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against Terry M. Phillips ("Phillips" 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 him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

Document 2 of 33

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

A. RESPONDENT

Phillips, 48, of Midlothian, Virginia, is the founder, 20 percent owner and principal operator of Capitol Distributing, L.L.C. ("Capitol") and the founder and 50 percent owner of Phillips Land Company ("PLC").

B. RELEVANT ENTITIES

1. **Capitol** is a privately-owned video game distributor organized as a limited liability company under the laws of the Commonwealth of Virginia. It was founded by Phillips in 1999. During the relevant period, Capitol had approximately ten employees.

2. **PLC** is a Virginia company 50 percent owned and principally operated by Phillips, has no employees and, in the ordinary course of business, has no involvement in the purchase, sale, or distribution of video games.

3. **Take-Two Interactive Software, Inc. ("Take-Two")** is a Delaware corporation headquartered in New York, New York. Take-Two develops, markets and publishes interactive entertainment software games for the personal computer as well as video game consoles. Since July 31, 2006, Take-Two's common stock has been registered with the Commission pursuant to Section 12(b) of the Exchange Act and currently trades on the NASDAQ NMS under the symbol "TTWO."

C. SUMMARY

Take-Two and certain of its officers committed numerous violations of the anti-fraud, financial reporting and recordkeeping provisions of the federal securities laws to inflate reported revenue during fiscal years 2000 and 2001.[2] Phillips was a cause of some of those violations which resulted from certain transactions between Take-Two, Capitol and PLC. Specifically, in four separate transactions with Capitol during that period, Take-Two fraudulently recorded as sales approximately $15 million in revenue

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[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.

[2] On June 1, 2005, the Commission authorized and simultaneously settled civil actions in federal court against Take-Two and several present and former members of senior management, obtaining injunctions, disgorgement, civil penalties, and officer and director bars. The Commission also authorized, and simultaneously settled, an administrative cease-and-desist proceeding against one officer and a Rule 102(e)(3) administrative proceeding against the former Chief Financial Officer.

from shipments of games to Capitol that Capitol parked and subsequently returned without making any effort to sell. In two of the transactions, Capitol created invoices falsely describing the returns as "purchases" of "assorted product" by Take-Two from PLC. In those two transactions, Take-Two also provided the funds to Capitol or PLC that those entities then used to cover checks they wrote to Take-Two to purportedly "pay" for the games.

Based on his participation in certain aspects of these transactions, Phillips was a cause of Take-Two's violations of Sections 10(b), 13(a) and 13(b)(2)(A) of the Exchange Act and Exchange Act Rules 10b-5, 12b-20, 13a-1, 13a-13 and 13b2-1.[3]

D. FACTS

1. From October 31, 2000 through at least July 31, 2001, Capitol accepted several hundred thousand video games from Take-Two with the understanding that it would temporarily warehouse or "park" the games until a subsequent Take-Two reporting period, and then return the games to Take-Two. Take-Two improperly recorded and reported approximately $15 million in revenue associated with these parking transactions.

2. Phillips and Take-Two began discussing Capitol's participation in the parking arrangement in July 2000. In an e-mail dated July 25, 2000, Phillips explained to two Capitol employees that "we can take whatever [Take-Two] needs to ship . . . [I]f it is a huge amount we will need to find someplace to stick it . . . but it shouldn't be a problem."

3. In October 2000, Take-Two discussed the first parking transaction with Phillips. A Take-Two representative asked Phillips if he had another company that Take-Two could issue a purchase order to for the games in lieu of Capitol sending the games back as a return. Phillips mentioned PLC. Phillips instructed a Capitol employee to work out the details with the Take-Two representative.

4. On October 31, 2000, the last day of Take-Two's fiscal year, Capitol accepted shipment of 230,000 video games from Take-Two with the understanding that Capitol would park them for a short time and then return the shipment to Take-Two. The games shipped to Capitol were selected by Take-Two based on Take-Two's warehouse inventory at the time. Capitol had no input regarding the games it accepted. Take-Two improperly recorded $5.4 million as revenue from the shipment – the most revenue from a single sale that Take-Two had recognized up to that time.

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[3] Simultaneously with the issuance of this Order, Phillips, without admitting or denying the allegations of the complaint, has consented to a judgment in an action filed against Phillips and Capitol in the United States District Court for the District of Columbia ordering him to pay a civil penalty in the amount of $50,000.

5. Phillips knew that Capitol made no effort to sell the games. Instead, Capitol returned all 230,000 games to Take-Two over the next two reporting periods. When the games were returned, Capitol provided Take-Two with invoices that falsely described the games as purchases of "assorted product" from Phillips' company PLC. Take-Two used those invoices to conceal in its books and records the fact that the October 31, 2000 "sale" had been returned in its entirety. PLC had no employees, no inventory, and did not distribute video games in the ordinary course of business.

6. Take-Two provided Capitol or PLC with money to make purported "payments" for the games to bolster the appearance that the shipments to Capitol were legitimate sales. For example, on December 20, 2000, Take-Two wired $2,557,239 to PLC. Six days later, PLC sent Take-Two a check for $2,557,137, purportedly in partial payment for the games associated with the October 31, 2000 transaction.

7. On February 28, 2001, Capitol accepted a second shipment of approximately 175,000 video games from Take-Two. Take-Two improperly recorded the transaction as a $4.6 million sale – second in revenue only to the October 31, 2000 transaction in Take-Two's history up to that time. All 175,000 games were subsequently returned to Take-Two with invoices that again falsely described the return as a purchase of "assorted product" from PLC. Capitol again used funds provided by Take-Two to purportedly "pay" for the games. Take-Two wired Capitol $4,594,100 on April 26, 2001 and Capitol sent Take-Two a check for the same amount the next day.

8. On April 27, 2001, three days before the end of Take-Two's second fiscal quarter, Capitol accepted approximately 55,000 games from Take-Two. Take-Two recorded $1.76 million as revenue from the purported sale. After the end of the quarter, Capitol returned all these games to Take-Two.

9. On July 31, 2001, the last day of Take-Two's third fiscal quarter, Capitol accepted a shipment of more than 85,000 games from Take-Two. Take-Two recorded more than $3 million as revenue from the purported sale. After the end of the quarter, Capitol returned all these games to Take-Two.

E. <u>LEGAL ANALYSIS</u>

Section 21C(a) of the Exchange Act specifies that a respondent is a cause of another's violation if the respondent knew or should have known that his act or omission would contribute to such violation.

Section 10(b) of the Exchange Act and Rule 10b-5 thereunder proscribe a variety of fraudulent practices. An issuer or individual may violate these provisions by either intentionally or recklessly making materially false or misleading statements in connection with the purchase or sale of securities. *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988). To violate Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, a defendant must act with scienter, *Aaron v. SEC,* 446 U.S. 680, 695, 701-02 (1980), which the Supreme Court has defined as "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n. 12 (1976). Scienter of a company's management is imputed to the company. *See, e.g., SEC v. Manor Nursing Centers*, 458 F.2d 1082, 1089-96 (2d Cir. 1972).

Take-Two violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by using the transactions with Capitol to materially inflate its operating results, and by filing and releasing to the public periodic reports, registration statements and press releases that were materially false and misleading, and that misrepresented Take-Two's financial condition. Based on his conduct described above, Phillips was a cause of Take-Two's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Section 13(a) of the Exchange Act and Exchange Act Rules 13a-1 and 13a-13 thereunder require all issuers with securities registered under Section 12 of the Exchange Act to file annual and quarterly reports on Forms 10-K and 10-Q respectively. Exchange Act Rule 12b-20 requires that, in addition to the information expressly required to be included in such reports, the issuer include such additional material information as may be necessary to make the required statements, in light of the circumstances under which they were made, not misleading. The obligation to file these periodic reports includes the obligation to ensure that they are complete and accurate in all material respects. *See, e.g., SEC v. Savoy Indus., Inc.*, 587 F.2d 1149, 1165 (D.C. Cir. 1978), *cert. denied,* 440 U.S. 913 (1979). No showing of scienter is required to establish violations of these provisions. *Id.* at 1167. Information regarding the financial condition of a company is presumptively material. *SEC v. Blavin,* 760 F.2d 706, 711 (6th Cir. 1985).

Take-Two violated Section 13(a) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1 and 13a-13 thereunder when, as a result of the parking transactions with Capitol described above, it filed with the Commission materially false and misleading annual reports on Forms 10-K for the fiscal years ending October 31, 2000 and October 31, 2001, and quarterly reports on Forms 10-Q for the quarters ending April 30, 2001 and July 31, 2001, which contained inflated operating results. Based on his conduct described above, Phillips was a cause of Take-Two's violations of Section 13(a) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1 and 13a-13 thereunder.

Section 13(b)(2)(A) of the Exchange Act requires issuers to "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer." Exchange Act Rule 13b2-1 prohibits direct or indirect falsification or causing falsification of books, records, or accounts subject to Section 13(b)(2)(A). No showing of scienter is required to establish violations of Exchange Act Section 13(b)(2)(A) (*see SEC v. World-Wide Coin Investments, Ltd.*, 567 F. Supp. 724, 749 (N.D. Georgia 1983)) or Exchange Act Rule 13b2-1 (*see SEC v. McNulty*, 137 F.3d 732, 740-41 (2d Cir. 1998)).

Take-Two failed to make and keep accurate books, records and accounts with respect to its transactions with Capitol. It also used those transactions to falsify its books and records. Based on his conduct described above, Phillips was a cause of Take-Two's violations of Section 13(b)(2)(A) of the Exchange Act and Exchange Act Rule 13b2-1.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Phillips' Offer.

Accordingly, it is hereby ORDERED that:

Pursuant to Section 21C of the Exchange Act, Respondent Phillips shall cease and desist from committing or causing any violations and any future violations of Section 10(b) of the Exchange Act and Exchange Act Rules 10b-5 and 13b2-1; and from causing any violations and any future violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1 and 13a-13.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Cox and Commissioner Nazareth Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55692 / May 2, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12624

In the Matter of **A.G. EDWARDS & SONS, INC.,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against A.G. Edwards & Sons, Inc. ("AG Edwards" 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 Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

[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.

Document 3 of 33

Respondent

1. AG Edwards is a Delaware corporation with headquarters located in St. Louis, Missouri. AG Edwards has been registered with the Commission as a broker-dealer pursuant to Section 15 of the Exchange Act since 1967 and is a member of the National Association of Securities Dealers, Inc. ("NASD") and the New York Stock Exchange ("NYSE"). It has approximately 730 offices staffed by approximately 6,824 registered representatives, referred to at AG Edwards as "financial consultants" ("FCs"), that provide retail brokerage services throughout the United States, Switzerland and the United Kingdom. AG Edwards is the principal operating subsidiary of A.G. Edwards, Inc., a Delaware corporation whose stock is traded on the NYSE under the symbol AGE.

Background

2. Between at least January 2001 and September 2003, AG Edwards failed reasonably to supervise certain of its registered FCs with a view to preventing their violations of the federal securities laws. During the relevant time period, registered FCs in several of AG Edwards' branch offices engaged in illegal market timing schemes on behalf of customers, including several large hedge funds.[2] These FCs defrauded over 200 mutual funds from approximately 50 different mutual fund companies and their shareholders by engaging in deceptive practices designed to circumvent restrictions that the mutual funds imposed on market timing. Through these activities the FCs violated the antifraud provisions of the federal securities laws.

3. AG Edwards failed reasonably to supervise its FCs with a view to detecting and preventing their illegal market timing schemes. AG Edwards failed to adopt reasonable policies, procedures or systems to monitor market timing in order to detect and prevent its FCs' misconduct. In particular, AG Edwards failed to develop reasonable policies, procedures or systems for monitoring and responding to red flags indicating that its FCs were using deceptive practices. In addition, AG Edwards failed to implement reasonable policies, procedures or systems to monitor whether its FCs discontinued their abusive trading in response to requests by mutual fund companies.

The FCs' Misconduct

4. Between at least January 2001 and September 2003, certain of AG Edwards' registered FCs opened accounts for customers who planned to place market timing trades.

5. The majority of these accounts were fee-based accounts in AG Edwards' Fund Navigator program, later called the Preferred Fund Advisor program. Customers with

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[2] "Market timing" refers to (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal *per se*, can harm other mutual fund shareholders because it can dilute the value of their shares if the market timer is exploiting pricing inefficiencies, disrupt the management of the mutual fund's investment portfolio or cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

fee-based accounts did not pay commissions to AG Edwards and its FCs for each transaction placed in their accounts. Instead, these customers paid AG Edwards a quarterly fee ranging from 1% to 1.5% of the total assets in the account. During the relevant time period, AG Edwards received approximately $1.93 million in fees from certain market timing customers.

6. Between at least January 2001 and September 2003, certain of AG Edwards' FCs placed tens of thousands of trades on behalf of their market timing customers. Most of these trades were in mutual funds that prohibited or specifically limited the number and frequency of trades in an effort to prevent market timing.

7. Over time, AG Edwards received hundreds of telephone calls, letters, e-mails and canceled trade notices (collectively "restriction notices") from mutual fund companies objecting to market timing trades placed by AG Edwards' FCs. The restriction notices informed AG Edwards that the fund companies rejected particular trades or restricted particular accounts, customers or FCs, either by FC name or by FC identification number, because they appeared to be market timing. Some restriction notices also warned AG Edwards that particular customer accounts were close to reaching their limits for trading. Many of the mutual fund companies who sent restriction notices to AG Edwards requested AG Edwards' assistance in helping them prevent further market timing by particular FCs, FC identification numbers, customers or accounts.

8. The majority of the written restriction notices were sent to the mutual fund order room at AG Edwards' headquarters in St. Louis, Missouri. As the restriction notices came in, employees in the order room updated AG Edwards' trading system to reflect canceled trades and then sent copies of the restriction notices to the FCs and branches involved in the trading and maintained the originals. AG Edwards, however, failed to develop reasonable policies, procedures or systems to monitor whether its employees followed up on the mutual fund companies' restriction notices and requests for assistance in preventing further market timing by particular FCs, customers or accounts.

9. In order to continue market timing on behalf of their customers after receiving copies of the restriction notices, certain FCs engaged in a series of acts and practices designed to conceal their customers' market timing activity from mutual fund companies that prohibited or restricted the trading. These acts and practices included: 1) using multiple account numbers for the same customer; 2) opening accounts in the names of multiple entities affiliated with the same customer; 3) opening accounts at different branch offices for the same customer; 4) placing trades using multiple FC identification numbers; and 5) transferring assets between related accounts.

10. By using these acts and practices, certain FCs disguised their own identities and the identities of their market timing customers and disguised the fact that multiple short-term trades were attributable to the same customers. Through these deceptive tactics, certain FCs enabled their market timing customers to continue trading with mutual funds that previously restricted their market timing activities.

AG Edwards' Supervisory Failures

11. At all relevant times, AG Edwards required its branch managers to approve FCs' requests to open new accounts for customers. Branch managers in several of AG Edwards' branches regularly approved the opening of new accounts for AG Edwards' market timing customers. These customers had multiple accounts through which AG Edwards' FCs were able to place the customers' market timing trades and evade restrictions imposed by mutual fund companies.

12. AG Edwards issued each of its registered FCs one unique identification number through which to place trades on behalf of customers. However, FCs could obtain additional FC identification numbers with which they could place trades by entering into a "split" with one or more other FCs. At all relevant times, AG Edwards required its FCs to submit requests for new split FC numbers to its registrations department in St. Louis, Missouri. A legitimate reason for an FC to request a new split FC number was to share commissions and fees with one or more additional FCs who serviced the same client.

13. In contrast, certain of AG Edwards' FCs regularly obtained additional split FC numbers not for the purpose of legitimately sharing commissions and fees with other FCs for servicing particular customer accounts, but instead to continue market timing mutual funds that previously restricted them from trading under other FC numbers and split FC numbers. Because many mutual fund companies restricted further trading by FC numbers rather than by FC names, these FCs were able to evade restrictions imposed by mutual fund companies by obtaining new split FC numbers.

14. During the Fall of 2002, a senior vice president in AG Edwards' operations department learned about the existence of the restriction notices from employees in AG Edwards' order room. At this time, this senior vice president and other officers and employees convened a working group to research whether AG Edwards should allow market timing to continue to occur at AG Edwards.

15. Between October 2002 and April 2003, the working group gathered restriction notices and identified many of the customers, FCs and branches that placed market timing trades through accounts at AG Edwards. In April 2003, the working group issued a report to members of AG Edwards' senior management detailing the extent of the continuing market timing at the firm and recommending that AG Edwards take steps to prevent any further market timing from occurring.

16. Notwithstanding the working group's report, AG Edwards did not develop or implement any policies or sufficient procedures to address the market timing activity at the firm until at least September 2003.

17. Starting in September 2003, AG Edwards began taking certain remedial actions to address market timing, including: adopting a policy to prohibit market timing activity through AG Edwards; and adopting and implementing new supervisory and operational procedures designed to detect and prevent mutual fund market timing.

18. Thus, between at least January 2001 and September 2003, AG Edwards failed reasonably to supervise certain of its FCs with a view to detecting and preventing their violations of the antifraud provisions of the Securities Act of 1933 ("Securities Act") and the Exchange Act. In particular, AG Edwards failed to adopt or implement reasonable supervisory and compliance policies, procedures or systems that could have detected or prevented its FCs' deceptive market timing schemes. AG Edwards failed to have reasonable policies, procedures or systems to monitor whether multiple accounts and multiple split FC numbers were used for legitimate purposes, rather than to conceal the FCs' identities and the identities of their market timing customers from mutual fund companies that restricted their market timing. In addition, AG Edwards failed to have reasonable policies, procedures or systems in place for employees to respond to red flags and warnings of improper conduct in the form of hundreds of restriction notices from mutual fund companies objecting to the market timing activity. If AG Edwards had had in place reasonable policies, procedures or systems to monitor its FCs' use of multiple account numbers and split FC numbers and provided guidance to its employees on responding to restriction notices, it is likely that AG Edwards could have detected and prevented the FCs' violations of the antifraud provisions of the Securities Act and the Exchange Act.

Violations

19. As a result of the conduct described above, certain of AG Edwards' FCs willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder which prohibit fraudulent conduct in connection with the offer, purchase or sale of securities.

Failure to Supervise

20. Section 15(b)(4)(E) of the Exchange Act provides for the imposition of a sanction against a broker or dealer who "has failed reasonably to supervise, with a view to preventing violations of the securities laws, another person who commits such a violation, if such other person is subject to [its] supervision." As a result of the conduct described above, AG Edwards failed reasonably to supervise its FCs with a view to preventing their willful violations of the federal securities laws.

Undertakings

21. AG Edwards undertakes the following:

a. AG Edwards shall retain, within 60 days of the date of entry of this Order, the services of an Independent Consultant not unacceptable to the staff of the Commission. AG Edwards shall exclusively bear all costs, including compensation and expenses, associated with the retention of the Independent Consultant. AG Edwards shall retain the Independent Consultant to: 1) conduct a review to determine whether the changes AG Edwards has adopted and implemented to its policies and procedures to correct the activities described in this Order are reasonably designed to detect and prevent any future market timing by AG Edwards' registered FCs on behalf of their customers and to ensure compliance with Section 15 of the Exchange Act; 2) determine whether and to what extent there is a need for additional or amended policies and procedures to detect and prevent market timing by AG Edwards' registered FCs on behalf of their customers and to ensure compliance with Section 15 of the Exchange Act; and 3) recommend that AG Edwards adopt such additional policies and procedures as the Independent Consultant believes are necessary to provide reasonable assurances that AG Edwards can detect and prevent market timing by AG Edwards' registered FCs on behalf of their customers.

b. AG Edwards shall cooperate fully with the Independent Consultant and provide the Independent Consultant with access to its files, books, records and personnel as reasonably requested for the Independent Consultant's review.

c. AG Edwards shall further retain the Independent Consultant to, at the conclusion of the review, which in no event shall be more than 180 days after the date of entry of this Order, submit to AG Edwards and to the Commission's staff a written Report regarding AG Edwards' compliance with its policies and procedures and the adequacy of those policies and procedures. The Report shall include a description of the review performed, the conclusions reached and, if necessary, recommendations for changes in or improvements to the policies and procedures and a procedure for implementing the recommended changes or improvements.

d. Within 30 days of receipt of the Independent Consultant's Report, AG Edwards shall adopt all recommendations contained in the Report and remedy any deficiencies in its policies and procedures; provided, however, that as to any recommendation that AG Edwards believes is unnecessary or inappropriate, AG Edwards may, within 30 days of receipt of the Report, advise the Independent Consultant and the Commission's staff in writing of any recommendations that it considers to be unnecessary or inappropriate. With respect to any recommendation that AG Edwards considers unnecessary or inappropriate, AG Edwards shall propose in writing an alternative policy, procedure or system designed to achieve the same objective or purpose.

e. With respect to any recommendation with which AG Edwards and the Independent Consultant do not agree, AG Edwards shall attempt in good faith to reach an agreement with the Independent Consultant within 45 days of receipt of the Report. In the event that AG Edwards and the Independent Consultant are unable to agree on an alternative proposal acceptable to the Commission's staff, AG Edwards will abide by the original recommendation of the Independent Consultant.

f. Within one year after the date of entry of this Order, AG Edwards shall submit an affidavit to the Commission's staff stating that it has implemented any and all recommendations of the Independent Consultant, or explaining the circumstances under which it has not implemented such recommendations.

g. To ensure the independence of the Independent Consultant, AG Edwards: 1) shall not have the authority to terminate the Independent Consultant without the prior written approval of the Commission's staff; 2) shall compensate the Independent Consultant, and persons engaged to assist the Independent Consultant, for services rendered pursuant to this Order at their reasonable and customary rates; and 3) shall not be in and shall not have an attorney-client relationship with the Independent Consultant and shall not seek to invoke the attorney-client privilege or any other doctrine or privilege to prevent the Independent Consultant from transmitting any information, reports or documents to the Commission or the Commission's staff.

h. To further ensure the independence of the Independent Consultant, AG Edwards shall require the Independent Consultant to enter into an agreement that provides that for the period of the engagement and for a period of two years from completion of the engagement, the Independent Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with AG Edwards, or any of its present or former affiliates, directors, officers, employees or agents acting in their capacity. This agreement shall also provide that the Independent Consultant will require any firm with which the Independent Consultant is affiliated or of which the Independent Consultant is a member, and any person engaged to assist the Independent Consultant in performance of his or her duties under this Order shall not, without prior written consent of the Commission's staff, enter into any employment consultant, attorney-client, auditing or other professional relationship with AG Edwards, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

22. For good cause shown, and upon a timely application from AG Edwards or the Independent Consultant, the Commission's staff may extend any of the procedural dates set forth above.

IV.

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

Accordingly, pursuant to Section 15(b) of the Exchange Act, it is hereby ORDERED that:

A. AG Edwards is hereby censured.

B. IT IS FURTHER ORDERED that:

1. AG Edwards shall, within 30 days of the entry of this Order, pay disgorgement of $1,930,000, prejudgment interest of $430,000 and a civil money penalty of $1,500,000, for a total payment of $3,860,000 to the United States Treasury. 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 AG Edwards as a Respondent in these proceedings and the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Merri Jo Gillette, Regional Director, Midwest Regional Office, Securities and Exchange Commission, 175 West Jackson Boulevard, Suite 900, Chicago, IL 60604.

C. AG Edwards shall comply with the undertakings enumerated in Section III.21 above.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

Chairman Cox and Commissioner Nazareth Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8796 / May 2, 2007

ADMINISTRATIVE PROCEEDING
FILE NO. 3-12624

In the Matter of **A.G. Edwards & Sons, Inc.,** **Respondent.**	**ORDER UNDER RULE 602(e) UNDER THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE DISQUALIFICATION PROVISION OF RULE 602(c)(3)**

A.G. Edwards & Sons, Inc. ("AG Edwards") has submitted a letter, dated December 22, 2006, requesting a waiver of the disqualification from the exemption under Regulation E arising from its settlement of administrative proceedings commenced by the Commission under Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act").

On May 2, 2007, pursuant to AG Edwards' offer of settlement, the Commission issued an Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Order"). The Order found that AG Edwards failed reasonably to supervise its registered representatives with a view to preventing their willful violations of the federal securities laws and censured AG Edwards. The Order also required AG Edwards to pay disgorgement of $1.93 million, prejudgment interest of $430,000 and a civil monetary penalty in the amount of $1.5 million and to comply with certain undertakings.

Regulation E provides an exemption from registration under the Securities Act, subject to certain conditions, for securities issued by certain small business investment companies and business development companies. The Regulation E exemption is not available for the securities of an issuer if, among other things, any investment adviser or underwriter for the securities to be offered is subject to an order of the Commission entered pursuant to Sections 15(b) or 15A(1) of the Exchange Act or Section 203(d) or (e) of the Investment Advisers Act of 1940. See Rule 602(c)(3) under the Securities Act. The Commission may waive the disqualification under a showing of good cause. See Rule 602(e) under the Securities Act.

Document 4 of 33

Based on the representations set forth in AG Edwards December 22, 2006 request, the Commission has determined that a showing of good cause has been made pursuant to Rule 602(e) and that the request for a waiver of the disqualification should be granted.

Accordingly, IT IS ORDERED, pursuant to Rule 602(e) under the Securities Act, that a waiver from the application of the disqualification provision of Rule 602(c)(3) under the Securities Act resulting from the entry of the Order is hereby granted.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Chairman Cox and Commissioner Nazareth Not Participating

SECURITIES ACT OF 1933
Release No. 8797 / May 2, 2007

SECURITIES EXCHANGE ACT OF 1934
Release No. 55694 / May 2, 2007

ADMINISTRATIVE PROCEEDING
FILE NO. 3-12624

In the Matter of **A.G. Edwards & Sons, Inc.,** **Respondent.**	**ORDER UNDER SECTION 27A(b) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b) OF THE SECURITIES EXCHANGE ACT OF 1934 GRANTING A WAIVER OF THE DISQUALIFICATION PROVISIONS OF SECTION 27A(b)(1)(A)(ii) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b)(1)(A)(ii) OF THE SECURITIES EXCHANGE ACT OF 1934**

A.G. Edwards & Sons, Inc. ("AG Edwards") has submitted a letter, dated October 4, 2006, requesting a waiver of the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act of 1933 ("Securities Act") and Section 21E(b)(1)(A)(ii) of the Securities Exchange Act of 1934 ("Exchange Act") arising from the proposed settlement of administrative and cease-and-desist proceedings against it.

On May 2, 2007, pursuant to AG Edwards' offer of settlement, the Commission issued an Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Order"). The Order found that AG Edwards failed reasonably to supervise its registered representatives with a view to preventing their willful violations of the federal securities laws and censured AG Edwards. The Order also required AG Edwards to pay disgorgement of $1.93 million, prejudgment interest of $430,000 and a civil monetary penalty in the amount of $1.5 million and to comply with certain undertakings.

The safe harbor provisions of Section 27A(c) of the Securities Act and Section 21E(c) of the Exchange Act are not available for any forward-looking statement that is "made with respect to the business or operations of the issuer, if the issuer . . . during the 3-year period preceding the date on which the statement was made . . . has been made the subject of a judicial or administrative decree or order arising out of a governmental action that . . . (III) determines that the issuer violated the antifraud provisions of the securities laws[.]" <u>See</u> Section 27A(b) of the Securities Act; Section 21E(b) of the Exchange Act.

Document 5 of 33

Based on the representations set forth in AG Edwards' October 4, 2006 request, the Commission has determined that, under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Order is appropriate and should be granted.

Accordingly, IT IS ORDERED, pursuant to Section 27A(b) of the Securities Act and Section 21E(b) of the Exchange Act, that a waiver from the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act and Section 21E(b)(1)(A)(ii) of the Exchange Act for AG Edwards and its affiliates resulting from the entry of the Order is hereby granted.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
May 2, 2007

Chairman Cox and Commissioner Nazareth Not Participating

ADMINISTRATIVE PROCEEDING
File No. 3-12626

In the Matter of **THOMAS C. BRIDGE,** **JAMES D. EDGE, AND** **JEFFREY K. ROBLES,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933, SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 9(b) OF THE INVESTMENT COMPANY ACT OF 1940**

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 Section 8A of the Securities Act of 1933 ("Securities Act"), Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act") against Thomas C. Bridge ("Bridge") and pursuant to Section 15(b) of the Exchange Act against James D. Edge ("Edge") and Jeffrey K. Robles ("Robles") (collectively, the "Respondents").

II.

After an investigation, the Division of Enforcement alleges that:

Summary

1. This matter concerns the use of deceptive means to place market timing or frequent trades in shares of mutual funds.[1] During the relevant time period, two A.G. Edwards & Sons, Inc. ("AG Edwards") registered representatives, referred to at AG Edwards as financial consultants ("FCs"), Bridge and Charles Sacco ("Sacco"), used deceptive tactics to place thousands of market timing trades on behalf of certain of their customers in contravention of

[1] "Market timing" includes (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal *per se*, can harm other mutual fund shareholders because it can dilute the value of their shares if the market timer is exploiting pricing inefficiencies, disrupt the management of the mutual fund's investment portfolio or cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

Document 6 of 33

hundreds of requests by mutual fund companies to stop market timing. These tactics included: 1) opening multiple accounts with different account numbers for the same customer; 2) naming accounts in the names of many different entities affiliated with the same customer; 3) opening new accounts or transferring existing accounts to different branch offices for the same customer; 4) placing trades using multiple FC identification numbers; and 5) transferring assets between related accounts. These tactics allowed Bridge and Sacco to conceal their identities and the identities of their market timing customers from mutual fund companies and to continue placing market timing trades after the mutual fund companies requested that they stop trading. Thus, Bridge and Sacco violated the antifraud provisions of the Securities Act and the Exchange Act. In addition, Bridge's and Sacco's branch managers, Edge and Robles, failed to respond to numerous red flags which indicated that Sacco and Bridge were employing deceptive tactics to market time on behalf of their market timing customers. Thus, Edge and Robles failed reasonably to supervise Bridge and Sacco with a view toward preventing and detecting their violations of the federal securities laws.

Respondents

2. Bridge, age 40, is a resident of Fort Lauderdale, Florida. Bridge has been employed as a registered FC at AG Edwards in its Boca Raton, Florida branch office since March 1995. Since 2002, Bridge also has acted as the assistant branch manager of the Boca Raton branch office. At all relevant times, Bridge has held the following licenses with the National Association of Securities Dealers, Inc. ("NASD"): General Securities Representative (Series 7), Uniform Securities Agent State Law (Series 63), and General Securities Sales Supervisor (Series 9 and Series 10).

3. Edge, age 45, is a resident of Lake Worth, Florida. Edge has been employed at AG Edwards since 1985 and has been the branch manager of the AG Edwards Boca Raton, Florida branch office since January 2001. Since February 2002, Edge also has overseen the AG Edwards Lake Worth, Florida branch office. At all relevant times, Edge has held the following NASD licenses: Registered Commodity Representative (Series 3), General Securities Representative (Series 7), Branch Manager (Series 8), and Uniform Securities Agent State Law (Series 63).

4. Robles, age 38, is a resident of Kingston, Massachusetts. Robles has been employed at AG Edwards since March 2002 and has been the branch manager of the AG Edwards Boston Back Bay office since June 2002. At all relevant times, Robles has held the following NASD licenses: General Securities Representative (Series 7), Uniform Securities Agent State Law (Series 63), Branch Manager (Series 8), and Registered Investment Adviser (Series 65).

Other Relevant Person and Entity

5. Sacco, age 29, is a resident of Medford, Massachusetts. Between December 2001 and October 2003, Sacco was employed as an FC in the Boston Back Bay branch office of AG Edwards. Robles was Sacco's direct supervisor from June 2002 to October 2003. On May 2, 2007, the Commission instituted settled administrative proceedings against Sacco in the Matter of Charles A. Sacco, in which the Commission found that Sacco willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by using

deceptive means to market time on behalf of his customers. Sacco consented to the issuance of the Commission's order without admitting or denying the Commission's findings.

6. AG Edwards is a Delaware corporation with headquarters located in St. Louis, Missouri that has been registered with the Commission as a broker-dealer pursuant to Section 15 of the Exchange Act since 1967. AG Edwards has approximately 730 offices staffed by approximately 6,824 registered FCs that provide retail brokerage services throughout the United States, Switzerland and the United Kingdom. AG Edwards is the principal operating subsidiary of A.G. Edwards, Inc., a Delaware corporation whose stock is traded on the NYSE under the symbol AGE. On May 2, 2007, the Commission instituted settled administrative proceedings against AG Edwards in the Matter of A.G. Edwards & Sons, Inc., in which the Commission found that AG Edwards failed reasonably to supervise its FCs with a view toward preventing and detecting their violations of the federal securities laws. AG Edwards consented to the issuance of the Commission's order without admitting or denying the Commission's findings.

Background

7. During the relevant time period, Bridge and Sacco engaged in illegal market timing schemes on behalf of certain of their customers. Bridge and Sacco defrauded mutual fund companies and their shareholders by engaging in a series of deceptive practices designed to conceal their identities and the identities of their customers in order to circumvent restrictions that the mutual fund companies imposed on market timing.

8. Many mutual fund companies screened for market timing or excessive short-term trading by reviewing the FC identification numbers and account numbers associated with trades over a certain dollar amount. Typically, if a mutual fund company concluded that a particular trade placed by one of AG Edwards' FCs violated the mutual fund company's exchange limitations or restrictions against market timing, it would attempt to prevent additional trades in that mutual fund or mutual fund family by contacting AG Edwards and/or the FC who placed the trade.

9. Over time, AG Edwards received at least 92 communications from the following 21 mutual fund companies objecting to Bridge's placement of market timing trades:

AIM Investments:	at least 2 communications;
Blackrock:	at least 2 communications;
CDC Nvest Funds:	at least 1 communication;
Credit Suisse:	at least 7 communications;
Dreyfus:	at least 3 communications;
Evergreen Investments:	at least 1 communication;
Franklin Templeton Investments:	at least 7 communications;
Goldman Sachs & Co.:	at least 2 communications;
John Hancock Funds:	at least 3 communications;
Janus:	at least 12 communications;
JP Morgan Funds:	at least 10 communications;
Liberty/Columbia Funds:	at least 9 communications;

Lord Abbett & Co.:	at least 1 communication;
Nuveen Investments:	at least 3 communications;
One Group Mutual Funds:	at least 8 communications;
Phoenix Investment Partners:	at least 1 communication;
PIMCO:	at least 2 communications;
Pioneer Investments:	at least 1 communication;
Scudder Investments:	at least 9 communications;
SunAmerica Mutual Funds:	at least 2 communications; and
Thornburg Investment Management:	at least 6 communications.

10. Over time, AG Edwards received more than 180 communications from the following 30 mutual fund companies objecting to Sacco's placement of market timing trades:

AIM Investments:	at least 36 communications;
AllianceBernstein:	at least 4 communications;
American Funds:	at least 2 communications;
Blackrock:	at least 4 communications;
Calvert Funds:	at least 1 communication;
CDC Nvest Funds:	at least 1 communication;
Credit Suisse:	at least 9 communications;
Dreyfus:	at least 16 communications;
Eaton Vance:	at least 6 communications;
Evergreen Investments:	at least 2 communications;
Fidelity Investments:	at least 3 communications;
First American Funds:	at least 1 communication;
Franklin Templeton Investments:	at least 2 communications;
John Hancock Funds:	at least 2 communications;
The Hartford:	at least 9 communications;
ING Funds:	at least 2 communications;
JP Morgan Funds:	at least 10 communications;
Liberty/Columbia Funds:	at least 10 communications;
Mainstay Funds:	at least 1 communication;
Managers Investment Group:	at least 2 communications;
One Group Mutual Funds:	at least 1 communication;
Phoenix Investment Partners:	at least 10 communications;
PIMCO:	at least 3 communications;
Pioneer Investments:	at least 4 communications;
Scudder:	at least 23 communications;
State Street Global Advisors:	at least 2 communications;
SunAmerica Mutual Funds:	at least 2 communications;
T. Rowe Price:	at least 16 communications;
Van Kampen Investments:	at least 2 communications; and
Wells Fargo:	at least 1 communication.

These communications were in the form of telephone calls, letters, e-mails and cancelled trade notices (collectively "restriction notices"). These restriction notices informed AG Edwards, Bridge and Sacco that the mutual fund companies had rejected particular trades or restricted Bridge, Sacco or their customers from further market timing.

11. The majority of the written restriction notices were sent to the mutual fund order room at AG Edwards' headquarters located in St. Louis, Missouri. As the restriction notices came in, employees in the order room updated AG Edwards' trading data and then sent copies of the restriction notices to the FC responsible for placing the trade and the branch manager responsible for supervising the FC. At all relevant times, AG Edwards' branch managers were responsible for reviewing all correspondence in their branches, including mutual fund restriction notices.

12. AG Edwards issued each of its registered FCs one unique identification number through which to place trades on behalf of their customers. However, FCs could obtain additional FC identification numbers with which they could place trades by entering into a "split" with one or more other FCs. A legitimate reason to request a new FC number was to share commissions and fees with one or more additional FCs who serviced the same customer. In contrast, Bridge and Sacco obtained split FC numbers to continue market timing mutual funds that previously restricted them from trading under other FC numbers or split FC numbers. Because many mutual fund companies restricted further trading by FC numbers rather than by FC names, an FC could evade restrictions by obtaining and trading under a new FC number.

13. During the relevant time period, FCs were not required to obtain approval from their branch managers before requesting additional split FC numbers. However, Bridge and Sacco both regularly sought their branch managers' approval before requesting any split FC numbers.

14. During the relevant time period, AG Edwards required its branch managers to approve the opening of all new customer accounts.

15. At all relevant times, AG Edwards' branch supervisory manual required all branch managers, including Edge and Robles, to review a daily trading report which detailed all trades placed by FCs under their supervision and originating from their branch office. Among other things, the daily trading report included the identity of the customer, the FC who placed the trade, and the mutual fund that was traded.

Bridge's Market Timing

16. In September 2001, Edge asked Bridge to take over a large market timing account from another FC whose employment had been terminated. Between September 2001 and September 2003, Bridge opened 15 different accounts for his market timing customer. At all relevant times, Bridge knew that his market timing customer planned to use the accounts to place market timing trades.

17. Bridge's market timing customer's accounts were fee-based accounts in AG Edwards' Fund Navigator Program, later called the Preferred Fund Advisor program. Through

these accounts, Bridge's market timing customer did not pay commissions to Bridge for each transaction placed on the market timing customer's behalf. Instead, Bridge and AG Edwards were paid quarterly fees ranging from 1% to 1.5% of the total assets in the market timing customer's accounts. Bridge received a total of $39,808.53 in compensation for trading on behalf of his market timing customer.

18. Between September 2001 and September 2003, Bridge placed at least 2,898 trades on behalf of his market timing customer. Most of these trades were in mutual funds that prohibited market timing or strictly limited the number and frequency of trades in an effort to prevent market timing.

19. Bridge regularly communicated with his market timing customer and discussed specific trades, the flow of assets into and out of the customer's accounts and the opening of new accounts.

20. Between September 2001 and September 2003, Bridge and AG Edwards received at least 92 restriction notices from at least 21 different mutual fund companies objecting to Bridge's placement of market timing trades on behalf of his market timing customer. In addition, Bridge received other telephone calls and messages which requested that he stop placing market timing trades on behalf of the same customer.

21. After receiving copies of the restriction notices, Bridge repeatedly ignored the mutual fund companies' requests to cease trading and continued market timing on behalf of his customer. In order to avoid further detection by the mutual fund companies, Bridge engaged in a series of deceptive acts and practices to conceal his market timing activity from mutual fund companies.

22. For example, between September 2001 and September 2003, Bridge opened seven accounts at the Boca Raton branch office using the names of five entities affiliated with his market timing customer to avoid further detection of his customer's market timing activity by mutual fund companies.

23. Between September 2001 and September 2003, Bridge also opened eight accounts at the Lake Worth branch office using the names of four entities affiliated with his market timing customer. The reason Bridge opened multiple accounts for his market timing customer at more than one of AG Edwards' branches was to avoid mutual fund companies' restrictions against market timing activity.

24. As Bridge obtained accounts for his market timing customer at the Boca Raton and Lake Worth branch offices, he transferred his market timing customer's assets between the related accounts. Bridge transferred assets between the related accounts in order to place market timing trades on behalf of his customer in accounts that had not been restricted by the mutual fund companies.

25. In addition, after Bridge's own FC number was restricted from trading by mutual fund companies, Bridge used several additional FC identification numbers to place market timing trades on behalf of his market timing customer.

26. Between September 2001 and September 2003, Bridge requested and obtained at least 17 different split FC numbers with which he traded on behalf of his market timing customer. These split FC numbers were with FCs located in both the Boca Raton and Lake Worth branch offices. Most of the splits were with individuals who did little to service the market timing accounts. These individuals typically received between 10% and 20% of the commissions or fees for trades executed under the split FC numbers.

27. By using these deceptive acts and practices, Bridge was able to disguise his identity and the identity of his market timing customer and thus, gain access to mutual funds that previously attempted to stop him from market timing on behalf of his market timing customer.

Sacco's Market Timing

28. Starting in approximately May 2002, Sacco began opening brokerage accounts for two market timing customers. Between May 2002 and September 2003, Sacco opened 142 separate accounts for his market timing customers. At all relevant times, Sacco knew that his market timing customers planned to use their accounts at AG Edwards to place market timing trades.

29. Between May 2002 and September 2003, Sacco placed more than 35,000 trades on behalf of his market timing customers. Most of these trades were in mutual funds that prohibited market timing or strictly limited the number and frequency of trades in an effort to prevent market timing.

30. Sacco regularly communicated with his market timing customers by telephone and e-mail concerning specific trades, the flow of assets into and out of their accounts and the opening of new accounts.

31. Between May 2002 and September 2003, Sacco and AG Edwards received more than 180 restriction notices from mutual fund companies objecting to Sacco's placement of market timing trades on behalf of his market timing customers. These restriction notices informed Sacco and AG Edwards that the fund companies had rejected particular trades or restricted Sacco and his market timing customers from further market timing.

32. After receiving copies of the restriction notices, Sacco repeatedly ignored the mutual fund companies' requests to cease trading and continued market timing on behalf of his customers. In order to avoid further detection by the mutual fund companies, Sacco engaged in a series of deceptive acts and practices to conceal his continuing market timing activity from mutual fund companies.

33. For example, between May 2002 and September 2003, Sacco opened 142 new accounts in the names of multiple entities affiliated with his market timing customers. Sacco used these accounts to avoid further detection of his market timing customers' market timing activity by mutual fund companies. Sacco also transferred assets between the related accounts after he received restriction notices.

34. Between May 2002 and September 2003, as Sacco received restriction notices from mutual fund companies related to his market timing trades, he requested and obtained at least nine different split FC numbers with which he traded on behalf of his market timing customers. Most of the splits were with individuals who did little to service Sacco's market timing customers and who received only 1% of the commissions or fees for trades executed under the split FC numbers.

35. By using these deceptive acts and practices, Sacco was able to disguise his identity and the identities of his market timing customers and thus, gain access to mutual funds that previously attempted to stop him from market timing on behalf of his market timing customers.

Edge's Supervisory Failures

36. At all relevant times, Edge was Bridge's direct supervisor.

37. Between September 2001 and September 2003, Bridge opened 15 accounts at both the Boca Raton and Lake Worth branch offices in the names of several entities affiliated with Bridge's market timing customer. Bridge sought Edge's approval for the opening of each of these accounts. Despite the red flags raised by opening all of these accounts in two different branch offices for the same customer, Edge approved the opening of all of the accounts. By approving the opening of multiple accounts for the same customer, Edge allowed Bridge to conceal his identity and the identity of his market timing customer in order to continue market timing on behalf of his market timing customer and to circumvent the mutual fund companies' restrictions against market timing.

38. During the relevant time period, AG Edwards' mutual fund order room in St. Louis, Missouri sent restriction notices relating to Bridge's market timing to Edge. Edge did not take reasonable steps to follow up on these restriction notices.

39. Between September 2001 and September 2003, Bridge obtained and used 17 different split FC numbers to place market timing trades on behalf of his market timing customer. Bridge sought Edge's authorization before he made requests for the new split FC numbers. Despite the red flags raised by Bridge's multiple requests for split FC numbers to trade on behalf of the same customer, Edge approved Bridge's use of all of the split FC numbers. By approving Bridge's use of multiple split FC numbers, Edge allowed Bridge to conceal his identity and the identity of his market timing customer in order to continue market timing on behalf of his market timing customer and to circumvent mutual fund companies' restrictions against market timing.

40. Edge not only was aware that Bridge used multiple split FC numbers to place market timing trades on behalf of Bridge's market timing customer, but also helped Bridge select the FCs in the Boca Raton branch office with whom Bridge obtained split FC numbers.

41. During the relevant period, Edge was responsible for reviewing a daily trading report which detailed all trades placed by FCs under his supervision from the Boca Raton and Lake Worth offices, including trades placed by Bridge. However, Edge unreasonably delegated this authority for reviewing trades to Bridge, including the authority to review all of the trades that Bridge himself placed.

42. As branch manager of AG Edwards' Boca Raton and Lake Worth branch offices, Edge was responsible for supervising Bridge. However, Edge failed to respond to red flags indicating that Bridge was using deceptive tactics to conceal his identity and the identity of his customer from mutual fund companies. Edge also authorized the opening of new accounts and the issuance of split FC numbers which allowed Bridge to engage in deceptive market timing activity. Edge also failed to reasonably respond to red flags in the form of multiple restriction notices from mutual fund companies objecting to Bridge's market timing activity and Bridge's trading activity reflected in the daily trading report. If Edge had reasonably responded to these red flags, it is likely that he could have prevented or detected Bridge's fraudulent conduct. Thus, Edge failed reasonably to supervise Bridge.

Robles' Supervisory Failures

43. From June 2002 to October 2003, Robles was Sacco's direct supervisor.

44. After Robles became Sacco's branch manager in June 2002, Sacco informed Robles that the majority of his business was related to his market timing customers.

45. Based on the revenue Sacco's market timing activity brought into the Boston Back Bay branch office, Robles rewarded Sacco by moving him to a window office which was located next to Robles' office, and provided Sacco with a parking space.

46. Between May 2002 and September 2003, Sacco opened 142 accounts in the names of several entities affiliated with his market timing customers. After Robles became Sacco's branch manager in June 2002, Sacco sought Robles' approval before he opened any new accounts on behalf of his market timing customers. Despite the red flags raised by opening all of these accounts for the same two customers, between June 2002 and October 2003, Robles himself, or through delegated authority to his assistant branch manager, approved the opening of most of the 142 accounts. By approving the opening of multiple accounts for the same customers, Robles allowed Sacco to conceal his identity and the identities of his market timing customers from mutual fund companies in order to continue market timing on behalf of his market timing customers and to circumvent mutual fund companies' restrictions against market timing.

47. Between June 2002 and September 2003, AG Edwards' mutual fund order room in St. Louis, Missouri sent restriction notices relating to Sacco's market timing to Robles. Robles did not take reasonable steps to follow up on these restriction notices.

48. Between May 2002 and September 2003, Sacco obtained and used nine different split FC numbers to place market timing trades on behalf of his market timing customer. Sacco sought Robles' authorization before he made requests for the new split FC numbers. Despite the red flags raised by Sacco's multiple requests for split FC numbers to trade on behalf of the same customers, Robles approved Sacco's use of most of these split FC numbers. By approving Sacco's use of multiple split FC numbers, Robles allowed Sacco to conceal his identity and the identities of his market timing customers from mutual fund companies in order to continue market timing on behalf of his market timing customers and to circumvent mutual fund companies' restrictions against market timing.

49. During the relevant time period, Robles reviewed the daily trading report which detailed all trades placed by FCs under his supervision from the Boston Back Bay branch office, including trades placed by Sacco.

50. As branch manager of AG Edwards' Boston Back Bay branch office, Robles was responsible for supervising Sacco. However, Robles failed to respond to red flags indicating that Sacco was using deceptive tactics to conceal his identity and the identity of his market timing customers from mutual fund companies. Robles also authorized the opening of new accounts and the issuance of split FC numbers which allowed Sacco to engage in deceptive market timing activity. Robles also failed to reasonably respond to red flags in the form of multiple restriction notices from mutual fund companies objecting to Sacco's market timing activity and Sacco's trading activity reflected in the daily trading report. If Robles had reasonably responded to these red flags, it is likely that he could have prevented or detected Sacco's fraudulent conduct. Thus, Robles failed reasonably to supervise Sacco.

Violations

51. As a result of the conduct described above, Bridge willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in the offer or sale of securities and in connection with the purchase or sale of securities.

52. As a result of the conduct described above, Edge and Robles failed reasonably to supervise Bridge and Sacco with a view to preventing their violations of the federal securities laws. Section 15(b)(6)(A)(i) of the Exchange Act provides for the imposition of sanctions against persons associated with a broker or dealer who have failed reasonably to supervise, with a view to preventing violations of the securities laws, other persons who commit such violations, if such persons are subject to their supervision.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondents an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondent Bridge pursuant to Section 15(b) of the Exchange Act including, but not limited to, disgorgement plus prejudgment interest and civil penalties pursuant to Section 21B of the Exchange Act;

C. What, if any, remedial action is appropriate in the public interest against Respondent Bridge pursuant to Section 9(b) of the Investment Company Act including, but not limited to, civil penalties pursuant to Section 9(d) of the Investment Company Act;

D. What, if any, remedial action is appropriate in the public interest against Respondents Edge and Robles pursuant to Section 15(b) of the Exchange Act including, but not limited to, civil penalties imposed pursuant to Section 21B of the Exchange Act.

E. Whether, pursuant to Section 8A of the Securities Act and Sections 15(b) and 21C of the Exchange Act, Respondent Bridge should be ordered to cease and desist from committing or causing violations of and any future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and whether Respondent Bridge should be ordered to pay disgorgement pursuant to Section 8A(e) of the Securities Act, Section 21C(e) of the Exchange Act and Section 9(e) of the Investment Company Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondents fail to file the directed answer, or fail to appear at a hearing after being duly notified, the Respondents may be deemed in default and the proceedings may be determined against them upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondents personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Cox and Commissioner Nazareth Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8795 / May 2, 2007

SECURITIES EXCHANGE ACT OF 1934
Release No. 55693 / May 2, 2007

INVESTMENT COMPANY ACT OF 1940
Release No. 27816 / May 2, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12625

In the Matter of CHARLES A. SACCO, Respondent.	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933, SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 9(b) OF THE INVESTMENT COMPANY ACT OF 1940**

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 Section 8A of the Securities Act of 1933 ("Securities Act"), Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act") against Charles A. Sacco ("Sacco" 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 him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making

Document 7 of 33

Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Section 8A of the Securities Act of 1933, Sections 15(b) and 21C of the Securities Exchange Act of 1934 and Section 9(b) of the Investment Company Act of 1940 ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

1. This is a proceeding against Sacco, a former registered representative at A.G. Edwards & Sons, Inc. ("AG Edwards"), a registered broker-dealer. Between May 2002 and September 2003, Sacco used deceptive means to market time mutual fund shares on behalf of two large hedge fund customers.[2] By virtue of his conduct, Sacco violated the antifraud provisions of the Securities Act and the Exchange Act.

Respondent

2. Sacco, age 29, is a resident of Medford, Massachusetts. Between December 2001 and October 2003, Sacco was employed as a registered representative, referred to at AG Edwards as a "financial consultant" ("FC"), in the Boston Back Bay, Massachusetts branch office of AG Edwards. At all relevant times, Sacco held the following licenses with the National Association of Securities Dealers, Inc. ("NASD"): General Securities Representative (Series 7); Uniform Securities Agent State Law (Series 63); and Registered Investment Adviser (Series 65).

Other Relevant Entity

3. AG Edwards is a Delaware corporation with headquarters located in St. Louis, Missouri that has been registered with the Commission as a broker-dealer pursuant to Section 15 of the Exchange Act since 1967. AG Edwards has approximately 730 offices staffed by approximately 6,824 registered FCs that provide retail brokerage services throughout the United States, Switzerland and the United Kingdom. AG Edwards is the principal operating subsidiary of A.G. Edwards, Inc., a Delaware corporation whose stock is traded on the NYSE under the symbol AGE.

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[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.

[2] "Market timing" refers to (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal *per se*, can harm other mutual fund shareholders because it can dilute the value of their shares if the market timer is exploiting pricing inefficiencies, disrupt the management of the mutual fund's investment portfolio or cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

Background

4. From approximately May 2002 to September 2003, Sacco engaged in an illegal market timing scheme on behalf of two large hedge fund customers ("Hedge Fund A" and "Hedge Fund B," collectively, "hedge fund customers"). Sacco defrauded more than 100 mutual funds from at least 25 different mutual fund companies and their shareholders by engaging in a series of deceptive practices designed to conceal his identity and the identities of his hedge fund customers from the mutual fund companies in order to circumvent restrictions that the mutual fund companies imposed on market timing.

Sacco's Trading Practices

5. Starting in approximately May 2002, based on a referral from a former colleague at another broker-dealer, Sacco began opening brokerage accounts for his hedge fund customers. Between May 2002 and September 2003, Sacco opened 129 accounts for Hedge Fund A and 13 accounts for Hedge Fund B. At all relevant times, Sacco knew that Hedge Fund A and Hedge Fund B planned to use their accounts at AG Edwards to place market timing trades.

6. Most of the hedge fund customers' accounts were fee-based accounts in AG Edwards' Fund Navigator program, later called the Preferred Fund Advisor program. Through these accounts, the hedge fund customers did not pay commissions for each transaction placed on their behalf. Instead, the customers paid Sacco and AG Edwards quarterly fees ranging from 1% to 1.5% of the total assets in the account. During the relevant time period, Sacco received $215,892.52 in compensation for trading on behalf of his hedge fund customers.

7. Between May 2002 and September 2003, Sacco placed more than 35,000 trades on behalf of his hedge fund customers. Most of these trades were in mutual funds that prohibited or strictly limited the number and frequency of trades in an effort to prevent market timing.

8. Sacco regularly communicated with his hedge fund customers by telephone and e-mail concerning specific trades, the flow of assets into and out of their accounts and the opening of new accounts.

9. Many of the mutual fund companies screened for market timing or excessive short-term trading by reviewing the FC identification numbers and account numbers associated with trades over a certain dollar amount. Typically, if a mutual fund company concluded that a particular trade placed by one of AG Edwards' FCs violated its exchange limitations or restrictions against market timing, it would attempt to prevent additional trades in that mutual fund or mutual fund family by contacting AG Edwards and/or the registered FC who placed the trade.

10. Over time, Sacco and AG Edwards received at least 180 telephone calls, letters, e-mails and canceled trade notices (collectively "restriction notices") from mutual fund

companies objecting to Sacco's placement of market timing trades on behalf of his hedge fund customers. These restriction notices informed Sacco and AG Edwards that the fund companies had rejected particular trades or restricted Sacco and his hedge fund customers from placing further market timing trades.

11. The majority of the written restriction notices were sent to the mutual fund order room at AG Edwards' headquarters in St. Louis, Missouri. As the restriction notices came in, employees in the order room updated AG Edwards' trading data and then sent copies of the restriction notices to Sacco and the Boston Back Bay branch of AG Edwards.

12. After receiving copies of the restriction notices, Sacco repeatedly ignored the mutual fund companies' requests to cease trading and continued market timing on behalf of his hedge fund customers. In order to avoid further detection by the mutual fund companies, Sacco engaged in a series of deceptive acts and practices to conceal his continuing market timing activity from mutual fund companies.

13. For example, Sacco opened 142 separate accounts for his two hedge fund customers in the names of multiple entities affiliated with Hedge Fund A and Hedge Fund B in order to avoid further detection of the customers' market timing activity. Sacco also transferred assets between the related accounts after he received restriction notices.

14. In addition, Sacco placed market timing trades on behalf of his hedge fund customers using several different FC identification numbers.

15. AG Edwards issued each of its registered FCs one unique identification number through which to place trades on behalf of customers. However, FCs could obtain additional FC identification numbers with which they could place trades by entering into a "split" with one or more other FCs. A legitimate reason to request a new split FC number was to share commissions and fees with one or more additional FCs who serviced the same customer. In contrast, an illegitimate reason to obtain additional split FC numbers was to continue market timing mutual funds that previously restricted an FC from trading under other FC numbers or split FC numbers. Because many mutual fund companies restricted further trading by FC numbers rather than by FC names, an FC could evade restrictions by obtaining and trading under a new FC number.

16. Between May 2002 and September 2003, Sacco requested and obtained at least nine different split FC numbers with which to trade on behalf of his hedge fund customers. Most of the splits were with FCs and other individuals who did not do anything to service Sacco's hedge fund customers and who received only 1% of the commissions or fees for trades executed under the split FC numbers.

17. By using these deceptive acts and practices, Sacco was able to disguise his identity and the identities of his hedge fund customers and thus, gain access to mutual funds that previously restricted him and his hedge fund customers from trading.

Violations

18. As a result of the conduct described above, Sacco willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase, offer, or sale of securities.

Disgorgement and Civil Penalties

19. Respondent Sacco has submitted a sworn Statement of Financial Condition dated June 5, 2006 and other evidence and has asserted his inability to pay the entire amount of disgorgement plus prejudgment interest and a civil penalty.

Undertakings

In determining whether to accept Respondent Sacco's Offer, the Commission has considered the following undertakings by Sacco:

20. Respondent Sacco shall cooperate fully with the Commission in any and all investigations, litigations or other proceedings relating to or arising from the matters described in this Order. In connection with such cooperation, Respondent Sacco has undertaken:

a. To produce, without service of a notice or subpoena, any and all documents and other information reasonably requested by the Commission's staff;

b. To be interviewed by the Commission's staff at such times as the staff reasonably may request and to appear and testify truthfully and completely without service of a notice or subpoena in such investigations, litigations, hearings or trials as may be requested by the Commission's staff; and

c. That in connection with any testimony of Respondent Sacco to be conducted at deposition, hearing or trial pursuant to a notice or subpoena, Respondent Sacco:

i. Agrees that any such notice or subpoena for his appearance and testimony may be served by regular mail on his counsel, Daniel Rabinovitz, Esq., Michaels & Ward, LLP, 12 Post Office Square, Boston,. MA 02109; and

ii. Agrees that any such notice or subpoena for his appearance and testimony in an action pending in a United States District Court may be served, and may require testimony, beyond the territorial limits imposed by the Federal Rules of Civil Procedure.

IV.

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

Accordingly, pursuant to Section 8A of the Securities Act, Sections 15(b) and 21C of the Exchange Act and Section 9(b) of the Investment Company Act, it is hereby ORDERED that:

A. Respondent Sacco cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

B. Respondent Sacco be, and hereby is barred from association with any broker or dealer, and is 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 reapply for association 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 Sacco 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 the Respondent, 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 Sacco shall be ordered to pay disgorgement of $215,892.52 plus prejudgment interest of $56,978.70 for a total payment of $272,871.22, but based upon Respondent Sacco's sworn representations in his Statement of Financial Condition dated June 5, 2006 and other documents submitted to the Commission, the payment of all but $15,000 of the disgorgement and prejudgment interest is waived and the Commission is not imposing a penalty against Respondent Sacco. Respondent Sacco shall pay disgorgement in the amount of $15,000 pursuant to the payment plan outlined below.

E. Respondent Sacco shall pay $15,000 in 12 installments of $1,250.00 over a 36 month period to the United States Treasury. Sacco's first payment of $1,250.00 shall be due thirty days after the date of entry of this Order and his remaining 11 payments shall be post-marked no later than the 30th of June, September, December and March of each year until December 30, 2009. Such payments 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 Charles Sacco as a Respondent in these proceedings and the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Merri Jo Gillette, Regional Director, Midwest Regional Office, Securities and Exchange Commission, 175 West Jackson Boulevard, Suite 900, Chicago, IL 60604.

F. Respondent Sacco agrees that if the full amount of any payment described above is not made within ten (10) days following the date the payment is required by this Order, the entire amount of disgorgement, prejudgment interest and civil penalties, plus post judgment interest minus payments made, if any, is due and payable immediately without further application.

G. The Division of Enforcement may, at any time following the entry of this Order, petition the Commission to: (1) reopen this matter to consider whether Respondent Sacco provided accurate and complete financial information at the time such representations were made; and (2) seek an order directing payment of disgorgement and prejudgment interest and the maximum civil penalty allowable under the law. No other issue shall be considered in connection with this petition other than whether the financial information provided by Respondent Sacco was fraudulent, misleading, inaccurate or incomplete in any material respect. Respondent Sacco may not, by way of defense to any such petition: (1) contest the findings in this Order; (2) assert that payment of disgorgement, interest and a penalty should not be ordered; (3) contest the amount of disgorgement and interest to be ordered or the imposition of the maximum penalty allowable under the law; or (4) assert any defense to liability or remedy, including, but not limited to, any statute of limitations defense.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

Chairman Cox
Not Participating

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55706 / May 4, 2007

Admin. Proc. File No. 3-12393

In the Matter of the Application of

HOWARD BRETT BERGER

c/o Andrew T. Solomon, Esq.
Sullivan & Worcester LLP
1290 Avenue of the Americas
New York, New York 10104

For Review of Disciplinary Action Taken by

NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION -- REVIEW OF DISCIPLINARY PROCEEDING

Failure to Provide Requested Testimony

Former associated person of member firm of registered securities association failed to appear at two on-the-record interviews. Held, association's findings of violation and the sanction imposed are sustained.

APPEARANCES:

Andrew T. Solomon, of Sullivan & Worcester LLP, for Howard Brett Berger.

Marc Menchel, Alan Lawhead, and Michael J. Garawski, for NASD.

Appeal filed: August 15, 2006
Last brief received: November 14, 2006

I.

Howard Brett Berger, an individual who applied for registration with Millennium Brokerage, LLC ("Millennium" or the "Firm"), an NASD member firm, appeals from NASD disciplinary action. NASD found that Berger failed to appear at two on-the-record interviews ("OTRs"), in violation of NASD Procedural Rule 8210 and NASD Conduct Rule 2110. 1/

1/ NASD Procedural Rule 8210 requires members and associated persons to provide
(continued...)

Document 8 of 33

NASD barred Berger from associating with any NASD member in any capacity. 2/ To the extent we make findings, we base them on an independent review of the record.

II.

Berger was registered with NASD from December 1, 1992 until April 19, 2001. During that period, he worked for several member firms in various capacities, including as a general securities representative and general securities principal, and also as an associate compliance director and compliance officer. 3/ Berger relinquished his registration on April 19, 2001 when his employer firm filed a withdrawal from membership. That firm filed a Uniform Termination Notice for Securities Industry Registration ("Form U5") for Berger on May 2, 2001.

For nearly two years afterward, Berger remained unregistered and was not associated with any member firm. Since April 2001, Berger has been employed as the chief financial officer of Mat/Financial Systems Group ("FSG") a financial-software company. He is also a fund manager at Professional Traders Fund, LLC ("PTF"), a hedge fund. Berger became acquainted with Millennium in 2002, when FSG entered into a licensing agreement with Millennium to provide the Firm with financial software. Soon thereafter, PTF became a Millennium client.

1/ (...continued)
testimony in connection with any NASD investigation, complaint, examination, or proceeding. NASD Conduct Rule 2110 requires members and associated persons to observe high standards of commercial honor and just and equitable principles of trade. Violations of NASD rules such as NASD Procedural Rule 8210 constitute conduct inconsistent with the just and equitable principles of trade provisions of NASD Conduct Rule 2110. See, e.g., Justin F. Ficken, Securities Exchange Act Rel. No. 54699 (Nov. 3, 2006), 89 SEC Docket 685 (holding that a violation of NASD Procedural Rule 8210 constitutes conduct inconsistent with the just and equitable principles of trade provisions of NASD Conduct Rule 2110); Elliot M. Hershberg, Exchange Act Rel. No. 53145 (Jan. 19, 2006), 87 SEC Docket 494, 497 (holding that the failure to provide information requested by NASD constitutes a failure to observe high standards of commercial honor and just and equitable principles of trade), aff'd, Hershberg v. SEC, No. 06-1086-og, 2006 U.S. App. LEXIS 32225 (2d Cir. 2006); Stephen J. Gluckman, 54 S.E.C. 175, 185 (1999) (same).

2/ NASD also assessed costs.

3/ In his capacity as associate compliance director and compliance officer at two member firms, Berger was responsible for, among other things, filing applications for securities industry registration.

Berger Initiates the Registration Process with Millennium

In late March or early April 2003, Berger discussed registration with Lisa Esposito, the Millennium registered representative who serviced PTF's accounts at the Firm. Berger testified at the hearing that he informed Esposito that he was considering "relicensing [himself]" and "reestablishing" his "registration status" in order to "capture some of the commissions" that PTF was paying to Millennium. Berger also sought to renew his registration because he "knew . . . [he] was coming up on the anniversary" of the renewal deadline for his securities licenses and wanted to avoid retaking the licensing examinations. 4/ He asked Esposito "what, if anything, [he could] do to get some preliminary information going in case [he made] this decision prior to [his] license lapsing, because the last thing [he wanted] to do is make a decision to do it and have to reregister."

According to Berger, Esposito said that she would "speak to the powers that be" at Millennium regarding his inquiry. Berger testified that Esposito "came back to [him] shortly thereafter" and informed him that she would be sending him an e-mail instructing him "to fill out [his] preliminary personal instruction for a [Form] U-4" and "proceed from there." Esposito subsequently e-mailed him a blank "template request for some information" that contained a "preset box to put information in." Berger then filled in his "full name, [his] Social Security number, . . . [his] personal information, which was [his] residential history and [his] employment history" and e-mailed the template back to Esposito. 5/

Millennium Files Berger's Initial Form U4 and Two Amendments Thereto

On April 15, 2003, four days before Berger's securities licenses were due to expire, Millennium filed Berger's initial application for securities industry registration (the "Initial Form U4") electronically with the Central Registration Depository ("CRD"). 6/ Christopher Ranni, at

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4/ NASD Membership and Registration Rules 1021(c) and 1031(c) require any formerly registered person who has been unregistered for a period of at least two years immediately preceding the receipt by NASD of a new application for registration to pass an examination in order to renew his registration. Under these rules, securities licenses do not lapse until two years after registration has been terminated. After they lapse, an applicant would have to retake the licensing examinations. Berger's securities licenses were due to expire on April 19, 2003.

5/ There is no copy of the template in the record, but the parties seem to agree that the template was not the Form U4 itself.

6/ As relevant here, a Form U4, or "Uniform Application for Securities Industry Registration or Transfer," is the application by which an individual registers with NASD. The record contains copies of the Form U4 and its subsequent amendments that were

(continued...)

the time Millennium's chief compliance officer and the individual responsible for filing Forms U4 at the Firm, had initiated and filed Berger's application at the direction of Millennium's chief executive officer. 7/

Ranni testified that he did not have direct contact with Berger. However, at the hearing, he explained his usual procedure for processing Forms U4. Ranni stated at the hearing that his practice was to send "out an e-mail to the candidate" and that normally the applicant would "make changes to the form or basically just sign it and send it back" to him. 8/ Ranni described his usual business practice – one that he followed "[w]ithout exception" – of exchanging e-mails with an applicant in order to obtain information for input into the web-based CRD system. 9/ Describing the registration procedure, Ranni explained that he would first "obtain the Social Security number, date of birth and name [of the applicant]." Ranni would use that information to access the applicant's historical information on the CRD website. Ranni would then "set up the initial application" by incorporating the applicant's personal history into an electronic draft Form U4 before e-mailing a hyperlink for the draft form to the applicant. The applicant would be able to access and edit the draft form electronically via the hyperlink. During that time, CRD automatically denied Ranni access to the form until the applicant released the form by e-mailing it back to Ranni. When the hyperlink would reappear on Ranni's pending Form U4 "staging window" – signaling that the applicant had released the form back to him – Ranni would "check [the form] for accuracy" and then "submit it to the NASD for registration." 10/

Ranni explained that the only parts of the draft Form U4 that he would fill out after it was returned to him by the applicant were "jurisdictions and other information that you don't leave up

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6/ (...continued)
filed electronically by Millennium on behalf of Berger. Both parties obtained their respective copies of those forms from CRD and submitted them as hearing exhibits.

7/ Millennium's chief executive officer ("CEO") had sent an e-mail to Ranni instructing him to initiate the registration process for Berger. At his OTR, the CEO testified that he had heard that Berger had filed a Form U4 with Millennium in March or April 2003. Millennium's president was also aware of Berger's interest in registration. At his OTR on February 6, 2004, Millennium's president testified that Millennium had attempted to register Berger and stated that he "believe[d] registration may have been – they – we might have started the process for registration" on Berger's behalf.

8/ At the hearing, Berger asserted that he did not "recall e-mail from Mr. Ranni."

9/ The record does not contain any e-mails between Ranni and Berger. However, Ranni testified at the hearing that he could "only assume" that the e-mail replies he received during his e-mail exchange with the applicant were from Berger.

10/ The Hearing Panel credited Ranni's testimony about his procedures. There is no explicit credibility finding with respect to Berger's testimony.

to the candidate to fill out themselves." When the Hearing Panel asked Ranni whether he ever deviated from his usual business practice, he responded, "Never. The only way to file U4s is electronically." Because he was the sole individual "handling the registrations for the [F]irm," he "chose the easiest route possible and that was to let the candidate do it themselves." Millennium did not produce manually-signed, paper copies of Berger's Form U4 to NASD staff because the Firm claimed that it had created only electronic versions of the form.

Berger's electronic signature was typed 11/ on the Initial Form U4 under the heading, "Signature of *Applicant*." 12/ Ranni's electronic signature followed under the heading, "Signature of *Appropriate Signatory*." The Initial Form U4 included an initial disclosure reporting page ("DRP") that reported a judgment entered against Berger on November 1, 2001, six months after his previous firm had filed a Form U5 terminating his registration. Because that judgment was identified as an "initial" disclosure, i.e., it was being reported for the first time, it would not have appeared in Berger's CRD record prior to the filing of the Initial Form U4. Ranni testified that he "never update[d] candidates' DRP pages," but instead, "[left] it up to the candidate" to do so.

11/ In his hearing testimony, Berger asserted that he did not recall signing a form electronically:

> Q: When is the next time you saw any kind of document that had "U-4" on it?
> A: I don't think I received another copy.
> Q: Did you ever electronically sign your name?
> A: Not that I recall.

Berger insisted that he "didn't see" the Form U4 application, but instead saw a "template document." When the Hearing Officer asked Berger what he understood would happen after supplying his personal information to Esposito, Berger replied that it was his "understanding that Millennium would hold that information and that would hold any expiration date on [his] license pending [his] making a decision on what we wanted to do."

12/ Italics in original. According to the "Signature Section" of the Form U4, a signature "includes a manual signature or an electronically transmitted equivalent"and "is effected by typing a name in the designated signature field" which constitutes a "legally binding signature." The language preceding the applicant's signature on the Form U4 also permits the "applicant's agent" to type the applicant's name in the form's signature field. The applicant's signature on the Form U4 indicates the applicant's agreement to comply with, among other things, all provisions, including by-laws, rules, and regulations of the self-regulatory organizations selected on the application.

On April 17, 2003, CRD notified Ranni that there were deficiencies in Berger's DRPs. According to Ranni, a Form U4 filing would not be approved for registration "until the deficiencies [were] cleaned up." He asserted that, whenever he received deficiency notices, he "would send an additional e-mail to the candidate saying there were discrepancies or deficiencies. . .[a]nd that they needed to be corrected." Ranni testified that he would then go through the same e-mail process with the candidate in order to correct the deficiencies.

On April 23, 2003, Millennium filed an electronic amendment to the Initial Form U4 (the "First Amended Form U4"), with both Berger's and Ranni's electronic signatures. 13/ The First Amended Form U4 contained several changes from the Initial Form U4. Among other things, the text of one DRP response was amended, and the First Amended Form U4 included two additional DRPs. For example, the response to a disclosure question asking whether Berger was involved in a sales practice violation that contained a claim for compensatory damages of at least $5,000 was changed from a "No" to a "Yes." The corresponding initial DRP disclosed an arbitration that concluded on October 4, 2001 with the explanation that "I was not employed at the firm at the time of the complaint." A second initial DRP disclosed a $162,000 arbitration award, with the explanation that "I was named as the chief compliance officer for failure to supervise." Many of the narrative responses in the First Amended Form U4 appeared in the first-person singular, giving the impression that Berger had made the revisions himself.

On April 25, 2003, CRD generated a second notice informing Ranni that the DRPs in the First Amended Form U4 contained additional deficiencies. Ranni testified at the hearing that, in response to the deficiency notice, he went through the same e-mail process to correct those deficiencies. Thereafter, on May 12, 2003, Millennium filed another electronic amendment to the Initial Form U4 (the "Second Amended Form U4") that included additional revisions. Both Berger's and Ranni's electronic signatures appeared on the Second Amended Form U4.

On May 13, 2003, CRD generated a third notice flagging deficiencies in the Second Amended Form U4. Those deficiencies were never resolved.

Millennium Files a Form U5 to Remove Berger from the Firm's Books

On August 13, 2003, Millennium filed a Form U5 terminating Berger's association with Millennium without registration. At the hearing, Ranni testified that once the deficiencies in an applicant's Form U4 "were over 90 days old, [he] U-5'd the candidate" because it was "the only way to get him off the [Firm's] books." The Form U5 listed Berger's withdrawal as "voluntary." There was no suggestion in the Form U5 that the Initial Form U4 was filed improperly.

13/ The "temporary registration" section of the First Amended Form U4 was completed. Berger's electronic signature was typed in the temporary registration signatory section. The temporary registration section of the Initial Form U4 had not been completed.

Berger Fails to Appear at Two OTRs

On January 14, 2004, NASD sent a letter to Berger requesting his appearance, pursuant to NASD Procedural Rule 8210, at an OTR scheduled for January 27, 2004 in connection with an NASD investigation into potential day trading violations at Millennium. 14/ Berger failed to appear at the January 27, 2004 OTR. Later that day, following Berger's failure to appear, Berger's counsel informed NASD staff that his failure to notify staff of Berger's unavailability for the scheduled OTR was "inadvertent" and requested that the OTR be rescheduled. Berger retained new counsel thereafter.

On January 30, 2004, after consultation with Berger's new counsel, NASD scheduled a second OTR for February 12, 2004. Also on January 30, 2004, Berger's new counsel sent NASD staff a letter confirming the second OTR and stating that, prior to the scheduled date, "we will determine whether the NASD has jurisdiction over Mr. Berger and will notify you of our intention as to whether or not Mr. Berger will testify on that date."

On February 2, 2004, NASD sent a letter to Berger requesting his appearance, pursuant to NASD Procedural Rule 8210, at the second OTR scheduled for February 12, 2004. On February 11, 2004, the day before the second OTR, NASD staff contacted Berger's new counsel to confirm Berger's appearance at the scheduled OTR. Berger's new counsel informed NASD staff that Berger would not appear at that OTR and challenged NASD's jurisdiction over Berger. Berger failed to appear at the February 12, 2004 OTR.

NASD Proceedings

On July 15, 2004, NASD filed a complaint against Berger alleging that he failed to appear at the two OTRs. In his answer to the complaint, Berger admitted to not appearing at the OTRs but asserted that NASD lacked jurisdiction over him. Following a hearing, the Hearing Panel barred Berger in all capacities.

Berger appealed the Hearing Panel's decision to NASD's National Adjudicatory Council (the "NAC"). On July 28, 2006, the NAC affirmed the Hearing Panel's findings and sanction. The NAC determined, among other things, that, by applying for registration with NASD, Berger became an associated person of Millennium subject to NASD jurisdiction. The NAC concluded

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14/ At the hearing, Gregory Marro, an NASD staff supervisor, testified that, while conducting a routine examination of Millennium, NASD staff detected the potential circumvention of day trading rules and noncompliance with certain regulations by the Firm's day trading clients, with the possible involvement and awareness of Millennium principals and personnel. Marro indicated that Millennium's filing of Berger's Forms U4 coincided with the suspected activities at the Firm, and that NASD staff had been inquiring into PTF's role in day trading at Millennium at that time.

that Berger violated NASD rules by failing to appear for the OTRs. The NAC affirmed the imposition of a bar against Berger. This appeal followed.

III.

We must determine whether Berger engaged in the conduct found by NASD, whether the conduct violated the NASD rules he was found to have violated, and whether those rules were applied in a manner consistent with the purposes of the Securities Exchange Act of 1934. 15/ NASD Procedural Rule 8210 requires that associated persons provide information requested by NASD. Berger does not dispute that he did not appear at the scheduled OTRs, nor does he dispute that he received notice of the OTRs. We have held previously that the failure to respond to NASD's requests for testimony demonstrates a prima facie violation of NASD Procedural Rule 8210. 16/

Berger argues that NASD lacked jurisdiction over him because he had been unregistered and not associated with any member firm for more than two years at the time that NASD sought his testimony. 17/ Both Berger and NASD agree that he never became registered through Millennium and that he neither was employed by nor acted for the Firm.

However, NASD By-Law Article I(dd)(1) defines a "person associated with a member" as "a natural person who is registered or has applied for registration." NASD Notice to Members 99-95 states that "any person who signs and submits a Form U4 is an associated person." 18/ NASD found that Berger filled in his personal information and executed an electronic signature on an application for registration with Millennium on April 15, 2003, a few days before the expiration of NASD's two-year period of retained jurisdiction over him.

Berger argues that he never signed the initial and amended Forms U4 (collectively, the "Forms U4") that Millennium submitted on his behalf, and therefore, was not an associated person of Millennium. Based on the preponderance of the evidence, we find that: (1) Berger signed and submitted the Initial Form U4, the First Amended Form U4, and the Second Amended Form U4 before the 2004 OTR requests; (2) Berger was "a person associated with" Millennium

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15/ See Exchange Act Section 19(e)(1), 15 U.S.C. § 78s(e)(1).

16/ Ficken, 89 SEC Docket at 690-91.

17/ NASD asserts jurisdiction over, and has the ability to obtain information from, a person whose association with a member has been terminated or whose registration has been canceled, for two years following the date of that person's termination of registration. NASD By-Laws, Article V, Section 4.

18/ NASD Notice to Members 99-95 (Dec. 1, 1999).

because he "applied for registration" under NASD rules; and (3) as an associated person of Millennium, Berger was subject to NASD disciplinary jurisdiction during the relevant period. 19/

In weighing the evidence, we look at the totality of the record and consider the full panoply of available evidence, instead of reviewing each piece of evidence in isolation. 20/ It is undisputed that Berger initiated discussions with Millennium regarding the renewal of his registration status. Berger had strong incentives to seek registration in April 2003. He testified at the hearing that he wanted to avoid retaking the licensing examinations that he would have to take if his securities licenses were to expire. He also sought to capture commission income that PTF was paying to Millennium. Berger progressed swiftly from the discussion stage to taking concrete steps to renew his registration. Within days of his conversation with Esposito, for example, Berger completed a "template" that Esposito sent him to initiate the registration process. Berger admits inputting his name, Social Security number, and other personal information into the template and e-mailing it back to Esposito for processing.

Berger asserts that it is irrelevant that he supplied information to Esposito in a "template" and that Ranni may have relied on such information to prepare the Forms U4. Berger also does not dispute that an electronic signature, purporting to be his, appears on the Initial Form U4 and its two subsequent amendments. Rather, Berger argues that, without evidence that he signed the forms or a witness to the signing, there is no way to prove that he "signed and submitted" the Forms U4. Berger asserts that this absence of proof of the "mechanical" process of "actually signing the document" destroys NASD jurisdictional claims.

19/ See, e.g., Kirk A. Knapp, 51 S.E.C. 115, 130 n.65 (1992) (stating that the "correct standard is preponderance of the evidence"); Roy Ray Seaton v. SEC, 670 F.2d 309, 311 (D.C. Cir. 1982) (same) (internal citations omitted). Cf. Sandra K. Simpson, 55 S.E.C. 766, 798 (applying preponderance of the evidence standard in administrative proceeding). See also United States v. Gumesindo Montano, 250 F.3d 709, 713 (9th Cir. 2001) (explaining that under the preponderance of the evidence standard, the relevant facts must be shown to be more likely than not).

20/ Cf. Terrance Yoshikawa, Exchange Act Rel. No. 53731 (Apr. 26, 2006), 87 SEC Docket 2924, 2933-34 (stating that "isolated instances of seemingly innocent conduct can, when viewed as a whole, constitute circumstantial evidence . . . ."); Laurie Jones Canady, 54 S.E.C. 65, 79 (1999) (noting that law judge's credibility determination was based on the totality of the record), petition denied, 230 F.3d 362 (D.C. Cir. 2000).

Berger points out that NASD Electronic Filing Rule 1140(c) requires that a member firm retain a signed, paper original of any Form U4 submitted to CRD. 21/ The representations and signature in an electronic Form U4 are to be "based" on the paper copy. Millennium stated that it had no paper copy of any of Berger's Forms U4. 22/ There were no witnesses to the signing of the Forms U4: nobody saw Berger complete or sign the forms. As a result, Berger asserts, there is no probative evidence that he signed a Form U4. Berger contends that, without proof of his signature, the circumstantial evidence of his association with Millennium is weak.

However, the Supreme Court has stated that "circumstantial evidence can be more than sufficient" in civil actions, 23/ and we have previously considered circumstantial evidence to be persuasive. 24/ We agree with NASD that the record demonstrates that Berger played an "active role in completing" the Initial Form U4 and the First and Second Amended Forms U4. In addition to initiating the registration process with Esposito and filling out the template, Berger appears to have supplied detailed information that was previously unavailable in CRD, particularly in response to the deficiency notices that followed the Initial and First Amended Forms U4. The information in those subsequent filings added data to Berger's CRD record that

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21/ NASD Electronic Filing Rule 1140(c) provides that, "[a]s part of the member's recordkeeping requirements, it shall retain the [applicant's] signed Form U4 and make it available promptly upon regulatory request." Approximately five months after the events at issue in this case, NASD published NASD Notice 03-56 (Sept. 29, 2003), which accompanied the announcement of amendments (effective October 2003) to NASD Rule 1140(c) and contains the following colloquy:

> Q: Is the electronic Form U4 based on a signed, paper Form U4?
> A: Yes, the electronic Form U4 is based on a signed, paper Form U4. Rule 1140(c) clarifies that all Forms U4 filed electronically must be based on a signed Form U4 that is provided to the member or applicant for membership by the person.
> Q: Who will retain the signed Form U4 and how will NASD obtain a copy if it needs it?
> A: NASD Rule 1140 requires the member to retain the signed Form U4 and make it available promptly upon regulatory request.

22/ Millennium was being investigated for other recordkeeping and reporting violations at this time.

23/ Herman & MacLean v. Huddleston, 459 U.S. 375, 390 and n.30 (1983) (declining to depart from preponderance of the evidence standard in civil actions and noting sufficiency of circumstantial evidence, particularly in fraud cases).

24/ See Donald M. Bickerstaff, 52 S.E.C. 232, 238 (1995) (finding witness's testimony to be persuasive even though it was "circumstantial").

were highly likely to have been provided by Berger, and the revisions made were, as NASD found, "expressed in first person language, demonstrating that Berger supplied all such information and statements himself." For example, the Initial Form U4 contains an initial DRP disclosing a November 1, 2001 judgment against Berger, information that was not previously available in CRD. Berger almost certainly supplied this data, as it is unlikely that Millennium personnel would have possessed such information. Similarly, the responses to the deficiency notices in the form of additional DRPs and amendments to an existing DRP contained information that would have been inaccessible to Millennium personnel. We note, moreover, that the DRPs contain first person language such as "I was not employed at the firm at the time of the complaint" and "I was named as the chief compliance officer for failure to supervise." 25/

This conclusion is augmented by Ranni's hearing testimony regarding the registration process. The Hearing Panel found that Ranni "testified credibly" that he likely followed his "usual business practice" of e-mailing to Berger a link to the CRD website, which prompted Berger to review his draft Form U4 and release it to the Firm when the form had been completed. The Hearing Panel also credited Ranni's "description of his customary procedure for submitting a Form U4," based on his "demeanor, the consistency of his testimony, and the lack of any motive to testify less than fully and truthfully." 26/

Berger claims that, to the extent that Ranni was "credible," it was about his standard practices, not Berger's application specifically. Berger argues that Ranni's testimony about his normal business practices therefore is irrelevant. As Berger states, Ranni admitted that he never

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25/ Berger states that, when he telephoned CRD shortly before the hearing to determine his status, he was informed by a telephone representative that the two-year window on his association had closed in April 2003. While the Hearing Panel excluded the recording of this telephone call, it permitted Berger to testify about the conversation at the hearing. Berger does not seek to adduce the recording into evidence before us.

In any event, Berger's hearsay evidence regarding what the CRD telephone representative told him is not dispositive. The telephone representative's statement that Berger's two-year "window" had closed is correct as far as it goes. If Berger sought registration after April 2003, he would have had to take the relevant licensing examinations. Berger's conversation with the telephone representative does not, however, go to the issue of whether he applied unsuccessfully for registration.

26/ The credibility determination of an initial fact finder is entitled to considerable weight and deference because it is based on hearing the witnesses' testimony and observing their demeanor. See Rita J. McConville, Exchange Act Rel. No. 51950 (June 30, 2005), 85 SEC Docket 3127, 3136 n.21, reh'g denied, 2007 U.S. App. LEXIS 926 (7th Cir. 2007), petition denied, 465 F.3d 780 (7th Cir. 2006); Daniel Joseph Alderman, 52 S.E.C. 366, 368 n.6 (1995), aff'd, 104 F.3d 285 (9th Cir. 1997); Jonathan Garrett Ornstein, 51 S.E.C. 135, 137 (1992).

spoke to Berger and never met him until the day of the hearing. Ranni assumed instead that he received responses from Berger, but has no specific memory of any dealings with Berger. Ranni also admitted that it was a superior at Millennium, and not Berger, who directed him to initiate the registration process for Berger. Ranni did not produce any e-mails showing that the Forms U4 were sent to Berger or to anybody else for review and completion, nor did he recall sending a draft form U4 to Berger to complete.

We have relied previously on standard business practices where a witness did not recall specific details. 27/ Here, Ranni testified that it was his practice to obtain the applicant's Social Security number, name, and other personal information in order to access the applicant's historical information on CRD. Ranni's account is consistent with Berger's testimony concerning the personal information that Berger provided to Millennium and with the information provided to Berger by CRD's telephone representative. Moreover, the Hearing Panel found specifically that "Ranni credibly testified that he did not update DRPs." Instead, Ranni sent the DRPs to the applicant to update. As discussed above, the First Amended Form U4 contained detailed changes, in the form of an amendment to an existing DRP page and the addition of two DRPs, largely expressed in the first person singular, with a level of detail suggesting that whoever made those changes was intimately familiar with Berger's disciplinary history. 28/ Nothing in the record suggests that Berger communicated any DRP information to Millennium personnel, nor does Berger assert that he shared such information with them. 29/

27/ See Micah C. Douglas, 52 S.E.C. 1055, 1057 (1996) (relying on business practice and standard firm procedure where witness did not have specific recollection regarding the matter at issue).

28/ Berger notes that the various Forms U4 contained errors such as incorrect addresses for his previous places of residence and business. The presence of such errors, asserts Berger, suggests that he never saw, much less executed, the Forms U4. We reject this argument. The errors in the addresses were de minimis: an old residential address was listed as a current address, while a former work address was listed as a residential address.

29/ For this reason, we reject Berger's claim that Esposito or "anyone" could have typed his name on the Forms U4.

The evidence describes an applicant so actively engaged in the registration process that he not only supplied information for the preparation of an initial Form U4, but also responded promptly to CRD requests for further information that resulted in the filing of two amended Forms U4. 30/ We find, therefore, that NASD had jurisdiction over Berger during the relevant period.

Having established that NASD had jurisdiction over Berger during the relevant period, we find that Berger violated NASD Rules 8210 and 2110 when he failed to appear at the two OTRs. Berger asserts that his failure to appear at the first OTR was "inadvertent – i.e., neither intentional nor reckless, and no worse than excusably negligent." We note that Berger did not respond in any manner to that OTR request until the day of the scheduled OTR, and then only after the time for the scheduled OTR had elapsed. The timing of that response demonstrates that Berger was aware of the date of the scheduled OTR and that a response was required. We also note that, even after NASD accommodated Berger by scheduling a second OTR after consultation with Berger's new counsel, Berger failed to appear. 31/ While Berger's failure to appear at the first OTR may have been inadvertent, his failure to appear at the second OTR was, under the circumstances, inexcusable.

IV.

Berger contends that he should have the ability to challenge NASD's jurisdiction without first appearing at an OTR, and that he should be entitled to do this without the risk that NASD will find that he refused to provide the information and bar him from association. Berger argues that, in order to meet Exchange Act requirements of fundamental fairness, NASD must provide an avenue to challenge jurisdiction before the OTR date (akin to a motion to quash a subpoena in federal court). 32/ He asserts that every state, the federal courts, and the New York Stock

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30/ In the alternative, Berger argues that even if he had signed the Form U4, he would not have been subject to NASD's jurisdiction because it was investigating Millennium's margin practices and not his conduct in connection with the completion of the application for registration. We disagree with Berger's selective interpretation of the scope of NASD's jurisdiction and remind him that NASD sought his testimony in connection with its investigation of Millennium.

31/ See Toni Valentino, Exchange Act Rel. No. 49255 (Feb. 13, 2004), 82 SEC Docket 711, 717 (noting that NASD made every effort to accommodate respondent by rescheduling the OTR on three occasions and by agreeing to date recommended by respondent's counsel).

32/ NASD suggests that Berger has waived his fairness argument because he did not raise the issue before the NAC. Nonetheless, we consider Berger's argument under our obligation of de novo review. See Schellenbach v. SEC, 989 F.2d 907, 909 (7th Cir. 1993) (noting our obligation to conduct an "independent review of facts and law").

Exchange ("NYSE") permit jurisdictional challenges without punishment. In support of his argument, Berger cites the Federal Rules of Civil Procedure and Exchange Act Section 21(c). 33/

NASD counters that the Federal Rules of Civil Procedure do not apply to NASD procedures. NASD also points out that the Commission's Rules Relating to Investigations do not afford any procedure for challenging Commission requests for compelled investigative testimony. NASD notes that "[t]echnically," Exchange Act Section 21(c), which authorizes the Commission to enforce its subpoenas in district court in the event of "contumacy by, or refusal to obey" a Commission subpoena, does not provide a procedure by which the recipient of a Commission subpoena may affirmatively challenge the subpoena. 34/ Rather, NASD argues, Exchange Act Section 21(c) is a means by which the Commission may enforce a subpoena. Exchange Act Section 21(c) provides that the failure to abide by a legitimate subpoena is a misdemeanor. 35/

We believe that NASD is correct. Unlike the NYSE, NASD does not have a mechanism for resolving questions of jurisdiction prior to the time of a respondent's scheduled appearance at an OTR. 36/ NASD followed its rules in this proceeding. Its procedures were in accordance

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33/ 15 U.S.C. § 78u(c).

34/ Generally, courts have held that a recipient of a Commission administrative subpoena is not permitted to challenge the subpoena in court before the Commission commences a subpoena enforcement action and instead must wait for the enforcement action. Bird v. SEC, 1980 U.S. Dist. LEXIS 11799, at *4 nn.5 and 7 (D.P.R. May 19, 1980) (noting that the Commission's "administrative subpoenas are not self-executing," that Commission rules "do not provide a procedure by which recipients of an administrative subpoena can move to quash it," and that "any person who is subpoenaed may refuse to comply for just cause and await the Commission's institution of a subpoena enforcement action. At that time, he has the right to contest the enforcement of the subpoena"). Some authority to the contrary exists. See, e.g., Ayers v. SEC, 482 F. Supp. 747 (D. Montana 1980) (finding that court had jurisdiction to stay Commission investigation pending evidentiary hearing in action by plaintiffs to enjoin investigation or quash subpoenas issued by Commission, prior to subpoena enforcement action, where plaintiffs alleged "irreparable harm" as a result of, among other things, Commission investigators implying to third parties that plaintiffs were guilty of fraud and wrongdoing).

35/ 15 U.S.C. § 78u(c).

36/ We disagree that the NYSE Hearing Panel Decisions which Berger cites in support of his conditional sanction argument are "directly analogous" to this proceeding. In fact, those NYSE decisions are not a proper basis for comparison and, moreover, would similarly have no precedential effect in a Commission review proceeding of NYSE disciplinary (continued...)

with the "fair procedure[s]" contemplated by Exchange Act Section 15A(b)(8). 37/ We have held, as we did in Jay Alan Ochanpaugh, that subjecting oneself to NASD's disciplinary process and relying on NASD's procedures is the appropriate route to challenge NASD jurisdiction. 38/

In the alternative, Berger urges that NASD be required to make its sanctions conditional, giving Berger an opportunity to testify in the event that the jurisdictional challenge is resolved against him and it is determined that he was in fact subject to NASD jurisdiction at the time of the OTR request, a practice employed by the NYSE. Berger asserts that, throughout the proceedings below, he assumed that (as his attorney argued), should any sanction be assessed against him, it would be conditional. NASD's procedures are no less "fair procedure[s]" under the Exchange Act even though the NYSE has different procedures. The fact that the NYSE permits persons from whom it seeks information to lift their bars by testifying does not compel the conclusion that NASD's practice is unfair. Moreover, we have recognized the importance of NASD's need for timely information. 39/

36/ (...continued)
action.

37/ 15 U.S.C. § 78*o*-3(b)(8).

38/ See Jay Alan Ochanpaugh, Exchange Act Rel. No. 54363 (Aug. 25, 2006), 88 SEC Docket 2653, 2662 (explaining that "the only recourse against possible overreaching by NASD is for the person to whom the [Rule 8210] request is directed to refuse to comply, and to appeal any consequent disciplinary action to the Commission"). See also Allen Douglas Secs., Inc., Exchange Act Rel. No. 50513 (Oct. 12, 2004), 83 SEC Docket 3570, 3579-80 (observing that if member firm had subjected itself deliberately to NASD disciplinary sanction by engaging in the conduct warned against in an NASD staff interpretative letter to the firm, NASD's disciplinary action would have been reviewable by the Commission).

39/ See, e.g., PAZ Secs., Inc., Exchange Act Rel. No. 52693 (Oct. 28, 2005), 86 SEC Docket 1880, 1889 (stating that "[w]hen members and associated persons delay their responses to requests for information, they impede the ability of NASD to conduct its investigations fully and expeditiously"), appeal filed, No. 05-1467 (D.C. Cir.).

V.

We may cancel, reduce, or require remission of a sanction imposed by NASD if we find, having due regard for the public interest and the protection of investors, that NASD's sanction is excessive or oppressive or imposes an unnecessary burden on competition. 40/ We make no such finding here.

NASD Sanction Guidelines provide that a bar is the standard sanction for an NASD Procedural Rule 8210 violation where an individual fails to respond in "any" manner; where mitigation exists, or where the individual did not respond in a timely manner, the recommended sanction is a two-year suspension. 41/ Berger contends that NASD erred in rejecting his reliance-on-advice-of-counsel defense as a mitigating factor. Berger states that, while we have held repeatedly that reliance on counsel's advice does not excuse an associated person's obligation to testify or cooperate with NASD investigations, 42/ our precedent "cannot possibly apply when the advice pertains to jurisdiction." Berger argues that, at the very least, his reliance on the advice of his counsel was a mitigating factor, and consequently, the sanction imposed against him should be a suspension of no more than two years. 43/

While we recognize that a valid claim of reliance upon counsel may have a mitigating effect on sanctions, we have held that, in order to establish such a defense, a respondent must show that he made complete disclosure to counsel, sought advice on the legality of the intended conduct, received advice that the intended conduct was legal, and relied in good faith on counsel's advice. 44/ We find no such showing here. Berger does not claim that his counsel

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40/ See Exchange Act Section 19(e)(2), 15 U.S.C. § 78s(e)(2). Berger does not claim, nor does the record show, that NASD's sanctions impose an unnecessary or inappropriate burden on competition.

41/ NASD Sanction Guidelines (2001 ed.) at 39. See also Ficken, 89 SEC Docket at 696 n.38; Hershberg, 87 SEC Docket at 498.

42/ Valentino, 82 SEC Docket at 718 and n.10. See also Joseph G. Chiulli, 54 S.E.C. 515, 524 (2000) (finding reliance on counsel no excuse from obligation to supply information to NASD); Sundra Escott-Russell, 54 S.E.C. 867, 874-75 (2000) (finding that respondent was not relieved from obligation to respond to NASD's requests by her lawyer's advice). Berger attempts to distinguish Valentino on the ground that her noncompliance was not based on jurisdiction, but on an unrelated issue. We reject this contrast; there are many reasons for noncompliance, and Berger's excuse is no more compelling than Valentino's.

43/ Berger claims that his reliance on the advice of counsel was reasonable because he knew that he did not sign and submit a Form U4.

44/ See, e.g., Valentino, 82 SEC Docket at 718 n.11 (citing SEC v. Savoy Indus. Inc., 665

(continued...)

advised him that noncompliance with an NASD request for information while contesting jurisdiction was legal. Moreover, Berger does not assert that his "inadvertent" failure to comply with the first OTR was based on reliance on the advice of counsel.

Berger's failure to appear at two OTRs is particularly troubling in light of the importance of NASD Procedural Rule 8210. Compliance with NASD's rules requiring cooperation in investigations is imperative if NASD is to perform its self-regulatory functions effectively. As we have stated previously, "NASD should not have to bring disciplinary proceedings, as it was required to do here, in order to obtain compliance with its rules governing its investigations." 45/ Accordingly, we find that the standard sanction of a bar is warranted.

An appropriate order will issue. 46/

By the Commission (Commissioners ATKINS, CAMPOS, CASEY, and NAZARETH); Chairman COX not participating.

Nancy M. Morris
Secretary

44/ (...continued)
F.2d 1310, 1314 n.28 (D.C. Cir. 1981)); Hal S. Herman, 55 S.E.C. 395, 403 (2001) (enumerating the same factors).

45/ Valentino, 82 SEC Docket at 719.

46/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55706 / May 4, 2007

Admin. Proc. File No. 3-12393

In the Matter of the Application of

HOWARD BRETT BERGER

c/o Andrew T. Solomon, Esq.
Sullivan & Worcester LLP
1290 Avenue of the Americas
New York, New York 10104

For Review of Disciplinary Action Taken by

NASD

ORDER SUSTAINING DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES ASSOCIATION

On the basis of the Commission's opinion issued this day, it is

ORDERED that the disciplinary action taken by NASD against Howard Brett Berger, and NASD's assessment of costs, be, and they hereby are, sustained.

By the Commission.

Nancy M. Morris
Secretary

Chairman Cox and
Commissioners Atkins
and Campos
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55711 / May 7, 2007

INVESTMENT COMPANY ACT OF 1940
Release No. 27819 / May 7, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12628

In the Matter of **ZURICH CAPITAL MARKETS INC.,** Respondent.	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, AND SECTION 9(b) OF THE INVESTMENT COMPANY ACT OF 1940**

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 15(b) and 21C of the Securities Exchange Act of 1934 (the "Exchange Act") and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act") against Zurich Capital Markets Inc. ("ZCM" and "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 and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities

Document 9 of 33

Exchange Act of 1934 and Section 9(b) of the Investment Company Act of 1940 ("Order"), as set forth below.

III.

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

A. Summary

1. ZCM, an entity that provided financing, aided and abetted four hedge funds that were carrying out schemes to defraud mutual funds that prohibited market timing. Specifically, ZCM provided financing to four market-timing hedge funds that employed various deceptive tactics to invest in mutual funds. ZCM and these hedge funds knew that many mutual funds in which they invested imposed restrictions on market timing activity. In order to buy, exchange and redeem shares in these mutual funds, these hedge funds employed deceptive techniques designed to avoid detection by these mutual funds. ZCM came to learn that the hedge funds were utilizing deceptive practices to market time mutual funds, and nonetheless ZCM provided financing to them and took administrative steps that substantially assisted them. By providing assistance to the hedge funds, ZCM aided and abetted the hedge funds' violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

B. Respondent

2. ZCM is a New York-based company, incorporated in Delaware, that is not registered with the Commission as a broker-dealer. During the relevant period, ZCM was an affiliate of Zurich Global Assets LLC (subsequently reorganized and re-named Crown Management Services Limited), and an indirect subsidiary of Zurich Financial Services ("ZFS"), a Swiss holding company. At all relevant times, ZCM wholly owned Zurich Capital Markets Securities Inc. ("ZCMSI"), a registered broker-dealer. As such, ZCM was a "person... directly controlling... [a] broker-dealer," making it "at the time of the alleged misconduct, . . . a person associated with a broker-dealer' subject to the Commission's jurisdiction under Section 15(b)(6) of the Exchange Act." *See* Section 3(a)(18) of the Exchange Act. ZCM was in the business of providing financing to hedge funds and funds of funds. Since mid-2003, ZCM effectively ceased its business operations, having sold its major assets to a third-party and shifted its remaining operations into wind-down mode.

C. Facts

Market Timing

3. Market timing of mutual funds includes (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal per se, can harm other mutual fund shareholders because it can dilute the value of their shares. Market timing can also disrupt the management of the mutual fund's investment portfolio, and frequent buying and selling of shares by market timers can cause the targeted mutual fund to incur costs it would not incur in the absence of the market timing.

4. Some hedge funds trade through variable annuities to market time the underlying mutual funds. Variable annuities are securities that are insurance contracts that provide for tax-deferred accumulation of investment proceeds during the accumulation period and various payout options, including a series of payments to be made to a person named as the "annuitant" in the contract or another beneficiary whom the owner of the policy designates. The payments typically are scheduled to support the annuitant's retirement. Hedge funds and others that engage in market timing through variable annuities, however, do not purchase the products in order to obtain the retirement income for themselves or family members or others dependent upon them. Rather, they purchase variable annuities to be able to market time the underlying mutual fund portfolios. Because issuers of variable annuities typically aggregate trades in their contracted fund complexes and transmit the trades on a net basis, trading through variable annuity contracts can make it more difficult for mutual funds that prohibit market timing to detect market timing activity or identify investors who are known market timers.

ZCM Aided and Abetted its Hedge Fund Clients' Violations of Federal Securities Laws

5. From 1999-2003, ZCM provided financing to various hedge funds, including some that utilized a market timing strategy. ZCM provided this financing through derivative structures known originally as "call options" and subsequently as "accreting strike basket transactions." They were structured and operated in a manner similar to total return swaps.

6. With respect to the financing arrangements, ZCM generally placed the "leverage" it contributed as well as the "premium" or "principal" that its hedge-fund client contributed in accounts at one or more broker-dealers ("the managed accounts"). The financing arrangements permitted the hedge fund to contribute additional premium and increase the leverage provided by ZCM subject to a total dollar cap for the transaction and a maximum ZCM contribution of 75% (in one instance 80%) of the total assets in the managed accounts. ZCM opened managed accounts at brokerage firms in the names of special purpose vehicles ("SPVs") that ZCM formed. Pursuant to a limited power of attorney, ZCM granted trading authority within the accounts to its hedge-fund client or the client's investment adviser. The hedge fund or its adviser made all trading decisions with respect to purchases and sales of shares of mutual funds in the managed accounts. The hedge fund or its adviser communicated those decisions directly to the brokers. ZCM, as the owner of the managed accounts, routinely received account statements. ZCM would then track the leverage ratio of the financing arrangement to ensure that it did not exceed the maximum percentage allowed under the applicable derivative agreements. To ensure against diversion or dissipation of the premium and leverage in the managed accounts, ZCM also retained authority over all transfers of funds into and out of these brokerage accounts. To transfer funds among SPVs or accounts, the hedge funds would need to request that ZCM's employees authorize wire transfers or journaling of funds between brokerage accounts.

7. The hedge-fund client was entitled to receive all gains, if any, resulting from its trading in the managed accounts, and bore any losses, while ZCM received only a financing charge on the leverage it provided of LIBOR plus a fixed amount ranging from 115 to 169 basis points, depending on the deal.

8. ZCM's hedge-fund clients knew that numerous mutual funds did not like market timing and that many of these mutual funds prohibited market timing. In an effort to avoid being detected and potentially blocked from making market-timing trades in these funds, each of these hedge funds submitted trades in ways designed to avoid detection by disguising their and ZCM's identities or masking the trades in omnibus transactions.

9. For example, ZCM and the hedge funds used SPVs to mask their identities and execute market timing trades. ZCM first used SPVs in connection with its market timing business in May 2000 when it opened eight SPVs for one hedge fund client ("Hedge Fund A").

10. In or around October, 2000, another hedge fund client ("Hedge Fund B") requested that ZCM create an SPV owned by ZCM but under a different name. In an email, a former ZCM managing director noted that Hedge Fund B had advised him that it would "cause problems if ZCM is viewed as being the direct investor." The managing director wrote that Hedge Fund B suggested setting up an SPV under a different name because a different name was needed to "intermediate" the purchase of mutual funds. When asked what would be problematic about ZCM being viewed as the direct investor, the ZCM managing director wrote that "[t]his is the familiar problem that mutual funds dislike mutual fund timers that arb their redemption policies." Another former ZCM managing director responded that ZCM had previously "set up subsidiaries of [ZCM] (with non-ZCM) names" in connection with its financing arrangement with Hedge Fund A and asked whether that would "solve the problem." ZCM proceeded to create for Hedge Fund B an SPV, to which it assigned a name not recognizable as connected to ZCM.

11. In addition, ZCM set up SPVs for use by two other hedge fund clients at the time the financing transactions were initiated in 2000 and 2001.

12. Further, in 1999, Hedge Fund B requested that ZCM purchase annuity policies with ZCM as owner and one of several ZCM employees named as annuitant on each policy. In December, 2000, a ZCM managing director wrote in an e-mail that Hedge Fund B was doing so because mutual funds were "constantly prohibiting" it from trading, and the variable annuity structure provided a "screen" that made it harder for the underlying mutual funds to detect its market timing activity. From 1999 to 2001, at the request of this counterparty, ZCM purchased at least nine variable annuity contracts. The annuitants named on these policies were ZCM employees, though ZCM was designated as the owner and beneficiary of the policies. Any profits or losses accrued for the benefit of Hedge Fund B. Hedge Fund B then engaged in market timing in the underlying mutual fund portfolios with financing provided by ZCM.

13. In or around February, 2002, a ZCM risk management employee cautioned ZCM's senior management by email that ZCM's hedge funds clients' market timing transactions exposed the company to potential "reputational" risk because some might view the practice of market timing as harmful to other mutual fund shareholders. ZCM management imposed a freeze on any new financing transactions with mutual fund market timers pending ZCM's review of and further inquiry into the business. In addition, internal auditors at Zurich Global Assets, acting at the request and direction of in-house counsel, were conducting a review of operational deficiencies with regard to ZCM's financing of Hedge

Fund B that had come to light in the fall of 2001, after Hedge Fund B's election to terminate its financing arrangement with ZCM. In March 2002, the auditors made a number of comments and recommendations, including the suggestion, with regard to potential reputational risks, that ZCM assess ZCM's continued participation in market timing deals given the prohibitions by some mutual fund companies. A new management team that was installed in April 2002 maintained the freeze on any new financing transactions with hedge funds engaged in market timing of mutual funds, and ZCM did not thereafter enter into such financing transactions. However, while the financing transaction with Hedge Fund B had already been terminated in August 2001, ZCM continued to finance its three other existing market timing clients until the fall of 2003.

ZCM Profited While Its Clients' Short-Term Trading Harmed Mutual Funds and Their Shareholders

14. ZCM profited from the fees it received from the business of providing derivative financing to hedge funds engaging in a mutual-fund market timing strategy. From 1999 through September, 2003, ZCM's revenue from providing financing to the four hedge fund clients was approximately $11 million. Numerous mutual funds and their shareholders suffered dilutive harm caused by short-term market timing trading done by these hedge funds with financing provided by ZCM.

D. ZCM Aided and Abetted and Caused Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder

15. As a result of the conduct described above, ZCM willfully aided and abetted and caused violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit, in connection with the purchase or sale of securities, the use of any manipulative or deceptive device, including any device, scheme or artifice to defraud; making any untrue statement of material fact or omitting to state a material fact when doing so makes the statement made misleading; or engaging in any act, practice or course of business which operates or would operate as a fraud. ZCM's market timing hedge fund clients engaged in a scheme to defraud mutual funds. Specifically, these clients utilized numerous deceptive practices to market time mutual funds. ZCM knowingly provided substantial assistance to these hedge funds. For example, ZCM created seemingly unaffiliated SPVs in whose name multiple brokerage accounts were opened, and this enabled its hedge fund clients to disguise their identities (and ZCM's identity) to market time mutual funds. Accordingly, ZCM willfully aided and abetted and caused violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

E. Respondent's Remedial Efforts

16. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff by Respondent during its investigation.

F. **Undertakings**

17. Ongoing Cooperation. Respondent shall cooperate fully with the Commission in any and all investigations, litigations or other proceedings relating to or arising from the matters described in this Order. In connection with such cooperation, Respondent has undertaken:

a. To use its best efforts to cause employees to be interviewed by the Commission's staff at such times as the staff reasonably may direct;

b. To use its best efforts to cause employees to appear and testify truthfully and completely without service of a notice or subpoena in such investigations, depositions, hearings or trials as may be requested by the Commission's Staff; and

c. To use its best efforts to facilitate access to its former employees.

18. Respondent undertakes pursuant to Rule 1101 of the Commission's Rules on Fair Fund and Disgorgement Plans [17 C.F.R. § 201.1101], and in consultation with the Staff of the Commission, to develop, with the assistance of an expert consultant, a plan to distribute the $16,809,354.42 in disgorgement, civil penalties, and interest as provided for in the Order ("Distribution Plan"), which will be submitted to the Commission within 180 days for notice in accordance with Rule 1103 [17 C.F.R. § 201.1103]. Following a Commission order approving a Distribution Plan, as provided in Rule 1104 [17 C.F.R. § 201.1104], Respondent shall take all necessary and appropriate steps to assist the Commission-appointed Administrator of the final Distribution Plan. Respondents shall bear the costs of administering and implementing the final Distribution Plan.

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 Section 15(b) and Section 21C of the Exchange Act and Section 9(b) of the Investment Company Act, it is hereby ORDERED that:

A. Respondent shall pay disgorgement in the amount of $11 million, pre-judgment interest in the amount of $1,809,354.42, and a civil money penalty in the amount of $4 million, for a total payment of $16,809,354.42.

B. Respondent shall cease and desist from committing or causing any violations and any future violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder;

C. Respondent is hereby censured; and

D. Respondent shall, within 30 days of the entry of this Order, pay disgorgement of $11 million, pre-judgment interest in the amount of $1,809,354.42, and a civil money penalty in the amount of $4 million to the Securities and Exchange Commission: Such payment shall be: (A) made by wire transfer, 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) wired, hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Alexandria, Stop 0-3, VA 22312; and (D) submitted under cover letter that identifies ZCM as 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 Helene T. Glotzer, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, Northeast Regional Office, 3 World Financial Center, New York, NY, 10281.

E. There shall be, pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, a Fair Fund established for the funds described in Section IV.A and D ("Fair Fund Distribution"), which shall be distributed to the affected mutual funds. 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, Respondent agrees that it shall not, after offset or reduction in any Related Investor Action based on Respondent's payment of disgorgement in this action, argue that it is entitled to, nor shall it further benefit by offset or reduction of any part of ZCM'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 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 Respondent by or on behalf of one or more investors or mutual funds based on substantially the same facts as alleged in this Order instituted by the Commission in this proceeding.

F. Respondents shall comply with the undertakings enumerated in Section III.F.18.

By the Commission.

Nancy M. Morris
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Atkins Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55712 / May 7, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12629

In the Matter of

Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc.,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc. ("Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement ("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, Respondent consents to the entry of this Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Order"), as set forth below.

Document 10 of 33

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:[1]

A. RESPONDENT

Citigroup Global Markets, Inc., a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act, is the successor by merger to Legg Mason Wood Walker Inc. ("LMWW"). LMWW was a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act during the relevant period. Thereafter, on December 1, 2005, Citigroup Inc. acquired LMWW and then merged LMWW into its subsidiary, Citigroup Global Markets Inc. Subsequently, a Form BDW was filed with respect to the registration of LMWW, and it was accepted by the Commission on June 6, 2006. Prior to Citigroup Inc.'s acquiring it, LMWW engaged in the conduct described in this Order.

B. SUMMARY

As part of its broker-dealer business, LMWW underwrote and managed a limited number of auctions for auction rate securities. From at least January 1, 2003 through June 30, 2004, in connection with certain auctions, LMWW engaged in the practice, described in Section III.C.2 below, that violates Section 17(a)(2) of the Securities Act of 1933 ("Securities Act"). Accordingly, Respondent violated that provision.

C. FACTS

1. The Auction Rate Securities Market

Auction rate securities are municipal bonds, corporate bonds, and preferred stocks with interest rates or dividend yields that are periodically re-set through auctions, typically every 7, 14, 28, or 35 days. Auction rate bonds are usually issued with maturities of 30 years, but the maturities can range from 5 years to perpetuity. Auction rate securities are often marketed to issuers as an alternative variable rate financing vehicle, and to investors as an alternative to money market funds. Auction rate securities were first developed in 1984, and the auction rate securities market has grown to well over $200 billion. Mostly institutional investors participate in the auction rate securities markets, although recently smaller investors also have begun participating in the market. Typically, the minimum investment is $25,000.

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[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.

a. Auction Mechanics. Auction rate securities are auctioned at par so the return on the investment to the investor and the cost of financing to the issuer between auction dates is determined by the interest rate or dividend yield set through the auctions.[2] According to the disclosure documents (the prospectus or official statement) for each security, the interest rate or dividend yield is set through an auction (commonly referred to as a "Dutch" auction) in which bids with successively higher rates are accepted until all of the securities in the auction are sold. Investors can only submit the following types of orders: 1) a "hold" order, which is the default order for current investors (i.e., the order that is entered for a current holder if the holder takes no action), where a current investor will keep the securities at the rate at which the auction clears; 2) a "hold-at-rate" bid, where a current investor will only keep the securities if the clearing rate is at or above the specified rate; 3) a "sell" order, where a current investor will sell the securities regardless of the clearing rate; or 4) a "buy" bid, where a prospective investor, or a current investor who wants more securities, will buy securities if the clearing rate is at or above the specified rate. Disclosure documents often state that an investor's order is an irrevocable offer.

The final rate at which all of the securities are sold is the "clearing rate" that applies to all of the securities in the auction until the next auction. Bids with the lowest rate and then successively higher rates are accepted until all of the sell orders are filled. The clearing rate is the lowest rate bid sufficient to cover all of the securities for sale in the auction.[3] If there are not enough bids to cover the securities for sale, then the auction fails, the issuer pays an above-market rate set by a pre-determined formula described in the disclosure documents, and all of the current holders continue to hold the securities, with minor exceptions. If all of the current holders of the security elect to hold their positions without bidding a particular rate, then the clearing rate is the all-hold rate, a below-market rate set by a formula described in the disclosure documents.

b. Broker-Dealers' Role in Auctions. The issuer of each security selects one or more broker-dealers to underwrite the offering and/or manage the auction process. Investors can only submit orders through the selected broker-dealers. The issuer pays an annualized fee to each broker-dealer engaged to manage an auction (typically 25 basis points for the par value of the securities that it manages). The issuer also selects an auction agent to collect the orders and determine the clearing rate for the auction.

Investors must submit orders for an auction to the broker-dealer by a specified time. Many broker-dealers have an internal deadline by which investors must submit their orders to the broker-

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[2] Between auctions, investors might be able to buy or sell auction rate securities in the secondary market at prices greater than, equal to, or less than par.

[3] For example, suppose $100,000 of securities were for sale and the auction received four buy bids. Bid A was for $50,000 at 1.10%, Bid B was for $50,000 at 1.15%, Bid C was for $50,000 at 1.15%, and Bid D was for $25,000 at 1.20%. Under these circumstances, the "clearing rate" would be 1.15%, meaning all of the securities in the auction would pay interest at a rate of 1.15% until the next auction. Bid A would be allocated $50,000, Bids B and C would receive pro-rata allocations ($25,000 each), and Bid D would receive no allocation.

dealer. This internal deadline allows the broker-dealer sufficient time to process and submit the orders to the auction agent. Other broker-dealers allow investors to submit orders up until the submission deadline, i.e., the deadline for broker-dealers to submit orders to the auction agent. The broker-dealers must submit the orders to the auction agent before the submission deadline, and usually must identify each separate order.

c. Auction Agents' Role in Auctions. After receiving the orders from the broker-dealers, the auction agent calculates the clearing rate that will apply until the next auction. In practice, however, if there is only one broker-dealer, the broker-dealer can discern the clearing rate before submitting the orders to the auction agent.

The auction agent allocates the securities to the broker-dealers based on the orders they submitted. The auction procedures generally state that orders are filled in the following order: hold orders, hold-at-rate and buy bids with a rate below the clearing rate, hold-at-rate orders with a rate at the clearing rate, and buy bids with a rate at the clearing rate. When there are more bids for securities at the clearing rate than securities remaining for sale, the securities are allocated on a pro rata basis first to the hold-at-rate bidders and then to the buy bidders. Generally, the auction procedures require broker-dealers to follow the same hierarchy in allocating the securities to their customers.

d. Disclosures Regarding Broker-Dealer Bidding. During the relevant period, the disclosure documents for different securities varied as to what, if anything, they disclosed about broker-dealers bidding in auctions that they were managing. Some disclosure documents did not disclose anything about bidding by broker-dealers. Other disclosure documents disclosed that broker-dealers may bid in auctions with language similar to the following: "[a] broker-dealer may submit orders in Auctions for its own accounts." Still other disclosure documents disclosed that broker-dealers may bid in auctions and may have an information advantage with language similar to the following: "[a] Broker-Dealer may submit orders in Auctions for its own accounts. Any Broker-Dealer submitting an order for its own account in any Auction might have an advantage over other bidders in that it would have knowledge of other orders placed through it for that Auction (but it would not have knowledge of orders submitted by other Broker-Dealers, if any)."

2. LMWW's Conduct

LMWW intervened in auctions by bidding for its proprietary account to prevent failed auctions without adequate disclosure. Failed auctions occur when there are more securities for sale than there are bids for securities and result in an above-market rate described in the disclosure documents. LMWW submitted bids to ensure that all of the securities would be purchased to avoid failed auctions and thereby, in certain instances, affected the clearing rate.[4]

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[4] The clearing rate determines the interest rate or yield the issuer must pay to investors until the next auction. In those instances when this practice lowered the clearing rate, investors received a lower rate of return on their investments. To the extent that this practice affected the clearing

D. LEGAL SECTION

Section 17(a)(2) of the Securities Act prohibits material misstatements and omissions in any offer or sale of securities. Negligent conduct can violate Section 17(a)(2). See, e.g., SEC v. Hughes Capital Corp., 124 F.3d 449, 453 (3d Cir. 1997). As a result of LMWW's conduct, Respondent willfully[5] violated Section 17(a)(2) of the Securities Act.

E. THE PENALTY AMOUNT

The Commission aims to promote voluntary disclosures in industry-wide investigations and to encourage firms to provide comprehensive information to the staff in such investigations. See In the Matter of Bear, Stearns & Co. Inc. et al., Securities Act Release No. 8684 (May, 31, 2006) ("Previous Settlement"). In determining the size of the penalty in this matter, the Commission considered LMWW's cooperation afforded the Commission staff and LMWW's relatively small share of the auction rate securities markets. The Commission, however, also considered that LMWW reported the practice described in Section III.C.2 later than the broker-dealers in the Previous Settlement reported their practices.

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. In determining not to seek or order that the Respondent cease and desist from committing or causing any violation and any future violations of Section 17(a)(2) of the Securities Act, the Commission considered that the Respondent already is subject to such an order concerning the same type of misconduct described in this Order. See In the Matter of Bear, Stearns & Co., Inc., Securities Act Release 8684 (May 31, 2006).

Accordingly, pursuant to Section 15(b) of the Exchange Act, it is hereby ORDERED that Respondent:

A. Be, and hereby is, censured, and

B. Shall, within 10 days of the entry of this Order, pay a civil money penalty of $200,000 to the United States Treasury. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank

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rate, investors may not have been aware of the liquidity and credit risks associated with certain securities.

[5] "Willfully" as used in this Order means intentionally committing the act which constitutes the violation, see Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000); Tager v. SEC, 344 F.2d 5, 8 (2d Cir. 1965). There is no requirement that the actor also be aware that he is violating one of the Rules or Acts.

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 the 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 Kenneth R. Lench, Division of Enforcement, Securities and Exchange Commission, 100 F Street N.E., Washington, D.C. 20549-6041.

By the Commission.

Nancy M. Morris
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Atkins
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8799 / May 7, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12629

In the Matter of **Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc.,** **Respondents.**	**ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933, GRANTING A WAIVER OF THE DISQUALIFICATION PROVISION OF RULE 602(c)(3)**

Citigroup Global Markets, Inc. has submitted a letter, dated February 7, 2007, for a waiver of the disqualification from the exemption under Regulation E arising from its settlement of an administrative proceeding commenced by the Commission. On May 7, 2007, pursuant to the offer of settlement by Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc., the Commission issued an Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 (the "Order"). Under the Order, the Commission found that Citigroup Global Markets willfully violated Section 17(a)(2) of the Securities Act of 1933 (the "Securities Act") because Legg Mason Wood Walker, which subsequently was merged into Citigroup Global Markets, engaged in a violative practice in connection with certain auctions for auction rate securities.

The Order censures Citigroup Global Markets and requires Citigroup Global Markets, within 10 days of the entry of this Order, to pay a civil money penalty in the amount of $200,000 to the United States Treasury.

The Regulation E exemption is not available for the securities of a small business investment company or business development company issuer if an investment adviser or underwriter of the securities to be offered is subject to a Commission order pursuant to Section 15(b) of the Exchange Act. *See* Rule 602(c)(3) under the Securities Act. The Commission may waive the disqualification upon a showing of good cause. *See* Rule 602(e).

Based on the representations set forth in the request made by Citigroup Global Markets, the Commission has determined that a showing of good cause has been made pursuant to Rule 602(e) and that the request for a waiver of the disqualification should be granted.

Document 11 of 33

Accordingly, **IT IS ORDERED**, pursuant to Rule 602(e) under the Securities Act, that a waiver from the application of the disqualification provision of Rule 602(c)(3) under the Securities Act resulting from the entry of the Order is hereby granted.

By the Commission.

Nancy M. Morris
Secretary

By: J. Lynn Taylor
Assistant Secretary

Commissioner Atkins
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8800 / May 7, 2007

SECURITIES EXCHANGE ACT OF 1934
Release No. 55713 / May 7, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12629

In the Matter of **Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc.,** **Respondent.**	**ORDER UNDER SECTION 27A(b) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b) OF THE SECURITIES EXCHANGE ACT OF 1934, GRANTING WAIVERS OF THE DISQUALIFICATION PROVISIONS OF SECTION 27A(b)(1)(A)(ii) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b)(1)(A)(ii) OF THE SECURITIES EXCHANGE ACT OF 1934**

Citigroup Global Markets, Inc. has submitted a letter on behalf of itself and its affiliates, dated February 28, 2007, for a waiver of the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act of 1933 ("Securities Act") and Section 21E(b)(1)(A)(ii) of the Securities Exchange Act of 1934 ("Exchange Act") arising from its settlement of an administrative proceeding commenced by the Commission. On May 7, 2007, pursuant to the Offer of Settlement by Citigroup Global Markets, Inc., successor by merger to Legg Mason Wood Walker Inc., the Commission issued an Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 (the "Order"). Under the Order, the Commission found that Citigroup Global Markets willfully violated Section 17(a)(2) of the Securities Act because Legg Mason Wood Walker, which subsequently was merged into Citigroup Global Markets, engaged in a violative practice in connection with certain auctions for auction rate securities.

The Order censures Citigroup Global Markets and requires Citigroup Global Markets, within 10 days of the entry of this Order, to pay a civil money penalty in the amount of $200,000 to the United States Treasury.

The safe harbor provisions of Section 27A(c) of the Securities Act and Section 21E(c) of the Exchange Act are not available for any forward looking statement that is "made with respect to the business or operations of an issuer, if the issuer . . . during the 3-year period preceding the

Document 12 of 33

date on which the statement was first made . . . has been made the subject of an . . . administrative decree or order arising out of a governmental action that (I) prohibits future violations of the antifraud provisions of the federal securities laws; (II) requires that the issuer cease and desist from violating the antifraud provisions of the securities laws; or (III) determines that the issuer violated the antifraud provisions of the securities laws[.]" Section 27A(b)(1)(A)(ii) of the Securities Act and Section 21E(b)(1)(A)(ii) of the Exchange Act. The disqualifications may be waived "to the extent otherwise specifically provided by rule, regulation, or order of the Commission." Section 27A(b) of the Securities Act and Section 21E(b) of the Exchange Act.

Based on the representations set forth in Citigroup Global Markets' letter, the Commission has determined that, under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Order is appropriate and should be granted.

Accordingly, **IT IS ORDERED**, pursuant to Section 27A(b) of the Securities Act and Section 27E(b) of the Exchange Act, that a waiver from the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act and Section 21E(b)(1)(A)(ii) of the Exchange Act as to Citigroup Global Markets and its affiliates resulting from the entry of the Order is hereby granted.

By the Commission.

Nancy M. Morris
Secretary

J Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

Securities Exchange Act of 1934
Release No. 55725 / May 8, 2007

Accounting and Auditing Enforcement
Release No. 2607 / May 8, 2007

Administrative Proceeding
File No. 3-12630

In the Matter of MOTOROLA, INC., Respondent.	ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Motorola, Inc. ("Motorola" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement ("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 Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

Document 13 of 33

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

A. Summary

1. This case involves a round-trip of cash between Motorola and Adelphia Communications Corporation ("Adelphia"). Pursuant to a purported marketing support agreement entered into in 2001, Adelphia paid money to Motorola which was immediately returned to Adelphia in the form of marketing support payments. No marketing was specified in the agreement and no marketing was done pursuant to the agreement. Adelphia used Motorola's marketing support payments to falsify its earnings in 2000 and 2001.

2. In the Fall of 2000, Adelphia, a cable television system owner and operator, asked Motorola, a vendor that provided digital cable television set-top boxes used by Adelphia, to enter into a marketing support agreement for the stated purpose of helping Adelphia fund its roll-out of digital cable television service. Adelphia proposed to pre-fund Motorola's marketing support payment obligation through a retroactive and offsetting price increase applied to digital cable television set-top boxes Motorola had supplied Adelphia in the past and was to supply Adelphia in the future pursuant to a pre-existing purchase contract.

3. The marketing support agreement, which was not finalized until March 2001, was backdated to the prior fiscal year and applied retroactively to set-top boxes that had already been sold to Adelphia. The agreement also contained a false reason for the retroactive price increase.

4. The transaction had no economic substance, amounting to a round-trip of cash, and was designed by Adelphia to increase artificially its Earnings Before Interest, Taxes, Depreciation, and Amortization ("EBITDA") by reducing operating costs by the amount of the marketing support payments from Motorola. In this manner, Adelphia was able to use the transaction to reduce improperly its operating costs and increase its earnings by approximately $18.3 million in 2000 and $28 million in 2001.

5. Motorola knew or should have known that Adelphia was misusing the marketing support agreement. The marketing support agreement was backdated to a prior fiscal year, it applied retroactively to set-top boxes that had already been sold to Adelphia, and it contained a false reason for the price increase. Motorola executives also knew that (i) the marketing support agreement did not identify any marketing to be done by Adelphia and Motorola did not require that any marketing be done pursuant to the agreement; (ii) the transaction was a round-trip transfer of cash; and (iii) Motorola accounted for the transaction as economically neutral to Motorola.

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

B. Respondent

6. Motorola is a Delaware corporation, with corporate headquarters in Schaumburg, Illinois. Motorola is a global manufacturer and seller of wireless, broadband, and automotive communications technologies. At all relevant times, Motorola's common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and was publicly traded on the New York Stock Exchange.

C. Relevant Entity

7. Adelphia is a Delaware corporation, headquartered in Greenwood Village, Colorado. During the relevant period, Adelphia was headquartered in Coudersport, Pennsylvania. Adelphia owns, operates, and manages cable television systems and other related telecommunications businesses. On March 27, 2002, Adelphia announced that it was liable for approximately $2.3 billion in debt that it had previously failed to disclose. In May 2002, certain members of the Rigas family, who controlled and held officer and director positions with Adelphia, resigned and Adelphia disclosed that it expected to restate its financial statements for fiscal years 2000 and 2001. On July 18, 2002, the Commission filed *SEC v. Adelphia Communications Corporation, et al.*, 02 Civ. 5776 (PKC) (S.D.N.Y.), alleging that widespread, multifaceted financial fraud occurred at Adelphia. On May 31, 2005, the U.S. District Court for the Southern District of New York entered a consent order enjoining Adelphia from violating Section 17(a) of the Securities Act of 1933, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, and 13a-13 under the Exchange Act.

D. Facts

Background

8. In January 2000, Motorola acquired General Instrument Corporation ("General Instrument") for $17 billion in stock. General Instrument was integrated into Motorola as its broadband communications sector and was a major supplier of digital cable television set-top boxes to Adelphia both prior to and after its integration into Motorola. In fiscal year 2000, the sector's earnings accounted for approximately 43% of the combined earnings reported by all of Motorola's profitable sectors in that year.

9. In May 2000, Adelphia and Motorola entered into a purchase agreement that governed the pricing of digital cable television set-top boxes through December 2001 based upon the contemplated purchase by Adelphia of 1.6 million set-top boxes over the life of the contract. The purchase agreement did not require Adelphia to purchase any set-top boxes and it did not provide for a penalty if Adelphia purchased less than the 1.6 million set-top boxes contemplated by the agreement.

10. In June 2000, Adelphia realized that its second quarter reported EBITDA would fall below analysts' expectations. Adelphia executives devised a plan to inflate artificially EBITDA by reducing operating costs through the purported marketing support agreement with Motorola.

11. In late August 2000, Adelphia approached Motorola with the idea of entering into the marketing support agreement.

Key Factors That Should Have Put Motorola On Notice That Adelphia Was Not Using The Marketing Support Agreement For Its Intended Purpose

12. Between August 2000 and March 2001, when the marketing support agreement documents were signed, the executives who reviewed, or were told the substance of, the proposed transaction, were confronted with the following unusual facts unique to this transaction:

- Adelphia's request was the first time any customer had asked the Motorola executives to increase the price of Motorola's products;

- The marketing support agreement, which Adelphia provided to Motorola, contained a false reason for the price increase;

- Motorola executives insisted as a condition to entering into the transaction that Adelphia provide a letter from its counsel that Adelphia would not use the transaction in contravention of federal regulations governing cable television rates. Instead, an Adelphia finance executive who was later implicated in Adelphia's fraud sent a short confirmatory letter to Motorola without advising Motorola whether its counsel had been consulted;

- The marketing support agreement did not contain any details of marketing to be done by Adelphia and required no input from Motorola's marketing department;

- The marketing support agreement was backdated and the price increase and marketing support payment obligation were made retroactive to the beginning of the prior fiscal year and applied to products that had already been sold to and paid for by Adelphia;

- The transaction was a "wash" transaction with no economic impact on Motorola; and

- Motorola did not treat the transaction as a marketing transaction for accounting purposes.

Motorola Asked Adelphia To Purchase More Set-Top Boxes Than Adelphia Needed In Exchange For Signing The Marketing Support Agreement

13. Shortly before the marketing support agreement was due to be signed in March 2001, Adelphia's orders for set-top boxes declined below the number called for under the May 2000 purchase agreement. Motorola knew that Adelphia did not need any additional set-top boxes at that time, but told Adelphia that it wanted Adelphia to purchase 100,000 additional set-top boxes. Adelphia agreed to make the purchase before the marketing support agreement was signed and before the close of Motorola's first quarter for fiscal year 2001.

Motorola Signed The Backdated Marketing Support Agreement And Made A Retroactive Marketing Support Payment

14. On or about March 21, 2001, Motorola signed the marketing support agreement documents that were backdated to the prior fiscal year. The marketing support agreement did not specify any marketing to be done by Adelphia and it contained a false reason for the price increase. In the document memorializing the price increase, Motorola stated falsely that the purpose of the price increase was to secure "incremental component volumes and factory capacity" to meet Adelphia's needs. In fact, Motorola executives knew that the true purpose of the price increase was to pre-fund Motorola's marketing support payment obligation to Adelphia.

15. In May 2001, Motorola made the first $18.3 million marketing support payment for marketing purportedly done in 2000. The payment was funded by Adelphia three days earlier when it paid Motorola the retroactive price increase on set-top boxes previously purchased by Adelphia in 2000.

Motorola Again Asked Adelphia To Purchase More Set-Top Boxes Than It Needed And Defrayed The Costs Of Warehousing The Boxes In A Third-Party Warehouse In Exchange For Maintaining The Marketing Support Agreement

16. In early June 2001, Adelphia told Motorola that it would be reducing its orders of set-top boxes due to decreased demand. Motorola knew that Adelphia had excess inventory that would carry it to the middle of the following year. Nevertheless, Motorola insisted that Adelphia purchase an additional 150,000 set-top boxes. Motorola proposed to finance the purchase through Motorola Credit Corporation, so that Adelphia would be able to pay for the additional set-top boxes in two installments over a period of one year and Motorola would be able to record the sales before the close of its second fiscal quarter.

17. To implement the deal and protect Motorola, Motorola insured the Adelphia receivable. Motorola knew or should have known that Adelphia did not actually need any additional set-top boxes, so it offered Adelphia credits that could be used for other Motorola services, including marketing, to offset the cost of warehousing the 150,000 set-top boxes in a third-party warehouse. Adelphia agreed to purchase the additional set-top boxes before the close of Motorola's second quarter for fiscal year 2001.

Motorola Agreed To Increase Its Marketing Support Payment Obligation In Exchange For Adelphia's Agreement To Purchase More Set-Top Boxes In 2002

18. In mid-December 2001, at the end of Adelphia's fiscal year, Adelphia asked Motorola to amend the marketing support agreement to require that Motorola make an additional $10 million marketing support payment for 2001 funded by an another retroactive price increase on set-top boxes previously delivered to Adelphia. Motorola agreed to the amendment after Adelphia agreed to purchase 200,000 set-top boxes in 2002. The amended marketing support agreement contained the same false reason for the price increase that the original agreement contained.

Adelphia Used The Marketing Support Agreement To Artificially Decrease Marketing Expenses And Increase EBITDA

19. Adelphia recorded the marketing support payments as a contra-expense to marketing costs. This accounting treatment lowered the amount of recorded marketing expenses and, in turn, artificially inflated Adelphia's EBITDA. Adelphia recorded the price increases paid to Motorola as capital expenditures, which are depreciated over time and, therefore, have no impact on EBITDA and a minimal impact on earnings.

20. In total, from April 2000 through December 2001, Adelphia recorded improperly approximately $46.3 million in marketing support payments as reductions in current operating expenses, with the intended effect of inflating its reported EBITDA by $46.3 million over that period. Adelphia's accounting treatment violated Generally Accepted Accounting Principles ("GAAP") because it reflected the round-trip transaction as decreasing its reported expenses and increasing its reported earnings when it did not have that effect.

Legal Analysis

21. The Exchange Act and Exchange Act rules require every issuer of registered securities to file reports with the Commission that accurately reflect the issuer's financial performance and provide other true and accurate information to the public.

22. Adelphia violated Section 13(a) and Rules 13a-1, 13a-13, and 12b-20 by filing with the Commission reports from April 2000 through December 2001, each containing materially false and misleading earnings in the financial statements for each reporting period.

23. Adelphia violated Section 13(b)(2)(A) by improperly recording the marketing support payments as a contra-expense to Adelphia's marketing costs, and by recording as capital expenditures the artificial price increase on the set-top boxes. Certain officers of Adelphia knowingly falsified, and caused others to falsify, Adelphia's books, records and accounts, including the fraudulent journal entries of the price increases and marketing support payments.

24. Section 21C of the Exchange Act provides that the Commission may issue a cease-and-desist order against a person who is "a cause of [another person's] violation, due to an act or omission the person knew or should have known would contribute to such violation."[2] Based on the conduct described above, Respondent was a cause of Adelphia's violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 of the Exchange Act.

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[2] Where the primary violations underlying a finding that a person is "a cause of" violations do not themselves require a finding of scienter, the standard of liability for being "a cause of" such violations under Section 21C of the Exchange Act is negligence. *See KPMG LLP v. SEC*, 289 F. 3d 109, 112 (DC Cir. 2002).

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanction agreed to in Respondent's Offer.

Accordingly, pursuant to Section 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondent cease and desist from committing or causing any violations and any future violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

B. Respondent is herby ordered pursuant to Section 21C(e) of the Exchange Act to pay disgorgement in the amount of $18 million and prejudgment interest in the amount of $7 million, for a total payment of $25,000,000. Within 10 days of entry of this Order, Motorola shall deliver this payment into the Registry of the Court for the United States District Court for the Southern District of New York in the case captioned *Securities and Exchange Commission v. Adelphia Communications Corp., et al.*, 02 Civ. 5776 (PKC). Simultaneously, Motorola shall transmit by hand delivery to the Clerk of the Court, United States District Court for the Southern District of New York, a letter specifying that the payment is made in connection with the Commission's administrative proceeding and a copy of the letter shall be simultaneously transmitted by facsimile to Alistaire Bambach, Assistant Regional Director, Division of Enforcement, Securities and Exchange Commission, Northeast Regional Office, 3 World Financial Center, New York, NY 10281 (212) 336-1324 (facsimile). In accordance with Rule 1102 of the Commission's Rules of Practice [17 C.F.R. 201.1102], the procedures set forth herein shall govern the distribution of any funds paid pursuant to this Order.

By the Commission.

Nancy M. Morris

Nancy M. Morris
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8801 / May 9, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12631

In the Matter of Morgan Stanley & Co., Incorporated Respondent.	CORRECTED ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE DISQUALIFICATION PROVISION OF RULE 602(c)(3)

I.

Morgan Stanley & Co., Incorporated ("MS & Co.") has submitted a letter, dated March 7, 2007, requesting a waiver of the Rule 602(c)(3) disqualification from the exemption from registration under Regulation E arising from MS & Co.'s settlement of an administrative proceeding commenced by the Commission.

II.

On May 9, 2007, pursuant to MS & Co.'s Offer of Settlement, the Commission issued an Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 against MS & Co. Under the Order, the Commission found that MS & Co. failed to seek to obtain best execution for certain orders for OTC securities placed by retail customers of MS & Co., MSDW and third party broker-dealers that routed orders to MS & Co. for execution. In the Order, the Commission ordered MS & Co. to cease-and-desist from committing or causing any violations and any future violations of Section 15(c)(1)(A) of the Securities Exchange Act of 1934 ("Exchange Act"). In the Order, the Commission also censured MS & Co. and ordered it to disgorge ill-gotten gains, pay a civil monetary penalty and comply with certain undertakings.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if a principal

Document 14 of 33

security holder, investment advisor or underwriter of the securities to be offered is subject to a Commission order pursuant to Section 15(b) of the Exchange Act. Rule 602(c)(3). Rule 602(e) of the Securities Act of 1933 ("Securities Act") provides, however, that disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances, that the exception be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in MS & Co.'s request, the Commission has determined that pursuant to Rule 602(e) under the Securities Act a showing of good cause has been made that it is not necessary under the circumstances that the exemption be denied as a result of the Order.

Accordingly, **IT IS ORDERED**, pursuant to Rule 602(e) under the Securities Act, that a waiver from the application of the disqualification provisions of Rule 602(c)(3) under the Securities Act resulting from the entry of the Order, respectively, is hereby granted.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8802 / May 9, 2007

SECURITIES EXCHANGE ACT OF 1934
Release No. 55727 / May 9, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12631

In the Matter of **MORGAN STANLEY & CO. INCORPORATED,** **Respondent.**	**CORRECTED** **ORDER UNDER SECTION 27A(b) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b) OF THE SECURITIES EXCHANGE ACT OF 1934 GRANTING WAIVERS OF THE DISQUALIFICATION PROVISIONS OF SECTION 27A(b)(1)(A)(ii) OF THE SECURITIES ACT OF 1933 AND SECTION 21E(b)(1)(A)(ii) OF THE SECURITIES EXCHANGE ACT OF 1934**

Morgan Stanley, the parent company of Morgan Stanley & Co., Incorporated ("MS & Co.") has submitted a letter, dated March 7, 2007, requesting a waiver of the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act of 1933 ("Securities Act") and Section 21E(b)(1)(A)(ii) of the Securities Exchange Act of 1934 ("Exchange Act") arising from MS & Co.'s settlement of an administrative proceeding commenced by the Commission.

On May 9, 2007, pursuant to MS & Co.'s Offer of Settlement, the Commission issued an Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 against MS & Co. In the Order, the Commission ordered MS & Co. to cease-and-desist from committing or causing any violations and any future violations of Section 15(c)(1)(A) of the Securities Exchange Act of 1934 ("Exchange Act"). In the Order, the Commission also censured MS & Co. and ordered it to disgorge ill-gotten gains, pay a civil monetary penalty and comply with certain undertakings.

The safe harbor provisions of Section 27A(c) of the Securities Act and Section 21E(c) of the Exchange Act are not available for any forward looking statement that is "made with respect to the business or operations of the issuer, if the issuer . . . during the 3-year period preceding the date on which the statement was first made . . . has been made the subject of a judicial or administrative

Document 15 of 33

decree or order arising out of a governmental action that (I) prohibits future violations of the antifraud provisions of the securities laws; (II) requires that the issuer cease and desist from violating the antifraud provisions of the securities laws; or (III) determines that the issuer violated the antifraud provisions of the securities laws[.]" Securities Act, Section 27A(b)(1)(A)(ii); Exchange Act, Section 21E(b)(1)(A)(ii). The disqualifications may be waived "to the extent otherwise specifically provided by rule, regulation, or order of the Commission." Securities Act, Section 27A(b); Exchange Act, Section 21E(b).

Based upon the representations set forth in Morgan Stanley's March 7, 2007 request, the Commission has determined that under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Final Judgment and the Order is appropriate and should be granted.

Accordingly, IT IS ORDERED, pursuant to Section 27A(b) of the Securities Act and Section 21E(b) of the Exchange Act, that a waiver from the disqualification provisions of Section 27A(b)(1)(A)(ii) of the Securities Act and Section 21E(b)(1)(A)(ii) of the Exchange Act resulting from the entry of the Final Judgment and the Order are hereby granted.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55726 / May 9, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12631

In the Matter of **Morgan Stanley & Co. Incorporated,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

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 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Morgan Stanley & Co. Incorporated ("MS & Co." 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 him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

Document 16 of 33

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

1. This matter arises from MS & Co.'s failure to provide best execution to certain retail orders for over-the-counter ("OTC") securities during the time period of October 24, 2001, through December 8, 2004 (hereinafter the "relevant time period"). MS & Co., as a broker-dealer, had a legal duty to seek to obtain for its retail customers' orders the most favorable terms reasonably available under the circumstances, taking into account price, order size, trading characteristics of the security, speed of execution, clearing costs, and the cost and difficulty of executing an order in a particular market, as well as the potential for price improvement (i.e., best execution).

2. MS & Co. breached the duty of best execution on certain retail OTC orders in three ways. First, on October 24, 2001, MS & Co. embedded undisclosed mark-ups and mark-downs[2] on certain not held[3] retail orders without retail customers' prior consent to do so.[4]

3. Second, MS & Co. developed and implemented a trading mechanism that sometimes slowed down the execution of orders so that MS & Co. could try to obtain price improvement for not held orders. The new trading mechanism improperly delayed the execution of certain held market orders for which MS & Co. had an obligation to execute without hesitation as required.

4. Third, MS & Co. embedded undisclosed mark-ups and mark-downs on certain retail orders for OTC stocks in which it made a market but filled with executions from other market centers (the "Street"). Such executions should have been passed along to retail customers' orders "print-for-print," which means those should have received the same execution prices that MS & Co. received from the Street without any mark-ups, mark-downs, commissions or other fees. MS & Co.'s practice was not consistent with its obligations to its retail customers' orders or its internal compliance policies.

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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.

2 Mark-ups are added to the current offering price of a security and mark-downs are subtracted from the current bid price of a security by a dealer acting as a principal.

3 Not held orders are orders for which the customer gives the broker time and price discretion. The customer vests the broker with the discretion as to when and at what price to buy or sell the stock. In contrast, held market orders are orders that a broker must execute without hesitation at the prevailing market price because it does not have time and price discretion.

4 This matter only involves retail orders, not institutional orders. In 2001, the NASD rules permitted broker-dealers to embed undisclosed mark-ups and mark-downs (i.e., trade on a net basis) on institutional orders provided that the institutional customers consented. MS & Co. obtained such consent through negative consent letters.

5. During the relevant time period, MS & Co. failed to provide best execution to approximately 1,253,666 executions (3.7% of its OTC executions) valued at $7,957,019,712.

6. MS & Co. recognized revenue of approximately $5.95 million through its improper use of undisclosed mark-ups and mark-downs on not held orders and held market orders.

Respondent

7. MS & Co. is a Delaware corporation with its principal place of business in New York, New York. MS & Co. is a broker-dealer registered with the Commission pursuant to Section 15 of the Exchange Act, and is a member of self-regulatory organizations including NASD and the New York Stock Exchange. MS & Co. is also a registered investment adviser pursuant to Section 203(c) of the Advisers Act. MS & Co. engages in a nationwide securities business.

MS & Co.'s Market Making Activities

8. During the relevant time period, MS & Co. was registered as a Nasdaq market maker in approximately between 500 and 2,100 stocks. While MS & Co. primarily served institutional customers during the relevant time period, it also executed orders placed by its retail customers serviced by its Private Wealth Management ("PWM") unit, and retail orders routed to it from its retail broker-dealer affiliate and other third party broker-dealers on behalf of their retail customers. To facilitate retail order flow from retail broker-dealers, MS & Co. made itself accessible to third-party retail broker-dealers via automatic, electronic connectivity to its market-making systems. These broker-dealers thereby automatically routed retail orders directly to MS & Co. for execution.

9. Historically, MS & Co. used a third party software package to facilitate its market making activities. The third party software package automated a portion of these activities, but still required a trader to manually handle and process many orders. In 2000, MS & Co. decided to improve the efficiencies of its market making business by developing a new market-making system (the "market-making system"). MS & Co. assembled a cross-divisional team to develop this system. The new system initially supplemented the third party software package by making markets in stocks in which MS & Co. did not currently make a market and eventually replaced the third party software package. The market-making system was intended to replace and improve upon the third party software package's order handling processes. The market-making system executed orders in the same general manner as the third party software package but with more automation. MS & Co. viewed its market-making system as a distinct improvement over the third party software package because, among other reasons, it could execute orders at much faster speeds. During the relevant time period, this system processed approximately 34 million executions valued at $476 billion.

10. When MS & Co. decided to fill a customer's order on a riskless principal basis, i.e., with executions from the Street, it routed an identical order to the Street for execution (hereinafter

"Street Executions").[5] MS & Co. referred to the price at which the Street executed the order as the "execution price." After receiving shares for the customer's order from the Street, the market-making system then filled the customer order by "flipping" the street execution to the customer. MS & Co. referred to the price at which the customer order was filled as the "flip price." For various reasons, the flip price may not have been the same as the execution price. When the market-making system filled the customer order at the same price, MS & Co. (consistent with industry practice) referred to the trade as giving "print-for-print."

11. MS & Co.'s internal compliance policy stated that when a customer order was filled with Street Executions the customer should get print-for-print. More specifically, MS & Co.'s policy expressly provided that "if a better price was obtained [from the Street] the Firm must pass the benefits of those executions on to the customer." This policy was not limited to orders received from PWM customers.

12. In addition, MS & Co. told certain third-party retail broker-dealers that it would seek to obtain best execution for retail orders routed to it by those broker-dealers and that it would not charge any mark-ups, mark-downs, commissions or other fees on those routed orders. The term "retail customers" refers to customers of MS & Co.'s PWM unit, retail customers of MS & Co.'s retail broker-dealer affiliate and retail customers of other third-party broker-dealers who routed orders to MS & Co. for execution.

MS & Co. Initially Programmed Its
<u>Market-Making System Not to Give Print-for-Print</u>

13. Contrary to MS & Co.'s best execution obligations, its internal policies and its historical practices, when MS & Co. developed the market-making system, it initially failed to program the system to properly handle Street Executions for retail orders. The initial coding was designed to ensure that customers received execution prices that did not exceed the National Best Bid or Offer ("NBBO") and also permitted MS & Co. to add a mark-up or mark-down to certain transactions. This resulted, in certain instances, in Street Executions being marked-up or marked-down. As a result, retail customers could have received inferior executions either because MS & Co. did not pass along the benefit of a superior execution or because the market had moved between the time of execution and the time of comparison.

14. MS & Co. began using the market-making system in late May 2001, to make a market in a handful of stocks. Soon thereafter, during a testing phase, the Compliance Department compared the order handling functions of the market-making system to the order handling functions of the third party software package. During the review, Compliance discovered that the market-making system would not pass along Street Executions print-for-print.

15. On or about June 14, 2001, MS & Co. reprogrammed the market-making system to ensure it passed along Street Executions print-for-print. Because no order actually failed to receive

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5 A riskless principal trade is a trade in which a broker-dealer, after having received an order to buy (sell) a security, buys (sells) the security from (to) another person and sell (buys) the security to (from) the person who placed the order at the same price.

print-for-print as a result of the programming issue described above during the short time it was in place, MS & Co. did not recognize additional revenue as a result of the code.

MS & Co. Added Undisclosed Mark-ups And
<u>Mark-downs to Certain Retail Not Held Orders</u>

16. In the Fall of 2001, MS & Co. developed a new trading mechanism to automatically trade certain orders that MS & Co. had traditionally used traders to execute manually. Instead of executing the entire order at once, the new trading mechanism executed portions of the order over a period of time so as to lessen the market impact thereby possibly getting price improvement on the average price given to the customer.

17. On October 24, 2001, MS & Co. introduced the new trading mechanism and traders used it for not held orders. In order to charge a mark-up or mark-down on those not held orders processed by the new trading mechanism, MS & Co. also changed the way the market-making system passed Street Executions with respect to not held orders. The flip price for a not held order depended on the type of customer. There were two options for determining a not held execution price. Under the first option, the trading system passed the trade to the customer "print-for-print," without any embedded mark-up, mark-down, commission or other fee. Under the second option, the market-making system passed the trade to the customer at the current NBBO, regardless of the execution price received by MS & Co. (hereinafter the "Fill at the Inside" Instruction). In this case, if MS & Co. received a better execution price, the customer received the current NBBO and MS & Co. realized a mark-up or mark-down on the trade. Embedding a mark-up or mark-down in this situation is proper if the customer consents or if it is disclosed and the customer does not object.

18. During the relevant time period, the option for retail customers on their not held orders was "Fill At The Inside" despite the fact that MS & Co. had never made appropriate disclosure or received consent from them to embed a mark-up or mark down in their orders. Accordingly, MS & Co. breached its duty of best execution by embedding mark-ups and mark-downs on its retail not held orders.

MS & Co. Failed to Execute Certain Held
<u>Market Orders Without Hesitation</u>

19. On or about December 10, 2001, MS & Co. caused certain retail held market orders to be processed by the new trading mechanism that sometimes delayed executions. Absent disclosure to the contrary, when broker-dealers accept held market orders, they agree to execute them without hesitation at the prevailing market price even if a delay would result in a better price for the customer. A broker-dealer has no discretion with respect to such orders. More specifically, MS & Co. caused held market orders to be processed through the trading mechanism. As a result, the executions of certain market held orders that should have been executed without hesitation were delayed. Accordingly, MS & Co. breached its duty of best execution by not executing all of its retail held orders without hesitation.

MS & Co. Added Undisclosed Mark-ups And
Mark-downs to Certain Retail Held Orders

20. Also on December 10, 2001, MS & Co. changed the way the market-making system passed Street Executions on held orders without display obligations.[6] MS & Co. referred to this new programming code as "Capture Spread for Non-Display Held Orders" (hereinafter the "Code").[7] The Code had an effect on executions that was similar, but not identical, to the effect of the code in the initial version of the market-making system that Compliance had identified as being problematic and was removed.

21. After December 10, 2001, MS & Co. did not pass along Street Executions to certain retail customers' held orders print-for-print. For held market buy orders, the market-making system compared the execution price MS & Co. received from the Street to the National Best Offer ("Best Offer") at the time of the comparison. If the execution price was less than the Best Offer, MS & Co. passed the execution to the customer order at the best offer price and MS & Co. retained the difference between the execution price and the Best Offer. For example, if MS & Co. received an execution price of 10.00 on a buy order and the Best Offer at the time of comparison was 10.01, MS & Co. passed the trade to the customer at 10.01 and MS & Co. recognized an undisclosed mark-up of 0.01.

22. For held market sell orders, the market-making system compared the execution price MS & Co. received from the Street to the National Best Bid ("Best Bid"). If the execution price was greater than the Best Bid, MS & Co. passed the execution to the customer order at the Best Bid and MS & Co. retained the difference between the execution price and the Best Bid. For example, if MS & Co. received an execution price of 10.01 on a sell order and the Best Bid at the time of comparison was 10.00; MS & Co. gave the customer an execution price of 10.00 and MS & Co. recognized an undisclosed mark-down of 0.01.

23. Although MS & Co.'s market-making system was extremely fast, in an active market the Best Bid and Best Offer can change between the time of execution and the time of comparison, which may have been only one second or less. Therefore, the Code not only prevented certain retail customers from receiving the benefit of superior Street Executions, it also sometimes resulted in customers receiving prices worse than what was reasonably available at the time of execution. Thus, MS & Co. breached its duty of best execution by not giving certain retail customers the same prices it received from the Street.

24. In summary, the application of the "Fill-At-The-Inside" Instruction to certain retail not held orders, the use of the trading mechanism to execute certain retail held market orders, and

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[6] Display obligations refer to a market maker's obligation to "display" a customer limit order to the market. Market makers "display" such limit orders by publishing certain orders' limit prices to the market or routing them to another market maker or qualified ECN for display purposes. Market orders, held or not held, are not required to be displayed as they do not carry any price restrictions.

[7] The Code affected held market orders.

the retention of differences between execution price and the Best Bid or Best Offer certain retail held orders caused by the Code resulted in MS & Co.'s failure to provide best execution to certain retail customers' orders during the relevant period.

MS & Co. Failed to Prevent or Timely
<u>Correct the Best Execution Problems</u>

25. MS & Co. was reckless in not knowing that, contrary to its representations and compliance policies, it did not provide best execution to certain retail customer orders.

26. As discussed above, Compliance professionals assisted and provided business managers with advice in connection with the development and implementation of the market-making system and discovered that the system was initially programmed incorrectly. Notwithstanding this initial discovery, MS & Co. had no procedure requiring Compliance's approval of changes to the market-making system by Information Technology personnel. As a result, Compliance's knowledge and understanding of specific programming changes, and their intended and actual effects, was either incomplete or non-existent. The supervisor involved with developing the new trading mechanism and flipping process believed that the computer programmers contacted Compliance for approval. The programmers believed that any requests for changes received from the supervisor had been previously approved by Compliance. In fact, no one had sought Compliance approval. Had anyone done so, it is possible that the best execution failures could have been prevented or at least corrected.

27. MS & Co.'s oversight of programming changes to the market-making system during the relevant period mainly consisted of the testing of the programming changes by Information Technology personnel. They tested code changes before the changes were introduced into the production version of the market-making system to see whether the code accomplished what the programmer had set out to change. No test examined whether the system handled orders properly or whether the programmed functions had effects that could be inconsistent with MS & Co.'s duty of best execution.

28. Unless a problem arose in connection with a particular section of the code, no one other than the programmer responsible for writing the code reviewed the actual code. During the developmental phase of the market-making system, an experienced supervisor who understood and wrote code, reviewed the code written by programmers before the programmers entered it into the market-making system. This review process stopped sometime after MS & Co. started using the market-making system.

29. The programmers used comments throughout the code to explain the purpose of particular functions. These comments, which had no effect on the program, identified, in plain English, certain functions. No coding or programming knowledge was required to understand these comments. MS & Co. had no procedure requiring anyone from Compliance, Information Technology or the business unit to review these comments. If MS & Co. had such a procedure, it is possible that MS & Co. could have detected the Code earlier and MS & Co. could have prevented the best execution failures.

30. MS & Co. had a number of opportunities to identify and to correct the coding issues causing its best execution failures. For example, in December 2001, MS & Co. modified the Code to exclude agency orders. In May 2002, a new programmer who read the Code and understood that the code resulted in undisclosed mark-ups or mark-downs on certain held orders without display obligations modified the Code in order to bring the execution price out to four decimal places. The programmer did not bring the Code to anyone's attention because he believed that others were aware of it and its effect. In February 2003, MS & Co. again modified the Code to eliminate market-on-close orders.[8] None of these coding changes were approved by Compliance or required Compliance to look at the Code and its effect.

31. In early 2003, MS & Co. created a section within Compliance to deal with technology related issues. Compliance drafted a checklist addressing programming changes to MS & Co.'s systems. The checklist included guidelines as to when to seek Compliance approval. A representative from the business unit, finding the checklist too cumbersome to employ, rejected the use of the checklist as "unreasonable" and it was never implemented. Accordingly, MS & Co. continued to have no procedures for monitoring changes to the program.

32. In late 2003, MS & Co. removed the code that caused the delay in execution of held orders. The Code remained and continued to allow MS & Co. to wrongfully embed a mark-up or mark-down when it used Street Executions to fill retail held market orders without display obligations.

33. On or about July 26, 2004, MS & Co. changed the Code to reflect the fact that MS & Co.'s affiliated broker-dealer, Morgan Stanley DW, Inc. ("MSDW"), had agreed to pay a set annual fee to MS & Co. for handling its Nasdaq orders. Accordingly, the computer programmer was advised that since MSDW was going to pay this set fee, all executions had to be passed along print-for-print, but no reference was made with respect to how other retail broker-dealers' orders should be treated. Thus, MS & Co. reprogrammed the Code to exclude only MSDW orders from the Code.

34. In November 2004, Compliance met with computer programmers responsible for the market-making system to discuss a finding by NASD that MS & Co. was not properly reporting riskless principal transactions. The computer programmers told Compliance that the market-making system compared execution prices to the current NBBO and gave a different execution price to the customer if the execution price was different than the current NBBO. Focused on the reporting, Compliance personnel believed this to be solely a limit order protection (or "Manning")[9] issue and instructed the programmers to resolve the reporting issue only.

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8 A "market-on-close" order is typically an order to buy or sell at the official closing price of the primary market on which a stock is listed.

9 NASD Conduct Rule 2110, inclusive of Interpretive Material 2110, often referred to as the Manning rule, requires that market makers fill customer limit orders at prices equal or superior to that of the limit orders if the market maker, acting for itself, trades ahead of those limit orders at prices that could satisfy the limit orders. NASD IM 2110-2. During the relevant period, the Manning Rule only applied to limit orders, which have display obligations.

Compliance personnel did not draw the conclusion that certain orders were not being transmitted print-for-print and did not examine the issue further.

35. On December 1, 2004, a MS & Co. employee discovered certain riskless principal orders that had not been filled print-for-print. The differences between the execution prices and the flip prices were sub-pennies, and the employee was not aware that the Code was the cause. The employee brought the issue to the attention of a MS & Co. lawyer who advised that the issue needed to be understood and resolved promptly. The employee planned to address the problem as soon as MS & Co. finished its preparations for the new Nasdaq Single Price Opening, which was to be rolled out in early December.

MS & Co. Removed The Code and
the "Fill at the Inside" Instruction

36. On December 8, 2004, unusually volatile trading in a stock in which MS & Co. made a market resulted in a short-term trading profit of $400,000 within the first few minutes of trading. This profit – like all the previous revenues caused by the Code – went into a short term risk account and appeared on the system of the trader responsible for that stock. The trader, who was not then actively trading that stock, noticed the unprecedented level of profit that morning and found the situation inexplicable. He immediately brought the facts to the attention of his manager and employees who provided system support for the market-making system. By mid-afternoon, a systems support employee discovered that the Code was responsible for the anomalous activity. MS & Co. immediately cancelled and rebilled the affected trades. MS & Co. changed the market-making system's code to eliminate any future mark-ups and mark-downs on retail held orders. MS & Co. also identified the existence of, and removed, the Instruction that caused undisclosed mark-ups and mark-downs on not held orders.

Legal Discussion

37. A broker-dealer has a legal duty to seek to obtain best execution of customer orders.[10] Failure to satisfy the duty of best execution may constitute a violation of Section 15(c)(1)(A) of the Exchange Act, which makes it unlawful for any broker or dealer to "effect any transaction in . . . any security by means of any manipulative, deceptive, or other fraudulent device or contrivance."[11]

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[10] See, e.g., Newton v. Merrill, Lynch, Pierce, Fenner & Smith, 135 F.3d 266, 269-70, 274 (3d Cir. 1998) (finding Merrill Lynch may have failed to maximize the economic benefit to its customers by failing to take advantage of prices better than the NBBO); In re Herzog, Heine, Geduld, LLC, Exchange Act Release No. 54148 (July 14, 2006) 2006 WL 1982741, at *5; In re Certain Market Making Activities on Nasdaq, Exchange Act Release No. 40900 (Jan. 11, 1999), 1998 WL 919673, at *5; see also Geman v. SEC, 334 F.3d 1183, 1192-93 (10th Cir. 2003) (finding that broker-dealer violated its duty of best execution by failing to disclose that its method of executing orders deprived customers of the possibility of getting a price better than the NBBO); Regulation NMS, Exchange Act Release No. 51808, 70 Fed Reg. 37,496, 37,538 (June 9, 2005).

[11] See In re Herzog, Heine, Geduld, LLC; Exchange Act Release No. 54148; In re Knight Securities, L.P., Exchange Act Release No. 50867, 2004 WL 2913488, at *8 (Dec. 16, 2004).

38. As described above, between October 24, 2001, and December 8, 2004, MS & Co. failed to seek to obtain best execution for certain orders for OTC securities placed by retail customers of MS & Co., MSDW and third party broker-dealers that routed orders to MS & Co. for execution. These best execution failures occurred because: (a) the Fill-at-the-Inside Instruction resulted in undisclosed mark-ups and mark-downs on certain not held retail orders filled at the NBBO when the orders should have been filled print-for-print; (b) the trading mechanism delayed the execution of certain retail held orders which should have been executed without hesitation; and (c) the Code resulted in undisclosed mark-ups and mark-downs on certain held market orders when the orders should have been filled print-for-print. MS & Co. acted recklessly in not knowing that this conduct resulted in MS & Co. breaching its duty of best execution with respect to the affected orders. Accordingly, MS & Co. willfully violated Section 15(c)(1)(A) of the Exchange Act.

Remedial Efforts

39. In determining to accept the Offer, the Commission considered remedial actions by the Respondent. Among other things, following the discovery of the Code, MS & Co. performed an internal investigation into the matter and enhanced its supervision and controls over the relevant trading technology.

Undertakings

40. MS & Co. undertakes the following:

Independent Compliance Consultant

a. MS & Co. shall retain, within 60 days of the date of entry of the Order, the services of an Independent Compliance Consultant ("ICC") not unacceptable to the staff of the Commission. The ICC's compensation and all related expenses shall be borne exclusively by MS & Co. MS & Co. shall require the ICC to conduct a comprehensive review of MS & Co.'s automated retail order handling practices to ensure that MS & Co. is complying with its duty of best execution to retail customers' orders. This review shall include, but should not be limited to, a review of MS & Co.'s market-making system's order handling procedures and MS & Co.'s controls relating to changes to those procedures. MS & Co. shall cooperate fully with the ICC and shall provide the ICC with access to its files, books, records, and personnel as reasonably requested for the review.

b. At the conclusion of the review, but no later than 120 days from the date of entry of this Order, MS & Co. shall require the ICC to submit a Report to MS & Co. and the staff of the Commission. The Report shall address the issues described in paragraph a. of these undertakings and shall include a description of the review performed, the conclusions reached, the ICC's recommendations for changes in or improvements to MS & Co.'s policies and procedures and a procedure for implementing the recommended changes in or improvements to such policies and procedures.

c. MS & Co. shall adopt all recommendations contained in the Report of the ICC; provided, however, that within 150 days from the date of entry of the Order, MS & Co. shall in writing advise the ICC and the staff of the Commission of any recommendations that it considers to be unnecessary or inappropriate. With respect to any recommendation that MS & Co. considers unnecessary or inappropriate, it need not adopt that recommendation at that time but shall propose in writing an alternative policy, procedure or system designed to achieve the same objective or purpose.

d. As to any recommendation with respect to MS & Co.'s policies and procedures on which it and the ICC do not agree, MS & Co. shall attempt in good faith to reach an agreement within 180 days from the date of entry of the Order. In the event MS & Co. and the ICC are unable to agree on an alternative proposal acceptable to the staff of the Commission, MS & Co. shall abide by the determinations of the ICC.

e. MS & Co.: (i) shall not have the authority to terminate the ICC, without the prior written approval of the staff of the Commission; (ii) shall compensate the ICC, and persons engaged to assist the ICC, for services rendered pursuant to the Order at their reasonable and customary rates; and (iii) shall not be in and shall not have an attorney-client relationship with the ICC and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the ICC from transmitting any information, reports, or documents to the Commission or the Commission's staff.

f. MS & Co. shall require the ICC to enter into an agreement that provides that for the period of the engagement and for a period of two years from completion of the engagement, the ICC shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with MS & Co., or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the ICC will require that any firm with which the ICC is affiliated or of which he is a member, and any person engaged to assist the ICC in performance of his duties under the Order shall not, without prior written consent of the Philadelphia District Office enter into any employment, consultant, attorney-client auditing or other professional relationship with MS & Co., or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

Independent Distribution Consultant

g. MS & Co. shall retain, within 60 days of the date of entry of the Order, the services of an Independent Distribution Consultant ("IDC") not unacceptable to the staff of the Commission. The IDC's compensation and all related expenses shall be borne exclusively by MS & Co. MS & Co. shall require that the IDC develop a Distribution Plan for the distribution of the disgorgement ordered in Paragraph IV.C. of the Order, and any interest thereon, according to a methodology developed in consultation with MS & Co. and acceptable to the staff of the Commission. The Distribution Plan shall address how such monetary sums shall be distributed to recompense customers whose orders were adversely affected by the Instruction and the Code. MS & Co. shall cooperate fully with the IDC and shall provide the IDC with access to its files, books, records, and personnel as reasonably requested for review.

h. At the conclusion of the review, which in no event shall be more than 120 days from the date of entry of the Order, MS & Co. shall require that the IDC submit a Distribution Plan to MS & Co. and the staff of the Commission. Within 150 days after the date of entry of the Order, MS & Co. or the staff of the Commission may advise, in writing, the IDC of any determination or calculation from the Distribution Plan that it considers to be inappropriate and states in writing the reasons for considering such determination or calculation inappropriate. With respect to any determination or calculation with which MS & Co. or the staff of the Commission do not agree such parties shall attempt in good faith to reach an agreement within 180 days of the date of entry of the Order. In the event that MS & Co. and the staff of the Commission are unable to agree on an alternative determination or calculation, the determinations and the calculations of the IDC shall be binding.

i. Within 180 days of the date of entry of the Order, MS & Co. shall require that the IDC submit the Distribution Plan for the administration and distribution of disgorgement funds pursuant to Rule 1101 of the Commission's Rules Regarding Fair Fund and Disgorgement Plans. Following a Commission order approving a final plan of disgorgement, as provided in Rule 1104 of the Commission's Rules Regarding Fair Fund and Disgorgement Plans, MS & Co. shall require that the IDC with MS & Co. take all necessary and appropriate steps to administer the final plan for distribution of disgorgement funds. MS & Co. shall pay all costs and expenses of the distribution, including but not limited to, taxes and the expenses of the Plan Administrator and the Tax Administrator.

j. MS & Co.: (i) shall not have the authority to terminate the IDC, without the prior written approval of the staff of the Commission; (ii) shall compensate the IDC, for services rendered pursuant to the Order at their reasonable and customary rates; and (iii) shall not be in and shall not have an attorney-client relationship with the IDC and shall not seek to invoke the attorney-client or any other doctrine or privilege to prevent the IDC from transmitting any information, reports, or documents to the Commission or the Commission's staff.

k. MS & Co. shall require the IDC to enter into an agreement that provides that for the period of the engagement and for a period of two years from completion of the engagement, the IDC shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with MS & Co. or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the IDC will require that any firm with which he is affiliated or of which he is a member, and any person engaged to assist the IDC in performance of his duties under this Order shall not, without prior written consent of the Commission's Philadelphia District Office, enter into any employment, consultant, attorney-client, auditing or other professional relationship with MS & Co., or any of their present or former affiliates, directors, officers, employees, or agents acting in their capacity for the period of the engagement and for a period of two years after the engagement.

Certification

l. MS & Co. agrees to certify in writing to the staff (at the address set forth herein), in the second year following the issuance of the Order, that MS & Co. has fully adopted and complied in all material respects with the undertakings set forth in paragraphs a. through k. above and with the recommendations of the ICC and IDC, or in the event of material non-adoption or non-compliance shall describe such material non-adoption and non-compliance.

Recordkeeping

m. MS & Co. shall preserve for a period of not less than six years from the end of the fiscal year last used, the first two years in an easily accessible place, any record of its compliance with the undertakings set forth in paragraphs a. through k. above.

Extension of Time

n. For good cause shown, the staff of the Commission may extend any of the procedural dates set forth above.

E. MS & Co. shall comply with the undertakings enumerated in Section III.B.40 above.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55731 / May 9, 2007

Admin. Proc. File No. 3-12316

In the Matter of the Application of

HANS N. BEERBAUM and
BEERBAUM & BEERBAUM FINANCIAL AND
INSURANCE SERVICES, INC.
5881 Roblar Rd.
Petaluma, California 94952

For Review of Disciplinary Action Taken by

NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION – REVIEW OF DISCIPLINARY PROCEEDINGS

Failure to Comply with Registration Requirements

Conduct Inconsistent with Just and Equitable Principles of Trade

Owner and president of member firm of registered securities association engaged in conduct requiring registration as a general securities principal without being so registered. Held, association's findings of violation and sanctions are sustained.

APPEARANCES:

Hans N. Beerbaum, pro se.

Marc Menchel, Alan Lawhead, Carla J. Carloni, and Jennifer C. Brooks, for NASD.

Appeal filed: May 30, 2006
Last brief received: September 5, 2006

Document 17 of 33

I.

Beerbaum & Beerbaum Financial and Insurance Services, Inc., an NASD member firm (the "Firm"), and Hans N. Beerbaum, the Firm's sole owner, director, and president (collectively with the Firm, "Applicants"), appeal from NASD disciplinary action. NASD found that the Firm and Beerbaum violated NASD Membership and Registration Rule 1021 1/ and NASD Conduct Rule 2110 2/ when Beerbaum, between 2002 and 2004, acted as a general securities principal for the Firm while his principal registration was suspended. NASD barred Beerbaum from associating with any NASD member firm in any capacity, fined the Firm $15,000, and assessed costs of $4,141.00. We base our findings on an independent review of the record.

II.

This appeal concerns Applicants' actions following NASD's 2002 suspension of Beerbaum as a general securities principal when Beerbaum continued to act in a principal capacity despite the suspension. The facts are as follows.

Beginning in 1986, Beerbaum was registered as a general securities principal with the Firm. On March 4, 1996, Beerbaum registered as a principal and representative with another firm, Walnut Street Securities, Inc. At that time, he withdrew his registrations with the Firm. Beerbaum terminated his registration with Walnut Street in December 1997 and re-registered as a general securities principal and representative with the Firm on January 23, 1998.

In a decision issued on February 15, 2002, NASD found that, between 1996 and 1997, when he was not registered as a principal with the Firm, Beerbaum nonetheless acted in that capacity. He remained the Firm's president, director, and an owner. NASD found that, during this time, Beerbaum "did the Firm's day-to-day bookkeeping and wrote checks on its bank account; continued to be solely responsible for [Firm salesperson Gary] Lee's 3/ supervision; prepared and filed the Firm's FOCUS reports; filed an Amendment to the Firm's Form BD on its behalf; and received compensation from the Firm[.]" NASD held that Beerbaum and the Firm violated Registration Rule 1021 and Conduct Rule 2110. NASD fined Beerbaum and the Firm each $2,500. NASD also required Beerbaum to requalify as a principal within ninety days after

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1/ NASD Membership and Registration Rule 1021 requires, among other things, that "[a]ll persons engaged . . . in the . . . securities business of a member who are to function as principals shall be registered as such with NASD . . . ." NASD Manual at 3131 (2003).

2/ NASD Conduct Rule 2110 requires NASD members to observe high standards of commercial honor and just and equitable principles of trade. NASD Manual at 4111.

3/ Lee was registered with the Firm as both a general securities representative and general securities principal.

the decision became final with the proviso that, if Beerbaum was unable to requalify during the ninety-day period, he would be suspended as a principal until he requalified.

Beerbaum did not attempt to requalify within the ninety-day period and, accordingly, his suspension as a general securities principal took effect on approximately July 5, 2002. 4/ Beerbaum failed the qualification examination for principals in July 2002. He did not take the examination again until August 2003, failed, and then took the examination a third time in November 2003, failing again. On June 3, 2004, Beerbaum passed the examination and qualified as a principal.

However, between July 5, 2002 and June 3, 2004, Beerbaum acted as a principal of the Firm. Beerbaum continued to supervise Gary Lee. Between July 2002 and August 26, 2003, Lee engaged in approximately 180 transactions. Beerbaum received an override on Lee's commissions. Beerbaum attested, as the Firm's president, to each of the Firm's two annual audit reports filed during the period at issue. 5/ Beerbaum also submitted, as the Firm's principal, all seven of the Firm's FOCUS reports that were due during that period. He filed, in his capacity as Firm president, a partial Form BDW regarding the Firm's withdrawal from registration in Utah. In February 2003, he filed, as Firm president, an amendment to the Firm's Form BD to reflect the disciplinary action to which he and the Firm were subject as a result of the February 2002 NASD proceeding. On February 4, 2003, Beerbaum updated the NASD Central Registration Depository ("CRD") contact report for the Firm, which listed him as the Firm's chief executive officer, executive representative, chief financial officer, and contact for compliance issues and for the training of registered representatives. 6/ On April 24, 2003, Beerbaum signed and approved, as president, the Firm's anti-money laundering ("AML") program–compliance and supervisory procedures. The Firm's AML procedures designated Beerbaum as its AML program compliance officer with full responsibility for the Firm's AML program.

4/ Beerbaum testified that he did not take the principal examination for the first time until July 31, 2002 because he "realized [he] was probably not going to pass based on the [practice] test results."

5/ Rule 17a-5(e)(2) of the Securities Exchange Act of 1934, 17 C.F.R. § 240.17a-5(e)(2), requires that a broker-dealer's annual audited report be accompanied by an oath or affirmation by a duly authorized officer that, to the best of the attester's knowledge, the financial statements and schedules are true and correct and neither the broker-dealer nor a principal has a proprietary interest in any customer account.

6/ Article IV, Section 3 of NASD's By-laws provides that "[e]ach member shall appoint and certify to the Secretary of the NASD one 'executive representative' who shall represent, vote, and act for the member in all the affairs of the NASD. . . . An executive representative of a member or a substitute shall be a member of senior management and registered principal of the member." NASD Manual at 1309.

In this proceeding, NASD concluded that Beerbaum's conduct between July 5, 2002 and June 3, 2004 violated Rules 1021 and 2110.

III.

Rule 1021(a) requires that all persons who act as a principal of an NASD member firm be properly registered as a principal with NASD. Rule 1021(b) defines a "principal" to include an officer or director of an NASD member firm who is "actively engaged in the management of the [member firm's] investment banking or securities business, including supervision, solicitation, conduct of business, or the training of persons associated" with the member. 7/

The evidence establishes that, while suspended as a principal of the Firm, Beerbaum was actively engaged in the management of the Firm's securities business. He supervised at least one Firm employee. 8/ He attested as president to the Firm's annual audit reports. He prepared and filed FOCUS reports as Firm "principal." He filed a partial Form BDW and an amendment to the Firm's Form BD in his capacity as Firm president, and approved, signed and filed anti-money laundering compliance and supervisory procedures. 9/ Supervision of firm personnel and approving, signing, and filing required periodic financial reports, required disclosure forms, and required compliance and supervisory procedures on behalf of a member firm come within those management responsibilities enumerated in Rule 1021(b) that are to be performed by a principal. 10/

7/ E.g., L.H. Alton & Co., 53 S.E.C. 1118, 1124 (1998) (citing NASD Rule 1021(b)).

8/ Beerbaum claimed, in testimony before NASD, that Gary Lee supervised himself. We have held, however, that a salesperson cannot supervise himself. See Kirk Montgomery, 55 S.E.C. 485, 504 & n.43 (2001) (finding that "[i]t is unreasonable to expect a salesperson to supervise himself") (citations omitted); Bradford John Titus, 52 S.E.C. 1154, 1158 (1996) (finding that salesperson could not supervise himself); see also Stuart K. Patrick, 51 S.E.C. 419, 422 (1993) (finding, in appeal of NYSE action, that "[s]upervision, by its very nature, cannot be performed by the employee himself"), aff'd, 19 F.3d 66 (2d Cir. 1994).

9/ Beerbaum notes that CRD identified Lee as the Firm's anti-money laundering compliance contact. The Firm's April 2003 AML procedures, however, were signed solely by Beerbaum as "President" and designated Beerbaum as the AML compliance officer.

10/ See, e.g., Gordon Kerr, 54 S.E.C. 930, 938 (2000) ("[A] person acting in a supervisory capacity must be registered as a general securities principal."); Exchange Act Rule 17a-5(e)(2), 17 C.F.R. § 240.17a-5(e)(2) (requiring that individual who attests annual audited report be duly authorized officer); Exchange Act Form X-17A-5 (requiring that individual who signs and submits FOCUS Report be principal); NASD Conduct Rule 3011

(continued...)

Moreover, Beerbaum held himself out to regulators as the Firm's principal. He executed numerous reports and forms, throughout this period, on the Firm's behalf as its president or its principal. Beerbaum also updated an NASD contact report in the first half of 2003 stating that he was the Firm's chief executive officer, executive representative, and chief financial officer, as well as the contact for compliance issues and for training registered representatives. 11/

Applicants claim that they believed, based on an inquiry to "the local [NASD] office," that Gary Lee, who had passed the Series 24 principal examination, became the Firm's managing general principal once Beerbaum's suspension took effect. However, even if Lee were the Firm's managing principal, Applicants would remain liable under Rule 1021. The fact that a member firm properly registers one principal who exercises managerial authority does not mean that other associated persons who act as principals need not be registered as principals. Rule 1021 requires that every associated person who holds one of the enumerated positions and who has managerial responsibilities must be registered as a principal. 12/

Moreover, Beerbaum did not effectively delegate his executive and supervisory duties to anyone else. Beerbaum admittedly failed to amend the Firm's Form BD or supervisory procedures to reflect a change in managing principals. He further admitted that he failed to show copies to Lee of the Firm's regulatory reports, such as its FOCUS reports, before filing.

Applicants assert that NASD granted Beerbaum an extension of time to pass the principal examination. In a letter dated August 22, 2003, NASD observed that Beerbaum remained an officer and sole owner of the Firm, and that he was designated "Executive Representative of [the Firm], a position that can only be held by a principal." The letter further informed Applicants that NASD would "take steps to cancel the membership of [the Firm] due to its failure to meet membership requirements if [Beerbaum was] not registered as a principal by September 25,

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10/ (...continued)
(requiring approval by member of senior management of firm's anti-money laundering program); cf. L.H. Alton & Co., 53 S.E.C. at 1125-26 (finding that the completion and execution of documents "obligating the firm to participate in a securities underwriting are clearly among those duties to be performed by a 'principal'").

11/ See L.H. Alton & Co., 53 S.E.C. at 1125 n.21 ("The fact that [one] held himself out to be a partner in the firm [was] additional relevant evidence of his [principal] status in the firm.") (citation omitted); see also William Jackson Blalock, 52 S.E.C. 77, 84 (1994) (finding a violation of the requirement that NASD members observe high standards of commercial honor and just and equitable principles of trade where person acted and held himself out as president of firm despite being unregistered because of his failure to pass an NASD qualification examination), aff'd, 96 F.3d 1475 (11th Cir. 1996) (Table).

12/ See L.H. Alton & Co., 53 S.E.C. at 1125-27.

2003." 13/ The letter also stated that NASD was not precluded from "taking any disciplinary action for violations of the rules and regulations that may have occurred prior to the issuance of [the] letter." As noted above, Beerbaum did not qualify until June 2004.

We believe that this letter in fact warned Applicants that, because Beerbaum had not requalified as a principal, the Firm's registration was subject to cancellation. NASD's statement that it would postpone action to cancel the Firm's membership did not authorize or ratify Beerbaum's acting as a principal and expressly did not preclude disciplinary proceedings against Beerbaum. Moreover, by the time NASD sent this letter, Beerbaum already had engaged in many of the management activities at issue.

The Firm also bears responsibility for Beerbaum's failure to qualify as a principal because he was the Firm's sole owner, president, and director. 14/ Based on the foregoing, we find that Beerbaum and the Firm violated Rule 1021 when Beerbaum acted as a principal of the Firm without being so registered. NASD further determined that Beerbaum's and the Firm's violation of Rule 1021 also constituted a violation of Rule 2110, which requires adherence to high standards of commercial honor and just and equitable principles of trade. It is well settled that a violation of a rule promulgated by the Commission or by NASD also violates Rule 2110. 15/ We accordingly sustain NASD's findings of violation.

IV.

Exchange Act Section 19(e)(2) directs us to sustain NASD's sanctions unless we find, having due regard for the public interest and the protection of investors, that the sanctions are

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13/ NASD subsequently extended this date to October 10, 2003.

14/ See, e.g., Gallagher & Co., 50 S.E.C. 557, 564 & n.18 (1991) (citing A.J. White & Co. v. SEC, 556 F.2d 619, 624 (1st Cir.) ("A firm . . . can act only through its agents, and is accountable for the actions of its responsible officers."), cert. denied, 434 U.S. 969 (1977)), aff'd, 963 F.2d 385 (11th Cir. 1992) (Table); C.E. Carlson, Inc. v. SEC, 859 F.2d 1429, 1435 (10th Cir. 1988) (citing A.J. White & Co., 556 F.2d at 624); see also R.B. Marich, Inc., 49 S.E.C. 991, 992-93 (1988) (finding that firm "must bear a measure of responsibility for its principals' failure to comply with NASD registration requirements" where firm permitted president, as well as executive vice president and operations manager, "to serve as officers and individuals actively engaged in management without registering them as principals") (emphasis in original).

15/ E.g., E. Magnus Oppenheim & Co., Inc., Securities Exchange Act Rel. No. 51479 (Apr. 6, 2005), 85 SEC Docket 475, 478 n.11 (citations omitted).

excessive or oppressive or impose an unnecessary or inappropriate burden on competition. 16/ Applicants argue that there are various mitigating circumstances that justify a reduction in the sanctions imposed by NASD. Although they claim that no sanction is necessary, Applicants suggest, as an alternative to the sanctions imposed by NASD, that Beerbaum be given "a short suspension" or merely a bar from acting as a principal.

As we previously have observed, "NASD's registration requirement 'provides an important safeguard in protecting public investors,' and 'strict adherence' to that requirement is 'essential'" because it "serves a significant purpose in the policing of the securities markets" and "in the protection of the public interest . . . ." 17/ As we also have observed, the "registered principal is the person at a broker-dealer to whom the NASD looks to ensure compliance with regulatory requirements." 18/ Thus, regulatory compliance is dependent, to a significant degree, on the qualifications of the principal, and those qualifications are assessed through the examination process.

We note in this connection that the sanctions imposed are consistent with NASD's own Sanction Guidelines. For violations of Rule 1021, the Guidelines provide for fines of $2,500 to $50,000 on the firm and/or the individual. In "egregious cases," the Guidelines recommend suspending the firm for up to thirty business days and suspending for up to two years, or barring, the individual in any or all capacities. The Guidelines list, as a "Principal Consideration" in determining the appropriate sanction for registration violations, the nature and extent of the unregistered person's responsibilities. The Guidelines also list as General Principles in determining the appropriate sanction the consideration of any relevant disciplinary history and whether the respondent's misconduct was the result of an intentional act.

The record amply establishes the seriousness of Beerbaum's and the Firm's misconduct. For almost two years, Beerbaum performed executive and supervisory responsibilities on behalf of the Firm despite Beerbaum's suspension as a principal. Beerbaum knew that he could not act in these management capacities unless he was registered as a principal. Many of Beerbaum's actions that are the basis of this proceeding are the same activities found in NASD's 2002

16/ 15 U.S.C. § 78s(e)(2). Beerbaum does not claim, and the record does not show, that NASD's action imposed an undue burden on competition.

17/ Michael F. Flannigan, 56 S.E.C. 8, 17 (2003) (finding that individuals engaged in conduct requiring registration as representatives of an NASD member firm without being so registered) (citations omitted). As we have held, the registration requirements are intended to ensure that principals "maintain the requisite levels of knowledge and competence." Jon G. Symon, 54 S.E.C. 102, 110 (1999) (ordering the requalification by examination of a former registered securities principal, whose registrations as a general securities principal and a financial and operations principal had lapsed).

18/ Douglas Conrad Black, 51 S.E.C. 791, 794 (1993).

proceeding. In 2002, NASD found that Beerbaum and the Firm violated Rules 1021 and 2110, the same rules at issue here. Notwithstanding this knowledge, Beerbaum made no attempt to requalify as a principal within the prescribed ninety-day time period, as ordered in that earlier proceeding. Although he eventually sought to requalify by taking the principal exam, he failed the exam on his first three attempts spread over seventeen months, and did not successfully qualify as a principal until the middle of 2004. Despite his repeated failures to requalify, however, Beerbaum continued to run the Firm as an unregistered principal.

Applicants contend that Beerbaum's "multiple efforts to pass the [principal examination] showed a good faith attempt to comply with [NASD's] requirement." According to Applicants, the general principal examination was more difficult than Beerbaum expected, has "little training value" and "no relevance to the kind of business [the Firm] conduct[s]" and, therefore, "some consideration should be accorded for the problem it caused," in being so difficult for Beerbaum to pass. Beerbaum's personal opinion about the merits of NASD's examination program did not allow Applicants to disregard the results of that program when they were adverse to their plans. As we have held, "[w]hatever negative opinion [applicant] has of the rule does not obviate the need to comply with it." 19/

Beerbaum's statements throughout these proceedings further evidence Beerbaum's lack of understanding of the requirements of the securities business. 20/ For example, Beerbaum justified his failure to update properly the NASD contact report, arguing that "it's just a form that we haven't looked at in years and years . . . since we are on dial-up [internet access], changing

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19/ See E. Magnus Oppenheim & Co., 85 SEC Docket at 483.

20/ Applicants complain that NASD "misused" an "IRS story . . . as proof that Beerbaum would violate rules if he needed to." Beerbaum volunteered at the NASD hearing that he falsified income information on a mortgage application in 1990, insisting that he did so at the behest of the lender who warned him that he would not otherwise qualify for the loan. Beerbaum claims that, upon discovering the inconsistency between the income disclosed in the mortgage application and the income disclosed in his federal income tax return, the "IRS chose to close its investigation without any action" after determining that the tax return was truthful. In Beerbaum's view, this information "adds proof that although a problem occurred at one time, no subsequent attempt to defraud a lender was ever attempted. NASD can be similarly certain . . . that a violation such as the one [at issue] is not likely to [re]cur [because t]he reason to attempt such a violation will not recur . . . ." In our view, Beerbaum cannot complain that NASD considered information that he voluntarily gave them.

anything is so time consuming we don't even think of doing it." 21/ Beerbaum's conduct and statements raise significant uncertainty about his willingness to comply with registration and other regulatory requirements in the future.

Applicants contend that, "while [Beerbaum] knew that a violation had occurred, mitigating circumstances would demonstrate that he had no choice but to file appropriate compliance reports." Applicants also argue that they sought to remain in compliance but that NASD "failed to suggest a practical way that [Beerbaum] could have met the firm's compliance responsibilities other than by filing the reports that only he had the power to file."

The appropriate answer to this is that, once Beerbaum was suspended, it was Applicants' obligation to cause these management responsibilities to be carried out by a properly registered principal. He and the Firm had an obligation to comply with all applicable rules. Applicants deliberately ignored the requirements of the registration rule and the suspension NASD imposed on Beerbaum as a result of similar misconduct. 22/

Beerbaum contends that he will face great economic hardship as a result of the bar and that it is unfair to apply sanctions to both him and the Firm because "Beerbaum is the [F]irm." Beerbaum asserts that no member of the public has ever complained about him or suffered any harm at his hand and that the fate of his "small clients" "is of no concern to [NASD]." We

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21/ He also stated that NASD made "a big deal that the anti-money laundering report was filed by [him] while the Series 24 was suspended" and that "the NASD is over the top in a prosecution like this[.]"

22/ Applicants further complain that NASD failed to devise a way in which the Firm could remain in business, and in compliance, despite Beerbaum's suspension. We have repeatedly held that members and their associated persons "cannot shift their burden of compliance to the NASD." B.R. Stickle & Co., 51 S.E.C. 1022, 1025 (1994). We noted in Stickle that "industry professionals are not released from their obligations" even when they receive "erroneous advice from NASD." Id.; see also Michael G. Keselica, 52 S.E.C. 33, 37 (1994) (stating that "attempts to blame others for his misconduct . . . demonstrate that [respondent] fails to understand the seriousness of . . . violations"); Kirk A. Knapp, 50 S.E.C. 858, 862 & n.15 (1992) (stating that applicant "cannot shift his responsibility for compliance with regulatory requirements to . . . NASD)" (internal citations omitted).

disagree with Applicants' view that allowing Beerbaum to remain in the industry would serve the interest of investors, small or otherwise. His actions evidenced a lack of appreciation for the requirements he was subject to as an associated person of an NASD member firm. Those requirements, which are intended to protect investors, are rendered meaningless if aspects of them are, as here, disregarded. Under the circumstances, therefore, we see no basis for concluding that the sanctions imposed by NASD are excessive or oppressive. 23/

An appropriate order will issue. 24/

By the Commission (Chairman COX and Commissioners ATKINS, CAMPOS, NAZARETH, and CASEY).

Nancy M. Morris
Secretary

23/ See, e.g., Gordon Kerr, 54 S.E.C. 930 (2000) (sustaining bar in all capacities of registered representative who acted as principal without being registered).

24/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55731 / May 9, 2007

Admin. Proc. File No. 3-12316

In the Matter of the Application of

HANS N. BEERBAUM and
BEERBAUM & BEERBAUM FINANCIAL AND
INSURANCE SERVICES, INC.
5881 Roblar Rd.
Petaluma, California 94952

For Review of Disciplinary Action Taken by

NASD

ORDER SUSTAINING DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES ASSOCIATION

On the basis of the Commission's opinion issued this day, it is

ORDERED that the disciplinary action taken by NASD against Hans N. Beerbaum and Beerbaum & Beerbaum Financial and Insurance Services, Inc., and NASD's assessment of costs, be, and they hereby are, sustained.

By the Commission.

Nancy M. Morris
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55728 / May 9, 2007

INVESTMENT ADVISERS ACT OF 1940
Release No. 2601 / May 9, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12632

In the Matter of **AMARANTH ADVISORS L.L.C.,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 203(e) OF THE INVESTMENT ADVISERS ACT OF 1940**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Section 203(e) of the Investment Advisers Act of 1940 ("Advisers Act"), against Amaranth Advisors L.L.C. ("Amaranth" 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 and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to

Document 18 of 33

Section 21C of the Securities Exchange Act of 1934 and Section 203(e) of the Investment Advisers Act of 1940 ("Advisers Act") ("Order"), as set forth below.

III.

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

Respondent

1. Amaranth Advisors L.L.C., a Delaware limited liability company which has its headquarters and principal place of business in Greenwich, Connecticut, is an unregistered investment adviser to five hedge funds. At all times, Amaranth has had full discretion to make investment decisions for the funds it advises.

Summary

2. In connection with five follow-on offerings conducted between November 2004 and February 2005, Amaranth sold securities short during the five business days before the pricing of those offerings and then covered the short positions with securities purchased in the offerings ("offering shares"). These transactions violated Rule 105 of Regulation M, and resulted in funds advised by Amaranth making profits of $507,627.

Legal Discussion

3. Rule 105 of Regulation M, "Short Selling in Connection with a Public Offering," prohibits covering a short sale with securities obtained in a public offering if the short sale occurred within the Rule 105 restricted period, which is the shorter of (1) the period five business days before pricing and ending with pricing or (2) the period beginning with the initial filing of the registration statement or notification on Form 1-A and ending with pricing (the "Rule 105 restricted period"). In pertinent part, Rule 105 provides:

> In connection with an offering of securities for cash pursuant to a registration statement… filed under the Securities Act, it shall be unlawful for any persons to cover a short sale with offered securities purchased from an underwriter or broker or dealer participating in the offering, if such short sale occurred during the… period beginning five business days before the pricing of the offered securities and ending with such pricing…."

17 C.F.R. § 242.105(a)(1). Rule 105 is prophylactic and prohibits the conduct irrespective of the short seller's intent in effecting the short sale. Interpretative guidance by the Commission provides that "where the transaction is structured such that there is no legitimate economic purpose or substance to the contemporaneous purchase and sale, no genuine change in beneficial ownership, and/or little or no market risk, that transaction may be a sham transaction that violates Rule 105." *Short Sales*, Exchange Act Release

No. 50103 (September 7, 2004). In an example of such a transaction, "a trader effects pre-pricing short sales during the Rule 105 restricted period, receives offering shares, sells the offering shares in to the open market, and then contemporaneously or nearly contemporaneously purchases an equivalent number of the same class of shares as the offering shares, which are then used to cover the short sales." *Id.*

Amaranth's Trades

4. Coeur D'Alene Mines Corp. (NYSE: CDE) announced a follow-on offering on November 12, 2004, and priced the offering on November 18, 2004. During the Rule 105 restricted period, funds advised by Amaranth sold short 1,269,900 Coeur D'Alene shares and purchased 2,500,000 shares in the offering. Those funds used 1,269,900 of the offering shares to cover short positions created during the Rule 105 restricted period and made profits of $449,481.

5. Catapult Communications Corp. (NASDAQ: CATT) announced and priced a follow-on offering on November 10, 2004, pursuant to a shelf registration. During the Rule 105 restricted period, and before the offering was priced and announced, funds advised by Amaranth had sold short 10,000 shares and purchased 8,582 shares of Catapult stock. These transactions resulted in a net short position of 1,418 shares created during the Rule 105 restricted period. Funds advised by Amaranth purchased 10,000 shares in the offering, and used 1,418 of those shares to cover the short position resulting from its trading during the Rule 105 restricted period. Funds advised by Amaranth made profits of $2,113 in covering short positions with shares received in the offering.

6. Cleco Corp. (NYSE: CNL) announced and priced a follow-on offering on November 9, 2004, pursuant to a shelf registration. During the Rule 105 restricted period, and before the offering was priced and announced, funds advised by Amaranth had sold short 6,000 shares and purchased 5,000 shares of Cleco stock. These transactions resulted in a net short position of 1,000 shares. Funds advised by Amaranth purchased 80,000 shares in the offering, and used 1,000 of those shares to cover the short position resulting from its trading during the Rule 105 restricted period. Funds advised by Amaranth made profits of $290 in covering short positions with shares received in the offering.

7. MEMC Electronic Materials, Inc. (NYSE: WFR) announced a follow-on offering on February 3, 2005, and priced the offering on February 16, 2005. During the Rule 105 restricted period, funds advised by Amaranth created a net short position of 101,300 shares. Funds advised by Amaranth purchased 250,000 shares in the offering. On February 17 and 18, 2005, after purchasing the offering shares, Amaranth engaged in a series of open market purchases and sales of MEMC stock. These open market purchases and sales were contemporaneous or nearly contemporaneous and resulted in Amaranth no longer holding any offering shares and covering the short position of 101,300 shares created during the Rule 105 restricted period. Funds advised by Amaranth made profits of $36,859 from these trades.

8. American Superconductor Corporation (NASDAQ: AMSC) announced a follow-on offering on January 11, 2005, and priced the offering on February 23, 2005. During the Rule 105 restricted period, funds advised by Amaranth sold short 32,600 shares of American Superconductor stock. Funds advised by Amaranth purchased 150,000 shares in the offering. On February 28, 2005, after purchasing the offering shares, Amaranth engaged in a series of open market purchases and sales of American Superconductor stock. These open market purchases and sales were contemporaneous or nearly contemporaneous and resulted in Amaranth no longer holding any offering shares and covering the short position of 32,600 shares created during the Rule 105 restricted period. With respect to the open market transactions, Amaranth began selling shares of American Superconductor on February 28, 2005 at 10:34 a.m. and completed the sale of its shares that day by 10:47 a.m. While it was selling these shares, Amaranth began purchasing shares of American Superconductor at 10:39 a.m. and finished buying American Superconductor shares at 10:56 a.m. Funds advised by Amaranth made profits of $18,883 from these trades.

Amaranth's Violations

9. As a result of the conduct described above, Amaranth willfully[1] violated Rule 105 of Regulation M, which makes it "unlawful for any person to cover a short sale with offered securities purchased from an underwriter or broker or dealer participating in an offering, if such short sale occurred during the . . . period beginning five business days before the pricing of the offered securities and ending with such pricing."

Amaranth's Remedial Efforts

10. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff.

IV.

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

Accordingly, it is hereby ORDERED that:

A. Respondent Amaranth cease and desist from committing or causing any violations and any future violations of Rule 105 of Regulation M.

B. Respondent Amaranth be, and hereby is, censured.

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[1] "Willfully" as used in this Order means intentionally committing the act which constitutes the violations, Cf. Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000). There is no requirement that the actor also be aware that he is violating one of the Rules or Acts.

C. IT IS FURTHERED ORDERED that Respondent shall, within 30 days of the entry of this Order, pay disgorgement of $507,627, prejudgment interest in the amount of $59,192, and a civil money penalty of $150,000 to the United States Treasury. 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, Alexandria, Stop 0-3, VA 22312; and (D) submitted under cover letter that identifies Amaranth 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 Kenneth Lench, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street N.E., Washington, D.C. 20549.

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 it shall not, after offset or reduction in any Related Investor Action based upon Respondent's payment of disgorgement in this action, argue that it is entitled to, nor shall it further benefit by offset or reduction 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 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 the 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.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

-2

Chairman Cox
Not Participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION
May 11, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12633

In the Matter of

LAWRENCE A. CAMPBELL,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934

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 Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Lawrence A. Campbell ("Campbell" or "Respondent").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

Lawrence A. Campbell, age 59, resides in Santa Ana, California. Campbell has never been registered with a broker-dealer.

B. FACTS

1. From at least November 2001 through July 2003, Campbell offered and sold securities issued by Sunrise Energy, Inc. ("Sunrise") to at least twelve investors.

2. Campbell cold called prospective investors in several states and offered them Sunrise securities using high pressure sales tactics. After Campbell spoke with investors, they received written materials detailing the investments.

3. Campbell made material misrepresentations to investors regarding the rates of return that investors would receive. For example, Campbell told investors during his telephone solicitations that they could expect to receive the returns projected in the Sunrise offering materials

Document 19 of 33

which ranged from 55% to 112% per year. However, Sunrise investors never received the promised returns and most Sunrise investors ultimately lost more than 95% of the principal they invested.

4. Campbell also misrepresented the risk involved in the Sunrise securities. Campbell told investors that their investments involved low risk and were safe. However, these representations were false as the investments were highly speculative.

5. Campbell did not take any steps to verify the accuracy of the claims he made to investors regarding the low risk, high return nature of the securities he was selling. Moreover, Campbell continued to make representations regarding the low risk, high return nature of the Sunrise investments even after he learned that investors were receiving returns that were far less than those he was telling them to expect.

6. Campbell received commissions from Sunrise in connection with the Sunrise investments he sold. From November 2001 to July 2003 Campbell received at least $162,000 in ill-gotten gains from bank accounts containing Sunrise investor funds.

7. Campbell acted at least recklessly in connection with his misrepresentations and omissions to investors relating to anticipated returns and risk involved.

8. No registration statement was filed with the Commission or was in effect as to the transactions in Sunrise securities. Moreover, the securities issued by Sunrise were not exempt from registration.

9. Campbell was not a registered broker-dealer nor was he associated with a registered broker-dealer while he sold the Sunrise securities. Moreover, Campbell received transaction-based compensation in connection with his sales of Sunrise securities.

10. As a result of the conduct described above, Campbell willfully violated Sections 5(a), 5(c), and 17(a) of the Securities Act and Sections 10(b) and 15(a) of the Exchange Act and Rule 10b-5 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondent pursuant to Section 15(b) of the Exchange Act including, but not limited to, an accounting, disgorgement, prejudgment interest, and civil penalties pursuant to Section 21B of the Exchange Act;[1]

C. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondent should be ordered to cease and desist from committing or causing violations of and any future violations of Sections 5(a), 5(c) and 17(a) of the Securities Act and Sections 10(b) and 15(a) of the Exchange Act and Rule 10b-5 thereunder and whether Respondent should be ordered to make an accounting and pay disgorgement and prejudgment interest pursuant to Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondent personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

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[1] Section 21B of the Exchange Act establishes three tiers of civil penalties the Commission may impose in administrative proceedings and each tier prescribes the maximum penalty for each violative act or omission. Under this provision, the Commission may assess a third tier penalty of up to $120,000 for each violative act or omission by a natural person.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Nancy M. Morris
Secretary

J. Lynn Taylor

Chairman Cox
Not Participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION
May 11, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12634

In the Matter of **DONALD J. LAKIN,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

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 Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Donald J. Lakin ("Lakin" or "Respondent").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

Donald J. Lakin, age 39, resides in Anaheim, California.

B. FACTS

1. From at least May 2002 through April 2003, Lakin offered and sold securities issued by Sunrise Energy, Inc. ("Sunrise") to approximately twenty to thirty investors.

2. Lakin cold called hundreds of prospective investors off of commercial "lead lists" and offered them Sunrise securities using high pressure sales tactics. After Lakin spoke with investors, they received written materials detailing the investments. Lakin sold Sunrise securities out of his own office and employed people through his company, Pacific Resources Group, Inc., who sold Sunrise securities on his behalf.

Document 20 of 33

3. Lakin made material misrepresentations to investors regarding the rates of return that investors would receive. For example, Lakin told investors during his telephone solicitations that they could expect to receive the returns projected in the Sunrise offering materials which ranged from 55% to 106% per year. However, Sunrise investors never received the promised returns and most Sunrise investors ultimately lost more than 95% of the principal they invested.

4. Lakin also misrepresented the risk involved in the Sunrise securities. Lakin told investors that their investments involved low risk and were secure. However, these representations were false as the investments were highly speculative.

5. Lakin did not take any steps to verify the accuracy of the claims he made to investors regarding the low risk, high return nature of the securities he was selling. Moreover, Lakin continued to make representations regarding the low risk, high return nature of the Sunrise investments even after he learned that investors were receiving minimal payments that were a small fraction of the returns that he told investors to expect.

6. Lakin received commissions from Sunrise of 40% to 50% of the amounts invested and did not disclose those commissions to investors. From May 2002 to April 2003, Lakin and Pacific Resources Group, Inc., received at least $374,000 in ill-gotten gains from Sunrise bank accounts holding investor funds. Lakin's failure to disclose the exorbitant commissions he received represents a material misstatement or omission.

7. Lakin acted at least recklessly in connection with his misrepresentations and omissions to investors relating to anticipated returns, risk involved, and commissions paid.

8. No registration statement was filed with the Commission or was in effect as to the transactions in Sunrise securities. Moreover, the securities issued by Sunrise were not exempt from registration.

9. Lakin was not a registered broker-dealer nor was he associated with a registered broker-dealer while he sold the Sunrise securities. Moreover, Lakin received transaction-based compensation in connection with his sales of Sunrise securities.

10. As a result of the conduct described above, Lakin willfully violated Sections 5(a), 5(c), and 17(a) of the Securities Act and Sections 10(b) and 15(a) of the Exchange Act and Rule 10b-5 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondent pursuant to Section 15(b) of the Exchange Act including, but not limited to, an accounting, disgorgement, prejudgment interest, and civil penalties pursuant to Section 21B of the Exchange Act;[1]

C. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondent should be ordered to cease and desist from committing or causing violations of and any future violations of Sections 5(a), 5(c) and 17(a) of the Securities Act and Sections 10(b) and 15(a) of the Exchange Act and Rule 10b-5 thereunder and whether Respondent should be ordered to make an accounting and pay disgorgement and prejudgment interest pursuant to Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondent personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

[1] Section 21B of the Exchange Act establishes three tiers of civil penalties the Commission may impose in administrative proceedings and each tier prescribes the maximum penalty for each violative act or omission. Under this provision, the Commission may assess a third tier penalty of up to $120,000 for each violative act or omission by a natural person.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Nancy M. Morris
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Respondent

1. Stephen J. Treadway, age 59, resides in New York, New York. Treadway was the Chief Executive Officer and a managing director of PA Distributors LLC from May 1996 until July 28, 2004. Likewise, from May 1996 until June 30, 2004, Treadway was the Chief Executive Officer and a managing director of PA Fund Management. Also during this time period, Treadway was Chairman of the Board of Trustees for the PIMCO Funds: Multi-Manager Series ("MMS Funds")[2] until he resigned from that position on May 19, 2004. On July 28, 2004, Treadway resigned as a trustee for the Board of Trustees for the MMS Funds ("MMS Board"). On this same date, Treadway resigned his position as a managing director at Allianz-Dresdner Asset Management of America, LLP. Treadway received a J.D. from Columbia Law School in 1972.

Related Entities

2. PA Distributors LLC ("PAD"), during the relevant time period, was a wholly owned, indirect subsidiary of Allianz-Dresdner Asset Management of America, LLP ("ADAM"). PAD was a Delaware limited liability company located in Stamford, Connecticut and a broker-dealer that had been registered with the Commission under the Exchange Act since 1989. PAD served as the distributor and underwriter for the PIMCO Complex of Funds.

3. PA Fund Management LLC ("PAFM"), during the relevant time period, was a wholly owned, indirect subsidiary of ADAM. PAFM was a Delaware limited liability company located in New York, New York that had been registered as an investment adviser with the Commission since 2000. PAFM was the investment adviser and administrator for the MMS Funds, a registered investment company comprised of separate series of mutual funds. PAFM was responsible for managing the investment activities of the MMS Funds either directly, or through others selected by it.

4. PEA Capital LLC ("PEA"), during the relevant time period, was a wholly owned, indirect subsidiary of ADAM. PEA was a Delaware limited liability company located in New York, New York that had been registered as an investment adviser with the Commission since 2001. Treadway, on December 31, 2001, in his capacity as CEO of PAFM, signed a Portfolio Management Agreement with PEA whereby PAFM engaged PEA, as a sub-adviser, to act as the portfolio manager to ten funds within the MMS Trust, including, PEA Growth, PEA Growth & Income, PEA Opportunity, PEA Target, PEA Innovation, PEA Value and PEA Renaissance Funds. Although PEA was subject to the supervision of PAFM and the MMS Board, PEA had full investment discretion, made all determinations with respect to the investment of these

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2 From January 2000 through July 31, 2003 (the "relevant time period"), there were two trusts within the PIMCO Complex of Funds: the MMS Funds and the Pacific Investment Manager Series ("PIMS") (collectively "the Funds"). Each trust was a registered investment company and consisted of separate series, each of which was functionally a separate investment company. Each trust had a separate board of trustees. The PIMS Funds are not a party to this proceeding.

F.. ;

Commissioner Campos
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 2602 / May 14, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12635

In the Matter of

STEPHEN J. TREADWAY,

Respondent.

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

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(f) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") against Stephen J. Treadway ("Respondent" or "Treadway").

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 him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 203(f) and 203(k) of the Investment Advisers Act of 1940 ("Order"), as set forth below.

III.

On the basis of this Order and Treadway's Offer, the Commission finds[1] that

[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.

Document 21 of 33

MMS Funds' assets and directed the MMS Funds' portfolio transactions to broker-dealers for execution.

Overview

5. This matter involves the failure of Treadway to disclose the conflict of interest that arose from PAD's arrangements with nine broker-dealers for increased "shelf space" within the broker-dealers' distribution systems. The shelf space arrangements were designed to promote the sale of all Funds distributed by PAD, not just the MMS Funds, and provide heightened visibility at the brokerage firms, including greater access to registered representatives and placement on preferred lists (hereinafter "Shelf Space arrangements"). PAFM and PAD encouraged PEA to direct brokerage commissions on the MMS Funds' portfolio transactions to certain broker-dealers in order for PAD to receive credit for part of the cost of these Shelf Space arrangements.

6. Treadway approved of PAD's participation in the Shelf Space arrangements and negotiated the terms of some of the arrangements. Because Treadway was aware that PAD was receiving credit for PEA's directed brokerage, Treadway enabled PAD to partially avoid using its own assets to pay for these distribution services and benefits. By encouraging PEA's use of fund assets to benefit, and in fact defray, the expenses of PAD, a third party to the MMS Funds, Treadway created a conflict of interest that Treadway, as CEO of PAFM and PAD and the individual who addressed the MMS Board, should have disclosed.

7. Treadway, however, when acting on behalf of PAFM and PAD, failed to disclose to the MMS Board this conflict of interest. In particular, during the annual reviews of the investment advisory and distribution agreements and during the quarterly presentations regarding the marketing of the MMS Funds, Treadway did not advise the MMS Board that the MMS Funds' brokerage commissions were being used to offset part of the cost of PAD's Shelf Space arrangements.

PAD's Shelf Space Arrangements with Broker-Dealers

8. Between 2000 and 2003, PAD was a party to nine Shelf Space arrangements with broker-dealers pursuant to which broker-dealers promised that the Funds sold and distributed by PAD would receive increased visibility within the broker-dealers' distribution systems; in return, PAD agreed to pay broker-dealers. PAD entered into these Shelf Space arrangements to further the sale of Funds that it sold and distributed. PAD negotiated the Shelf Space arrangements for PAFM and PAD's benefit. PAFM and Treadway knew of and approved the arrangements. Although the Shelf Space arrangements were negotiated by PAD, PAFM and PAD were functionally the same entity and shared the same CEO, Treadway; it was mere convenience that PAD was the entity that negotiated the shelf space arrangements.

9. The broker-dealers promised PAD that it would receive various distribution services in connection with these Shelf Space arrangements, including, but not limited to: participation in meetings with registered representatives, such as annual attendance at broker-

dealers' sales and marketing conferences; the opportunity for the Funds distributed by PAD to be mentioned in communications with broker-dealers' customers, such as prominent placement on the broker-dealers' websites; and most often, placement on preferred or focus lists at the broker-dealers.

10. Although Treadway was involved in the negotiations with certain broker-dealers for the Shelf Space arrangements, PAD's employees conducted the majority of the negotiations. Because of his position as CEO of PAFM and PAD, PAD's employees sought and obtained Treadway's approval of each arrangement they negotiated and how PAD would pay for them.

Treadway Asked PEA to Direct Brokerage Commissions which <u>PAD then Used to Satisfy its Shelf Space Obligations</u>

11. Although most broker-dealers preferred Shelf Space payments to be made in cash (i.e., "hard dollars"), many broker-dealers accepted payments in the form of brokerage commissions on portfolio transactions. While hard dollars were paid from PAD's assets, the brokerage commissions were paid from the MMS Funds' assets.

12. Beginning in late 2000, Treadway and employees of PAFM and PAD discussed the possibility of helping PAD obtain "Shelf Space" for the MMS Funds through PEA directing brokerage commissions on the MMS Funds' portfolio transactions.

13. After Treadway approved the concept of using brokerage commissions to pay for Shelf Space arrangements, he and other members of PAD approached PEA, the sub-adviser to the largest MMS equity funds, to discuss whether PEA would be able to direct brokerage commissions to certain broker-dealers whom PAD selected.

14. Treadway did not tell PEA that he and PAD were asking PEA to direct trades to these broker-dealers to reduce PAD's cash payments for Shelf Space arrangements. He instead simply told PEA that trading with these firms would "benefit" PAD.

15. Initially, in late 2000 and 2001, Treadway and PAD requested that PEA direct trades to three broker-dealers, which PEA did. At that time, there was no formal communication between PAD and PEA about the amount of brokerage commissions directed to each broker-dealer. By 2002, however, the process was more formalized and PEA advised PAD, in response to PAD's request, that $5 million in brokerage commissions would likely be available to direct to distributing broker-dealers. At the same time, PAD increased, and Treadway approved, the number of Shelf Space arrangements in which brokerage commissions would be used to reduce PAD's cash payments from three to nine broker-dealers.

16. PAD subsequently divided the available commissions among the nine broker-dealers with whom it had Shelf Space arrangements and who had agreed to give PAD credit for the directed brokerage commissions. PAD then assigned a target amount of brokerage commissions to be directed to each broker-dealer and provided such targeted amounts to PEA.

PAD or PEA then reduced these targeted amounts to a written list. The head trader at PEA then provided this list to the other traders.

17. PEA's traders sought to execute portfolio transactions for the MMS Funds with such broker-dealers in the amounts requested by PAD, subject to best execution. At the end of the trading day, after the trades had been executed, the traders designated certain commissions for Shelf Space arrangements.

18. Treadway was aware that PAD occasionally received invoices from some of the nine broker-dealers that reflected the amounts that were due under the Shelf Space arrangements. The amounts due were based on an agreed upon basis point formula and the level of sales and aged assets for the period. The invoices reflected how much credit PAD had received as a result of the trading through PEA and requested that any difference between the amount owed and the credited commissions be addressed with a cash payment. Treadway approved PAD's cash payments to satisfy these invoices.

Treadway Failed to Disclose to the MMS Board the Alternatives for Satisfying Shelf Space Arrangements and the Conflict of Interest that Existed

19. As a fiduciary, PAFM had a duty to disclose to the MMS Board any conflict of interest created by the use of fund brokerage commissions to satisfy Shelf Space arrangements or defray the expenses of a third party, yet it failed to do so. As CEO and the individual through which PAFM addressed the MMS Board, Treadway was responsible for ensuring that PAFM met this duty.

20. Treadway did not disclose to the MMS Board that MMS Funds' brokerage commissions were being directed to reduce PAD's payments for the Shelf Space arrangements or that a corresponding conflict of interest existed for PAFM and PEA.

21. Further, although Treadway, on behalf of PAFM disclosed to the MMS Board information regarding PEA's use of brokerage commissions for research and other services, he did not disclose the use of the brokerage commissions to satisfy Shelf Space arrangements. Treadway also did not inform the MMS Board that PAD had the option of paying for these arrangements completely from its own assets and that, by receiving a credit for certain brokerage commissions, PAD avoided using its own assets to pay for the services obtained under the Shelf Space arrangements. Although Treadway had knowledge of the Shelf Space arrangements and had opportunities to disclose this information to the MMS Board, he did not disclose this information to the MMS Board and did not ensure that anyone else disclosed this information.

22. As a result of the conduct described above, Treadway willfully aided and abetted and caused PAFM's violation of Section 206(2) of the Advisers Act, which provides that it is "unlawful for any investment adviser, by the use of the mails or any means or instrumentality of interstate commerce, directly or indirectly . . . to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client."

IV.

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

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

A. Treadway is censured.

B. Treadway shall cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act.

C. Within 30 days from the date of entry of the Order, Treadway shall pay a civil money penalty in the amount of $75,000 to the United States Treasury. 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 Treadway as a Respondent in these proceedings, and the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Daniel M. Hawke, District Administrator, Philadelphia District Office, Securities and Exchange Commission, Mellon Independence Center, 701 Market Street, Suite 2000, Philadelphia, PA 19106.

By the Commission.

Nancy M. Morris

Nancy M. Morris
Secretary

Commissioner Nazareth
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55763 / May 15, 2007

INVESTMENT ADVISERS ACT OF 1940
Release No. 2603 / May 15, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12636

In the Matter of **GEORGE B. FASCIANO,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940 MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against George B. Fasciano ("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 him and the subject matter of these proceedings, and the findings contained in Section III., Paragraph 2, below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Section 203(f) of the

Document 22 of 33

Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

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

1. Fasciano, age 34, was a Vice President and registered representative in the Private Client Group at Southwest Securities, Inc. ("Southwest" or the "Firm"), a dually registered broker-dealer and investment adviser, until the Firm terminated his employment in April 2004. Fasciano has the following NASD licenses: General Securities Representative (Series 7), Uniform Securities Agent State Law (Series 63), and Registered Investment Adviser (Series 65).

2. On April 23, 2007, a final judgment was entered by consent against Fasciano, permanently enjoining him from future violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in the civil action entitled *SEC v. Gann*, Civil Action Number 3:05-CV-0063-L/NDTX, in the United States District Court for the Northern District of Texas, Dallas Division. The Court further ordered Fasciano to pay disgorgement in the amount of $56,000, plus prejudgment interest thereon in the amount of $4,929.91, and a civil penalty in the amount of $30,000.

3. The Commission's complaint alleged that Fasciano and others ("Defendants") engaged in a scheme to defraud hundreds of mutual funds and their shareholders by engaging in deceptive market timing practices on behalf of a single client, a hedge fund adviser based in New York ("Hedge Fund"). Knowing that the mutual fund companies in which the Defendants wished to trade monitored activity in their family of mutual funds, restricted excessive trading and had previously blocked the Hedge Fund from trading, Defendants engaged in a fraudulent scheme to disguise their market timing trading, and thereby circumvented trading restrictions imposed by the fund companies. Specifically, Defendants routinely and systematically (i) concealed their own identities and the identity of the Hedge Fund, (ii) created multiple accounts for the Hedge Fund and used several broker identification numbers to process market timing trades, (iii) divided trades into amounts designed to evade detection, and (iv) used different branch identification numbers to disguise their trading activity. Using these fraudulent tactics, Defendants placed thousands of market timing trades for the Hedge Fund that would have otherwise been rejected by the fund companies. As a result, Defendants caused harm to mutual fund companies and their shareholders by diluting the value of the mutual fund shares and increasing the transaction costs associated with the management of the mutual funds.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act and Section 203(f) of the Advisers Act, that Respondent Fasciano be, and hereby is barred from association with any broker, dealer, or investment adviser, with a right to reapply for association after two (2) years to the appropriate self-regulatory organization, or if there is none, to the Commission;

Any reapplication for association by the Respondent 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: (i) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (ii) any arbitration award related to the conduct that served as the basis for the Commission order; (iii) 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 (iv) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Nancy M. Morris

Nancy M. Morris
Secretary

Commissioner Nazareth Not Participating

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55771 / May 16, 2007

INVESTMENT ADVISERS ACT OF 1940
Rel. No.2604 / May 16, 2007

Admin. Proc. File No. 3-12267

In the Matter of

BRADLEY T. SMITH

c/o Karl E. May, Esq.
Cowden, Humphrey, Nagorney & Lovett
1414 Terminal Tower
50 Public Square
Cleveland, OH 44113-2204

OPINION OF THE COMMISSION

BROKER-DEALER PROCEEDING
INVESTMENT ADVISER PROCEEDING

Ground for Remedial Action

Injunction

Former president of investment advisory firm and of broker-dealer was enjoined from violating the antifraud provisions of the securities laws in connection with misrepresentations that he made to investors concerning his use of offering proceeds and his diversion of the proceeds to pay expenses of his other businesses and for his personal use. Held, it is in the public interest to bar respondent from associating with any broker or dealer or investment adviser.

APPEARANCES:

Karl E. May, of Cowden, Humphrey, Nagorney & Lovett, for Bradley T. Smith.

Steven J. Levine, Andrea R. Wood, and Erik J. Lillya, for the Division of Enforcement.

Document 23 of 33

Appeal filed: October 17, 2006
Last brief received: December 26, 2006

I.

Bradley T. Smith, the former president of Bancshareholders of America, Inc. ("BSA"), a firm registered as an investment adviser with the state of Ohio, and of BancShares First, Inc. ("BancShares First"), a former broker-dealer, appeals from the decision of an administrative law judge. 1/ The law judge found that Smith had been enjoined from violating the antifraud provisions of the securities laws. The law judge found further that it was in the public interest to bar Smith from associating with any broker or dealer or investment adviser. We base our findings on an independent review of the record, except with respect to those findings of the law judge not challenged on appeal.

II.

On September 27, 2005, the United States District Court for the Southern District of Ohio granted partial summary judgment to the Commission in an injunctive action against Smith, his co-defendants, Continental Midwest Financial, Inc. ("Continental") and Scioto National, Inc. ("Scioto"), and relief defendants BSA and Bancshare Investors Brokerage, Inc. ("BSIB"). 2/ The district court found that Smith, Continental, and Scioto violated Sections 17(a)(1), (2), and (3) of the Securities Act of 1933, 3/ Section 10(b) of the Securities Exchange Act of 1934, and Exchange Act Rule 10b-5 4/ in connection with the private offerings of securities of Continental and Scioto. The district court also found Smith liable as a control person under Exchange Act Section 20(a) for Continental's and Scioto's Exchange Act violations. 5/

1/ According to Smith, BancShares First ceased operations in 2004, a few months after the Commission filed its action against him. Smith was licensed with the state of Ohio as a securities salesperson and an investment adviser representative when we commenced this action in August 2004. Smith withdrew his licenses in November 2004.

2/ SEC v. Bradley T. Smith, 2005 U.S. Dist. LEXIS 21427 (S.D. Ohio Sept. 27, 2005), aff'd per curiam, 2006 U.S. App. LEXIS 30976 (6th Cir. 2006). The district court denied the Commission's motion for summary judgment against Smith regarding an aiding and abetting claim. The Commission subsequently dismissed that claim.

3/ 15 U.S.C. §§ 77q(a)(1), (2), and (3).

4/ 15 U.S.C. § 78j(b) and 17 C.F.R. § 240.10b-5.

5/ 15 U.S.C. § 78t(a).

On December 6, 2005, the district court permanently enjoined Smith, Continental, and Scioto from violating Securities Act Section 17(a), Exchange Act Section 10(b), and Exchange Act Rule 10b-5. The district court imposed a civil money penalty of $120,000 on Smith. The district court ordered Continental to disgorge $1,272,665.93, plus prejudgment interest, for a total of $1,409,149.35, and ordered Scioto to disgorge $822,852, plus prejudgment interest, for a total of $885,048.37. The district court held Smith jointly and severally liable with Continental and Scioto for their respective disgorgement amounts and prejudgment interest. 6/ On December 14, 2006, the United States Court of Appeals for the Sixth Circuit affirmed the district court's decision. 7/

On April 20, 2006, we instituted administrative proceedings against Smith. In July 2006, the law judge held a three-day hearing at which twenty-one witnesses testified and numerous exhibits were admitted into evidence.

III.

A. Background

Smith held himself out to the public as an expert in small community bank stocks. The district court found that Smith's business consisted primarily of establishing and operating private companies whose stated purpose was "to serve as vehicles for investors to buy small community bank stocks." Before the law judge, Smith testified that he was the primary decisionmaker for each of his companies and was responsible for deciding how they would spend their money and whether or not they would invest in bank stocks.

B. The Offerings

Between 1999 and 2004, five of Smith's companies conducted private offerings of securities that raised a total of approximately $3.7 million. One offering followed another almost immediately once the proceeds from the previous offering had been depleted by transfers to affiliated companies and by business and personal expenses. The Continental and Scioto offerings were the last two in a series of five similar offerings conducted by Smith's companies, and these two offerings were the subject of the injunctive proceeding before the district court. In addition, the record contains evidence regarding the three offerings conducted by Smith that

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6/ The district court ordered relief defendant BSA to disgorge $631,292, plus prejudgment interest, for a total of $679,009, and ordered relief defendant BSIB to disgorge $313,012, plus prejudgment interest, for a total of $336,581. The district court did not hold Smith jointly and severally liable for these amounts.

7/ SEC v. Bradley T. Smith, 2006 U.S. App. LEXIS 30976 (6th Cir. 2006) (per curiam). The record does not indicate whether or not Smith has paid the penalty and disgorgement amounts for which he is liable.

preceded the Continental and Scioto offerings. Accordingly, we summarize the relevant facts from those offerings here.

The Continental Offering. Smith was the chairman, president, treasurer, and sole director of Continental from approximately July 2002 until September 2004. Continental conducted a private offering of its common stock between July 2002 and September 2003. The district court found that Smith prepared and distributed copies of a private offering memorandum (the "Continental POM") to potential investors in connection with that offering. The Continental POM stated that the purpose of the offering was to raise a maximum of $2.27 million to invest in financial services companies and small Midwestern banks. The Continental POM represented that 80% of the offering proceeds would be invested in small bank stocks. Before the law judge, several Continental investors testified that they understood that their investments in Continental would be used to purchase bank stocks. For example, one witness testified that the "money that was collected from investors was, we were told over and over again, to be invested in small community bank stocks . . . ."

The district court found that Smith and his employees also provided copies of Continental's Business Plan to prospective investors before they invested in Continental. Continental's Business Plan represented that 81% of the anticipated offering proceeds of $2.27 million would be used to "build a community bank stock portfolio." The remainder was to be used for working capital. The district court noted that Smith in his deposition had stated that the term "working capital" referred to general administrative and operating expenses generated solely by Continental.

The Continental offering raised $1,272,665 from forty-nine investors. 8/ Only $125,532, or 9%, of the offering proceeds were invested in bank or financial services company stocks. Before the district court, Smith admitted that he used the offering proceeds "in a manner contrary to the Continental POM's representations." The district court found, for example, that "Smith used some of the proceeds to pay his credit card bill, which included charges for men's clothing, nutritional supplements, and a dating/escort service." The district court found further that Smith spent $133,532 of the Continental offering proceeds to pay BSA's bills, including payments to "himself and his employees, and to pay taxes and rent for Smith's offices." The district court found, however, that Smith and his employees did not inform Continental investors that their investments would be used to pay the expenses of Smith's other businesses and to cover his personal expenses. The district court determined that "only 9% of the proceeds [contributed by investors] were used to purchase small bank stocks, in contrast to the 80% represented in the Continental POM." The district court found that, in reality, "85% of the proceeds [contributed by investors] were used to cover other expenses of Smith's businesses." The district court found that, by June 30, 2004, Continental had only $10,000 worth of investments. The district court found that ultimately Continental liquidated all of its investments.

8/ Continental also received funds from Smith-affiliated companies, liquidated investments, and other sources that were not identified in the record.

Smith admitted before the law judge that he had prepared the Continental POM himself. Smith conceded that he did not expect Continental to use the majority of the offering proceeds to invest in bank stocks. Under cross-examination, Smith conceded that he should have prepared an accurate POM for Continental.

The Scioto Offering. Smith was the chairman, president, treasurer, and sole director of Scioto from approximately January 2004 to September 2004. Scioto initiated a private offering of its common stock in January 2004. The district court found that Smith drafted and provided each potential Scioto investor with a private offering memorandum (the "Scioto POM") and other marketing materials. The Scioto POM stated that the purpose of the offering was to invest in financial services companies and small Midwestern banks. The Scioto POM anticipated that the offering would raise a maximum of $1,008,000, and that approximately 70% of the proceeds would be invested in small bank stocks. Several of the Scioto investors confirmed at the hearing that they understood that their investments would be used to purchase bank stocks.

The Scioto offering raised $822,852 from twenty-nine investors. The district court found that, of that amount, approximately $170,000, or 21%, was transferred into an investment account. The district court also determined that Smith spent $503,208 of the investor funds on the expenses of his other businesses, and that Scioto spent $86,092 for Smith's salary and for his personal use. By August 17, 2004, Scioto's bank account had dwindled to approximately $3,392.

The district court found further that Smith did not reimburse Continental and Scioto for the personal expenses that were charged to his companies' credit cards. Continental and Scioto investors lost over $2 million in the aggregate. 9/

The district court found that Smith engaged in misrepresentations or omissions of material facts in connection with the offer, sale, or purchase of securities with scienter. The district court noted that the Continental and Scioto POMs each contained a separate section setting forth the estimated use of proceeds that represented that "the bulk of the proceeds would be used primarily to buy stock in small Midwestern banks." The district court found that Smith was responsible for both Continental's and Scioto's financial decisions. Smith admitted that he used the offering proceeds for personal and unrelated business expenses. The district court noted that, although Smith knew that neither Continental nor Scioto would be using the proceeds in the manner set forth in the POMs, he nonetheless distributed the erroneous POMs and marketing materials to investors. He used the Continental POM as a template for the Scioto POM, but did not correct the misrepresentations before distributing the Scioto POM to investors. Nor did he issue amended POMs containing the correct information.

9/ Although several Continental and Scioto investors testified against Smith at the hearing, some other investors who had accounts at BSA and who had invested in Continental or Scioto testified in support of Smith's continuing to provide research to BSA.

In addition to the Continental and Scioto offerings, which were the subject of the injunctive action before the district court, the law judge also considered evidence concerning the three earlier offerings conducted by Smith.

The BIG Offering. Smith was the president, treasurer, and sole director of BancInvestment Group, Inc. ("BIG"). BIG conducted a private securities offering from 1998 to 1999. BIG's private placement memorandum represented that the company sought to raise a maximum of $1,002,000 and that $912,000 of the anticipated offering proceeds would be invested in bank stocks, with the remainder allocated to offering and operating expenses. The BIG offering eventually raised only $171,425 from investors. 10/ None of those funds were invested in bank stocks. Instead, BIG's funds were used to make payments to Smith or for his benefit, and for his personal credit card expenses, business credit card expenses, payments to BIG staff, and other unspecified expenditures. Before the law judge, Smith conceded that he "believe[d] that [it was] the case" that funds raised from the BIG offering ultimately were spent on items other than investments in bank stocks. All of BIG's funds were expended by January 2000.

The BSA Offering. Smith was the president, treasurer, and sole director of BSA from January 2000 until September 2004. BSA conducted a private securities offering beginning in January 2000. BSA's private placement memorandum stated that the company sought to raise a maximum of $2 million, and that up to $1.4 million of the anticipated offering proceeds would be invested in bank stocks and a lesser amount in the shares of an investment company, with the rest of the proceeds allocated to general and administrative expenses and start-up costs. The offering raised approximately $797,750 from investors. 11/ Although $209,104 of the offering proceeds initially was invested in bank stocks, those investments were subsequently liquidated. Smith testified at the hearing that the proceeds from the sale of those bank stocks were spent on "[e]xpenses of the company." Smith spent BSA's funds on payments to himself or for his benefit, and on his personal credit card expenses, business credit card expenses, payments to BSA staff, transfers to affiliated companies, and other unspecified expenditures. By May 14, 2001, BSA's bank accounts contained less than $5,000.

The BSIB Offering. Smith was the chairman, president, treasurer, and sole director of BSIB from approximately April 2001 until September 2004. As set forth in an offering memorandum dated April 15, 2001, BSIB sought to raise a maximum of $1,050,000, with $445,000 of the offering proceeds to be used to purchase stock in small banks. The BSIB offering eventually raised only $698,700 from investors, and in reality, only $4,022 of the offering proceeds was invested in bank stocks, which were subsequently liquidated. BSIB's

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10/ BIG also received funds from Smith-affiliated companies and other sources that were not identified in the record. None of these funds were invested in bank stocks.

11/ BSA also received funds from Smith-affiliated companies, liquidated investments, and other sources that were not identified in the record.

funds, including the liquidated bank stock proceeds, were spent on what Smith characterized as "company expenses." 12/ Smith spent BSIB's funds on payments to himself or for his benefit, and on his personal credit card expenses, business credit card expenses, payments to BSIB staff, transfers to affiliated companies, and other unspecified expenditures. Smith conceded that, as of the time of the hearing, BSIB did not have a significant portfolio of bank stocks. By July 2002, the BSIB account had less than $600 in it.

C. Recent Activities

Smith relinquished his positions as an officer and director of his various companies in 2004, following the filing of the injunctive action against him. He thereafter appointed new directors to the boards of BSA, Continental, and Scioto. Smith testified at the hearing that he wished to remain in the securities industry. He also testified that, at the time of the hearing, he was a "consultant" to BSA. In that capacity, Smith makes recommendations regarding the types of bank stocks that BSA should purchase for its clients' accounts. Smith received compensation for a time for his consulting work for BSA. He was compensated through funds raised from a second private offering of BSIB common stock in December 2004. 13/ Before the law judge, BSA's chief operating officer testified that BSA had approximately $4 million in assets under management and was operating at a loss. He estimated that the company would need approximately $15 million in assets under management to break even.

IV.

Under Sections 203(e) and (f) of the Investment Advisers Act of 1940 and Exchange Act Section 15(b)(6), we may bar a person associated with an investment adviser or a broker-dealer if the associated person is enjoined from, among other things, engaging in any conduct or practice in connection with the purchase or sale of a security. 14/ Smith was the president, treasurer, and sole director of investment adviser BSA and the president of broker-dealer BancShares First during the relevant period. Smith does not dispute that the district court granted summary judgment against him, based on findings that he had violated the antifraud provisions of the securities laws in connection with the purchase or sale of a security. Nor does he dispute the factual bases for the injunction.

12/ BSIB also received funds from Smith-affiliated companies and liquidated investments that were not identified in the record.

13/ This offering occurred after the injunctive action had been filed and was not addressed by the district court or the law judge. The December 2004 BSIB confidential private offering summary represented that a trust that controlled BSIB was selling shares of BSIB "to fund or pay the expenses of" BancShares First, BSA, BSIB and/or their affiliates. At the time of the offering, Smith was a beneficiary of the trust.

14/ 15 U.S.C. §§ 80b-3(e)(4), 80b-3(f), 78*o*(b)(6).

However, Smith objects to the law judge's "principle [sic] conclusions" regarding the sanctions imposed. He challenges the law judge's determinations that Smith's "expressions of remorse were 'tempered' by blaming others, that his assurances against future misconduct, when placed beside the fact that he is not in a controlling position of the companies and has no access to funds, are not sincere, and that, having been statutorily disqualified and enjoined by the [d]istrict [c]ourt, he would still somehow be in a position to have the 'opportunity' to violate the law in the future."

In evaluating whether an administrative sanction serves the public interest, we consider, among other things, the egregiousness of a respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his or her conduct, and the likelihood that the respondent's occupation will present opportunities for future violations. 15/ We also consider the extent to which the sanction will have a deterrent effect. 16/ The appropriate sanction depends on the facts and circumstances of each case. 17/ Taken as a whole, these factors support the imposition of a bar against Smith from associating with any broker or dealer or investment adviser.

Smith's conduct was egregious and involved scienter. Smith prepared and distributed the Continental and Scioto POMs that contained material misrepresentations concerning the proposed use of offering proceeds. 18/ Forty-nine investors invested $1,272,665 in Continental. Twenty-nine investors invested $822,852 in Scioto. Contrary to the representations in the Continental and Scioto POMs, Smith diverted the bulk of both offerings' proceeds away from the

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15/ See Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981).

16/ See, e.g., Ahmed Mohamed Soliman, 52 S.E.C. 227, 231 n.12 (1995) (stating that the selection of an appropriate sanction involves consideration of several elements, including deterrence); Lester Kuznetz, 48 S.E.C. 551, 554 (1986) (noting that the sanction of a bar "serves the purpose of general deterrence"); see also McCarthy v. SEC, 406 F.3d 179, 190 (2d Cir. 2005) (noting that deterrent value is a relevant factor to consider in deciding sanctions).

17/ See Butz v. Glover Livestock Comm'n Co., 411 U.S. 182, 187 (1973); Michael Batterman, Investment Advisers Act Rel. No. 2334 (Dec. 3, 2004), 84 SEC Docket 1349, 1358, aff'd, No. 05-0404 (2d Cir. 2005) (unpublished).

18/ When asked at the hearing whether she would want to continue doing business with Smith, one witness who had invested in both Continental and Scioto responded "Absolutely not. I've lost my trust." Another witness who had lost his $70,000 investment in Scioto testified at the hearing that he had no interest in continuing to do business with Smith because he "[v]iolated my trust."

offerings' stated purpose of investing in bank stocks or financial services companies, and toward his personal and other business expenses. The Continental and Scioto investors lost a combined $2 million.

Smith drafted the representations with respect to how the Continental and Scioto offering proceeds would be spent. Despite his awareness that neither Continental nor Scioto would be using the proceeds in the manner described in their respective POMs, he nonetheless distributed those erroneous POMs and related marketing materials to investors. Nor did he make any attempt to cure those misrepresentations by issuing amended POMs.

Smith claims that the district court's "decision was based on a finding of recklessness and not actual scienter." However, the district court found scienter. As the district court stated, "Sixth Circuit precedent establishes that the [Commission] may establish scienter by producing proof of recklessness – 'highly unreasonable conduct which is an extreme departure from the standards of ordinary care.'" 19/ The district court concluded that "Smith's admissions coupled with vast evidence of reckless conduct" supported a finding of scienter. 20/

Smith's misconduct was not an isolated occurrence. The record shows that the Continental and Scioto offerings were two of the more recent in a history of successive private securities offerings initiated by Smith's various companies. This pattern began in 1998, when Smith launched the BIG offering. In what would become his modus operandi, after the proceeds from that offering had been exhausted by business and personal expenses, Smith initiated the BSA offering in 2000, and when the proceeds of that offering had been similarly depleted, he commenced the BSIB offering in 2001. These offerings were succeeded by the Continental offering from 2002 to 2003, and by the Scioto offering in 2004. By arranging these transactions into a sequence of consecutive offerings over time, Smith arrogated the proceeds of one company to cover the expenses of his other companies and his personal expenditures, instead of investing the proceeds as stated in each company's private placement memorandum or POM.

While Smith has expressed remorse at his misconduct, he characterized his conduct as "cutting corners" and neglecting matters that he should have "paid more attention to." As discussed above, we believe his conduct was more serious. 21/ Indeed, as the law judge

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19/ 2005 U.S. Dist. LEXIS 21427, at *21 (quoting Mansbach v. Prescott, Ball & Turben, 598 F.2d 1017, 1025 (6th Cir. 1979)).

20/ Under the doctrine of collateral estoppel, the district court's findings cannot be challenged in a "follow-on" administrative proceeding. See, e.g., Batterman, 84 SEC Docket at 1356 & n.18 (stating that collateral attacks on district court decisions are not permitted in follow-on proceedings).

21/ See Christopher Lowry, 55 S.E.C. 1133, 1145 (2002) (barring president of investment adviser for violating antifraud provisions of the securities laws in connection with determined, Smith's showing of remorse was tempered by his blaming of others or his "incredible excuses for specific shortfalls." 22/

Smith also states that he has "separat[ed] himself completely from daily operations and from access to funds and financial matters, as well as stepping down as officer and director." He asserts that BSA has implemented safeguards which would be overseen by directors who would understand their fiduciary duties.

We have stated previously that, even if we accepted a respondent's assertions that he is voluntarily isolated from a company's management, actions to limit a respondent's involvement are not irrevocable and can be reversed at the company's option. 23/ The new BSA board of directors was selected by Smith after we commenced the injunctive action against him. In contrast to the hearing testimony of the Continental and Scioto witnesses who had been injured by Smith's misconduct, the BSA directors' testimony was deferential toward Smith. One BSA board member acknowledged that nothing would prevent the board from giving Smith management responsibilities at BSA. Moreover, Smith's description of the services he provides to BSA strongly suggests that he considers himself indispensable to BSA and anticipates a larger role at the company. 24/

In any event, even if BSA's measures reduced the likelihood that Smith would play a significant role at BSA, they would have no effect on any position that Smith might assume at another company. 25/ Absent a bar, there would be no obstacle to Smith's associating with

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misrepresentations that he made to investors regarding use of offering proceeds and diversion of proceeds to his personal use), aff'd, 340 F.3d 501 (8th Cir. 2003).

22/ The credibility determination of an initial fact finder is entitled to considerable weight and deference because it is based on hearing the witnesses' testimony and observing their demeanor. See Rita J. McConville, Securities Exchange Act Rel. No. 51950 (June 30, 2005), 85 SEC Docket 3127, 3136 n.21, petition denied, 465 F.3d 780 (7th Cir. 2006), reh'g denied, 2007 U.S. App. LEXIS 926 (7th Cir. 2007); Daniel Joseph Alderman, 52 S.E.C. 366, 368 n.6 (1995), aff'd, 104 F.3d 285 (9th Cir. 1997); Jonathan Garrett Ornstein, 51 S.E.C. 135, 137 (1992).

23/ Schield Mgmt. Co., Exchange Act Rel. No. 53201 (Jan. 31, 2006), 87 SEC Docket 848, 865 (barring president of investment adviser based on his injunction against future violations of the antifraud and investment adviser provisions of the Advisers Act).

24/ Id. at 864.

25/ Id.

another investment adviser or broker-dealer that would neither restrict his conduct nor his access to funds. 26/

Smith's primary argument appears to be that the imposition of a bar is not in the public interest because of "important mitigating factors" and the harm that such a bar would cause to existing BSA shareholders. Specifically, Smith states that he continues to provide "critical research" to BSA, which remains an operating entity, "for virtually no compensation." 27/ He contends further that "there is no one but Mr. Smith who can provide the expertise in community bank stocks needed for the survival of the business of BSA, and to therefore prevent the collapse of BSA and injure its shareholders." He relies on the hearing testimony of the BSA, Continental, and Scioto directors and the Continental and Scioto investors who continue to support him. He argues that BSA's "innocent shareholders" will be harmed if he is not permitted to provide services to BSA and to his related companies. Smith contends further that the sanctions will deter others from admitting their wrongdoing, taking responsibility for their actions, and implementing remedial steps to help investors. We are not persuaded by these arguments.

Smith's actions harmed many of his existing shareholders, in serial securities offerings, misstating the use of those offerings' proceeds and using them instead for his personal and unrelated business expenses. Indeed, even if we were to accept Smith's testimony and arguments about harm to existing shareholders, we have long held that the "public interest determination extends beyond the consideration of particular investors to the public-at-large." 28/ Given that Smith conducted five separate offerings in which most of the funds raised were not invested as represented in the various offering documents, we believe that the sanction of a bar would protect the general public.

Moreover, we are skeptical of Smith's claims that the existing BSA shareholders will be harmed if he is barred. 29/ Nothing precludes BSA's current board and management from finding another investment adviser or broker-dealer or associated individual with similar

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26/ See id.

27/ It appears that Smith in fact was compensated for some of his BSA consulting work through a second private offering of BSIB stock.

28/ Lowry, 55 S.E.C. at 1145 (citing Steadman, 603 F.2d 1126).

29/ We note that BSA's chief operating officer admitted before the law judge that BSA was operating at a loss and that its funds under management were well below the amount needed to break even. The district court reported that BSA had sought bankruptcy protection. See SEC v. Smith, 2005 U.S. Dist. LEXIS 26421 (S.D. Ohio Nov. 2, 2005).

expertise. Further, BSA's clients are free to move their investment accounts elsewhere without losing their assets. 30/

Finally, we do not accept Smith's argument that the sanction will deter others from admitting their wrongdoing, taking responsibility for their actions, and implementing remedial steps. As discussed above, Smith has failed to admit fully his wrongdoing and continues to minimize his conduct. It appears that he failed to disclose the nature and result of the injunctive action to at least some of the investors. We do not believe that the record substantiates his claims of remediation.

Taken as a whole, the district court's findings and the record evidence before the law judge warrant Smith's exclusion from the securities industry. Accordingly, we find that it is in the public interest to bar Smith from associating with any broker or dealer or investment adviser.

An appropriate order will issue. 31/

By the Commission (Chairman COX and Commissioners ATKINS, CAMPOS, and CASEY); Commissioner NAZARETH not participating.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

30/ See Lowry, 55 S.E.C. at 1145.

31/ We have considered all of the contentions advanced by the parties. We have rejected or sustained these contentions to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55771 / May 16, 2007

INVESTMENT ADVISERS ACT OF 1940
Rel. No. 2604 / May 16, 2007

Admin. Proc. File No. 3-12267

In the Matter of

BRADLEY T. SMITH

c/o Karl E. May, Esq.
Cowden, Humphrey, Nagorney & Lovett
1414 Terminal Tower
50 Public Square
Cleveland, OH 44113-2204

ORDER IMPOSING REMEDIAL SANCTIONS

On the basis of the Commission's opinion issued this day, it is

ORDERED that Bradley T. Smith, be, and he hereby is, barred from association with any broker or dealer or investment adviser.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34-55777; File No. S7-08-07]

RIN 3235-AJ85

Amendments to Financial Responsibility Rules for Broker-Dealers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; Extension of comment period.

SUMMARY: The Securities and Exchange Commission is extending the comment period for a release proposing amendments to its net capital, customer protection, books and records, and notification rules for broker-dealers under the Securities Exchange Act of 1934 ("Exchange Act"), which was issued by the Commission on March 9, 2007 (Exchange Act Release No. 55431, 72 FR 12862 (Mar. 19, 2007)). The original comment period for Release No. 34-55431 is scheduled to end on May 18, 2007. The Commission is extending the time period in which to provide the Commission with comments on the proposed amendments described in Release No. 34-55431 for thirty-one days until Monday, June 18, 2007. This action will allow all interested persons additional time to analyze the issues and prepare their comments.

DATES: Comments should be received on or before June 18, 2007.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/proposed); or

Document 24 of 33

- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-08-07 on the subject line; or
- Use the Federal eRulemaking Portal (http://www.regulations.gov). Follow the instructions for submitting comments.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-08-07. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (http://www.sec.gov/rules/proposed). Comments will also be available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, at (202) 551-5525; Thomas K. McGowan, Assistant Director, at (202) 551-5521; Randall Roy, Branch Chief, at (202) 551-5522; or Bonnie Gauch, Attorney, (202) 551-5524; Division of Market Regulation, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-6628.

SUPPLEMENTARY INFORMATION: On March 9, 2007, the Commission requested comment on proposed amendments to the Commission's net capital, customer protection, books and records, and notification rules for broker-dealers under the Exchange Act.[1] Specifically, the proposed amendments are designed to address several emerging areas of concern regarding the financial requirements for broker-dealers. They also would update the financial responsibility rules and make certain technical amendments.

The Commission originally requested that comments on this proposal be received by May 18, 2007. The Commission thus far has received few public comments and believes that extending the comment period would be appropriate in order to give the public additional time to thoroughly consider the matters addressed by the release.[2] Therefore, the Commission is extending the comment period for Release No. 34-55431 (Amendments to Financial Responsibility Rules for Broker-Dealers) for thirty-one days, to Monday, June 18, 2007.[3]

By the Commission.

Nancy M. Morris

Nancy M. Morris
Secretary

Dated: May 17, 2007

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1 See Exchange Act Release No. 55431, 72 FR 12862 (Mar. 19, 2007).

2 See also Letter from Gerard J. Quinn, Vice President and Associate General Counsel of SIFMA to Michael Macchiaroli, date May 4, 2007 (noting the importance of the issues discussed in the release and the complexity of the issues involved).

3 If the comment period was estended for thirty days, the due date would fall on a Sunday. Therefore, the Commission is extending the comment period for thirty-one days.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Commissioner Campos
Not Participating

SECURITIES EXCHANGE ACT OF 1934
Release No. 55778 / May 17, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12637

In the Matter of Michael Edward Zimmerman, Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The United States Securities and Exchange Commission (the "Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Michael Edward Zimmerman ("Zimmerman" 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 him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

Document 25 of 33

III.

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

1. From April 2004 through April 2005, Zimmerman was a 50 percent stockholder of Z-Par Holdings, Inc., as well as a director of Z-Par Investment Fund II, LLC. Zimmerman associated with Wellstone Securities LLC, which is a Georgia-based broker-dealer and investment advisor registered with the NASD, in connection with the marketing and sales of investments in a prime bank security trading program through Z-Par Investment Fund II, LLC. Zimmerman, 38 years old, is a resident of Jefferson, Maryland.

2. On April 26, 2006, a final judgment was entered by consent against Zimmerman, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in the civil action entitled United States Securities & Exchange Commission v. Z-Par Holdings, Inc., et al., Civil Action Number 05cv1031, in the United States District Court for the District of Maryland, Baltimore Division.

3. The Commission's complaint alleged that from at least April 2004 to April 2005, Zimmerman marketed a fraudulent prime bank investment scheme in which he raised approximately $8.2 million from eleven investors in Florida and others elsewhere throughout the United States. The complaint also alleged that Zimmerman fraudulently represented to investors that their funds would be pooled with those of other investors in $1 million lots for the purchase of "debt obligations of the top 50 banks in the world," which would be safe and secure investments yielding high rates of return. The complaint further alleged that Zimmerman fraudulently sold interests in fictitious prime bank debt instruments and payment obligations, claiming that they carried a financial insurance guarantee that wraps the debt obligations to further enhance their value and lower their risks from any default. The complaint further alleged that in furtherance of the fraudulent scheme, Zimmerman sent investor funds to third-parties who, unbeknownst to Zimmerman, used the funds to purchase precious metals on margin.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act, that Respondent Zimmerman be, and hereby is barred from association with any broker or dealer, with the right to reapply for association after five years to the appropriate self-regulatory organization, or if there is none, to the Commission;

Any reapplication for association by the Respondent 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 the Respondent, 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.

By the Commission.

Nancy M. Morris
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Campos
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55779 / May 17, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12638

In the Matter of Larry Michael Parrish, Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The United States Securities and Exchange Commission (the "Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Larry Michael Parrish ("Parrish" 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 him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

Document 26 of 33

III.

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

1. From April 2004 through April 2005, Parrish was a 50 percent stockholder of Z-Par Holdings, Inc., as well as a director of Z-Par Investment Fund II, LLC. Parrish associated with Wellstone Securities LLC, which is a broker-dealer and an investment advisor registered with the NASD, in connection with the marketing and sales of investments in a prime bank security trading program through Z-Par Investment Fund II, LLC. Parrish, 42 years old, is a resident of Frederick, Maryland.

2. On April 26, 2007, a final judgment was entered by consent against Parrish, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, in the civil action entitled United States Securities & Exchange Commission v. Z-Par Holdings, Inc., et al., Civil Action Number 05cv1031, in the United States District Court for the District of Maryland, Baltimore Division.

3. The Commission's complaint alleged that from at least April 2004 to April 2005, Parrish marketed a fraudulent prime bank investment scheme in which he raised approximately $8.2 million from eleven investors in Florida and others elsewhere throughout the United States. The complaint also alleged that Parrish fraudulently represented to investors that their funds would be pooled with those of other investors in $1 million lots for the purchase of "debt obligations of the top 50 banks in the world," which would be safe and secure investments yielding high rates of return. The complaint further alleged that Parrish fraudulently sold interests in fictitious prime bank debt instruments and payment obligations, claiming that they carried a financial insurance guarantee that wraps the debt obligations to further enhance their value and lower their risks from any default. The complaint further alleged that in furtherance of the fraudulent scheme, Parrish sent investor funds to third-parties who, unbeknownst to Parrish, used the funds to purchase precious metals on margin.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act, that Respondent Parrish be, and hereby is barred from association with any broker or dealer with the right to reapply for association after five years to the appropriate self-regulatory organization, or if there is none, to the Commission;

Any reapplication for association by the Respondent 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 the Respondent, 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.

By the Commission.

Nancy M. Morris
Secretary

By: J. Lynn Taylor
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Securities Act of 1933
Release No. 8805 / May 23, 2007

Securities Exchange Act of 1934
Release No. 55805 / May 23, 2007

Administrative Proceeding
File Number 3-11893

In the Matter of David A. Finnerty, Donald R. Foley II, Scott G. Hunt, Thomas J. Murphy, Jr., Kevin M. Fee, Frank A. Delaney IV, Freddy DeBoer, Todd J. Christie, James V. Parolisi, Robert W. Luckow, Patrick E. Murphy, Robert A. Johnson, Jr., Patrick J. McGagh, Jr., Joseph Bongiorno, Michael J. Hayward, Richard P. Volpe, Michael F. Stern, Warren E. Turk, Gerard T. Hayes, and Robert A. Scavone, Jr. Respondents.	ORDER MAKING FINDINGS, IMPOSING REMEDIAL SANCTIONS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTIONS 15(b)(6), 21C AND 11(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 11b-1 THEREUNDER AS TO PATRICK J. MCGAGH, JR.

Document 27 of 33

I.

On April 12, 2005, the Securities and Exchange Commission ("Commission") entered an Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b)(6), 21C and 11(b) of the Securities Exchange Act of 1934 and Rule 11b-1 Thereunder ("OIP") against respondent Patrick J. McGagh, Jr. ("McGagh").

II.

McGagh has submitted an Offer of Settlement ("Offer") in these administrative proceedings, 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 him and the subject matter of these proceedings, which are admitted, McGagh consents to the entry of this Order Making Findings, Imposing Remedial Sanctions, and Imposing a Cease-and-Desist Order Pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b)(6), 21C and 11(b) of the Securities Exchange Act of 1934, and Rule 11b-1 Thereunder as to Patrick J. McGagh, Jr. ("Order"), as set forth below.

III.

On the basis of this Order and McGagh's Offer, the Commission finds[1] that:

FACTS

1. McGagh is one of twenty respondents in pending administrative and cease-and-desist proceedings, file number 3-11893, who have been charged with fraudulent and other improper trading during the period from at least 1999 through June 30, 2003, while they were acting as specialists on the New York Stock Exchange ("NYSE").

2. McGagh, age 41, acted as a specialist on the NYSE at Van der Moolen Specialists USA, LLC ("Van der Moolen") from at least January 1, 1999 to approximately March 2004 (the "Relevant Period").

3. During the Relevant Period, McGagh was the specialist in the following securities: Nortel Networks Corp. ("NT") (from January 1999 to January 2001) and Pfizer, Inc. ("PFE") (from May 2001 to approximately April 2003, with absences from the panel where that security was traded in February 2002 and March 2002).

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

4. As a specialist, McGagh had an obligation to serve public customer orders over the proprietary interests of the firm with whom he was formerly employed, Van der Moolen. In his role as a specialist, McGagh had a general duty to match executable public customer or "agency" buy and sell orders and not to fill customer orders through trades from Van der Moolen's own account when those customer orders could be matched with other customer orders. McGagh violated this obligation by filling orders through proprietary trades rather than through other customer orders, through two types of improper trading referred to herein as "interpositioning" and "trading ahead."

5. Interpositioning involves a two-step process that allows the specialist to generate a profit for the specialist firm from the spread between two opposite trades. Interpositioning can take various forms. In one form, the specialist purchases stock for the specialist firm's proprietary account from the customer sell order, and then fills the customer buy order by selling from the specialist firm's proprietary account at a higher price – thus locking in a riskless profit for the specialist firm's proprietary account. A second form of interpositioning involves the specialist selling stock into the customer buy order, and then filling the customer sell order by buying for the specialist firm's proprietary account at a lower price – again, locking in a riskless profit for the specialist firm's proprietary account. In both forms of interpositioning, the specialist participates on both sides of the trade, thereby capturing the spread between the purchase and sale prices, disadvantaging at least one of the parties to the transaction.

6. Trading ahead involves a practice whereby the specialist fills an agency order through a proprietary trade for the specialist firm's proprietary account – and thereby improperly 'steps in front' of, or 'trades ahead' of, another agency order – simply to allow the specialist firm to take advantage of market conditions promptly. Unlike interpositioning, the practice of "trading ahead" does not necessarily involve a second specialist trade for the specialist firm's proprietary account into the opposite, disadvantaged agency order. For example, in a declining market, a specialist may "trade ahead" by filling a market buy order by selling stock from the specialist firm's proprietary account in front of an agency market sell order. In so doing, the specialist would lock in a higher price for the proprietary trade, then fill the agency sell order *after* the proprietary trade, and thereby force the agency market sell order to accept a slightly lower price as the price of the stock fell.

7. During the Relevant Period, in NT and PFE, McGagh knowingly or recklessly engaged in approximately 20,043 instances of interpositioning, locking in a riskless profit of approximately $3,271,406 for his firm's proprietary account at the expense of customer orders, and approximately 4,014 instances of trading ahead, causing approximately $1,178,892 in customer harm.

8. On May 12, 2006, McGagh pled guilty to one count of securities fraud, in U.S. v. Joseph Bongiorno, et al., 05 Crim. 390 (S.D.N.Y.), stemming from the same conduct as that charged in the OIP as it relates to PFE. On October 13, 2006, McGagh was sentenced to 27 months imprisonment and assessed a $250,000 fine. McGagh paid the fine in full on November 1, 2006. McGagh is currently incarcerated in the satellite prison camp at the Federal Correctional Institution – McKean in Bradford, Pennsylvania.

APPLICABLE LAW

Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act of 1934 and Rule 10b-5 Thereunder

9. The antifraud provisions of Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit, among other things, any schemes to defraud or fraudulent or deceptive acts and practices in the offer or sale (Section 17(a)) or in connection with the purchase or sale (Section 10(b) and Rule 10b-5) of securities. Basic, Inc. v. Levinson, 485 US 224, 235 n.13 (1988) (citing SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 862 (2d Cir. 1968) (en banc)). To prove a violation of Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, the Commission must prove that the respondent acted with scienter. Aaron v. SEC, 446 U.S. 680, 691 (1980). Scienter may be established by proof of conscious behavior or recklessness on the part of the respondent. In re Scholastic Corp. Sec. Litig., 252 F.3d 63, 74 (2d Cir. 2001); SEC v. U.S. Environmental, Inc., 155 F.3d 107, 111 (2d Cir. 1998), cert. denied, 526 U.S. 1111 (1999). Scienter need not be shown in order to establish violations of Sections 17(a)(2) and (3) of the Securities Act. Aaron v. SEC, 446 U.S. 680, 696-97 (1980).

10. As a result of the described conduct above, McGagh willfully violated Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Section 11(b) of the Exchange Act and Rule 11b-1 Thereunder

11. Section 11(b) of the Exchange Act and Rule 11b-1 thereunder impose various limitations on the operations of specialists, including limiting a specialist's dealer transactions to those "reasonably necessary to permit him to maintain a fair and orderly market."

12. Where specialists make trades for their firm's proprietary accounts that are not "reasonably necessary to permit [such specialists] to maintain a fair and orderly market," and "were not effected in a manner consistent with the rules adopted by [the pertinent national securities exchange]," they have violated Section 11(b) and

Rule 11b-1 of the Exchange Act. See In the Matter of Albert Fried & Co. and Albert Fried, Jr., 1978 WL 196046, S.E.C. Release No. 34-15293 (Nov. 3, 1978).

13. Several NYSE rules prohibit a specialist from trading ahead of a customer order, as well as from engaging in interpositioning, and require agency orders to be matched whenever possible, consistent with a specialist's duty to maintain a fair and orderly market.

14. NYSE Rule 104 (Dealings by Specialists), which sets forth specialists' obligations, prohibits specialists from trading for their own accounts unless it is reasonably necessary to maintain a fair and orderly market. This is known as the negative obligation. Rule 104 states in relevant part: "No specialist shall effect . . . purchases or sales of any security in which such specialist is registered . . ., unless such dealings are reasonably necessary to permit such specialist to maintain a fair and orderly market."[2]

15. NYSE Rule 92 (Limitations on Members' Trading Because of Customers Orders) generally prohibits a member from entering a proprietary order to buy (or sell) a security while in possession of an executable buy (or sell) agency order that could be executed at the same price. During the Relevant Period, Rule 92 stated in relevant part:

> No member shall personally buy . . . any security . . . for his own account or for any account in which he is . . . interested . . . while such member personally holds or has knowledge that his member organization holds an unexecuted market order to buy such security . . . for a customer.[3]

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2 Rule 104.10(3), which describes specialists' affirmative obligations, also expands on the negative obligation:

> Transactions on the Exchange for his own Account effected by a member acting as a specialist must constitute a course of dealings reasonably calculated to contribute to the maintenance of price continuity with reasonable depth, and to minimizing of the effects of temporary disparity between supply and demand, immediate or reasonably to be anticipated. Transactions not part of such a course of dealings ... are not to be effected.

3 Rule 92 was amended on January 7, 2002 to read in relevant part:

> [n]o member or member organization shall cause the entry of an order to buy (sell) any Exchange-listed security for any account in which such member or member organization or any approved person thereof is directly or indirectly interested ("a proprietary

16. Similarly, NYSE Rule 92 also applies to the specialist buying or selling a security while holding an unexecuted market buy or sell order, as well as to circumstances where the specialist holds unexecuted customer limit orders at a price that could be satisfied by the proprietary transaction effected by the specialist.

17. NYSE Rule 123B (Exchange Automated Order Routing Systems) requires specialists to cross orders received over the DOT system. Rule 123B(d) states in relevant part: "a specialist shall execute System orders in accordance with the Exchange auction market rules and procedures, including requirements to expose orders to buying and selling interest in the trading crowd and *to cross orders before buying or selling from his own account.*" (Emphasis added).

18. NYSE Rule 401 requires NYSE members to "adhere to the principles of good business practice in the conduct of his or its business affairs." Similarly, NYSE Rule 476(a)(6) provides sanctions if NYSE members are adjudged guilty of "conduct or proceeding inconsistent with just and equitable principles of trade."

19. As a result of the conduct described above, McGagh willfully violated all of the aforementioned NYSE rules as well as Section 11(b) of the Exchange Act and Rule 11b-1 thereunder.

IV.

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

Accordingly, it is hereby ORDERED that:

1. Pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, McGagh shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act, and Sections 10(b) and 11(b) of the Exchange Act and Rules 10b-5 and 11b-1 thereunder.

2. Pursuant to Section 15(b)(6) of the Exchange Act, McGagh be, and hereby is, barred from association with any broker or dealer.

   Any reapplication for association by McGagh 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

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order"), if the person responsible for the entry of such order has knowledge of any particular unexecuted customer's order to buy (sell) such security which could be executed at the same price.

satisfaction of any or all of the following: (a) any disgorgement ordered against McGagh, 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.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

Securities Act of 1933
Release No. 8806 / May 23, 2007

Securities Exchange Act of 1934
Release No. 55802 / May 23, 2007

Administrative Proceeding
File Number 3-11893

In the Matter of David A. Finnerty, Donald R. Foley II, Scott G. Hunt, Thomas J. Murphy, Jr., Kevin M. Fee, Frank A. Delaney IV, Freddy DeBoer, Todd J. Christie, James V. Parolisi, Robert W. Luckow, Patrick E. Murphy, Robert A. Johnson, Jr., Patrick J. McGagh, Jr., Joseph Bongiorno, Michael J. Hayward, Richard P. Volpe, Michael F. Stern, Warren E. Turk, Gerard T. Hayes, and Robert A. Scavone, Jr. Respondents.	ORDER MAKING FINDINGS, IMPOSING REMEDIAL SANCTIONS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTIONS 15(b)(6), 21C AND 11(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 11b-1 THEREUNDER AS TO JOSEPH BONGIORNO

Document 28 of 33

I.

On April 12, 2005, the Securities and Exchange Commission ("Commission") entered an Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b)(6), 21C and 11(b) of the Securities Exchange Act of 1934 and Rule 11b-1 Thereunder ("OIP") against respondent Joseph Bongiorno ("Bongiorno").

II.

Bongiorno has submitted an Offer of Settlement ("Offer") in these administrative proceedings, 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 him and the subject matter of these proceedings, which are admitted, Bongiorno consents to the entry of this Order Making Findings, Imposing Remedial Sanctions, and Imposing a Cease-and-Desist Order Pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b)(6), 21C and 11(b) of the Securities Exchange Act of 1934 and Rule 11b-1 Thereunder as to Joseph Bongiorno ("Order"), as set forth below.

III.

On the basis of this Order and Bongiorno's Offer, the Commission finds[1] that:

FACTS

1. Bongiorno is one of twenty respondents in pending administrative and cease-and-desist proceedings, file number 3-11893, who have been charged with fraudulent and other improper trading during the period from at least 1999 through June 30, 2003, while they were acting as specialists on the New York Stock Exchange ("NYSE").

2. Bongiorno, age 52, acted as a specialist on the NYSE at Van der Moolen Specialists USA, LLC ("Van der Moolen") from at least January 1, 1999 to approximately March 2004 (the "Relevant Period").

3. From January 1999 to June 2003, Bongiorno was the specialist in Hewlett-Packard Co. ("HPQ").

4. As a specialist, Bongiorno had an obligation to serve public customer orders over the proprietary interests of the firm with whom he was formerly employed, Van der Moolen. In his role as a specialist, Bongiorno had a general duty to match executable public customer or "agency" buy and sell orders and not to fill

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

customer orders through trades from Van der Moolen's own account when those customer orders could be matched with other customer orders. Bongiorno violated this obligation by filling orders through proprietary trades rather than through other customer orders, through two types of improper trading referred to herein as "interpositioning" and "trading ahead."

5. Interpositioning involves a two-step process that allows the specialist to generate a profit for the specialist firm from the spread between two opposite trades. Interpositioning can take various forms. In one form, the specialist purchases stock for the specialist firm's proprietary account from the customer sell order, and then fills the customer buy order by selling from the specialist firm's proprietary account at a higher price – thus locking in a riskless profit for the specialist firm's proprietary account. A second form of interpositioning involves the specialist selling stock into the customer buy order, and then filling the customer sell order by buying for the specialist firm's proprietary account at a lower price – again, locking in a riskless profit for the specialist firm's proprietary account. In both forms of interpositioning, the specialist participates on both sides of the trade, thereby capturing the spread between the purchase and sale prices, disadvantaging at least one of the parties to the transaction.

6. Trading ahead involves a practice whereby the specialist fills an agency order through a proprietary trade for the specialist firm's proprietary account – and thereby improperly 'steps in front' of, or 'trades ahead' of, another agency order – simply to allow the specialist firm to take advantage of market conditions promptly. Unlike interpositioning, the practice of "trading ahead" does not necessarily involve a second specialist trade for the specialist firm's proprietary account into the opposite, disadvantaged agency order. For example, in a declining market, a specialist may "trade ahead" by filling a market buy order by selling stock from the specialist firm's proprietary account in front of an agency market sell order. In so doing, the specialist would lock in a higher price for the proprietary trade, then fill the agency sell order *after* the proprietary trade, and thereby force the agency market sell order to accept a slightly lower price as the price of the stock fell.

7. During the Relevant Period, in HPQ, Bongiorno knowingly or recklessly engaged in approximately 14,688 instances of interpositioning, locking in a riskless profit of approximately $1,321,869 for his firm's proprietary account at the expense of customer orders, and approximately 7,550 instances of trading ahead, causing approximately $1,199,452 in customer harm.

8. On May 12, 2006, Bongiorno pled guilty to one count of securities fraud, in U.S. v. Joseph Bongiorno, et al., 05 Crim. 390 (S.D.N.Y.), stemming from the same conduct as that charged in the OIP. On October 13, 2006, Bongiorno was sentenced to 27 months imprisonment and assessed a $250,000 fine. Bongiorno paid the fine in full on November 6, 2006. Bongiorno is currently incarcerated in the satellite

prison camp at the United States Penitentiary – Lewisburg in Lewisburg, Pennsylvania.

APPLICABLE LAW

Section 17(a) of the Securities Act and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 Thereunder

9. The antifraud provisions of Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit, among other things, any schemes to defraud or fraudulent or deceptive acts and practices in the offer or sale (Section 17(a)) or in connection with the purchase or sale (Section 10(b) and Rule 10b-5) of securities. Basic, Inc. v. Levinson, 485 US 224, 235 n.13 (1988) (citing SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 862 (2d Cir. 1968) (en banc)). To prove a violation of Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, the Commission must prove that the respondent acted with scienter. Aaron v. SEC, 446 U.S. 680, 691 (1980). Scienter may be established by proof of conscious behavior or recklessness on the part of the respondent. In re Scholastic Corp. Sec. Litig., 252 F.3d 63, 74 (2d Cir. 2001); SEC v. U.S. Environmental, Inc., 155 F.3d 107, 111 (2d Cir. 1998), cert. denied, 526 U.S. 1111 (1999). Scienter need not be shown in order to establish violations of Sections 17(a)(2) and (3) of the Securities Act. Aaron v. SEC, 446 U.S. 680, 696-97 (1980).

10. As a result of the described conduct above, Bongiorno willfully violated Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Section 11(b) of the Exchange Act and Rule 11b-1 Thereunder

11. Section 11(b) of the Exchange Act and Rule 11b-1 thereunder impose various limitations on the operations of specialists, including limiting a specialist's dealer transactions to those "reasonably necessary to permit him to maintain a fair and orderly market."

12. Where specialists make trades for their firm's proprietary accounts that are not "reasonably necessary to permit [such specialists] to maintain a fair and orderly market," and "were not effected in a manner consistent with the rules adopted by [the pertinent national securities exchange]," they have violated Section 11(b) and Rule 11b-1 of the Exchange Act. See In the Matter of Albert Fried & Co. and Albert Fried, Jr., 1978 WL 196046, S.E.C. Release No. 34-15293 (Nov. 3, 1978).

13. Several NYSE rules prohibit a specialist from trading ahead of a customer order, as well as from engaging in interpositioning, and require agency orders to be

matched whenever possible, consistent with a specialist's duty to maintain a fair and orderly market.

14. NYSE Rule 104 (Dealings by Specialists), which sets forth specialists' obligations, prohibits specialists from trading for their own accounts unless it is reasonably necessary to maintain a fair and orderly market. This is known as the negative obligation. Rule 104 states in relevant part: "No specialist shall effect . . . purchases or sales of any security in which such specialist is registered . . ., unless such dealings are reasonably necessary to permit such specialist to maintain a fair and orderly market."[2]

15. NYSE Rule 92 (Limitations on Members' Trading Because of Customers Orders) generally prohibits a member from entering a proprietary order to buy (or sell) a security while in possession of an executable buy (or sell) agency order that could be executed at the same price. During the Relevant Period, Rule 92 stated in relevant part:

> No member shall personally buy . . . any security . . . for his own account or for any account in which he is . . . interested . . . while such member personally holds or has knowledge that his member organization holds an unexecuted market order to buy such security . . . for a customer.[3]

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2 Rule 104.10(3), which describes specialists' affirmative obligations, also expands on the negative obligation:

> Transactions on the Exchange for his own Account effected by a member acting as a specialist must constitute a course of dealings reasonably calculated to contribute to the maintenance of price continuity with reasonable depth, and to minimizing of the effects of temporary disparity between supply and demand, immediate or reasonably to be anticipated. Transactions not part of such a course of dealings ... are not to be effected.

3 Rule 92 was amended on January 7, 2002 to read in relevant part:

> [n]o member or member organization shall cause the entry of an order to buy (sell) any Exchange-listed security for any account in which such member or member organization or any approved person thereof is directly or indirectly interested ("a proprietary order"), if the person responsible for the entry of such order has knowledge of any particular unexecuted customer's order to buy (sell) such security which could be executed at the same price.

16. Similarly, NYSE Rule 92 also applies to the specialist buying or selling a security while holding an unexecuted market buy or sell order, as well as to circumstances where the specialist holds unexecuted customer limit orders at a price that could be satisfied by the proprietary transaction effected by the specialist.

17. NYSE Rule 123B (Exchange Automated Order Routing Systems) requires specialists to cross orders received over the DOT system. Rule 123B(d) states in relevant part: "a specialist shall execute System orders in accordance with the Exchange auction market rules and procedures, including requirements to expose orders to buying and selling interest in the trading crowd and *to cross orders before buying or selling from his own account.*" (Emphasis added).

18. NYSE Rule 401 requires NYSE members to "adhere to the principles of good business practice in the conduct of his or its business affairs." Similarly, NYSE Rule 476(a)(6) provides sanctions if NYSE members are adjudged guilty of "conduct or proceeding inconsistent with just and equitable principles of trade."

19. As a result of the conduct described above, Bongiorno willfully violated all of the aforementioned NYSE rules as well as Section 11(b) of the Exchange Act and Rule 11b-1 thereunder.

IV.

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

Accordingly, it is hereby ORDERED that:

1. Pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Bongiorno shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act, and Sections 10(b) and 11(b) of the Exchange Act and Rules 10b-5 and 11b-1 thereunder.

2. Pursuant to Section 15(b)(6) of the Exchange Act, Bongiorno be, and hereby is, barred from association with any broker or dealer.

Any reapplication for association by Bongiorno 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 Bongiorno, 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.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Nazareth
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55801 / May 23, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12643

In the Matter of **HEWLETT-PACKARD COMPANY,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against Hewlett-Packard Company ("HP," "Hewlett-Packard," 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 Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

III.

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

Document 29 of 33

A. Summary

1. This matter involves Hewlett-Packard's failure to disclose the circumstances surrounding a board member's resignation amidst the company's controversial investigation into boardroom leaks. On May 18, 2006, HP's Board of Directors learned the findings of the company's leak investigation and voted to request the resignation of a director believed to have violated HP's policies by providing confidential information to the press. Silicon Valley venture capitalist and fellow director Thomas Perkins (not the source of the leak) voiced his strong objections to the handling of the matter, announced his resignation, and walked out of the Board meeting. Contrary to the reporting requirements of the federal securities laws, HP failed to disclose to investors the circumstances of Mr. Perkins' disagreement with the company.

B. Respondent

2. Hewlett-Packard is a Delaware corporation headquartered in Palo Alto, California. HP sells computers, computer equipment, and support services. HP's common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is listed on the New York Stock Exchange under the stock symbol "HPQ."

C. Facts

Legal Background

3. Under the Exchange Act, a public company must file with the Commission a report on Form 8-K when a director resigns from the board. If a director has resigned because of a disagreement with the company, known to an executive officer, on any matter relating to the company's operations, policies, or practices, the company must, among other things, disclose a brief description of the circumstances of the disagreement. In addition, the company must give the director the opportunity to timely review and respond to the company's disclosure about the director's resignation, and the company is required to file any letter written by the director to the company in response to the company's disclosure. Absent such a disagreement, the company must report the resignation, but need not provide the reasons.

HP's Leak Investigation

4. In or around January 2006, in response to apparent unauthorized disclosures of confidential information about HP Board meetings to the press, HP initiated an investigation to determine the source of the leaks. HP Board member Thomas Perkins, Chairman of the Board's Nominating and Governance Committee (which was responsible for, among other things, establishing board member qualifications and evaluating board operations), was generally informed of the inquiry. Mr. Perkins believed that he and HP's Chairman had agreed that, upon completion of the investigation, they would approach any individual implicated privately, obtain an assurance that it would not happen again, and inform the full Board that the matter had been resolved without identifying the source of the leak.

5. By April 2006, HP investigators tentatively concluded that a long-standing HP director had leaked information in connection with a January 23, 2006 press article. After consulting with HP's Chief Executive Officer, General Counsel, outside counsel, and Chairman of the Audit Committee, the Chairman of the Board determined that the leak investigation findings should be presented to the full Board.

Mr. Perkins Resigns During the May 18, 2006 Board Meeting

6. HP's Board of Directors met beginning at 12:30 p.m. on May 18, 2006 at HP's headquarters in Palo Alto, California. All but one of the directors attended, including the CEO (who is a director), as did the company's General Counsel (acting as the Board secretary).

7. At the start of the meeting, the head of HP's Audit Committee discussed the leak investigation and its findings. After some discussion, the identity of the director who provided information for the January 2006 article was revealed. The director addressed the Board, explained his actions, and left the room to permit additional deliberations. The Board discussed HP's policy on unauthorized public disclosures, and considered measures that could be taken in response to the director's actions, including asking him to resign.

8. During the course of the Board's deliberations, which lasted approximately 90 minutes, Mr. Perkins voiced his strong objections to the manner in which the matter was being handled. Among other things, he repeatedly told the Board that the source of the leak should have been approached "off-line" for an explanation and a warning, rather than identified to the whole Board. He affirmed his belief that the matter should have been handled confidentially by the Chairman of the Board and himself as Chairman of the Nominating and Governance Committee. He also questioned the wisdom of requesting the director to resign over what he perceived to be a relatively minor offense, noting that the director had made significant contributions to HP.

9. After a lengthy and heated discussion, the Board, by a secret written ballot, passed a motion to ask the director to resign from the Board. When HP's General Counsel announced the results of the vote on whether to ask the director to resign, Mr. Perkins continued to voice disagreement. As noted in the Board minutes, Mr. Perkins "restated his strong objections to the process, specifically [the Chairman's] decision to bring the matter to the full Board and the manner in which the meeting was conducted." Mr. Perkins then resigned from the Board and departed the meeting at approximately 2:00 p.m. The director identified by the leak investigation was asked to resign following the vote, but declined to resign at that time.

HP Fails to Disclose the Reasons for Mr. Perkins' Resignation

10. HP executives understood that, in the event a director resigned over a disagreement with the company on a matter relating to its operations, policies, or practices, the company would need to report to the Commission (and thereby disclose to investors) the circumstances of the disagreement.

11. On May 22, 2006, HP filed a report on Form 8-K, pursuant to Item 5.02(b), reporting Mr. Perkins' resignation, but did not comply with Item 5.02(a) by failing to disclose that there had been a disagreement with the company. HP also filed with the Form 8-K a May 19 press release, which announced that Mr. Perkins had resigned without disclosing the circumstances of his disagreement.

12. HP concluded, with the advice of outside legal counsel and the General Counsel, that it need not disclose the reasons for Mr. Perkins' resignation because he merely had a disagreement with the company's Chairman, and not a disagreement with the company on a matter relating to its operations, policies, or practices. Contrary to HP's conclusion, the disagreement and the reasons for Mr. Perkins' resignation should have been disclosed, pursuant to Item 5.02(a), in the May 22 Form 8-K. Mr. Perkins resigned as a result of a disagreement with HP on the following matters: (1) the decision to present the leak investigation findings to the full Board; and (2) the decision by majority vote of the Board of Directors to ask the director identified in the leak investigation to resign. Mr. Perkins' disagreement related to important corporate governance matters and HP policies regarding handling sensitive information, and thus constituted a disagreement over HP's operations, policies or practices.

13. HP did not disclose further information relating to Mr. Perkins' resignation until September 6, 2006, after Mr. Perkins (and the staff of the Securities and Exchange Commission) had begun to raise questions about the adequacy of the company's disclosures.

D. Violations

14. Section 13(a) of the Exchange Act and Rule 13a-11 promulgated thereunder require issuers of securities registered pursuant to Section 12 of the Exchange Act to file with the Commission current reports on Form 8-K upon the occurrence of certain events, including the departure of directors or principal officers. Item 5.02(a) of Form 8-K specifies that if a director has resigned because of a disagreement with the registrant, known to an executive officer of the registrant, on any matter relating to the registrant's operations, policies, or practices, the registrant must, among other things, disclose a brief description of the circumstances representing the disagreement that the registrant believes caused, in whole or in part, the director's resignation. In addition, the registrant must provide the resigning director with a copy of the disclosure no later than the day the company files the disclosure with the Commission. Also, the registrant must provide the director with the opportunity to furnish a response letter stating whether the director agrees with the disclosure in the registrant's Form 8-K. In the event that the registrant receives a response letter from the former director, the letter must be filed by the registrant as an amendment to its Form 8-K within two business days of its receipt. No showing of scienter is required to establish a violation of Section 13(a) of the Exchange Act. SEC v. Savoy, 587 F.2d 1149, 1167 (D.C. Cir. 1978).

15. On May 18, 2006, director Thomas Perkins resigned because of a disagreement with HP regarding the decision to present the leak investigation findings to the full Board and the decision by the Board to ask the director identified in the leak investigation to resign. The disagreement was known to HP executive officers. Mr. Perkins' disagreement with HP related to

the operations, policies, or practices of HP. Consequently, HP was required by Item 5.02(a) of Form 8-K to disclose a brief description of the circumstances representing the disagreement, and was required to provide Mr. Perkins with a copy of this disclosure no later than the day of filing. By disclosing the resignation of Mr. Perkins pursuant to Item 5.02(b) in a Form 8-K filed on May 22, 2006, HP failed to disclose the circumstances of Mr. Perkins' disagreement with HP and also failed to provide the director with a copy of such a filing. As a result, HP violated Section 13(a) of the Exchange Act and Rule 13a-11 thereunder.

IV.

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

Accordingly, it is hereby ORDERED that Respondent HP cease and desist from committing or causing any violations and any future violations of Section 13(a) of the Exchange Act and Rule 13a-11 thereunder.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

7

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 2606 / May 23, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12641

In the Matter of **ALLOCATION PLUS ASSET MANAGEMENT COMPANY, INC.,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(e) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(e) of the Investment Advisers Act of 1940 ("Advisers Act") against Allocation Plus Asset Management Company, Inc. ("APAM" 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, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(e) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

Document 30 of 33

III.

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

1. APAM is an investment adviser registered with the Commission from March 1994 to the present. Bradford C. Bleidt ("Bleidt") was the sole shareholder, officer and director of APAM.

2. On May 8, 2007, a final judgment was entered by consent against APAM and Bleidt, permanently enjoining both from future violations of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and Sections 206(1) and 206(2) of the Advisers Act, in the civil action entitled Securities and Exchange Commission v. Bradford C. Bleidt, et al., Civil Action Number 104-12415-NG, in the District of Massachusetts.

3. The Commission's complaint alleged that Bleidt, through APAM, diverted investor funds into his personal bank account, falsely stated to investors that their funds were invested, and otherwise engaged in a variety of conduct which operated as a fraud and deceit on investors.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(e) of the Advisers Act, that the registration of Respondent APAM be, and hereby is revoked.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55800 / May 23, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12642

In the Matter of **JAMES PROFFITT,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTION**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against James Proffitt ("Respondent" or "Proffitt").

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 him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanction ("Order"), as set forth below.

III.

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

1. Proffitt, 69 years old, is a resident of Tomkinsville, Kentucky. Between January 1999 and March 2001, Proffitt solicited investors for Growth Benefit Systems. During that time period, Proffitt acted as an unregistered broker or dealer when he offered and sold securities for

Document 31 of 33

Growth Benefit Systems, and was associated with unregistered brokers or dealers. Proffitt has never been associated with a registered broker or dealer.

2. On May 9, 2007, a final judgment was entered by consent against Proffitt, permanently enjoining him from future violations of Sections 5(a), 5(c) and 17(a) of the Securities Act of 1933 and Sections 10(b) and 15(a) of the Exchange Act and Rule 10b-5 thereunder, in a civil action entitled Securities and Exchange Commission v. Jack Calvin, et al., Civil Action No. 03-CV-10586-MEL (D. Mass.), in the United States District Court for the District of Massachusetts.

3. The Commission's complaint alleged, among other things, that Proffitt fraudulently offered and sold unregistered securities--while not being registered as a broker or dealer or associated with a registered broker or dealer--in Growth Benefit Systems, a purported "Prime Bank" trading program that was completely fictitious. The complaint also alleged that the Growth Benefit Systems securities were sold through Proffitt and salespeople that he recruited. The salespeople recruited by Proffitt were not registered as brokers or dealers. Proffitt received commission payments and shared commissions with the salespeople that he recruited. Based on his conduct, Proffitt was associated with salespeople who were operating as brokers or dealers.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act, that Respondent Proffitt be, and hereby is, barred from association with any broker or dealer.

Any reapplication for association by the Respondent 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 the Respondent, 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.

By the Commission.

Nancy M. Morris
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

Commissioners Atkins and Campos Not participating

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55828 / May 30, 2007

Admin. Proc. File No. 3-12498

In the Matter of the Application of

SKY CAPITAL LLC

For Review of Action Taken by

NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION - REVIEW OF ASSOCIATION ACTION

Jurisdiction to Review Association Action

NASD member firm applied for Commission review of certain actions by NASD staff directed at firm. Held, the matter is not reviewable under Section 19(d) of the Securities Exchange Act of 1934. Application for review is therefore dismissed.

APPEARANCES:

Steven Altman, of Altman & Company P.C., for Sky Capital LLC.

Marc Menchel, Alan Lawhead, and Terry L. Reicher, for NASD.

Appeal filed: November 28, 2006
Last brief received: December 27, 2006

I.

Sky Capital LLC ("Sky Capital"), an NASD member firm, seeks Commission review of what it characterizes as NASD staff's "campaign of harassment" against the firm and of NASD's purported failure to provide an internal procedure for member complaints of staff misconduct. NASD has moved to dismiss the application. The parties do not differ substantially in their description of the facts. For purposes of our review, we accept the facts as described in NASD's

Document 32 of 33

decisions and the parties' briefs. 1/ For the reasons set forth below, we conclude that we lack jurisdiction to consider Sky Capital's application under Section 19(d) of the Securities Exchange Act of 1934. 2/

II.

Sky Capital is a broker-dealer firm principally located in New York City. 3/ Sky Capital applied for NASD membership in June 2001. On February 13, 2002, NASD's Department of Member Regulation for District No. 10 ("Member Regulation") denied the membership application. Sky Capital appealed the membership application denial to NASD's National Adjudicatory Council ("NAC"). During the pendency of that appeal, Member Regulation and Sky Capital agreed to a membership agreement that included restrictions on certain activities of Ross H. Mandell, Sky Capital's chief executive officer. Member Regulation withdrew its denial decision and approved the firm's membership application, subject to the agreed-to restrictions imposed on Mandell. Sky Capital became an NASD member in May 2002. Sky Capital alleges that NASD staff employed "delay tactics" in reviewing its membership application, and that NASD staff was biased against Mandell due to his regulatory history and past substance abuse problems. Sky Capital acknowledges, however, that following the firm's appeal to the NAC, Member Regulation "reverse[d] course" and approved its membership application.

Subsequently, the firm sought to expand its business. Sky Capital's NASD membership agreement limited the firm's market making activities to forty over-the-counter securities. It also limited the number of associated persons that Sky Capital could employ to seventy-five. In November 2002, Sky Capital applied to expand its market making activities to 600 securities and

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1/ See Joseph Dillon & Co., 54 S.E.C. 960, 962 (2000) (dismissing appeal of NASD decision denying firm exemption from NASD Conduct Rule 3010(b)(2) for lack of jurisdiction under Exchange Act Section 19(d)).

2/ See 15 U.S.C. § 78s(d). Sky Capital has requested oral argument. The Commission's Rule of Practice 154(a) states that "[n]o oral argument shall be heard on any motion unless the Commission or the hearing officer otherwise directs." 17 C.F.R. § 201.154(a). We have determined that the presentation in the briefs and the decisional process would not be significantly aided by oral argument. See 17 C.F.R. § 201.451(a) (stating that "[t]he Commission will consider appeals, motions and other matters properly before it on the basis of the papers filed by the parties without oral argument unless the Commission determines that the presentation of facts and legal arguments in the briefs and record and the decisional process would be significantly aided by oral argument"). Accordingly, Sky Capital's request for oral argument is denied.

3/ Sky Capital is wholly owned by Sky Capital Holdings Ltd., a Delaware corporation whose common stock is listed on the Alternative Investments Market of the London Stock Exchange.

to relocate the majority of its trading operations from New York to Red Bank, New Jersey. In December 2002, Sky Capital applied to increase the number of associated persons it could employ to 200. Member Regulation initially denied both applications, and Sky Capital appealed. The NAC vacated the denials and remanded for reconsideration. Member Regulation ultimately allowed Sky Capital to expand as requested.

Sky Capital further asserts that, in 2002, NASD staff "obstructed" its plans to acquire assets from The Thornwater Company, L.P., another member firm, by imposing restrictions on Thornwater. Sky Capital admits, however, that NASD subsequently lifted those restrictions. In 2003, Sky Capital sought to acquire a Florida broker-dealer. Sky Capital concedes that NASD staff approved the transaction, but asserts that it did so only after substantial delay.

Sky Capital complains that, between 2002 and 2005, NASD staff initiated eight separate examinations of the firm and its employees. NASD states that the first examination, which concerned deficiencies in Mandell's Form U-4, resulted in the issuance of a "letter of caution" and Minor Rule Violation Letter against Mandell. 4/ Mandell agreed to waive his right to appeal to the Commission in connection with the matter. The second examination, a routine examination of Sky Capital's first six months of operation, closed without any action taken by NASD. The third examination, also routine, related to Sky Capital's operations in 2003. It resulted in the firm's execution of a Letter of Acceptance, Waiver and Consent and payment of two fines. 5/ Sky Capital agreed to waive its right to appeal to the Commission in connection with the matter.

According to NASD, the fourth, fifth, and sixth examinations were instituted for cause. The fourth examination related to a customer complaint against a Sky Capital broker for alleged misconduct at the broker's previous place of employment. The fifth examination related to Mandell's adherence to certain restrictions placed upon him by the firm's membership agreement. The sixth examination related to political contributions made by Sky Capital employees. All three examinations closed without any action taken by NASD.

4/ Mandell paid a $2,500 fine for failing to amend his Form U-4 to disclose the fact that he had been named as a defendant in an investment-related civil litigation, in contravention of Article V, Section 2 of NASD's By-Laws.

5/ Sky Capital paid a $12,000 fine for acting as a placement agent in three best-efforts private placement offerings involving minimum-maximum contingencies without being a party to escrow agreements regarding the funds raised, in violation of Exchange Act Rule 15c2-4. Sky Capital paid a $3,000 fine for permitting an employee, who was inactive due to the failure to complete the Regulatory Element of NASD's Continuing Education Requirement, to act in a capacity that required NASD registration, in violation of NASD Rule 1120.

The seventh examination relates to late trading and market timing practices by a Sky Capital trader. NASD states that this examination, as well as an eighth, routine examination of Sky Capital, are ongoing. NASD represents that, if either examination results in a disciplinary complaint against the firm, Sky Capital will have the right to litigate the issues raised and to seek appellate review.

Sky Capital does not dispute that it will have the right to litigate. However, Sky Capital asserts that all of the examinations were designed to drain its financial resources and harass its personnel. Sky Capital acknowledges that none of the examinations has resulted to date in any enforcement action against the firm.

In 2003, Sky Capital filed a complaint with NASD's Department of Internal Review concerning the staff's "inappropriate treatment of [its] membership applications and harassment through the examination process." Sky Capital's complaint was referred to the Office of the Ombudsman. Sky Capital states that no action was taken by the Ombudsman at that time. In 2006, Sky Capital complained to the Ombudsman about the actions of a former NASD examiner, J. Kirby Neill, who allegedly provided a Sky Capital customer with the name and number of an attorney and encouraged the customer to complain about the firm. 6/ Sky Capital asserts that its complaints to the Ombudsman have "fallen on deaf ears." 7/

III.

Sky Capital alleges that NASD staff's actions with respect to the firm violate the fair process requirements of Exchange Act Section 15A(b)(8) 8/ and the constitutional requirements of due process. In addition, Sky Capital asserts that the lack of an internal procedure for NASD member complaints of staff mistreatment constitutes a denial or limitation of access to NASD

6/ NASD states that it has terminated the examiner's employment.

7/ In its application, Sky Capital alleges further that the staff "provoked, caused and/or aided and abetted" a recent federal criminal investigation of the firm. Sky Capital bases this allegation on "information and belief," but does not set forth the sources of its information or the grounds for its belief. The United States Supreme Court has stated that a prosecutor has considerable discretion in determining matters such as which persons should be targets of investigation and what methods of investigation should be used. See Young v. U.S. ex rel. Vuitton et Fils SA, 481 U.S. 787, 807 (1987).

8/ 15 U.S.C. § 78o-3(b)(8) (requiring self-regulatory organizations to provide "fair procedures").

services, as well as a violation of NASD rules and a 1996 Commission report issued under Exchange Act Section 21(a). 9/

Our authority to review an action of a self-regulatory organization ("SRO"), including NASD, is governed by Exchange Act Section 19(d). 10/ That provision authorizes Commission review of an SRO action that: (1) imposes a final disciplinary sanction on any member or person associated with a member; (2) denies membership or participation to any applicant; (3) prohibits or limits any person in respect to access to services offered by such organization or a member of the organization; or (4) bars any person from becoming associated with a member. If we find that we do not have jurisdiction, we must dismiss the proceeding. 11/ Sky Capital's allegations fail to invoke any of these four jurisdictional categories.

9/ See NASD and The Nasdaq Market, Report Pursuant to Section 21(a) of the Securities Exchange Act of 1934, 52 S.E.C. 882 (1996) ("Report"). In the Report, the Commission made certain findings regarding deficiencies in NASD's oversight of Nasdaq and NASD's failure to enforce compliance with NASD rules and the federal securities laws. NASD entered into a settlement with the Commission, pursuant to which NASD agreed to certain undertakings, including undertakings to ensure the existence of a substantial internal audit staff to address complaints from NASD members. See Order Instituting Public Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions, 52 S.E.C. 875, 880 (1996).

10/ Contrary to Sky Capital's assertions, Exchange Act Section 19(f) does not establish a basis for Commission jurisdiction here. We have stated that, "[u]nless an appeal meets the threshold requirement for jurisdiction under Section 19(d), the standard of review under Section 19(f) is not an issue." Larry A. Saylor, Securities Exchange Act Rel. No. 51949 (June 30, 2005), 85 SEC Docket 3118, 3120-21 n.3.

11/ If, on the other hand, we find that jurisdiction is present, we are authorized, pursuant to Exchange Act Section 19(e), 15 U.S.C. § 78s(e), to affirm, modify, or set aside an SRO's sanctions in any proceeding to review a final disciplinary sanction. Pursuant to Exchange Act Section 19(f), 15 U.S.C. § 78s(f), we are authorized to dismiss or set aside any SRO action in a proceeding to review a denial of membership or participation in an SRO, the barring of any person from association with a member, or a prohibition or limitation by an SRO of a person's access to SRO services.

The Commission has no authority to grant much of the relief sought by Sky Capital. In its application, Sky Capital requests, among other things, that the Commission award the firm at least $300 million in damages and penalties and "reassign regulatory oversight of Sky Capital to another qualified self-regulatory organization . . . or to another NASD District Office." Under Exchange Act Sections 19(e) and (f), we do not have the authority to order such relief.

We have stated that a "disciplinary action" is "an action that responds to an alleged violation of an SRO rule or Commission statute or rule, or an action in which a punishment or sanction is sought or intended." 12/ We also have stated that Section 19(d) grants us jurisdiction to review only those disciplinary actions in which a final disciplinary sanction is imposed. 13/

Sky Capital alleges generally that "punishment has been inflicted" against the firm. However, the only final disciplinary sanctions cited are a Minor Rule Violation Letter (as well as a "letter of caution") and Letter of Acceptance, Waiver and Consent. Sky Capital and Mandell consented to those sanctions and waived their rights to appeal to the Commission. Two NASD staff examinations remain ongoing. Neither one has led to the institution of any disciplinary action, let alone a final sanction. 14/ We have stated that SRO action "is not reviewable merely because it adversely affects the applicant." 15/

Sky Capital has not been denied NASD membership or barred from associating with an NASD member. Sky Capital complains about the staff's handling of its application for NASD membership. However, the staff approved that application. Sky Capital does not allege, nor do we find, that it has been barred from associating with an NASD member.

Sky Capital has not been denied access to any services offered by NASD. Sky Capital complains about the staff's handling of the firm's applications to expand its business. 16/ Yet, NASD staff ultimately rendered decisions on those applications that were favorable to the firm.

12/ Russell A. Simpson, 53 S.E.C. 1042, 1046 (1998).

13/ Id.

14/ Thus, there was no action for which notice to the Commission was required under Exchange Act Section 19(d)(1). See 15 U.S.C. § 78s(d)(1) (requiring, in part, that an SRO promptly file with the Commission notice of any final disciplinary action taken with respect to any person or organization); see also, e.g., Tague Sec. Corp., 47 S.E.C. 743, 745 (1982) (dismissing proceeding for lack of jurisdiction where SRO did not attempt to penalize or discipline applicant and no notice of disciplinary action was filed by SRO, as required by Section 19(d)(1)).

15/ Joseph Dillon, 54 S.E.C. at 964.

16/ The Commission reviews denials of requests to modify NASD membership agreements as denials of access to NASD services under Exchange Act Section 19(f). See, e.g., Sierra Nevada Sec., Inc., 54 S.E.C. 112 (1999) (upholding NASD's denial of member's request to modify the terms of its restrictive agreement to permit it to make markets in the securities of more than fifty issuers).

Sky Capital also complains that it was denied access to NASD's internal complaint process. 17/ NASD created the Office of the Ombudsman, a position within NASD's Department of Internal Review, 18/ in order to provide a forum for members to voice their concerns of unfair practices or disparate treatment by the staff. 19/ Sky Capital's application makes clear that the firm has had access to the Ombudsman's Office and voiced its complaints about the staff's actions. 20/

Moreover, "[i]n those cases in which we have found a denial of access, an SRO had denied or limited the applicant's ability to utilize one of the fundamentally important services offered by the SRO. The services at issue were not merely important to the applicant but were central to the function of the SRO." 21/ In William J. Higgins, 22/ for example, we held that the New York Stock Exchange's denial of a member's request to install telephone link-ups on the trading floor to permit direct communication between the floor and non-member customers constituted a denial of access to the Exchange's services. We found that "[t]he operation of a

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17/ Sky Capital notes that, under NASD's settlement with the Commission, NASD was required to "ensure the existence of a substantial, independent internal audit staff which reviews all aspects of the NASD (including the regulatory function, the disciplinary process and [Nasdaq])," which would report directly to the Board of Governors' audit committee. 52 S.E.C. at 880. In the accompanying Report, the Commission stated that "[t]his measure should ensure that the NASD engages in a process of comprehensive ongoing self-evaluation." 52 S.E.C at 920.

18/ NASD Notice to Members 96-45, NASD Appoints Ombudsman (July 1996).

19/ NASD has stated that complaints regarding decisions made or actions taken by the staff that are "inconsistent, biased, or result in disparate treatment" may be directed to the Office of the Ombudsman. NASD Notice to Members 98-30, NASD Office of the Ombudsman Clarifies its Role (Mar. 1998).

20/ Under "The Ombudsman Association Standard of Practice," the Ombudsman has discretion in determining whether to act on a concern brought to its attention. See http://www.nasd.com/AboutNASD/CorporateInformation/OfficeoftheOmbudsman/index.htm.

21/ Morgan Stanley & Co., Inc., 53 S.E.C. 379, 385 (1997).

22/ 48 S.E.C. 713 (1987).

trading floor . . . is the principal service offered by a national securities exchange to its members, and by its members to investors." 23/ By contrast, Sky Capital has not shown that the Office of the Ombudsman provides a "fundamentally important service" that is central to the function of NASD. 24/

Sky Capital seems to complain that the current examinations of the firm continue. NASD actions generally may not be appealed to the Commission until they have been reviewed by the NAC. 25/ A hearing before a Hearing Panel and review of any Hearing Panel decision by the NAC would be available to Sky Capital if the current examinations result in disciplinary action against the firm. Sky Capital cannot now deprive NASD of its review function by filing a premature appeal to us. 26/

23/ Id. at 718; see also Scattered Corp., 52 S.E.C. 812, 813 (1996) (finding jurisdiction to review Chicago Stock Exchange's refusal to process firm's request for registration as a market maker in certain issues because such action limited the firm's access to Exchange services); Creative Med. Dev., Inc., 52 S.E.C. 968 (1996) (assuming jurisdiction over NASD action denying issuer temporary exception from automatic quotation system's inclusion standards).

24/ We have stated that "[w]e do not view permitting any person to file a complaint against an NASD member or associated person and conducting any resulting proceeding as offering a 'service' for purposes of Section 19(d)." Simpson, 53 S.E.C. at 1047.

25/ See, e.g., Avello v. SEC, 454 F.3d 619, 623 (7th Cir. 2006) (noting that an appeal to the NAC precedes a petition for review by the Commission). We reject the suggestion that Sky Capital's "efforts for relief internally at the NASD are in any event futile, as the bias and prejudice against it permeates, and emanates from, the highest levels at the NASD." Sky Capital has not shown the kind of "thoroughgoing taint" necessary to establish that resort to the proper appeals procedure would be a "futile" act. Swirsky v. NASD, 124 F.3d 59, 63 & n.3 (1st Cir. 1997).

26/ Insofar as Sky Capital suggests that the Commission investigate NASD's treatment of the firm, we point out that the determination of whether to investigate is a matter that resides within our discretion. See Exchange Act Sections 17(d)(1), 19(h), & 21(a)(1), 15 U.S.C. §§ 78q(d)(1), 78s(h), 78u(a)(1). The Supreme Court has recognized that "an agency's decision not to prosecute or enforce . . . is a decision generally committed to an agency's absolute discretion. This recognition of the existence of discretion is attributable . . . to the general unsuitability for judicial review of agency decisions to refuse enforcement." Heckler v. Chaney, 470 U.S. 821, 831 (1985); see also Bd. of Trade v. SEC, 883 F.2d 525, 530 (7th Cir. 1989) (citing Heckler v. Chaney). Our decision whether to undertake such matters is separate from our disposition of this proceeding.

Sky Capital's application for review is dismissed. An appropriate order will issue. 27/

By the Commission (Chairman COX and Commissioners NAZARETH and CASEY); Commissioners ATKINS and CAMPOS not participating.

Nancy M. Morris
Secretary

27/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 55828 / May 30, 2007

Admin. Proc. File No. 3-12498

In the Matter of the Application of

SKY CAPITAL LLC

For Review of Action Taken by

NASD

ORDER DISMISSING APPLICATION FOR REVIEW OF ACTION OF REGISTERED SECURITIES ASSOCIATION

On the basis of the Commission's opinion issued this day, it is

ORDERED that Sky Capital LL's application for review be, and it hereby is, dismissed.

By the Commission.

Nancy M. Morris
Secretary

Commissioner Nazareth
Not Participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 55834 / May 31, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12549

In the Matter of TEMPO SECURITIES CORPORATION, ROBERT SHIFFRA, and DENNIS ZAUSZNIEWSKI	ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934

I.

On January 24, 2007, the Securities and Exchange Commission ("Commission") instituted public administrative proceedings pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Tempo Securities Corporation, Robert Shiffra, and Dennis Zauszniewski (collectively "Respondents")

II.

Tempo Securities Corporation, Robert Shiffra, and Dennis Zauszniewski (collectively "Respondents") have submitted an Offer of Settlement ("Offer") in these proceedings, 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, each of the Respondents consents to the entry of this Order Making Findings and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Order"), as set forth below.

Document 33 of 33

III.

On the basis of this Order and Respondents' Offer, the Commission finds that:

Respondents

1. Tempo Securities Corporation ("Tempo"), a broker-dealer registered with the Commission since 1986, is a member of the National Association of Securities Dealers ("NASD"). Tempo conducts a general securities business in over-the-counter and listed securities. Tempo is headquartered in Cleveland, Ohio. From in or about 1995 to in or about 2004, Tempo had up to twenty registered representatives who operated off-site one-person offices.

2. Robert Shiffra ("Shiffra"), age 73, is the president of Tempo and owns two-thirds of the company. Shiffra has been an owner and officer of Tempo since 1991. Shiffra has been a licensed but nonpracticing attorney since 1966 and also occasionally serves as an arbitrator in the securities industry, including for the NASD. Shiffra has been working in the securities industry for at least 40 years and has held his Series 24 license since 1978. Shiffra was previously the head of the compliance department for a broker-dealer, where he wrote the firm's compliance and procedures manual.

3. Dennis Zauszniewski ("Zauszniewski"), age 55, is a founder and the senior vice president of Tempo. Zauszniewski owns one-third of the company, has been an owner and officer of Tempo since 1986, and has held his Series 24 license since 1986. Zauszniewski occasionally serves as an arbitrator in the securities industry.

Related Party

4. Gregory A. Applegate ("Applegate"), age 46, is currently serving a five-year prison term at the Federal Correctional Institute in Morgantown, West Virginia. Applegate was a registered representative associated with Tempo Securities from approximately April 1995 until approximately the end of December 2004, operating out of an office in Ashland, Ohio.

Summary

5. From in or about 2001 through approximately the end of 2004, while employed by and associated with Tempo as a registered representative, Applegate made misrepresentations of material facts to over 110 investors and defrauded them regarding the investment of at least $3.1 million in what they were told to be securities. Throughout this time, Respondents supervised Applegate. Respondents, however, failed reasonably to supervise Applegate with a view to preventing and/or detecting his fraudulent conduct. Respondents failed to establish reasonable supervisory procedures for conducting on-site inspections and reviewing DBA accounts, and they failed to establish a reasonable system to effectively implement supervisory procedures that did exist for review of customer communications and review of customer account statements.

Finally, Shiffra and Zauszniewski failed reasonably to respond to serious "red flags" indicating possible misconduct by Applegate.

Applegate Came to Tempo Amid Allegations of Fraud

6. Applegate joined Tempo in 1995. Approximately two years later, customers at Applegate's former brokerage firm filed an NASD arbitration claim against Applegate and his former firm, alleging that Applegate had committed fraud and breach of fiduciary duty, causing damages of approximately $140,000. Applegate was accused of providing his customers fraudulent account statements that concealed his excessive trading activity on their accounts. This alleged fraudulent conduct took place just before Applegate left for Tempo.

7. Respondents were aware of the substance of these allegations soon after the claim was filed. During investigative testimony before the staff of the Division of Enforcement, Shiffra claimed that he did not remember Applegate's explanation regarding the allegations, but Shiffra testified that he "didn't buy it when [he] heard it." At no time did Respondents attempt to contact Applegate's former supervisor or the complaining customers regarding the allegations.

8. During investigative testimony before the staff of the Division of Enforcement, Shiffra admitted that the timing of this alleged fraud and Applegate's move to Tempo "would raise concern. All of these things would be flags . . . it looks like that would be a reason he'd be leaving: under the scrutiny of Ohio Company checking with his customer."

Applegate's Ponzi Scheme

9. From in or about 2001 through the end of August 2005, Applegate solicited at least 160 investors to invest at least $9.5 million in a supposed "hedge fund" and other investment vehicles, purportedly through an entity called "Applegate Investments" and other similar names. Applegate orally guaranteed an annual rate of return to these investors. In reality, "Applegate Investments" was a Ponzi scheme: Applegate misappropriated investor funds, using them to finance an unrelated personal business, pay personal expenses, and pay "investment returns" to earlier investors. To carry out this scheme, Applegate mailed to investors false monthly "customer statements" maintained on his office computer, reflecting securities holdings and returns that did not exist, as well as monthly "dividend checks."

10. Throughout the period from in or about 2001 through approximately the end of 2004, Applegate was associated with Tempo as a registered representative.

11. While Applegate was associated with Tempo, at least 50% of "Applegate Investments" Ponzi scheme investors were also Tempo customers, and at least 40% of Applegate's Tempo customers with equity accounts also invested in the "Applegate Investments" Ponzi scheme.

12. Applegate continued operating the "Applegate Investments" Ponzi scheme after leaving Tempo at the end of 2004 for another brokerage firm. In August 2005, Applegate's supervisor at his new firm learned that one of Applegate's customers had received possibly false account

statements directly from Applegate. Applegate's supervisor immediately conducted an unannounced review of Applegate's office in Ashland and discovered evidence of the "Applegate Investments" Ponzi scheme in Applegate's customer files. These customers had also been Tempo customers when Applegate was with Tempo.

13. Applegate's misconduct described above violated Section 17(a) of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder.

14. On October 7, 2005, the Commission filed a complaint in SEC v. Gregory Applegate, No. 1:05CV2363, in the Northern District of Ohio, and obtained a temporary restraining order against Applegate, including an asset freeze. The complaint alleged the facts referred to in the first sentence of paragraph 5 above, and sought injunctive as well as monetary relief against Applegate.

15. On January 9, 2006, in the case of U.S. v. Gregory A. Applegate, No. 1:05-cr-00577-PAG in the Northern District of Ohio, Applegate pled guilty to a one count information charging mail fraud, in violation of Title 18, U.S. Code, Section 1341, for conduct related to the "Applegate Investments" Ponzi scheme.

16. During the plea colloquy in the criminal case referred to in the previous paragraph, Applegate admitted that as early as 2001 and continuing until September 2005, he "executed a scheme and artifice to defraud certain clients of his and to obtain money by means of fraudulent pretenses, representations and promises." Applegate also admitted that "in order to conceal this fraudulent scheme . . . [he] caused statements to be mailed to his clients, usually on a monthly or quarterly basis, from his office in Ashland, which falsely reflected the nature of his clients' investments and the balances in his clients' accounts."

17. On April 26, 2006, Applegate was sentenced to 5 years in prison and was ordered to pay approximately $2.9 million in restitution to aggrieved investors of the "Applegate Investments" Ponzi scheme.

18. On October 17, 2006, in SEC v. Gregory Applegate, the District Court entered a final judgment against Applegate including the entry of an order of permanent injunction enjoining him from violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

19. On October 30, 2006, the SEC instituted settled Administrative Proceedings against Applegate, barring him from association with any broker or dealer.

Respondents held all supervisory authority at Tempo

20. Tempo, Shiffra, and Zauszniewski supervised Applegate while he was associated with Tempo as a registered representative, from approximately April 1996 to approximately the end of 2004.

21. Shiffra and Zauszniewski jointly made all decisions regarding establishing Tempo's supervisory and compliance procedures and were jointly responsible for implementing and enforcing existing procedures. Shiffra and Zauszniewski jointly held all supervisory authority at Tempo, including the ability to discipline, hire and fire registered representatives.

22. Shiffra was Applegate's designated supervisor at Tempo, and Shiffra performed all on-site visits of Applegate's office and reviews of Applegate's operations.

Respondents failed to establish reasonable supervisory procedures or a system to implement existing procedures

23. During investigative testimony before the staff of the Division of Enforcement, Zauszniewski stated that Tempo is "not a real brokerage firm" and that Tempo does not follow compliance procedures that "real firms" use because they would be "cost [prohibitive]."

24. At all relevant times, Tempo registered representatives have been characterized by Tempo as "independent contractors," operating out of their own offices or homes without on-site supervision.

25. Applegate operated a one-person branch office in Ashland, Ohio, over an hour's drive from Tempo's main office. Tempo thus did not provide on-site supervision for Applegate.

Annual Reviews

26. Respondents did not establish reasonable procedures for inspections of registered representatives' offices, or implement the procedures for inspections of registered representatives' offices that did exist.

27. Respondents conducted only pre-announced scheduled "annual reviews" of its registered representatives' offices and operations. Respondents never conducted any unannounced visits or inspections.

28. During investigative testimony before the staff of the Division of Enforcement, Zauszniewski admitted that, because Respondents' reviews were always announced, Applegate "could have hid a lot of stuff, which he obviously did and intentionally hid."

29. Respondents' on-site visits to Applegate's office did not include reasonable inspection or review of his operations or offices.

30. During all reviews of Applegate's office and operations, Shiffra did not request to review Applegate's account records or customer account files.

31. Besides looking at the top of Applegate's desk and what was visible on his computer screen, Shiffra never conducted any physical inspection of Applegate's office.

32. From approximately 2001 until the end of 2004, Applegate maintained his "Applegate Investments" Ponzi scheme records on his office computer and in a binder labeled "Applegate Investments Accounts" in his office in Ashland, Ohio. At any given time, at least one month's worth of fraudulent customer statements, one for every "Applegate Investments" investor, was maintained in that binder.

33. The binder referenced in the previous paragraph and its label, "Applegate Investments Accounts," were clearly visible during all compliance reviews conducted by Shiffra. Shiffra never inquired about the binder's contents or attempted to inspect the binder.

34. During investigative testimony before the staff of the Division of Enforcement, Shiffra testified that he doubted that he had "the authority to check [Applegate's] computer or file cabinets or desk drawers" as part of a compliance review of Applegate's office. In fact, as Applegate's supervisor, Shiffra had the authority to do so as part of a compliance review.

35. As part of Respondents' annual review of Applegate's office, a survey was mailed to him asking for responses to various compliance questions. No attempt was made to verify Applegate's answers to the annual survey.

36. During investigative testimony before the staff of the Division of Enforcement, Shiffra stated, "I never understood what [Applegate's assistants] did . . . . I don't know what kept her busy full-time, especially with his production."

37. Respondents did not ask Applegate, or his administrative assistants, what work the assistants were performing in Applegate's office. Respondents did not attempt to interview Applegate's administrative assistants about any compliance matters. Respondents did not monitor how many administrative assistants Applegate retained.

38. Applegate's administrative assistants helped Applegate create and update the "Applegate Investments" Ponzi scheme customer statements every month, as well as to help mail them to customers. They also helped organize the customer files, including keeping "Applegate Investments" files separate from the legitimate Tempo customer account files.

39. Despite Tempo's own requirements to conduct on-site reviews at least annually, Respondents failed to implement this procedure by failing to conduct an on-site review of Applegate's office during at least one year: 2004, Applegate's last year associated with Tempo.

40. Zauszniewski admitted to examiners from the Commission's Office of Compliance Inspections and Examinations that Respondents did not conduct an on-site review of Applegate's office in 2004, citing "personal issues."

Lack of Procedures for Review of Applegate's DBA Bank Accounts

41. As an "independent contractor," Applegate was responsible for his own business expenses, such as office rent, phone, and electricity.

42. Respondents did not establish procedures to review or inspect, nor did they ever review or inspect, Applegate's business "DBA" bank accounts from which he paid his business expenses.

43. Had Respondents ever asked to review or audit Applegate's "DBA" bank accounts during approximately 2001 through the end of 2004, they would have discovered personal checks from Applegate's Tempo customers being deposited into his "DBA" bank accounts, and funds being diverted from those accounts to his personal bank accounts, as part of the "Applegate Investments" Ponzi scheme.

44. One of Applegate's "DBA" bank accounts was in the name of "Applegate Investments."

Inadequate Implementation of Procedures for Review of Customer Communications

45. The Tempo Compliance and Procedure Manual required that branch supervisors "devise and institute a program whereby all communication from the public to any registered representative under his authority or control is reviewed daily prior to such material being given to the registered representative." The Tempo Manual also required that branch supervisors "institute and supervise a system whereby the registered representative's communications to the public concerning securities transactions for the business of this organization are reviewed and a copy retained in the branch office filed and a copy sent to the Compliance Director."

46. During investigative testimony before the staff of the Division of Enforcement, Shiffra stated that the requirements in the previous paragraph are "referring to a real branch where all of the incoming mail is opened by one person or supervisor and read and looked at before it's passed out. Where you've got one guy in an office, it doesn't work." Instead, for one-person offices with no on-site supervision such as Applegate's, registered representatives were simply asked to forward copies of all customer correspondence to Respondents. However, no systems were established to effectively implement this requirement.

Lack of Systems to Implement Procedures for Customer Account Statement Review

47. Tempo's Compliance and Procedure Manual requires that supervisors "review all monthly statements at least four times per year and initial as evidence of such review." Tempo's clearing firm produced monthly account statements for Tempo's customers, and copies of these statements were mailed to Tempo every month. The Tempo Manual also requires that supervisors of branch offices "review monthly the customer statements" to check for unusual activity, excessive commissions, and unusual patterns of buying or selling.

48. Starting some time in 2000, Tempo's clearing firm stopped providing paper copies of the monthly statements, instead providing only electronic copies of customers' monthly account statements on its web site, to which Tempo had access. Tempo had dial-up internet access at its main office.

49. After the clearing firm stopped providing paper copies of the monthly statements some time in 2000 until at least January 2006, Respondents failed to develop a reasonable system to implement procedures regarding review of customer account statements. No one at Tempo reviewed customers' monthly account statements, despite having access to them through the clearing firm's web site.

<u>Shiffra and Zauszniewski failed reasonably to respond to red flags concerning Applegate</u>

Applegate's Commission Decline

50. Between 1995 and 2004, Applegate generally was one of Tempo's highest "producers" in terms of commission, at times generating approximately one-third of Tempo's total revenue and well over $100,000 in annual gross commissions.

51. Applegate's annual gross commissions then dropped nearly in half between July 1, 2002 and June 30, 2003, Tempo's fiscal year. Shiffra and Zauszniewski did not investigate this dramatic drop in commissions or ask Applegate why his production had declined.

52. During the same period that Applegate's gross commissions dropped nearly in half, customer investments in the "Applegate Investments" Ponzi scheme more than doubled.

Applegate's Repeated Violation of Tempo Advertisement Policy

53. Applegate repeatedly violated Tempo's advertisement policy when he listed his office in the local Yellow pages as "Applegate Investments" and other variations of that name, instead of "Tempo Securities." Shiffra and Zauszniewski repeatedly told Applegate that this listing was unacceptable, but the listing remained the same for the next nine years without any follow-up, further investigation, or disciplinary action taken against Applegate.

54. Shiffra and Zauszniewski failed reasonably to enforce Tempo's advertisement policy when they failed to follow up or take any action against Applegate for the recurring violation described in the previous paragraph.

55. In addition, Applegate's repeated violation of this Tempo policy was a red flag of suspicious conduct, which Shiffra and Zauszniewski should have investigated.

Significant Customer Liquidations

56. Shiffra and Zauszniewski were aware of numerous liquidations by Applegate's customers from their Tempo securities accounts.

57. Shiffra and Zauszniewski never attempted to contact any of these customers regarding liquidations.

58. With respect to certain significant liquidations, Shiffra testified that he asked Applegate, not the customer, why the customer decided to liquidate their holdings.

59. At least $900,000 worth of customer liquidations in 2003 and 2004 were deposited in the "Applegate Investments" Ponzi scheme soon thereafter.

60. One of Applegate's Tempo customers liquidated at least $400,000 worth of securities held with Tempo within an eight-month period. This customer countersigned all of her liquidation checks directly over to Applegate.

Applegate Claimed No Correspondence with Customers

61. During annual reviews, Shiffra asked Applegate for copies of all correspondence with customers.

62. During investigative testimony before the staff of the Division of Enforcement, Shiffra testified that Applegate always told him that he had engaged in no written correspondence with his customers, except for brief notes referring the customers to newspaper articles.

63. Shiffra and Zauszniewski never attempted to verify Applegate's repeated claims that he never engaged in any substantive customer correspondence. For example, Shiffra and Zauszniewski never communicated with customers to verify that Applegate never corresponded with them.

64. Applegate engaged in regular written correspondence with a large proportion of his Tempo customers: he mailed them monthly account statements regarding their "Applegate Investments" Ponzi scheme investments.

65. Shiffra and Zauszniewski took no independent steps to communicate with Applegate's customers, such as periodic "happiness letters," "activity letters" or any other regular attempts to ascertain customer satisfaction or familiarity with their accounts.

Applegate's Fraud Violations

66. By virtue of the conduct alleged above, Applegate violated Section 17(a) of the Securities Act and 10(b) of the Exchange Act and Rule 10b-5 thereunder when he made intentional misrepresentations regarding the investment activity of "Applegate Investments."

67. Applegate represented to some customers that their investments would be pooled into a "hedge fund" invested in various securities. Other investors were told that they were investing directly into mutual funds or municipal funds.

68. In reality, Applegate misappropriated investor deposits, using customers' funds to pay off previous investors and for various personal expenses.

69. Applegate also created false "Applegate Investments" monthly statements to support his misrepresentations as to the status of customers' investments.

Respondents' Failure Reasonably to Supervise Applegate

70. Section 15(b)(4)(E) of the Exchange Act provides that the Commission can impose various sanctions against a broker-dealer, if it "has failed reasonably to supervise, with a view to preventing violations of the provisions of such statutes, rules, and regulations, another person who commits such a violation, if such other person is subject to his supervision." Section 15(b)(6)(A)(i) of the Exchange Act similarly provides that the Commission can impose various sanctions against individuals who fail to supervise others who are subject to their supervision, within the meaning of Section 15(b)(4)(E).

71. By virtue of the conduct alleged above, Tempo, Shiffra, and Zauszniewski failed reasonably to supervise Applegate within the meaning of Section 15(b) of the Exchange Act when they failed to supervise Applegate with a view to preventing and detecting violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

72. Respondents failed to establish reasonable supervisory procedures or a system to implement the procedures that did exist. In addition, while Applegate was associated with Tempo, several incidents occurred that should have raised red flags concerning Applegate's conduct. Shiffra and Zauszniewski, however, did not reasonably respond to these red flags. If Respondents had developed reasonable supervisory procedures for conducting on-site inspections and reviewing DBA accounts, or reasonable systems to implement supervisory procedures for reviewing customer communications and customer account statements, or if Shiffra and Zauszniewski had responded reasonably to red flags, it is likely that they could have prevented and detected Applegate's fraud.

Undertakings

73. Respondents undertake to cease all securities business of Tempo Securities Corporation within 90 days of the entry of this Order.

74. In determining whether to accept the Offer, the Commission considered this undertaking.

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 Section 15(b) of the Securities Exchange Act of 1934, it is hereby ORDERED:

A. It is ordered that within 30 days of the entry of this Order, Respondents Shiffra and Zauszniewski shall each pay a civil money penalty in the amount of $30,000 to the United States Treasury. 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 Shiffra and Zauszniewski as Respondents in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Peter K.M. Chan, Securities and Exchange Commission, 175 W. Jackson Blvd., Suite 900, Chicago, IL 60604.

B. It is further ordered that 90 days after the entry of this Order, Respondents Shiffra and Zauszniewski shall be barred from association with any broker or dealer in a supervisory capacity, with the right to reapply for association in such capacity after one (1) year to the appropriate self-regulatory organization, or if there is none, to the Commission;

C. Any reapplication for association by any of the Respondents will be subject to the applicable laws and regulations governing the reentry process, and the reentry may be conditioned upon a number of facts, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, 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. It is further ordered that 180 days after the entry of this Order, the broker-dealer registration of Tempo Securities Corporation with the Commission shall be revoked.

By the Commission.

Nancy Morris
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary