SECURITIES AND EXCHANGE COMMISSION

This file is maintained pursuant to the Freedom of Information Act (5 U.S.C. 552). It contains a copy of each decision, order, rule or similar action of the Commission, for **June 2009**, with respect to which the final votes of individual Members of the Commission are required to be made available for public inspection pursuant to the provisions of that Act.

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

MARY L. SCHAPIRO, CHAIRMAN

KATHLEEN L. CASEY, COMMISSIONER

ELISSE B. WALTER, COMMISSIONER

LUIS A. AGUILAR, COMMISSIONER

TROY A. PAREDES, COMMISSIONER

56 Documents

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

February 12, 2009

IN THE MATTER OF **AVICENA GROUP, INC.,** **NORTHERN ETHANOL, INC.,** **HYDROGEN HYBRID TECHNOLOGIES, INC. and** **STOCK-TRAK GROUP, INC.** **File No. 500-1**	**ORDER OF SUSPENSION OF TRADING**

It appears to the Securities and Exchange Commission that the public interest and the protection of investors require a suspension of trading in the securities of Avicena Group, Inc., Northern Ethanol, Inc., Hydrogen Hybrid Technologies, Inc. and Stock-Trak Group, Inc. Questions have arisen concerning the trading in the companies' stocks and the accuracy and adequacy of publicly available information regarding the ownership and control of each company.

Avicena Group, Inc. is incorporated in Delaware and headquartered in Palo Alto, California. The company's common stock is quoted on Pink Sheets operated by Pink OTC Markets Inc. ("Pink Sheets") under the ticker symbol "AVCE."

Northern Ethanol, Inc. is incorporated in Delaware and headquartered in Toronto, Ontario. The company's common stock is quoted on Pink Sheets under the ticker symbol "NOET."

Hydrogen Hybrid Technologies, Inc. is incorporated in Nevada and headquartered in Pickering, Ontario. The company's common stock is quoted on the OTC Bulletin Board and Pink Sheets under the ticker symbol "HYHY."

Stock-Trak Group, Inc. (formerly Neutron Enterprises, Inc.) is incorporated in Nevada and headquartered in Montreal, Quebec. The company's common stock is quoted on the OTC Bulletin Board and Pink Sheets under the ticker symbol "STKG" (formerly "NTRN").

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed companies.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading of the securities of the above-listed companies is suspended for the period commencing at 9:30 a.m. EST, February 12, 2009, and terminating at 11:59 p.m. EST, on February 26, 2009.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60016 / June 1, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13499

In the Matter of DAVID B. STOCKER, Esq. Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against David B. Stocker ("Respondent" or "Stocker") instituted pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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 paragraphs III. 1 through 7 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order . . . suspend from appearing or practicing before it any . . . attorney . . . who has been by name . . . [p]ermanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating . . . any provision of the Federal securities laws or of the rules and regulations thereunder.

III.

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

1. Stocker, age 49, is and has been an attorney licensed to practice law in the State of Arizona. During 2004, Stocker acted as an attorney for American Television & Film Company, Auction Mills, Inc., AVL Global, Inc., Custom Designed Compressor Systems, Inc., Ecogate Inc., Media International Concepts, Inc., and Vanquish Productions, Inc. During 2006, Stocker acted as an attorney for Accel International Corporation, Access Developers, Inc., Avalon Stores, Inc., Chemtrack, Inc., Computer Communications, Inc., Electronic Transmission Corporation, and Westmark Holdings, Inc.

2. On June 14, 2007, the Commission filed a complaint in the United States District Court for the Eastern District of Michigan alleging that Stocker violated Sections 5(a) and 5(c) of the Securities Act of 1933 ("Securities Act"). *SEC v. Peter W. Fisher, et al.*, Civil Action No. 07-cv-12552 GER PJK (E.D. Mich.). The complaint alleges that Stocker, directly or indirectly, offered and sold the securities of AVL Global, Inc. when no registration statements were filed or in effect for his transactions and no exemption from registration applied. As the attorney for AVL Global, Stocker prepared subscription agreements and corporate resolutions in connection with three offerings and sales of shares of the company's stock. Stocker also provided legal opinion letters to AVL Global and its transfer agent concluding that the offers and sales were exempt from registration under Rule 504 of Regulation D of the Securities Act [17 C.F.R. § 230.504]. The documents that Stocker prepared were designed to give the appearance that the company's offers and sales of shares were limited to accredited investors who intended to purchase for investment, not resale. As alleged in the Commission's complaint, however, the exemption cited by Stocker was not available for purchasers who acquired the securities with a view to distribution of the securities. In fact, in each of the three transactions, with Stocker's participation, the initial purchasers resold the AVL Global shares within days or weeks.

3. On May 18, 2009, the U.S. District Court for the Eastern District of Michigan entered a final judgment by consent against Stocker, permanently enjoining him from future violations of Sections 5(a) and (c) of the Securities Act. *SEC v. Peter W. Fisher, et al.*, Civil Action No. 07-cv-12552 GER PJK (E.D. Mich.). Pursuant to the final judgment, Stocker was ordered to pay $37,480 in disgorgement and $13,228 in prejudgment interest, and barred from participating in the offering of penny stocks.

4. On September 26, 2007, the Commission filed a complaint in the United States District Court for the Northern District of Texas alleging that Stocker violated Sections 5(a) and 5(c) of the Securities Act. *SEC v. Phillip P. Offill, Jr., et al.*, Civil Action No. 07-cv-1643 (N.D. Tex.). The complaint alleges that Stocker directly or indirectly, offered and sold the securities of American Television & Film Company, Auction Mills, Inc., Custom Designed Compressor Systems, Inc., Ecogate Inc., Media International Concepts, Inc., and Vanquish Productions, Inc., when no registration statements were filed or in effect for his transactions and no exemption from registration applied. As the attorney for each of the companies, Stocker prepared subscription agreements and corporate resolutions in connection with offerings and sales of shares of the companies' stock. Stocker also provided legal opinion letters to the companies and

their transfer agents concluding that the offers and sales were exempt from registration under rule 504 of Regulation D of the Securities Act. [17 C.F.R. § 230.504]. The documents that Stocker prepared were designed to give the appearance that the offers and sales of shares were limited to accredited investors who intended to purchase for investment, not resale. As alleged in the Commission's complaint, however, the exemption cited by Stocker was not available for purchasers who acquired the securities with a view to a distribution of the securities. In fact, in each of the transactions, Stocker and other underwriters, with Stocker's participation, resold the shares within days or weeks.

5. On May 7, 2009, the United States District Court for the Northern District of Texas entered a final judgment by consent against Stocker, permanently enjoining him from future violations of Sections 5(a) and 5(c) of the Securities Act. *SEC v. Phillip P. Offill, Jr., et al.*, Civil Action No. 07-cv-1643-D (N.D. Tex.). Pursuant to the final judgment, Stocker was required to pay $888,693 in disgorgement and $298,040 in prejudgment interest, and was barred from participating in the offering of penny stocks.

6. On August 11, 2008, the Commission filed a complaint in the United States District Court for the District of Arizona alleging that Stocker violated Sections 5(a), 5(c) and 17(a) of the Securities Act, and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder. *SEC v. David B. Stocker, et al.*, Civil Action No. CIV-08-1475-PHX-FJM (D. Ariz.). The complaint alleges that Stocker engaged in corporate identity theft by making false and misleading statements to cause stock in certain companies to be exchanged for stock in other companies, to obtain controlling interests in such companies, and to sell stock when no registration statement was filed or in effect for his transactions and no exemption from registration applied. The seven corporations involved in the transactions are Accel International Corporation, Access Developers, Inc., Avalon Stores, Inc., Chemtrack, Inc., Computer Communications, Inc., Electronic Transmission Corporation, and Westmark Holdings, Inc.

7. On May 12, 2009, the U.S. District Court for the District of Arizona entered a final judgment by consent against Stocker, permanently enjoining him from violating Sections 5(a), 5(c), and 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. *SEC v. David B. Stocker, et al.*, Civil Action No. CIV-08-1475-PHX-FJM (D. Ariz.). Pursuant to the final judgment, Stocker was ordered to pay $505,000 in disgorgement and $87,802 in prejudgment interest, and barred from participating in the offering of penny stocks.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that Stocker is suspended from appearing or practicing before the Commission as an attorney.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Paredes
Disapproved

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60017 / June 1, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2983 / June 1, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13500

In the Matter of SHARLENE ABRAMS, CPA Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission (the "Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against Sharlene Abrams (the "Respondent" or "Abrams") pursuant to Rule 102(e)(3) of the Commission's Rules of Practice.[1]

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

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

herein, except as to the Commission's jurisdiction over her and the subject matter of these proceedings, and the findings contained in Section III.3. below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions (the "Order"), as set forth below.

III.

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

1. Sharlene Abrams, age 51, is a resident of the state of Nevada. Abrams served as Chief Financial Officer, Vice-President of Finance and Administration, and Secretary of Mercury Interactive Corporation ("Mercury") between November 1993 and November 2001. Prior to her tenure at Mercury, she was employed at Price Waterhouse LLP, rising to the position of senior manager. Abrams was, beginning on or about July 1, 1981, a CPA licensed in the state of Massachusetts, but that license lapsed no later than June 30, 2003 and she is no longer licensed as a CPA in any state.

2. Mercury was acquired by the Hewlett-Packard Company ("HP") by an agreement consummated on November 8, 2006, and is now Mercury Interactive, LLC, a non-trading subsidiary of HP. Prior to the consummation of the merger, Mercury was a corporation headquartered in Mountain View, California, and organized under the laws of Delaware. Mercury made software used to test and optimize information technology systems and software applications. At the time of the conduct described in this Order, the company's common stock was registered with the Commission pursuant to Section 12(g) of the Securities Exchange Act of 1934 ("Exchange Act") and listed on the NASDAQ under the symbol MERQ.

3. On March 24, 2009, a final judgment was entered by consent against Abrams in the civil action entitled Securities and Exchange Commission v. Mercury Interactive, et. al, Civil Action Number C 07-2822 (JF), in the United States District Court for the Northern District of California. The final judgment permanently enjoined Abrams from future violations of Section 17(a) of the Securities Act of 1933, Sections 10(b), 13(b)(5), 14(a), and 16(a) of the Securities Exchange Act of 1934 ("Exchange Act"), and Exchange Act Rules 10b-5, 13a-14, 13b2-1, 13b2-2, 14a-9, and 16a-3, and from aiding and abetting violations of Section 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, and 13a-13. The final judgment also prohibited Abrams from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act, and ordered her to pay disgorgement of $2,287,914, prejudgment interest in the amount of $112,086, and a $425,000 civil penalty.

4. The Commission's Complaint alleged, among other things, that no later than 1997, Abrams engaged in a fraudulent scheme with Mercury's former Chief Executive Officer, former General Counsel and others to grant undisclosed, in-the-money stock options to themselves and others, by backdating stock option grants to coincide with historically low closing prices for Mercury's stock. According to the Complaint, Abrams' fraudulent misconduct caused Mercury,

between 1997 and 2005, (i) to file materially false and misleading financial statements that materially understated its compensation expenses and materially overstated its quarterly and annual net income and earnings per share, and (ii) to make disclosures in its periodic filings and proxy statements that falsely portrayed Mercury's options as having been granted at exercise prices equal to the fair market value of Mercury's common stock on the date of the grant. According to the Complaint, Abrams also misled Mercury's outside auditors in an attempt to hide the scheme. The Complaint alleged that Abrams, and others, filed Forms 3 and 4 with the Commission that contained false or misleading statements with regard to the options' grant dates and the exercise prices. The Complaint also alleged that from 1998 through 2001, Abrams and others fraudulently backdated the dates of option exercises of certain senior Mercury officers, including Abrams, to low-points of the company's stock price, in order to minimize the officers' taxable gain on exercise or receive more favorable long-term capital gains treatment on profits they earned upon the later sale of the stock acquired through exercise. The benefits reaped from the backdated exercises were concealed through fraudulent proxy disclosures and in Forms 4 filed with the Commission. The Complaint further alleged that during at least 1997 through 2001, Abrams participated in a scheme to manipulate Mercury's reported earnings per share ("EPS") by holding shipping of its products once revenue targets for a period had been achieved, pushing the recognition of the revenue into subsequent periods, while concealing these practices from the public through fraudulent and misleading disclosures and omissions. The Complaint additionally alleged that between 1999 and 2005, Abrams and others participated in the fraudulent structuring of overseas employee stock option exercise transactions to conceal the variable accounting consequences of those transactions, causing the company to fail to report the approximately $24 million in compensation expense required under variable accounting.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that:

Abrams is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

[Release Nos. 33-9037; 34-60032; IC-28757]

File No. 265-25

SUBJECT: Investor Advisory Committee.

AGENCY: Securities and Exchange Commission.

ACTION: Notice of Federal Advisory Committee Establishment.

SUMMARY: The Chairman of the Securities and Exchange Commission ("Commission"), with the concurrence of the other Commissioners, intends to establish the Securities and Exchange Commission Investor Advisory Committee ("the Committee").

ADDRESSES: Written comments may be submitted by the following methods:

Electronic Comments

- Use the Commission's Internet comment form (http://www.sec.gov/rules/other/shtml); or
- Send an email to rule-comments@sec.gov. Please include File No. 265-25 on the subject line.

Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington 20549-1090.

All submissions should refer to File No. 265-25. 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/other/shtml). Comments will also be available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. 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: Kayla Gillan, Deputy Chief of Staff, at (202) 551-2100, Securities and Exchange Commission, 100 F Street, NE, Washington DC 20549.

SUPPLEMENTARY INFORMATION: In accordance with the requirements of the Federal Advisory Committee Act, 5 U.S.C. – App.1, the Commission is publishing this notice that the Chairman of the Commission, with the concurrence of the other Commissioners, intends to establish the Committee. The Committee's objective is to provide the Commission with the views of a broad spectrum of investors on their priorities concerning the Commission's regulatory agenda.

To achieve the Committee's goals, between 14 and 18 members will be appointed who can represent effectively the varied interests affected by the range of issues to be considered. The Committee's membership may include investors or investor representatives from a broad spectrum of institutions, such as mutual funds, foundations, and pension funds; investors representing different geographical regions; investors of different sizes and investment strategies; and individual investors. The Committee's membership will be fairly balanced in terms of points of view represented and the functions to be performed.

The Committee may be established 15 days after publication of this notice by filing a charter for the Committee with the Committee on Banking, Housing, and Urban Affairs of the United States Senate and the Committee on Financial Services of the United States House of Representatives. A copy of the charter as so filed also will be filed with the Chairman of the Commission, furnished to the Library of Congress, placed in the Public Reference Room at the Commission's headquarters and posted on the Commission's Web site at www.sec.gov. The Committee's objective is to provide the Commission with the views of a broad spectrum of investors on their priorities concerning the Commission's regulatory agenda, including:

(1) advising the Commission regarding matters of concern to investors in the securities markets;

(2) providing the Commission with investors' perspectives on current, non-enforcement, regulatory issues; and

(3) serving as a source of information and recommendations to the Commission regarding the Commission's regulatory programs from the point of view of investors.

The Committee will operate for two years from the date it is established unless, before the expiration of that time period, its charter is re-established or renewed in accordance with the Federal Advisory Committee Act or unless the Commission determines that the Committee's continuance is no longer in the public interest.

The Committee will meet at such intervals as are necessary to carry out its functions. The charter will provide that meetings of the full Committee are expected to occur no more frequently than four times per year. Meetings of subgroups or subcommittees of the full Committee may occur more frequently.

The charter will provide that the duties of the Committee are to be solely advisory. The Commission alone will make any determinations of action to be taken and policy to be expressed with respect to matters within the Commission's authority as to which the Committee provides advice or makes recommendations.

The Chairman of the Commission affirms that the establishment of the Committee is necessary and in the public interest.

By the Commission.

BY: Elizabeth M. Murphy
Secretary

Elizabeth M. Murphy
Secretary

Dated: June 3, 2009

Commissioner Walter
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60042 / June 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13501

In the Matter of

LEXINGTON RESOURCES, INC.,

Respondent.

ORDER INSTITUTING PROCEEDINGS PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND REVOKING REGISTRATION OF SECURITIES

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act"), against Lexington Resources, Inc. ("Lexington" 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 Proceedings Pursuant to Section 12(j) of the Securities Exchange Act of 1934, Making Findings, and Revoking Registration of Securities ("Order"), as set forth below.

III.

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

A. Lexington is a Nevada corporation that is or previously was engaged in the acquisition and development of oil and natural gas properties in the U.S. Lexington's common stock has been registered under Section 12(g) of the Exchange Act since 1999 and is currently quoted on the "Pink Sheets," operated by Pink OTC Markets, Inc., under the symbol "LXRS." Until 2007, Lexington stock was quoted on the OTC Bulletin Board.

[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.

B. Lexington has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1, 13a-11 and 13a-13 thereunder, while its common stock was registered with the Commission, in that it has not filed an Annual Report on Form 10-KSB since May 17, 2007, periodic or quarterly reports on Form 10-QSB for any fiscal period subsequent to its fiscal quarter ending September 30, 2007, or current reports disclosing Chapter 7 liquidation proceedings involving Lexington's only prior operating subsidiaries.

IV.

Section 12(j) of the Exchange Act provides as follows:

The Commission is authorized, by order, as it deems necessary or appropriate for the protection of investors to deny, to suspend the effective date of, to suspend for a period not exceeding twelve months, or to revoke the registration of a security, if the Commission finds, on the record after notice and opportunity for hearing, that the issuer of such security has failed to comply with any provision of this title or the rules and regulations thereunder. No member of a national securities exchange, broker, or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security the registration of which has been and is suspended or revoked pursuant to the preceding sentence.

In view of the foregoing, the Commission finds that it is necessary and appropriate for the protection of investors to impose the sanction specified in Respondent's Offer.

Accordingly, it is hereby ORDERED, pursuant to Section 12(j) of the Exchange Act, that registration of each class of Repondent's securities registered pursuant to Section 12 of the Exchange Act be, and hereby is, revoked.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Commissioner Casey and
Commissioner Aguilar
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60043 / June 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13502

In the Matter of **Merchant Capital, L.L.C.,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 15(b), 15B(c)(2) and 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b), 15B(c)(2), and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Merchant Capital, L.L.C. ("Merchant Capital" 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 Pursuant to Sections 15(b), 15B(c)(2) and 21C of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

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

SUMMARY

1. These proceedings arise out of Merchant Capital's violations of the gifts and gratuities, fair dealing and supervisory rules of the Municipal Securities Rulemaking Board

("MSRB") by paying for travel and entertainment expenses of family members, friends or associates of senior officials at two public finance clients (the "Issuers") and later receiving reimbursement for such expenses from the Issuers, and, in certain instances, directly from the proceeds of bond offerings made by the Issuers. From 2003 through 2005, the Issuers obtained bond insurance and credit ratings for their bond offerings from bond insurance firms and credit rating agencies based in New York City. In connection with the Issuers' efforts to obtain bond insurance and favorable credit ratings, officials of the Issuers traveled with Merchant Capital's investment bankers to New York City on several occasions to meet with analysts from the bond insurance firms and credit rating agencies. Issuer officials brought family members, friends or associates, some of whom were employed by the Issuers, on these trips who, although they did not attend business meetings, incurred expenses for airfare, car service, meals at upscale restaurants, and tickets to Broadway shows and various sporting events. Based on input from representatives of the Issuers, Merchant Capital organized the activities for these trips, and advanced the payment for nearly all of the expenses incurred by the Issuer officials and their family members, friends or associates. Merchant Capital then sought and obtained, with the knowledge and approval of the senior officials of the Issuers who participated in the trips, reimbursement for expenses incurred on the trips.

RESPONDENT

2. Merchant Capital, L.L.C. ("Merchant Capital"), an Alabama corporation, has been registered with the Commission as a broker and dealer since 1985, with the Financial Industry Regulatory Authority (or its predecessor) since April 12, 1971 and with the MSRB as a municipal securities dealer since December 29, 1975. Merchant Capital is primarily owned by Merchant Capital Investments, Inc., the firm's parent company.

FACTS

BACKGROUND

3. Over the past ten years, Merchant Capital has underwritten several bond issues through which the Issuers raised capital for various infrastructure projects. From 2003 through 2005, Merchant Capital investment bankers and Issuer officials took trips to New York City to discuss planned bond issues with bond insurers and credit rating agencies.

4. Several Issuer officials took family members, friends or associates on these trips. The travel and entertainment expenses incurred by these family members, friends or associates, some of whom were employed by the Issuers, were advanced by Merchant Capital and subsequently reimbursed by the Issuers from the proceeds of bond offerings associated with the trips. Merchant Capital did not adequately consider whether the officials reimbursed the Issuers for those expenses. In fact, the Issuer officials made no effort to reimburse the Issuers for the expenses incurred by their family members, friends or associates.

5. On each of these trips, Issuer officials coordinated with Merchant Capital in planning and organizing the trips' various activities. Merchant Capital scheduled meetings with

the bond insurers and credit rating agencies, paid for airline tickets of Issuer officials as well as their family members and friends or associates, made hotel reservations for all of the trip participants and reserved a car service to transport Issuer officials and their family members, friends or associates around New York City for business purposes and non-business excursions. Issuer officials typically advised Merchant Capital regarding restaurants and entertainment activities they had selected for the trips, and thereafter Merchant Capital made the necessary reservations, paid for meals, and advanced the funds to purchase the requested entertainment tickets for Issuer officials as well as their family members and friends or associates.

6. Merchant Capital later invoiced the Issuers for the travel and entertainment expenses incurred on the trips along with other expenses associated with the relevant bond offerings, such as: (1) third-party bond registration-related fees; (2) printing and mailing costs; and (3) a credit rating agency fee. Merchant Capital's underwriting fee, known as an underwriter's discount, was not included on the invoices, but instead was set forth in underwriter's agreements associated with each bond offering. The expenses incurred on the trips to New York City were billed to the Issuers under a single line-item called "rating trip expenses" on the underwriting invoices. This line item included the travel and entertainment expenses incurred by Issuer officials and their family, friends or associates on the rating trips associated with the invoiced bond offerings as well as the travel and entertainment expenses incurred by Merchant Capital bankers on those trips. Merchant Capital obtained reimbursement for the invoiced travel and entertainment expenses.

7. For the relevant time period, Merchant Capital did not have adequate compliance policies and procedures in place to prevent violations of the rules that prohibit any broker, dealer, or municipal securities dealer from, directly or indirectly, giving or permitting to be given any thing or service of value in excess of $100 per year to Issuer officials.

TRIPS ON BEHALF OF ISSUER A

June 2003 Trip

8. In June 2003, Merchant Capital investment bankers and officials from one of the Issuers ("Issuer A") went to New York City to meet with three bond insurers to discuss upcoming bond offerings by Issuer A.

9. One Issuer official brought his wife and two other family members on the trip. Although his wife was an employee of Issuer A, she was not involved in the bond issuance process and did not attend any of the bond insurer meetings. The other two family members were not Issuer A employees and also did not attend any meetings. Instead, the Issuer official's wife and other family members attended the Broadway shows "Gypsy" and "Hairspray" and dined at the Gotham Bar & Grill and other New York City restaurants.

10. This same Issuer official also invited his aunt and uncle to join him on the June 2003 trip. His aunt and uncle did not attend any of the meetings with bond insurers. Instead, they visited a college where their son had recently been accepted for admission. They also attended the

above-referenced Broadway shows, dined at fine restaurants, and attended a New York Yankees game.

11. Another official of Issuer A also attended the June 2003 trip as an important participant in the meetings with the bond insurers. This Issuer official brought an adult child on the trip. The Issuer official's adult child did not attend any of the meetings with bond insurers. Merchant Capital arranged for the adult child to attend two Broadway shows. The adult child also dined at three upscale restaurants.

12. Merchant Capital provided car service for the Issuer officials' family members in New York City.

13. Six of the eight individuals who went on the June 2003 trip with the investment bankers were family members of Issuer officials. Although some of these individuals were employed by Issuer A, they were unnecessary participants on the trip. Merchant Capital paid and was subsequently reimbursed for the expenses incurred on behalf of the six individuals, including airfare, car service, meals and entertainment.

14. Merchant Capital invoiced Issuer A to seek reimbursement for the expenses it incurred during this June 2003 trip, including those expenses it advanced on behalf of the Issuer officials' family members. Merchant Capital billed the expenses for the June 2003 trip in a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, the Issuer paid the invoices, which included $8,969 in travel and entertainment expenses improperly advanced on behalf of the unnecessary participants on the trip. These expenses were paid out of the proceeds of Issuer A's bond sales in 2003 as a cost of the issuances.

September 2003 Trip

15. Merchant Capital investment bankers and officials from Issuer A made a second trip to New York City in September 2003, this time to meet with credit rating agencies. One Issuer official brought his wife, also an employee of Issuer A, on this trip. His wife did not attend any credit rating agency meetings. Instead, she attended the Broadway show "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club. The same Issuer official also invited his friend along, who was a part-time employee of Issuer A. The part-time employee took his wife along. The part-time employee's wife did not attend any credit rating agency meetings. Instead, she also saw "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club.

16. Two other officials of Issuer A also went on this trip. One brought her boyfriend; the other brought his wife. Although the boyfriend was an employee of Issuer A, neither the boyfriend nor the wife attended any credit rating agency meetings on this trip. Instead, they saw "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club.

17. Four of the eight individuals who went on the September 2003 trip with the investment bankers were family members, friends or associates of Issuer officials. Although some were employees of Issuer A, they were unnecessary participants on the trip. Merchant Capital paid

and was subsequently reimbursed for expenses incurred on behalf of the four individuals, including airfare, car service, meals and entertainment.

18. Merchant Capital invoiced Issuer A to seek reimbursement for expenses it incurred during this September 2003 trip, including those expenses it advanced on behalf of the Issuer officials' family members, friends or associates. Merchant Capital billed the expenses under a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, when Issuer A's 2003 bond offerings closed, it paid the invoices directly out of the proceeds of the bond offerings as a cost of the issuances. The invoices included $4,549 in travel and entertainment expenses improperly advanced on behalf of the unnecessary participants on the trip.

19. In total, the expenses incurred for these individuals during the June and September 2003 rating trips accounted for approximately eight percent of Issuer A's 2003 bond issuance costs, excluding the underwriter's discount.

November 2004 Trip

20. Merchant Capital investment bankers made a third trip to New York City on behalf of Issuer A in November 2004 to meet with bond insurers and credit rating agencies. Several Issuer officials' family members went on this trip.

21. One Issuer official took his wife, also an employee of the Issuer, and three other relatives, two of whom were Issuer employees, on this trip. None of these family members had any business purpose for accompanying the Issuer official to New York City, and, accordingly, none of them attended any of the bond insurer or credit rating agency meetings.

22. Instead, the Issuer official's family members attended the Radio City Music Hall Christmas Spectacular, saw the Broadway show "Wicked" and dined at the Blue Water Grill. Additionally, two of the family members saw the Broadway show "Avenue Q," while two others attended a world heavyweight championship boxing match at Madison Square Garden.

23. Another Issuer official brought an adult child on this November 2004 trip. The adult child did not attend any bond insurer or credit rating agency meetings. Instead, the Issuer official's adult child attended the Radio City Music Hall Christmas Spectacular and saw two Broadway shows.

24. A third employee of Issuer A made this trip and brought her husband. The husband was an employee of Issuer A, but he had no role in the bond issuance process and, accordingly, did not attend any bond insurer or credit rating agency meetings during the trip. Instead, the husband attended the Radio City Music Hall Christmas Spectacular, saw "Wicked" and dined at the Blue Water Grill. The husband also went to the world heavyweight championship boxing match.

25. In all, six of the ten individuals who went on the November 2004 trip with the investment bankers were family members of Issuer officials and, although some were employed by the Issuer, they did not attend any meetings and were unnecessary participants on the trip.

Merchant Capital advanced and was subsequently reimbursed for expenses incurred on behalf of the six family members, including airfare, car service, meals and entertainment.

26. Merchant Capital invoiced Issuer A to seek reimbursement for most of the expenses it incurred during this November 2004 trip, including most of the expenses it advanced on behalf of the Issuer officials' family members. Merchant Capital billed the expenses under a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, when Issuer A's 2005 bond offerings closed, Merchant Capital sought and obtained reimbursement for the November 2004 rating trip expenses directly out of the proceeds of the bond offerings as a cost of the issuances. In total, Merchant Capital improperly advanced $8,925 in travel and entertainment expenses on behalf of the family members of the Issuer officials and subsequently obtained reimbursement for at least $7,809 of those expenses.

27. In total, the expenses incurred for these family members during the November 2004 rating trip accounted for approximately seven percent of Issuer A's 2005 bond issuance costs, excluding the underwriter's discount.

28. The state government travel laws and Issuer A's guidelines and policies in effect during the relevant time period required officials of Issuer A to: (1) obtain advance approval for their out of state travel; (2) provide an itemization of expenses to identify those that are actual and necessary and subject to reimbursement; and (3) identify, in advance, the source of the funds that would be used to pay for the trip. The Issuer officials who attended the out-of-state rating trips did not comply with these state travel laws, guidelines and policies. Moreover, the relevant state travel laws and Issuer guidelines and policies contain no provisions that would allow Issuer officials to permit the travel expenses of friends or associates and family members who accompany them on official out-of-state business to be advanced by a municipal securities dealer and later reimbursed by the Issuer.

29. After it advanced the funds for the Issuer officials' family members, friends or associates, Merchant Capital did not adequately consider whether the officials reimbursed the Issuer for those expenses. In fact, the officials did not reimburse Issuer A for the travel and entertainment expenses incurred by their family members, friends or associates on the July 2003, September 2003 or November 2004 trips.

30. In total, Merchant Capital paid and was subsequently reimbursed at least $21,327 for travel and entertainment expenses incurred by family members, friends or associates in connection with the June 2003, September 2003 and November 2004 trips to New York City on behalf of Issuer A.

TRIPS ON BEHALF OF ISSUER B

June 2004 Trip

31. In June 2004, Merchant Capital investment bankers, an official from another of the Issuers ("Issuer B"), and an advisor to Issuer B went to New York City to meet with credit rating

agencies and bond insurers in connection with an upcoming bond issuance. The advisor brought his wife and two children, and the Issuer official brought his wife.

32. The Issuer's advisor traveled to New York City with his wife and two children on a Friday, three days prior to the meetings scheduled for the following Monday. The advisor paid personally for his family's airfare and hotel costs.

33. None of the Issuer official's or advisor's family members attended any of the meetings with credit rating agencies or bond insurers. Rather, the family members enjoyed meals at Oceana, Estiatorio Milos and the Gotham Bar & Grill. They also attended the Broadway show "Mamma Mia" and a New York Mets game.

34. Four of the eight individuals who went on the June 2004 trip with the investment bankers were family members, did not participate in any of the meetings, and were unnecessary participants on the trip. Merchant Capital advanced and was subsequently reimbursed for expenses incurred on behalf of the four family members, including car service, meals, and entertainment.

35. Merchant Capital invoiced Issuer B to seek reimbursement for the expenses it advanced during this June 2004 trip, including those expenses it advanced on behalf of the Issuer official's and the advisor's family members. Thereafter, the Issuer paid the invoice, which included $2,247 in travel and meal expenses improperly advanced on behalf of the official's wife and the advisor's family members.

36. In total, the expenses incurred by the family members during the June 2004 rating trip accounted for approximately fifteen percent of Issuer B's 2004 bond issuance costs, excluding the underwriter's discount.

May 2005 Trip

37. In May 2005, Merchant Capital investment bankers and the officials from Issuer B made another trip to New York City to meet with credit rating agencies. One of the Issuer officials brought his wife.

38. Merchant Capital paid and was subsequently reimbursed for expenses advanced on behalf of the wife, including airfare and a meal at the Blue Water Grill.

39. Merchant Capital invoiced Issuer B to seek reimbursement for certain expenses it incurred during this May 2005 trip, including those expenses it advanced on behalf of the Issuer official's wife. Thereafter, the Issuer paid the invoice, which included $543 in travel and meal expenses improperly advanced on behalf of the official's wife.

40. After it advanced the funds for the Issuer official's wife and the advisor's family members, Merchant Capital did not adequately consider whether the official or the advisor reimbursed the Issuer for those expenses. In fact, the Issuer B official and advisor did not reimburse the Issuer for the travel and entertainment expenses advanced by Merchant Capital and

paid by Issuer B in connection with the June 2004 and May 2005 trip.

41. In total, Merchant Capital paid and was subsequently reimbursed $2,790 for travel and entertainment expenses incurred by family members in connection with the June 2004 and May 2005 trips to New York City on behalf of Issuer B.

42. Since the time of the above-referenced rating trips, Merchant Capital has taken significant steps to improve the way it organizes and oversees rating trips taken by its clients, including the implementation of employee training programs.

VIOLATIONS

43. Section 15B(b) of the Exchange Act established the MSRB and empowered it to propose and adopt rules with respect to transactions in municipal securities by brokers, dealers, and municipal securities dealers. Section 15B(c)(1) prohibits a broker, dealer or municipal securities dealer from using the mails or any instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security in violation of any MSRB rule. As a municipal securities dealer, Merchant Capital was subject to Section 15B(c)(1) of the Exchange Act and the MSRB rules.

44. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-17, which requires municipal securities dealers to deal fairly with all persons and not to engage in any deceptive, dishonest, or unfair practice.

45. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-20(a), which prohibits any broker, dealer, or municipal securities dealer from, directly or indirectly, giving or permitting to be given any thing or service of value, including gratuities, in excess of $100 per year to a person other than an employee or partner of such broker, dealer, or municipal securities dealer, if such payments or services are in relation to the municipal securities activities of the recipient's employer.

46. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-27, which requires, among other things, that (a) each broker, dealer and municipal securities dealer supervise the conduct of its municipal securities business and the municipal securities activities of its associated persons to ensure compliance with MSRB rules as well as the applicable provisions of the Exchange Act and the rules promulgated thereunder; and (b) each broker, dealer and municipal securities dealer to adopt, maintain, and enforce written supervisory procedures reasonably designed to ensure compliance with the same rules and Exchange Act provisions.

47. As a result of Merchant Capital's violations of MSRB Rules G-17, G-20, and G-27, Merchant Capital willfully[1] violated Section 15B(c)(1) of the Exchange Act.

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[1] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (*quoting Hughes v. SEC*, 174 F.2d 969, 977 (D.C.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer. Accordingly, pursuant to Sections 15(b), 15B(c)(2) and 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 Section 15B(c)(1) of the Exchange Act, and MSRB Rules G-17, G-20 and G-27.

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

C. Respondent shall, within 10 days of the date of entry of this Order, pay a civil money penalty in the amount of $55,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Merchant Capital, L.L.C. 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 Gerald W. Hodgkins, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549.

By the Commission.

Elizabeth M. Murphy,
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Cir. 1949)). There is no requirement that the actor "'also be aware that he is violating one of the Rules or Acts.'" *Id.* (*quoting Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13503

In the Matter of H-Entertainment, Inc., Hamburger Hamlet Restaurants, Inc., Harvard International Technologies, Ltd., HealthCentral.com, Helian Health Group, Inc., and Hemisphere Development Corp. (n/k/a Hemisphere Energy Corp., Respondents.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents H-Entertainment, Inc., Hamburger Hamlet Restaurants, Inc., Harvard International Technologies, Ltd., HealthCentral.com, Helian Health Group, Inc., and Hemisphere Development Corp. (n/k/a Hemisphere Energy Corp.).

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. H-Entertainment, Inc. (CIK No. 751145) is a permanently revoked Nevada corporation located in Woodland Hills, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). H-Entertainment is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 2001, which reported a net loss of over $4 million for the prior three months. As of June 3, 2009, the company's common stock (symbol "HENI") was traded on the over-the-counter markets.

2. Hamburger Hamlet Restaurants, Inc. (CIK No. 879501) is a forfeited Delaware corporation located in Sherman Oaks, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Hamburger Hamlet is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 24, 1995, which reported a net loss of over $1 million for the prior three months. On December 6, 1995, Hamburger Hamlet filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Central District of California, and the case was terminated on January 23, 2001. As of June 3, 2009, the company's common stock (symbol "HMBQ") was traded on the over-the-counter markets.

3. Harvard International Technologies, Ltd. (CIK No. 899659) is a British Columbia corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Harvard International is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F for the period ended December 31, 1993, which reported a net loss of $12 million (Canadian) for the prior twelve months. As of June 3, 2009, the company's common stock (symbol "HAVI") was traded on the over-the-counter markets.

4. HealthCentral.com (CIK No. 1095016) is an inactive Delaware corporation located in Emeryville, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). HealthCentral is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 2001, which reported a net loss of $10 million for the prior three months. On October 9, 2001, HealthCentral filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Northern District of California, and the case was terminated on February 8, 2008. As of June 3, 2009, the company's common stock (symbol "HCENQ") was traded on the over-the-counter markets.

5. Helian Health Group, Inc. (CIK No. 856288) is a Delaware corporation located in Monterey, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Helian Health is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q/A for the period ended August 31, 1995, which reported a net loss of $429,352 for the prior three months. On September 13, 1999, Helian Health filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Delaware, and the case was terminated on June 5, 2003.

6. Hemisphere Development Corp. (n/k/a Hemisphere Energy Corp.) (CIK No. 701756) is a British Columbia corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Hemisphere Development is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F for the period ended February 28, 1992, which reported a net loss of $89,812 (Canadian) for the prior twelve months. On January 18, 2000, Hemisphere Development Corp. changed its name to Northern Hemisphere Development Corp., and on April 27, 2009, Northern

Hemisphere Development Corp. changed its name to Hemisphere Energy Corp., but failed to report these changes through the Commission's EDGAR database as required by Commission rules. As of June 3, 2009, the company's stock (symbol "HMENF") was traded on the over-the-counter markets.

B. DELINQUENT PERIODIC FILINGS

7. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

8. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires domestic issuers to file quarterly reports. Rule 13a-16 requires certain foreign private issuers to furnish quarterly and other material reports to the Commission under cover of Form 6-K if they make or are required to make the information public under the laws of the jurisdiction of their domicile or in which they are incorporated or organized; if they file or are required to file information with a stock exchange on which their securities are traded and the information was made public by the exchange; or if they distribute or are required to distribute information to their security holders.

9. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 or 13a-16 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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 it 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 or Express Mail, or by other means permitted by the Commission's Rules of Practice.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Attachment

Chart of Delinquent Filings
H-Entertainment, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
H-Entertainment, Inc.					
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**30**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Hamburger Hamlet Restaurants, Inc.					
	10-K	12/31/95	04/01/96	Not filed	158
	10-Q	03/31/96	05/15/96	Not filed	157
	10-Q	06/30/96	08/14/96	Not filed	154
	10-Q	09/29/96	11/13/96	Not filed	151
	10-K	12/29/96	03/31/97	Not filed	147
	10-Q	03/30/97	05/14/97	Not filed	145
	10-Q	06/29/97	08/13/97	Not filed	142
	10-Q	09/28/97	11/12/97	Not filed	139
	10-K	12/28/97	03/30/98	Not filed	135
	10-Q	03/29/98	05/13/98	Not filed	133
	10-Q	06/28/98	08/12/98	Not filed	130
	10-Q	09/27/98	11/11/98	Not filed	127
	10-K	12/27/98	03/29/99	Not filed	123
	10-Q	03/28/99	05/12/99	Not filed	121
	10-Q	06/27/99	08/11/99	Not filed	118
	10-Q	09/26/99	11/10/99	Not filed	115
	10-K	12/26/99	03/27/00	Not filed	111
	10-Q	03/26/00	05/10/00	Not filed	109
	10-Q	06/25/00	08/09/00	Not filed	106
	10-Q	09/24/00	11/08/00	Not filed	103
	10-K	12/31/00	04/02/01	Not filed	98
	10-Q	03/25/01	05/09/01	Not filed	97
	10-Q	06/24/01	08/08/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/30/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/29/02	11/13/02	Not filed	79
	10-K	12/29/02	03/31/03	Not filed	75
	10-Q	03/30/03	05/14/03	Not filed	73
	10-Q	06/29/03	08/13/03	Not filed	70
	10-Q	09/28/03	11/12/03	Not filed	67
	10-K	12/28/03	03/29/04	Not filed	63
	10-Q	03/28/04	05/12/04	Not filed	61
	10-Q	06/27/04	08/11/04	Not filed	58

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
***Hamburger Hamlet Restaurants, Inc.* (Continued)**	*10-Q*	09/26/04	11/10/04	Not filed	55
	10-K	12/26/04	03/28/05	Not filed	51
	10-Q	03/27/05	05/11/05	Not filed	49
	10-Q	06/26/05	08/10/05	Not filed	46
	10-Q	09/25/05	11/09/05	Not filed	43
	10-K	12/25/05	03/27/06	Not filed	39
	10-Q	03/26/06	05/10/06	Not filed	37
	10-Q	06/25/06	08/09/06	Not filed	34
	10-Q	09/24/06	11/08/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/25/07	05/09/07	Not filed	25
	10-Q	06/24/07	08/08/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-K	12/30/07	03/31/08	Not filed	15
	10-Q	03/30/08	05/14/08	Not filed	13
	10-Q	06/29/08	08/13/08	Not filed	10
	10-Q	09/28/08	11/12/08	Not filed	7
	10-K	12/28/08	03/30/09	Not filed	3
	10-Q	03/29/09	05/13/09	Not filed	1
Total Filings Delinquent	**54**				
Harvard International Technologies, Ltd.					
	20-F	12/31/94	06/30/95	Not filed	168
	20-F	12/31/95	07/01/96	Not filed	155
	20-F	12/31/96	06/30/97	Not filed	144
	20-F	12/31/97	06/30/98	Not filed	132
	20-F	12/31/98	06/30/99	Not filed	120
	20-F	12/31/99	06/30/00	Not filed	108
	20-F	12/31/00	07/02/01	Not filed	95
	20-F	12/31/01	07/01/02	Not filed	83
	20-F	12/31/02	06/30/03	Not filed	72
	20-F	12/31/03	06/30/04	Not filed	60
	20-F	12/31/04	06/30/05	Not filed	48
	20-F	12/31/05	06/30/06	Not filed	36

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
***Harvard International Technologies, Ltd.* (Continued)**	*20-F*	12/31/06	07/02/07	Not filed	23
	20-F	12/31/07	06/30/08	Not filed	12
Total Filings Delinquent	**14**				
HealthCentral.com					
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/31/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-K	12/31/02	03/31/03	Not filed	75
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-K	12/31/03	03/30/04	Not filed	63
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-K	12/31/04	03/31/05	Not filed	51
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-K	12/31/05	03/31/06	Not filed	39
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-K	12/31/07	03/31/08	Not filed	15
	10-Q	03/31/08	05/15/08	Not filed	13
	10-Q	06/30/08	08/14/08	Not filed	10
	10-Q	09/30/08	11/14/08	Not filed	7

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
***HealthCentral.com* (Continued)**	*10-K*	12/31/08	03/31/09	Not filed	3
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**31**				
Helian Health Group, Inc.					
	10-K	11/30/95	02/28/96	Not filed	160
	10-Q	02/29/96	04/15/96	Not filed	158
	10-Q	05/31/96	07/15/96	Not filed	155
	10-Q	08/31/96	10/15/96	Not filed	152
	10-K	11/30/96	02/28/97	Not filed	148
	10-Q	02/28/97	04/14/97	Not filed	146
	10-Q	05/31/97	07/15/97	Not filed	143
	10-Q	08/31/97	10/15/97	Not filed	140
	10-K	11/30/97	03/02/98	Not filed	135
	10-Q	02/28/98	04/14/98	Not filed	134
	10-Q	05/31/98	07/15/98	Not filed	131
	10-Q	08/31/98	10/15/98	Not filed	128
	10-K	11/30/98	03/01/99	Not filed	123
	10-Q	02/28/99	04/14/99	Not filed	122
	10-Q	05/31/99	07/15/99	Not filed	119
	10-Q	08/31/99	10/15/99	Not filed	116
	10-K	11/30/99	02/28/00	Not filed	112
	10-Q	02/29/00	04/14/00	Not filed	110
	10-Q	05/31/00	07/17/00	Not filed	107
	10-Q	08/31/00	10/16/00	Not filed	104
	10-K	11/30/00	02/28/01	Not filed	100
	10-Q	02/28/01	04/16/01	Not filed	98
	10-Q	05/31/01	07/16/01	Not filed	95
	10-Q	08/31/01	10/15/01	Not filed	92
	10-K	11/30/01	02/28/02	Not filed	88
	10-Q	02/28/02	04/15/02	Not filed	86
	10-Q	05/31/02	07/15/02	Not filed	83
	10-Q	08/31/02	10/15/02	Not filed	80
	10-K	11/30/02	02/28/03	Not filed	76

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Helian Health Group, Inc. **(Continued)**	*10-Q*	02/28/03	04/14/03	Not filed	74
	10-Q	05/31/03	07/15/03	Not filed	71
	10-Q	08/31/03	10/15/03	Not filed	68
	10-K	11/30/03	03/01/04	Not filed	63
	10-Q	02/29/04	04/14/04	Not filed	62
	10-Q	05/31/04	07/15/04	Not filed	59
	10-Q	08/31/04	10/15/04	Not filed	56
	10-K	11/30/04	02/28/05	Not filed	52
	10-Q	02/28/05	04/14/05	Not filed	50
	10-Q	05/31/05	07/15/05	Not filed	47
	10-Q	08/31/05	10/17/05	Not filed	44
	10-K	11/30/05	02/28/06	Not filed	40
	10-Q	02/28/06	04/14/06	Not filed	38
	10-Q	05/31/06	07/17/06	Not filed	35
	10-Q	08/31/06	10/16/06	Not filed	32
	10-K	11/30/06	02/28/07	Not filed	28
	10-Q	02/28/07	04/16/07	Not filed	26
	10-Q	05/31/07	07/16/07	Not filed	23
	10-Q	08/31/07	10/15/07	Not filed	20
	10-K	11/30/07	02/28/08	Not filed	16
	10-Q	02/28/08	04/14/08	Not filed	14
	10-Q	05/31/08	07/15/08	Not filed	11
	10-Q	08/31/08	10/15/08	Not filed	8
	10-K	11/30/08	03/02/09	Not filed	3
	10-Q	02/28/09	04/14/09	Not filed	2
Total Filings Delinquent	**55**				
Hemisphere Development Corp. (n/k/a Hemisphere Energy Corp.)					
	20-F	02/28/93	08/31/93	Not filed	190
	20-F	02/28/94	08/31/94	Not filed	178
	20-F	02/28/95	08/31/95	Not filed	166

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Hemisphere Development Corp. (n/k/a Hemisphere Energy Corp.) **(Continued)**	*20-F*	02/28/96	09/03/96	Not filed	153
	20-F	02/28/97	09/02/97	Not filed	141
	20-F	02/28/98	08/31/98	Not filed	130
	20-F	02/28/99	08/31/99	Not filed	118
	20-F	02/28/00	08/31/00	Not filed	106
	20-F	02/08/01	08/31/01	Not filed	94
	20-F	02/28/02	09/03/02	Not filed	81
	20-F	02/28/03	09/02/03	Not filed	69
	20-F	02/28/04	08/31/04	Not filed	58
	20-F	02/28/05	08/31/05	Not filed	46
	20-F	02/28/06	08/31/06	Not filed	34
	20-F	02/28/07	08/31/07	Not filed	22
	20-F	02/28/08	09/02/08	Not filed	9

Total Filings Delinquent **16**

*Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, have been removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal took effect over a transition period that concluded on March 15, 2009. All reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB are now required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

Commissioner Casey and Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60047 / June 4, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2984 / June 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13504

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

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 Dyadic International, Inc. ("Dyadic" 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 Cease-And-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

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

Respondent

1. Dyadic is a biotechnology company incorporated in Delaware and based in Jupiter, Florida. Dyadic became a public company in October 2004 through a reverse merger, and on May 26, 2005, it registered its common stock with the Commission pursuant to Section 12(b) of the Exchange Act. From May 2005 through January 2008, Dyadic's common stock was listed on the American Stock Exchange ("AMEX"). In January 2008, the AMEX delisted and deregistered Dyadic's common stock. Since its delisting through the present, Dyadic's common stock has been quoted on the "Pink Sheets" disseminated by Pink OTC Markets, Inc. but has not been registered pursuant to Section 12 of the Exchange Act.

Summary

2. For fiscal years ended December 31, 2005 and 2006, Dyadic filed periodic reports with the Commission incorporating financial statements that materially misstated its revenues and accounts receivable balances. Specially, in contravention of Generally Accepted Accounting Principles ("GAAP"), Dyadic improperly recognized revenue from sales made by its wholly-owned subsidiary, Puridet (Asia) Limited ("Puridet"), overstated Puridet's accounts receivable balances and failed to disclose material related party transactions by Puridet with members of Puridet's management. During this time period, Dyadic did not maintain accurate books and records and had deficient internal accounting controls. As a result of these deficiencies, Dyadic has been unable to restate its prior quarterly and annual financial statements for the periods ended June 30, 2005 through December 31, 2006.

Dyadic Improperly Recognized Sales by its Asian Subsidiary

3. Dyadic acquired a majority voting interest in Puridet in 2003. Puridet, which manufactures and distributes textile enzymes in Asia, is based in Hong Kong. In April 2006, Puridet became a wholly-owned subsidiary of Dyadic. Puridet's sales in 2005 and 2006 represented approximately 40% of Dyadic's consolidated revenues as reflected in its financial statements filed with the Commission during that time period.

4. In April 2007, Dyadic's management became aware of potential material operational and financial improprieties at Puridet through an anonymous whistle-blower complaint following the death of Puridet's managing director. An internal investigation conducted by Dyadic determined that the subsidiary's largest customer, an entity named Pui Shing Detergent Company and a predecessor entity, South Dragon Detergent Company

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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.

(collectively "Pui Shing"), was secretly controlled by Puridet's management, including the deceased managing director. According to the internal investigation, Puridet's management created Pui Shing as a customer on Puridet's books and records. In reality, Pui Shing was only used as a vehicle for Puridet to recognize revenue from product it sold on a cash basis to local businesses throughout mainland China. As such, sales to Pui Shing were not bona fide. These cash transactions may have also allowed Puridet's management to possibly misappropriate funds and certain of these Chinese businesses to avoid their local reporting and sales tax requirements. The effect of these transactions on Puridet's financial statements could not be quantified by Dyadic because the underlying transactions were in cash, not properly documented and Pui Shing's books and records could not be obtained from Puridet's management.

5. Puridet conducted approximately 25% of its business through Pui Shing with the intent to conceal the true nature of its relationship to that entity and its customers. For the year ended December 31, 2006, sales to Pui Shing alone represented almost 10% of Dyadic's net sales on a consolidated basis and over 20% of Dyadic's consolidated net receivable balance.

6. As a result, Dyadic materially misstated figures reported for its revenue and accounts receivable and failed to disclose material related-party transactions in its financial statements for the years ended December 31, 2005 and 2006 and the quarters ended June and September of 2005 and March, June and September of 2006. Dyadic included its misleading financial results in press releases and its filings with the Commission relating to these periods. Dyadic has been unable to fully quantify the financial impact of these Puridet transactions, or restate its financial statements for this time period, because the necessary records did not exist or could not be obtained.

7. In May 2007, Dyadic abandoned its Asian operations because of its concerns over these material operational and financial improprieties at Puridet.

Dyadic Failed to File Periodic Reports with the Commission

8. Dyadic has not filed an Annual Report on Form 10-KSB with the Commission since December 31, 2006 or periodic or quarterly reports on Form 10-QSB for any fiscal period subsequent to its fiscal quarter ending September 30, 2006 up through its delisting and deregistration by AMEX in January 2008. Dyadic's failure to file these reports stems from its violations of GAAP, as well as certain record keeping and internal control deficiencies.

Dyadic's Violations

Dyadic's Violations of the Books and Records and Internal Control Provisions

9. Section 13(a) of the Exchange Act and Rules 13a-1, 13a-13 and 12b-20 thereunder, require every issuer of a security registered pursuant to Section 12 of the Exchange Act file with the Commission information, documents, and annual and quarterly reports as the Commission may require, and mandate that periodic reports contain such further material information as may be necessary to make the required statements not misleading. Section 13(b)(2)(A) of the Exchange

Act, requires reporting companies to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect their transactions and dispositions of their assets. Section 13(b)(2)(B) of the Exchange Act requires all reporting companies to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP.

10. Because Dyadic improperly recorded its revenue, accounts receivable, and related-party transactions, its books, records and accounts did not, in reasonable detail, accurately and fairly reflect its transactions and dispositions of assets. In addition, Dyadic failed to implement internal accounting controls relating to its revenue, accounts receivable and related party transactions which were sufficient to provide reasonable assurances that these accounts were accurately stated in accordance with GAAP.

Dyadic's Violations of the Reporting Provisions

11. Dyadic has also failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder, while its common stock was registered with the Commission in that it has not filed an Annual Report on Form 10-KSB since December 31, 2006 or periodic or quarterly reports on Form 10-QSB for any fiscal period subsequent to its fiscal quarter ending September 30, 2006 up through its delisting and deregistration by AMEX in January 2008.

Dyadic's Remedial Efforts

In determining to accept the Offer, the Commission considered remedial acts 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 Dyadic's Offer.

Accordingly, it is hereby ORDERED that:

Pursuant to Section 21C of the Exchange Act, Respondent Dyadic cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Aguilar
Disapproved

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60051 / June 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13505

In the Matter of POWERCOLD CORPORATION, Respondent.	ORDER INSTITUTING PROCEEDINGS PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND REVOKING REGISTRATION OF SECURITIES

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act"), against PowerCold Corporation ("PowerCold" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") that 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 Proceedings, Making Findings, and Revoking Registration of Securities Pursuant to Section 12(j) 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.

A. PowerCold, a Nevada corporation with its principal place of business in LaVernia, Texas, designs and builds heating, ventilation, and air conditioning systems. At all relevant times, PowerCold's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act, and traded on the Pink OTC Markets.

B. PowerCold has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1, 13a-11, and 13a-13 thereunder, while its common stock was registered with the Commission in that it has not filed an Annual Report on Form 10-K since September 7, 2006 or periodic or quarterly reports on Form 10-Q for any fiscal period subsequent to its fiscal quarter ending June 30, 2006.

IV.

Section 12(j) of the Exchange Act provides as follows:

> The Commission is authorized, by order, as it deems necessary or appropriate for the protection of investors to deny, to suspend the effective date of, to suspend for a period not exceeding twelve months, or to revoke the registration of a security, if the Commission finds, on the record after notice and opportunity for hearing, that the issuer of such security has failed to comply with any provision of this title or the rules and regulations thereunder. No member of a national securities exchange, broker, or dealer shall make use of the mails or any means of instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security the registration of which has been and is suspended or revoked pursuant to the preceding sentence.

In view of the foregoing, the Commission finds that it is necessary and appropriate for the protection of investors to impose the sanction specified in Respondent's Offer.

Accordingly, it is hereby ORDERED, pursuant to Section 12(j) of the Exchange Act, that registration of each class of Repondent's securities registered pursuant to Section 12 of the Exchange Act be, and hereby is, revoked.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Aguilar Disapproved

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60052 / June 5, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2985 / June 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13506

In the Matter of GRAYLING R. HOFER, Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Grayling R. Hofer ("Respondent" or "Hofer") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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

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[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

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.3 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Hofer, age 51, served as chief accounting officer, corporate controller, treasurer, and a director of PowerCold Corporation ("PowerCold") from March 2002 through November 2006. Hofer was also PowerCold's Chief Financial Officer from January 2006 to November 2006. Hofer currently serves as PowerCold's Vice President of Operations.

2. PowerCold was, at all relevant times, a Nevada corporation with its principal place of business in LaVernia, Texas. PowerCold is engaged in the business of designing and building heating, ventilation, and air conditioning systems. At all relevant times, PowerCold's common stock was registered with the Commission pursuant to Section 12(g) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the Pink OTC Markets.

3. On April 6, 2009, a final judgment was entered against Hofer, permanently enjoining him from future violations of Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5, 13b2-1, and 13b2-2 thereunder, and aiding and abetting violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder, in the civil action entitled Securities and Exchange Commission v. Grayling R. Hofer et. al, Civil Action Number SA09CA0185-FB, in the United States District Court for the Western District of Texas. Hofer was also barred from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act for a period of five years.

4. The Commission's complaint alleged, among other things, that PowerCold engaged in a fraudulent scheme that resulted in the company filing materially false and misleading financial statements in the company's annual reports on Forms 10-K for the fiscal years ended December 31, 2003 and 2004, and in the company's quarterly reports on Forms 10-Q for the first three quarters of fiscal years 2003, 2004, and 2005. The Complaint further alleged that Hofer engaged in a number of improper accounting practices that constituted a departure from generally accepted accounting principles. In addition, the complaint alleged that Hofer failed to disclose information in response to questions by PowerCold's independent auditors about certain of the company's fraudulent revenue recognition practices.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that Hofer is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60059 / June 8, 2009

INVESTMENT ADVISERS ACT OF 1940
Release No. 2888 / June 8, 2009

INVESTMENT COMPANY ACT OF 1940
Release No. 28759 / June 8, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13507

In the Matter of EVERGREEN INVESTMENT MANAGEMENT COMPANY, LLC and EVERGREEN INVESTMENT SERVICES, INC., Respondents.	ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 15(b)(4) and 21C OF THE SECURITIES EXCHANGE ACT OF 1934, SECTIONS 203(e) and 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940, AND SECTIONS 9(b) and 9(f) OF THE INVESTMENT COMPANY ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER

I.

The United States Securities and Exchange Commission (the "Commission") deems it appropriate and in the public interest that administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"), and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act") against Evergreen Investment Management Company, LLC and Evergreen Investment Services, Inc. (collectively, "Respondents").

II.

In anticipation of the institution of these proceedings, the Respondents have submitted an Offer of Settlement (the "Offer") that 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 in which the Commission is a party, and without admitting or denying the findings, except those findings pertaining to the jurisdiction of the Commission over Respondents and the subject matter of these proceedings, which are admitted, the Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings pursuant to Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934, Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, and Sections 9(b) and 9(f) of the Investment Company Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order") as set forth below. The Order is instituted as to Evergreen Investment Management Company, LLC pursuant to Sections 203(e) and 203(k) of the Advisers Act and Sections 9(b) and 9(f) of the Investment Company Act. The Order is instituted as to Evergreen Investment Services, Inc. pursuant to Section 15(b)(4) and 21C of the Exchange Act, Section 203(k) of the Advisers Act, and Sections 9(b) and 9(f) of the Investment Company Act.

III.

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

Summary

1. The Evergreen Ultra Short Opportunities Fund (the "Ultra Fund" or the "Fund") was a mutual fund that invested primarily in mortgage-backed securities. The Fund's investment adviser was Evergreen Investment Management Company, LLC (the "Evergreen Adviser"). From February 2007 through its closing on June 18, 2008, the Ultra Fund overstated its per share net asset value ("NAV") by as much as 17%. The Fund's NAV was overstated because the Evergreen Adviser, through the Fund's portfolio management team, did not properly take into account various readily-available information when recommending valuations to the Evergreen Valuation Committee (whose responsibility it was to value such securities) for certain residential mortgage-backed securities held by the Fund. For example, beginning at least in February 2007, the media widely reported that a benchmark asset-backed derivative index had substantially weakened, with the portion of the index based on subprime mortgages hitting record levels. This was a significant change in the market for securities held by the Ultra Fund, yet the Evergreen Adviser did not take this change into account when valuing mortgage-backed securities. Moreover, at certain times, the Fund's portfolio management team withheld relevant negative information about certain residential mortgage-backed securities the Fund held from the Evergreen Valuation Committee. As a result, certain shareholders redeemed their shares at prices higher than they should have received – to the detriment of remaining shareholders – and certain shareholders purchased shares at higher prices than they should have paid. Moreover, due to its overstated NAV, the Ultra Fund appeared to be performing better than it actually was from February 2007 to June 2008 as compared to similar mutual funds. In terms of performance, the Ultra Fund was consistently ranked as one of the top five to ten funds of the 40-50 funds in its category during this period. If the Ultra Fund's NAV had been accurately reported, its performance would have ranked at or near the bottom of its fund category. Consequently, by causing the Ultra Fund to overstate

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

its NAV from February 2007 to June 2008, the Evergreen Adviser denied the investors who owned Ultra Fund shares during this period and those investors considering purchasing Fund shares the opportunity to consider accurate information about the Fund's performance when deciding whether to retain, redeem,.or purchase those shares.

2. The Ultra Fund's Board of Trustees decided to liquidate the Fund in June 2008 after a three-week period during which the Ultra Fund reduced the prices at which it valued numerous securities it held. Many of these re-pricings resulted not from market-related events but rather from a change in the way the Ultra Fund valued the securities it held. The re-pricings had a substantial negative impact on the Ultra Fund's reported NAV, causing the Fund's reported NAV to decline from $9.20 per share on May 23, 2008, to $7.48 per share on June 18, 2008, the date the Fund's board decided to liquidate the Fund (the "liquidation date"). After substantial reductions in the Fund's NAV on June 10 and 11, 2008, the Evergreen Adviser and its affiliated broker-dealer, Evergreen Investment Services, Inc. (the "Evergreen Distributor"), disclosed to select Ultra Fund shareholders or their financial intermediaries that the decreased NAV was the result of the re-pricings and that the re-pricings may continue. More specifically, the Evergreen Adviser provided information concerning the re-pricings to one of its clients, which promptly sold its position in the Ultra Fund. In addition, the Evergreen Distributor, with the knowledge of the Evergreen Adviser, directed its wholesalers to provide the information concerning the re-pricings that it had obtained from the Evergreen Adviser to: (a) those shareholders, registered representatives and broker-dealers who made incoming calls to the Evergreen Distributor about the recent decreases in the NAV; and (b) each registered representative of another broker-dealer affiliated with the Evergreen Adviser and the Evergreen Distributor who had customers who had invested in the Fund. The Evergreen Distributor also directed its wholesalers to provide this information to the representatives of certain other financial services providers. By limiting the dissemination of this important information, Respondents improperly gave some Ultra Fund shareholders, including customers of one of their own affiliates, an unfair advantage over other shareholders of the Fund. The shareholders who were provided the material nonpublic information were then able to use it in deciding whether to redeem their shares before further potential re-pricings of the securities held by the Fund. In fact, many of the shareholders who received this information then redeemed their shares in the Ultra Fund prior to the liquidation date – and at a higher price than those shareholders who held their shares in the Fund until the liquidation date. At no point during the three week period leading up to the liquidation date did the Respondents disseminate any press release or statement conveying this material, nonpublic information to the general investing public in a manner designed to reach all Ultra Fund shareholders and prospective shareholders. The significant decline in the Ultra Fund's NAV resulting from the re-pricing of securities, combined with the large number of redemption requests that could force the Fund to sell its illiquid securities, ultimately led the Fund's Board of Trustees to decide to liquidate the Fund and make a liquidating distribution to shareholders on June 18.

3. In addition, from as early as January 2008, the Evergreen Adviser caused the Fund to engage in prohibited securities transactions with other mutual funds in the Evergreen family of mutual funds. Finally, the Evergreen Distributor failed to preserve certain business-related electronic communications as required by federal securities laws and in violation of a Commission Order entered against it on September 19, 2007, in a separate enforcement action.

Respondents

4. **Evergreen Investment Management Company, LLC**, is registered with the Commission as an investment adviser (SEC File No. 801-8327), with its principal place of business in Boston, Massachusetts. The Evergreen Adviser is the registered investment adviser for the Evergreen family of mutual funds, including the Ultra Fund, and received payment of advisory fees based on the NAV of each fund. As of December 31, 2008, the Evergreen Adviser had more than $175 billion in assets under management. During the relevant period, the Evergreen Adviser was a wholly-owned subsidiary of Wachovia Corporation and currently is a wholly-owned subsidiary of Wells Fargo & Company, a San Francisco, California-based company whose common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange.

5. **Evergreen Investment Services, Inc.** (the "Evergreen Distributor") is the Evergreen Adviser's affiliated broker-dealer that is registered with the Commission (SEC File No. 8-395), with its principal place of business in Boston, Massachusetts. The Evergreen Distributor is the principal underwriter of the Evergreen family of mutual funds, including the Ultra Fund, utilizing employees known as wholesalers to interact with broker-dealers who sell shares of the various mutual funds directly to customers. During the relevant period, the Evergreen Distributor was a wholly-owned subsidiary of Wachovia Corporation and currently is a wholly-owned subsidiary of Wells Fargo & Company

Related Parties

6. **Evergreen Ultra Short Opportunities Fund** is a series of the Evergreen Fixed Income Trust, an open-end management investment company (*i.e.*, a mutual fund) registered with the Commission (SEC File No. 811-07246). The Ultra Fund invested primarily in commercial and residential fixed and variable rate mortgages-backed securities, including collateralized mortgage obligations, collateralized debt obligations, and other mortgage-related investments.

7. **Wachovia Securities, LLC** is a broker-dealer registered with the Commission (SEC File No. 8-37180), with its principal place of business in St. Louis, Missouri. During the relevant period, Wachovia Securities was a subsidiary of Wachovia Corporation and currently is a majority-owned subsidiary of Wells Fargo & Company.

Background

8. During the period from at least February 2007 through June 2008 ("the relevant period"), the prospectus for the Ultra Fund stated that the Fund would, as a general rule, value each security it owned at the price at which the security could be sold in the market. The prospectus stated that, for each security for which current market prices were available, the Ultra Fund would value the security in accordance with its market price. The prospectus stated that, for each security for which a market price was not readily available or was deemed unreliable, the Ultra Fund would determine a "fair value" for that security under policies

established by the Fund's Board of Trustees. The valuation policies established by the Ultra Fund's Board of Trustees entrusted the determination of the valuation of fair-valued securities to the Evergreen Valuation Committee. The valuation policies directed that the Valuation Committee's membership include the Evergreen Adviser's chief investment officers for fixed income, equity, high yield and international products, as well as representatives from the Evergreen Adviser's legal, risk management and fund administration departments. The valuation policies further required that the Valuation Committee report on a quarterly basis to the Audit Committee of the Board with respect to the results of the Valuation Committee's determinations regarding fair valued securities. Given the nature of the securities held by the Ultra Fund – primarily residential mortgage-backed securities and collateralized debt obligations backed by such securities – there was no market price readily available for many of the Fund's holdings. Accordingly, the process for fair valuing the Fund's holdings was critical to the proper calculation of the Fund's NAV.

9. During the relevant period, pursuant to procedures established by the Fund's Board of Trustees, the Evergreen Valuation Committee employed a three-tier system in fair valuing securities held by the Ultra Fund. Under the first – and, according to the Valuation Committee, the most preferred – tier, securities were valued in accordance with prices provided by a third-party pricing vendor. Under the second tier, such securities were valued in accordance with prices provided by one or more third-party broker-dealers. Under the third – and, according to the Valuation Committee, least preferred – tier, such securities were valued in accordance with the prices recommended by the Fund's portfolio management team. At least as far back as August 2007, and pursuant to the procedures established by the Fund's Board, the Valuation Committee valued certain securities held by the Ultra Fund in accordance with the prices provided by a single broker-dealer or recommended by the Fund's portfolio management team rather than in accordance with the prices provided by a third-party pricing vendor. The Valuation Committee referred to these types of valuations as "vendor overrides."

The Ultra Fund's NAV Was Overstated for at Least 17 Months

10. Since its inception, the Ultra Fund valued many of the securities it held in accordance with prices provided by a vendor such as Standard & Poor's, PricingDirect, Interactive Data Corporation, and Reuters. In addition, at least as far back as August 2007, the Ultra Fund valued one or more of the securities it held in accordance with prices provided either by a single broker-dealer or the Fund's portfolio management team -- sometimes in the form of a vendor override (when a vendor price was available) and sometimes not (when no vendor price was available). However, as early as February 2007, the Ultra Fund failed to take into account in its valuation of certain vendor-priced, broker-priced and/or portfolio management team-priced residential mortgage-backed securities readily-available negative information concerning the value of those holdings. For example, beginning at least in February 2007, the media widely reported that, due to rising mortgage defaults and delinquencies, an index that served as a benchmark measure of the riskiness of residential mortgage-backed securities had substantially weakened, with the portion of the index based on subprime mortgages hitting record levels. In addition, on multiple occasions, the Fund's portfolio management team did not properly factor readily-available data showing an increase in the default or delinquency rate for the subprime residential mortgages backing a collateralized debt obligation security ("CDO") owned by the Fund into the security's valuation. As a result, the Evergreen Adviser caused the Fund's NAV to

be overstated from February 2007 through June 2008.

11. In addition, from at least July 25, 2007, to June 16, 2008, the Valuation Committee valued one or more of the securities owned by the Ultra Fund in accordance with prices obtained from an individual broker-dealer located in Florida, whose method for determining prices it had not reviewed or approved. On various occasions in 2007 and 2008, third-party pricing vendors reduced prices on securities held by the Ultra Fund, but rather than reducing the prices for purposes of calculating the Fund's NAV, the portfolio management team recommended – and the Valuation Committee approved – vendor overrides, through which the Fund valued the securities in question in accordance with prices provided by the Florida broker-dealer rather than in accordance with the prices provided by the vendor. By the middle of May 2008, the Evergreen Valuation Committee learned that: (1) despite its expectation that broker-dealers would only be used to price a security on an exception basis, the Ultra Fund's portfolio management team was using the Florida broker-dealer to price a significant portion of the Fund's holdings; and (2) far less due diligence was being conducted on the Florida broker-dealer than was being conducted on other pricing sources. Fifteen of the sixteen securities valued based on prices provided by the Florida broker-dealer were re-priced downward in June 2008, eight by more than 90%. Ten of these fifteen securities were overvalued from at least as far back as September 2007.

12. Moreover, at certain times from March 2008 to June 2008, the Ultra Fund's portfolio management team caused the Ultra Fund to overstate its NAV by withholding relevant negative information about one or more of the Fund's fair valued securities from the Evergreen Valuation Committee. For example, the Fund owned an interest in a CDO backed by subprime residential mortgage-backed securities issued by a company that shall be referred to herein as "Company A." The Ultra Fund's portfolio management team learned by at least March 27, 2008, that the tranche of this CDO owned by the Ultra Fund would not receive any more cash flow until the senior tranche had been repaid in full. The Fund's portfolio management team failed to disclose this information to the Valuation Committee. On June 10, 2008, the Valuation Committee finally became aware of this information and, based at least in part on this information, the Valuation Committee lowered the valuation on this security from $53.72 (down from an issued value of $100) to $0. The Valuation Committee's decision to lower the value of the Company A security to $0 decreased the Ultra Fund's NAV by nearly $0.10 per share to $8.95 per share. Because day-to-day volatility in the Fund's NAV was very low (for most of the prior year, the Ultra Fund's NAV had consistently been in a range of $9.20-$9.73 per share), this NAV change was significant.

13. In addition, after the close of trading on May 23, 2008, a different Evergreen mutual fund purchased a CDO backed by subprime residential mortgages issued by a company that shall be referred to herein as "Company B" for $9.50 (down from an issued value of $100). At that time, the Ultra Fund owned the same security and was valuing it at $98.93. After learning of this transaction, the Ultra Fund's portfolio management team contacted the selling broker-dealer to determine whether the sale was "distressed" (and thus could potentially be disregarded for purposes of determining the fair value of the security). On May 28, 2008, the broker-dealer responded that the security was "not coming from a distressed seller, just one that wanted to get out." Notwithstanding this response, the Ultra Fund's portfolio management team informed the Valuation Committee that they believed the sale was distressed and did not disclose

the broker-dealer's statement to the Valuation Committee. Based at least in part on the assertion by the portfolio management team that the $9.50 sale was distressed, the Ultra Fund failed to lower the value of this security to $9.50 until June 2, 2008. The June 2, 2008, decision to lower the value of the Company B security to $9.50 decreased the Ultra Fund's NAV by $0.025 per share, which, for the Ultra Fund, was significant.

14. Because its NAV was overstated from February 2007 to June 2008 by as much as 17%, Ultra Fund shareholders who redeemed their Fund shares during this period received more money per share than they should have -- to the detriment of the remaining shareholders -- and those investors who purchased shares during this period paid more per share than they should have. Moreover, due to its overstated NAV, the Ultra Fund appeared to be performing better than it actually was from February 2007 to June 2008. In terms of performance, the Ultra Fund was consistently ranked by a national ranking firm as one of the top five to ten funds of the 40-50 funds in its category during this period based upon its reported NAV. If the Ultra Fund's NAV had been accurately reported, however, its performance would have ranked at or near the bottom of its fund category. Consequently, by causing the Ultra Fund to overstate its NAV from February 2007 through June 2008 (and by at least 10% from February 8, 2008, through June 13, 2008), the Evergreen Adviser denied the investors who owned Ultra Fund shares during this period and those investors considering purchasing Fund shares the opportunity to consider accurate information about the Fund's performance when deciding whether to retain, redeem, or purchase those shares. In addition, as a result of the overstated NAV, the Evergreen Adviser received higher advisory fees than it would have had the NAV been accurately reported.

Selective Disclosure of Material, Nonpublic Information

15. On June 11, 2008, the day after it decided to reprice the Company A security at $0, the Evergreen Valuation Committee decided to stop using vendor overrides for securities held by the Ultra Fund due, in part, to growing concerns about the accuracy of valuations provided by the Fund's portfolio management team. (From August 2007 to June 4, 2008, the Company A security had been valued in accordance with prices provided by the Florida broker-dealer and from June 4, 2008, through June 9, 2008, it was valued in accordance with prices provided by the Fund's portfolio management team.) On June 11, 2008, the Valuation Committee re-valued approximately 11 securities owned by the Ultra Fund. The 11 securities had previously been valued either in accordance with the prices provided by the Florida broker-dealer or in accordance with prices provided by the Fund's portfolio management team. The Valuation Committee re-priced these securities in accordance with the prices provided by a third-party pricing vendor, almost all of which were lower than the previous valuations. This action resulted in a decrease of the Ultra Fund's NAV by $0.12, reducing it to $8.83 per share.

16. By June 12, 2008, the Evergreen Distributor determined that the decreases in the Ultra Fund's NAV might prompt inquiries from the Fund's shareholders as well as from broker-dealers whose customers owned Ultra Fund shares. There had been no public announcement, via a press release or otherwise, regarding the reasons for the Fund's NAV decreases. Consequently, the Evergreen Distributor began to gather from the Evergreen Adviser information about the reasons for the decreasing NAV. On June 12-13, 2008, the Evergreen Distributor prepared "talking points" consisting of material, nonpublic information it received from the Evergreen Adviser to enable its wholesalers to provide information in response to any inquiries about the

NAV from shareholders or broker-dealers. The talking points indicated that the recent declines in the Ultra Fund's NAV were the result of a process of re-pricing of securities rather than market events and that the re-pricings may continue.

17. Specifically, on June 12, 2008, the Evergreen Distributor prepared talking points outlining the Evergreen Valuation Committee's decision on June 10, 2008 to re-price downward the security issued by Company A, the Valuation Committee's June 11 decision to re-price 11 additional securities, and the NAV declines associated with these decisions. The talking points further stated, "We continue to review pricing and will revalue securities as prudently as appropriate in this unique market environment. It is difficult to quantify to what extent we may reprice additional holdings."

18. On June 13, 2008, the Evergreen Distributor prepared a second set of talking points for use in responding to inquiries from shareholders or registered representatives, which stated:

> For the third day in a row, Ultra Short experienced a significant NAV decline. Yesterday's decline of $0.21 or 2.4% has been the largest so far. This NAV drop was the result of 3 additional securities being repriced; the [vendor] provided values are significantly below those at which we had been carrying the positions based on internal estimates of fair value. Over the last three days we have repriced 15 positions in total. As was previously mentioned it is difficult to assess how many additional positions will be subject to repricing. We continue to follow the situation closely and will share information with you as it becomes available.

19. The talking points provided insight into a process that was ongoing. A reasonable investor hearing the talking points would view this information as important in making the decision whether to redeem Ultra Fund shares. Consequently, the information concerning the Fund's process of re-pricing of securities constituted material, nonpublic information.

20. A senior officer of the Evergreen Distributor emailed both the June 12 and the June 13 talking points to most Evergreen Distributor wholesalers for use in responding to incoming telephone calls from shareholders or registered representatives concerning the Ultra Fund's recent NAV drops. Senior officers of the Evergreen Distributor explicitly informed a significant number of the wholesalers that they could convey to registered representatives of broker-dealers and shareholders who called all of the information included in the talking points. On the morning of June 13, 2008, a senior officer of the Evergreen Adviser received a copy of both sets of talking points and understood that the content of these talking points was intended to be shared with any Ultra Fund shareholder or registered representative who made an incoming call to any of the Evergreen Distributor's wholesalers to discuss the Fund's recent NAV decreases. In addition, this senior officer of the Evergreen Adviser forwarded both sets of talking points to an employee of the Evergreen Adviser who served as the client manager for a client of the Evergreen Adviser. The client manager conveyed the content of the talking points to the client, which promptly sold its position in the Ultra Fund.

21. In the early morning of June 13, 2008, citing "last evening's third significant decline in NAV," the Evergreen Distributor instructed its wholesalers assigned to the

Wachovia Securities broker-dealer distribution channel to call each Wachovia Securities registered representative who had any customers who were shareholders of the Ultra Fund. Wachovia Securities was at the time an affiliate of the Evergreen Distributor and the Evergreen Adviser. From June 13 through June 17, 2008, the Evergreen Distributor's wholesalers initiated hundreds of telephone calls to Wachovia Securities registered representatives and relayed the June 12 and June 13 talking points concerning the recent drops in the Ultra Fund's NAV. Multiple wholesalers making these calls told registered representatives that their customers could transfer their Ultra Fund holdings to other Evergreen mutual funds that, according to the wholesalers, did not hold any of the same securities held by the Ultra Fund. From June 13 through June 17, many of the customers of the Wachovia Securities registered representatives who received the information in the talking points redeemed their Ultra Fund shares at an NAV that exceeded the Fund's liquidating per-share NAV of $7.48 per share on June 18. On June 13 alone, approximately 20% of the Ultra Fund shares purchased through the Wachovia Securities channel were redeemed at a price of $8.55, accounting for approximately 53% of all Fund shares redeemed that day. At some point between June 13 and midday on June 17, a senior officer of the Evergreen Distributor informed one or more senior officers of the Evergreen Adviser about the calls made to registered representatives of Wachovia Securities. In addition, starting on June 13, the Evergreen Distributor directed the wholesalers in certain of its other distribution channels to initiate similar outgoing calls to representatives of certain other financial services providers concerning the recent drops in the Ultra Fund's NAV. However, the Evergreen Distributor did not direct the wholesalers in all of its distribution channels to initiate such calls to all financial services providers. Moreover, the Evergreen Distributor failed to make calls to many of the Wachovia Securities registered representatives prior to the Ultra Fund's liquidation date.

22. During the three-week period leading up to the closure of the Ultra Fund on June 18, 2008 (during which time the re-pricing was occurring and the Fund's NAV was dropping from $9.20 per share to $7.48 per share), Respondents never disseminated any press release or statement conveying the material, nonpublic information contained in the talking points to the general investing public in a manner designed to reach all Ultra Fund shareholders and prospective shareholders. Instead, the Evergreen Adviser and the Evergreen Distributor, with the knowledge of the Evergreen Adviser, provided information about the recent decreases in the Fund's NAV to select shareholders or their financial intermediaries. By limiting the dissemination of this important information, Respondents improperly gave some Ultra Fund shareholders, including customers of one of their own affiliates, an unfair advantage over other shareholders of the Fund. The shareholders who were provided the material nonpublic information were then able to use it in deciding whether to redeem their shares before further potential re-pricings of the securities held by the Fund. In fact, many of the shareholders who received this information then redeemed their shares in the Ultra Fund and received a higher price than other shareholders -- including those who did not receive the information -- who held their shares until the Fund's liquidation date on June 18. Because these redemptions were made before the Fund had completed the process of re-pricing securities, the redeeming shareholders received a higher NAV than they should have. Consequently, these redemptions diluted the Ultra Fund's assets and thus harmed the Fund and its remaining shareholders. The significant decline in the Ultra Fund's NAV resulting from the re-pricing of securities, combined with the large number of

redemption requests that could force the Fund to sell its illiquid securities, ultimately led the Fund's Board of Trustees to liquidate the Fund and make a liquidating distribution to shareholders on June 18.

23. During this period, neither the Evergreen Adviser nor the Evergreen Distributor established, maintained, or enforced written policies and procedures reasonably designed to prevent this type of misuse of material, non-public information by persons associated with them – *i.e.*, the disclosure of material, non-public information about a fund they advised or distributed to select shareholders.

Prohibited Securities Transactions

24. Beginning at least on January 23, 2008, the Evergreen Adviser caused other Evergreen mutual funds to purchase securities from the Ultra Fund. These funds were also managed by the Ultra Fund's portfolio management team. In order to make such trades, the Fund was required to follow specific procedures to ensure the transactions did not benefit another Evergreen mutual fund at the expense of the Ultra Fund. Rule 17a-7 under the Investment Company Act allows certain affiliated cross trades despite the general prohibition against affiliated transactions contained in Section 17(a) of the Investment Company Act. Among other things, affiliated cross trades must be executed at a price equal to the average of the highest current independent bid to purchase that security and the lowest current independent offer to sell that security (for securities other than NMS stocks, exchange-traded securities, or securities quoted on the NASDAQ system). Despite this requirement, the Evergreen Adviser caused other Evergreen mutual funds to purchase securities from the Ultra Fund at a price other than that average. In at least some instances, the Fund's portfolio management team did not even obtain the necessary price information to calculate the required average. In addition, these cross trades were made through one or more broker-dealers who received remuneration in connection with these transactions, thus precluding reliance on Rule 17a-7.

25. Moreover, on June 12, 2008, a trader for the Fund's portfolio management team received an indication from a broker-dealer that the broker-dealer would consider paying a higher price for a security held by the Ultra Fund if the broker-dealer would be allowed to re-sell that security to a third party rather than selling it back to another Evergreen mutual fund managed by the portfolio management team. In breach of the Evergreen Adviser's fiduciary duty to the Fund, the trader for the Fund's portfolio management team refused to discuss a higher price and, as a result, the Ultra Fund received less money for this security than it may have if this prospect for a higher offer had been pursued.

Evergreen Distributor Failed to Preserve Text and Instant Messages

26. On September 19, 2007, in a different enforcement action, the Commission issued an order: (a) finding that the Evergreen Distributor had willfully violated Section 17(a) of the Exchange Act and Rule 17a-4(b)(4) thereunder by failing to preserve certain communications related to its business as such, including e-mails, for a period of three years; and (b) ordering the Evergreen Distributor to cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Exchange Act and Rule 17a-4

thereunder. However, from at least September 19, 2007 to August 2008, the Evergreen Distributor issued to approximately 177 of its employees personal digital assistant devices that permitted these employees to send text messages and instant messages related to the Evergreen Distributor's business as such over certain messaging systems that the Evergreen Distributor had not configured for retention within its electronic communications archival system. Consequently, throughout this period, the Evergreen Distributor failed to preserve certain electronic communications in the form of text messages and instant messages related to its business as such.

Violations

27. As a result of the conduct described above, the Evergreen Adviser willfully[2] violated Sections 206(2) of the Advisers Act in that it engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon clients or prospective clients. The Evergreen Adviser and the Evergreen Distributor, with the knowledge and acquiescence of the Evergreen Adviser, disclosed the information about the process of repricing of Ultra Fund holdings to select Ultra Fund shareholders or their financial intermediaries, specifically including shareholders who were customers of an affiliated broker-dealer, and failed to inform the Ultra Fund Board about these disclosures. The Evergreen Adviser knew or should have known that the selective disclosures would lead to substantial redemptions by shareholders at an inaccurately high NAV, which would dilute the Fund, and as a result, this conduct operated as a fraud or deceit upon the Fund.

28. As a result of the conduct described above, the Evergreen Distributor willfully aided and abetted and caused the Evergreen Adviser's violations of Section 206(2) of the Advisers Act in that it knowingly provided the Evergreen Adviser with substantial assistance by making the selective disclosure to certain shareholders of the Ultra Fund.

29. As a result of the conduct described above, the Evergreen Adviser willfully violated Sections 206(2) of the Advisers Act in that it engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon clients or prospective clients. Specifically, by providing an overstated NAV to the Fund (through its failure to factor readily-available negative information into its recommended valuations of certain securities and its recommending valuations for a significant portion of the Ultra Fund's holdings based on prices provided by the Florida broker-dealer), which in turn generated higher advisory fees paid by the Fund, the Evergreen Adviser breached its fiduciary duty to and defrauded the Ultra Fund.

30. As a result of the conduct described above, the Evergreen Adviser willfully violated Section 204A of the Advisers Act in that it failed to establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of its business, to prevent the misuse of material, nonpublic information by it or any person affiliated with it. Specifically, the Evergreen Adviser disclosed material, non-public

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[2] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting Hughes v. SEC, 174 F.2d 969, 977 (D.C. Cir. 1949)).

information about the Ultra Fund to one of its clients, which owned shares in the Fund. In addition, the Evergreen Adviser disclosed material, nonpublic information about the Ultra Fund to an affiliate, the Evergreen Distributor, without taking any steps to ensure that the Evergreen Distributor did not further disclose such information. The Evergreen Adviser's procedures were not reasonably designed to prevent the misuse of material, nonpublic information about the Ultra Fund through the disclosure of this information to, among others, registered representatives of an affiliated broker-dealer for the purpose of further disclosing such information to certain Ultra Fund shareholders.

31. As a result of the conduct described above, the Evergreen Distributor willfully violated Section 15(f) of the Exchange Act in that it failed to establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of its business, to prevent the misuse of material, nonpublic information by it or any person with it. Specifically, the Evergreen Distributor's procedures were not reasonably designed to prevent the misuse of material, nonpublic information about the Ultra Fund through the disclosure of this information to, among others, registered representatives of an affiliated broker-dealer for the purpose of further disclosing such information to certain Ultra Fund shareholders.

32. As a result of the conduct described above, the Ultra Fund violated Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act, and the Evergreen Adviser willfully aided and abetted and caused such violation. Specifically, by improperly pricing certain securities held by the Fund, the Evergreen Adviser caused the Ultra Fund to: (a) materially overstate its NAV from as early as February 1, 2007, through June 18, 2008; and (b) sell and redeem its shares at a price other than its current net asset value.

33. As a result of the conduct described above, the Evergreen Distributor willfully violated Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act in that, while acting as Ultra Fund's principal underwriter, it sold and redeemed shares of the Ultra Fund from at least June 13, 2008, through June 18, 2008, at a price that was not based on the current NAV of those shares in light of the Fund's overstated NAV.

34. As a result of the conduct described above, the Evergreen Adviser also willfully violated Section 206(2) of the Advisers Act in that it engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon clients or prospective clients. Specifically, by rejecting the prospect of an offer from a broker-dealer to pay a higher price for a particular security held by the Ultra Fund on the condition that the broker-dealer would be allowed to purchase the security outright rather than being required to immediately re-sell the security to another Evergreen mutual fund advised by the Evergreen Adviser, the Evergreen Adviser failed to seek to obtain best execution of the trade for the Ultra Fund and favored another client over the Ultra Fund in breach of its fiduciary duty.

35. As a result of the conduct described above, one or more Evergreen funds violated Section 17(a)(2) of the Investment Company Act, and the Evergreen Adviser willfully aided and abetted and caused such violations by causing such funds, acting as principal, to knowingly purchase securities from the Ultra Fund (other than NMS stocks, exchange-traded securities, or securities quoted on the NASDAQ system). The transactions

were not exempt from the prohibition by virtue of Rule 17a-7 because the trades were not executed at a price equal to the average of the highest current independent bid to purchase that security and the lowest current independent offer to sell that security and that were made through one or more broker-dealers who received remuneration in connection these transactions.

36. As a result of the conduct described above, the Evergreen Adviser willfully violated Section 34(b) of the Investment Company Act because it was responsible for the inclusion of untrue statements of material fact in a registration statement, application, report, account, record, or other document filed or transmitted pursuant to the Investment Company Act, or omitted to state therein, any fact necessary in order to prevent the statements made therein, in the light of the circumstances under which they were made, from being materially misleading. Specifically, in reviewing and approving the registration statements filed with the Commission by the Evergreen Distributor and the Fund prospectus incorporated therein, the Evergreen Adviser misrepresented the Fund's performance and NAV beginning on at least February 1, 2007.

37. The Evergreen Distributor willfully violated Section 17(a) of the Exchange Act and Rule 17a-4(b)(4) thereunder, because it failed to preserve for three years certain communications related to its business as such, including text messages and instant messages.

Undertakings

38. Independent Compliance Consultant.

a. The Evergreen Adviser and Evergreen Distributor shall retain, within 30 days of the date of entry of the Order, the services of an Independent Compliance Consultant not unacceptable to the staff of the Commission or to a majority of the independent Trustees of any Evergreen fund. The Independent Compliance Consultant's compensation and expenses shall be borne exclusively by the Evergreen Adviser or its affiliates. The Evergreen Adviser and Evergreen Distributor shall require the Independent Compliance Consultant to conduct a comprehensive review of: (1) the Evergreen Adviser's procedures for valuing portfolio securities and the enforcement of same; (2) the Evergreen Adviser's and the Evergreen Distributor's policies and procedures for preventing the misuse of material, nonpublic information and the enforcement of same; and (3) the Evergreen Adviser's policies and procedures for preventing prohibited cross trades of its registered investment company clients and the enforcement of same. The Evergreen Adviser and Evergreen Distributor shall cooperate fully with the Independent Compliance Consultant and shall provide the Independent Compliance Consultant with access to files, books, records, and personnel as reasonably requested for the review.

b. The Evergreen Adviser and Evergreen Distributor shall require that, at the conclusion of the review, which in no event shall be more than 180 days after the date of entry of the Order, the Independent Compliance Consultant shall submit a Report to it, the Trustees of each Evergreen fund, and the staff of the

Commission. The Report shall address the issues described in the subparagraph set forth above, and shall include a description of the review performed, the conclusions reached, the Independent Compliance Consultant's recommendations for changes in or improvements to policies and procedures of the Evergreen Adviser, the Evergreen Distributor and each Evergreen fund, and a procedure for implementing the recommended changes in or improvements to those policies and procedures.

c. The Evergreen Adviser and Evergreen Distributor shall adopt all recommendations contained in the Report of the Independent Compliance Consultant; provided, however, that, within 210 days after the date of entry of the Order, the Evergreen Adviser and shall, in writing, advise the Independent Compliance Consultant, the Trustees of each Evergreen fund and the staff of the Commission of any recommendations that one or the other of them considers to be unnecessary or inappropriate. With respect to any such recommendation, neither the Evergreen Adviser nor the Evergreen Distributor need 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 the Evergreen Adviser or the Evergreen Distributor's policies and procedures on which the Evergreen Adviser or the Evergreen Distributor and the Independent Compliance Consultant do not agree, such parties shall attempt in good faith to reach an agreement within 240 days of the date of entry of the Order. In the event the Evergreen Adviser or the Evergreen Distributor and the Independent Compliance Consultant are unable to agree on an alternative proposal, the Evergreen Adviser and Evergreen Distributor will abide by the determinations of the Independent Compliance Consultant.

e. Neither the Evergreen Adviser nor the Evergreen Distributor, either acting alone or in concert, (i) shall have the authority to terminate the Independent Compliance Consultant, without the prior written approval of the majority of the independent Trustees of each Evergreen fund and the staff of the Commission. The Evergreen Adviser shall compensate the Independent Compliance Consultant, and persons engaged to assist the Independent Compliance Consultant, for services rendered pursuant to the Order at their reasonable and customary rates. Neither the Evergreen Adviser nor the Evergreen Distributor shall be in or have an attorney-client relationship with the Independent Compliance Consultant and neither the Evergreen Adviser nor the Evergreen Distributor shall seek to invoke the attorney-client or any other doctrine or privilege to prevent the Independent Compliance Consultant from transmitting any information, reports, or documents to the Trustees or to the Commission.

f. The Evergreen Adviser and Evergreen Distributor shall require that the Independent Compliance Consultant, for the period of the engagement and for a period of two years from completion of the engagement, shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Evergreen Adviser, the Evergreen Distributor or any of their present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. The Evergreen Adviser and Evergreen Distributor shall require that any firm with which the Independent Compliance Consultant is affiliated in the performance of his or her duties under the Order shall not, without prior written consent of the independent Trustees and the staff of the Commission, enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Evergreen Adviser, the Evergreen Distributor or any of their 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.

39. The Evergreen Adviser and the Evergreen Distributor have undertaken to make, within 10 business days of the entry of this Order, a payment, jointly and severally, to the Fair Fund established pursuant to this Order in the amount of $33,000,000 to compensate shareholders for harm caused by the conduct set forth in this Order. This amount shall be deposited into the same account to be opened in the name of the Ultra Short Opportunities Fund Qualified Settlement Fund pursuant to Paragraphs IV.H. and IV.I. below.

40. The Evergreen Adviser has undertaken to review other Evergreen investment companies that held either the same securities as the Ultra Fund or securities for which the Ultra Fund portfolio management team was responsible for recommending valuations to determine the extent of any errors in the calculations of such investment companies' NAVs. To the extent the NAV of such funds was materially overstated as a result of errors in the valuations of such securities, the Evergreen Adviser has undertaken to compensate shareholders for any harm caused in the same manner in which it will compensate Ultra Fund shareholders for the harm caused by the mispricing of that fund as set forth in this Order in a manner subject to the review and approval of the Commission staff. To the extent that the NAV of such funds was not materially overstated as a result of such errors, the Evergreen Adviser has undertaken to compensate the funds for any harm caused by processing transactions at an erroneous NAV. The Evergreen Adviser has also undertaken to report to the Commission staff the results of the review referred to above and any remedial steps taken in response thereto within 90 days of the entry of this Order.

41. The Evergreen Adviser has undertaken to review any cross trades that occurred during the relevant period between the Ultra Fund and any other Evergreen fund to determine whether they violate Section 17 of the Investment Company Act and, to the extent that such violations caused harm to any Evergreen fund, to compensate such fund or its shareholders for such harm in a manner subject to the review and approval of the Commission staff. The Evergreen Adviser has also undertaken to report to the Commission staff the results of the review referred to above and any remedial steps taken in response thereto within 90 days of the entry of this Order.

42. Distribution of Funds.

a. Respondents shall be responsible for self administering the distribution of sums ordered as disgorgement, prejudgment interest and civil penalty in Paragraphs IV.H. and IV.I. below, as well as the payment Respondents have undertaken to make to the Fair Fund established pursuant to this Order referenced in Paragraph III.39. above (collectively, the "Settlement Funds").

b. Respondents shall identify and make distributions to the Ultra Fund shareholders using the Ultra Fund's records and those of its transfer agent to identify all direct investors, whether in direct purchase accounts, disclosed accounts, or non-disclosed accounts. Respondents will also identify and make distributions to the beneficial owners of Ultra Fund shares held in omnibus accounts. To that end, Respondents will use their best efforts to identify omnibus accounts that are reflected on the Ultra Fund's records and those of its transfer agent, determine the shares traded by each such omnibus account and estimate the total amount of money to be allocated to each such omnibus account using the methodology set forth in this Order. The Respondents will conduct an "Outreach Process" by which they will contact the intermediary associated with each omnibus account with provisional distributions of $1,000 or more and request records for each account underlying the omnibus account, including, but not limited to, the closing share balance on January 31, 2007, any trades thereafter until the fund was liquidated, and the underlying account holder's name, address and tax identification number(s). In the event that, after receiving such data, Respondents become aware that an account underlying an omnibus account is itself an omnibus account, Respondents will use reasonable efforts to obtain the foregoing data through an Outreach Process, as described above, with respect to the intermediary associated with that underlying omnibus account. Respondents are not required to contact the intermediaries associated with (i) omnibus accounts with provisional distributions of less than $1,000; or (ii) omnibus accounts that are held by an omnibus account within an omnibus account (*i.e.*, no more than a second level omnibus account). As an alternative to providing Respondents with underlying account identifying information, omnibus account intermediaries may provide the relevant account activity data to Respondents pursuant to this paragraph by using unique identification numbers for underlying accounts. Respondents will apply the distribution methodologies described below to that underlying account data and shall provide the results to the intermediary sufficient for the intermediary to allocate distribution amounts to the individual underlying accounts consistent with the methodologies. Upon receipt by the Respondents of a certification by the account intermediary that it will distribute the funds consistent with the results provided, Respondent will make the appropriate distribution to the intermediary which shall then distribute the amounts to the underlying accounts within 45 days. Such intermediaries shall also certify that they will return any undistributed amounts to the Respondents within 90 days of disbursement of such amounts by the Respondents. Any such undistributed amounts returned to Respondents will be returned to the Settlement Funds. Under this paragraph, omnibus account intermediaries shall have 10 calendar days after being contacted by Respondents to notify Respondents as to whether they intend to produce the requested information pursuant to this paragraph and shall have 60 calendar days thereafter to provide the requested data to Respondents. Respondents will pay the reasonable administrative costs incurred by omnibus account intermediaries for providing data pursuant to this paragraph, and such costs will not be paid from the Settlement Funds. Requests for reimbursement from omnibus account intermediaries shall be made to Respondents within 60 days of submission of all requested records to Respondents. Any omnibus account intermediary which elects to make the distribution to its underlying account holders pursuant to this paragraph shall bear all costs and expenses associated with that distribution.

c. With respect to direct accounts for which Respondents have transactional data, but do not have the complete account holder's name, address, and tax identification number ("non-disclosed accounts"), Respondents will conduct an Outreach Process by which they will contact the intermediary associated with each non-disclosed account for which a payment of funds is required under the methodology below and request such information for each account. When the Respondents receive such information, they will make the distribution to each account. As an alternative to providing Respondents with the account holder identifying information, a non-disclosed account intermediary may provide Respondents with a certification that it will distribute the funds from Respondents to the account holder and that they will return any undistributed amounts to the Respondents. If a certification is received, Respondents will make the appropriate distribution pursuant to this Order to the non-disclosed account intermediary which shall then distribute the amounts to the account holder within 45 days. Such intermediaries shall also certify that they will return any undistributed amounts to the Respondents within 90 days of disbursement of such amounts by the Respondents. Any undistributed amounts returned to Respondents by an intermediary will be returned to the Settlement Funds. Under this paragraph, non-disclosed account intermediaries shall have 10 calendar days after being contacted by Respondents to notify Respondents as to whether they intend to produce the requested information pursuant to this paragraph and shall have 30 calendar days thereafter to provide the requested data to Respondents. Respondents will pay the reasonable administrative costs incurred by non-disclosed account intermediaries for providing data pursuant to this paragraph, and such costs will not be paid from the Settlement Funds. Requests for reimbursement from non-disclosed account intermediaries shall be made to Respondents within 60 days of submission of all requested records to Respondents. Any non-disclosed account intermediary which elects not to provide account data and elects to make the distribution to its account holders pursuant to this paragraph shall bear the costs and expenses associated with that distribution.

d. The Respondents will keep records of each contact attempt for information from an omnibus account and non-disclosed account, each response received, if any, and the reason for not providing the requested information, if any. The Respondents will provide the Commission staff with information relating to each omnibus or non-disclosed account intermediary that does not provide the requested information under Paragraph III.42.b. and/or 42.c. This information will be provided to the staff within 5 business days after Respondents receive notice from any account intermediary that it will not provide the requested information under Paragraph III.42.b. and/or 42.c. or if no response is received, within 5 business days after the 10 day period provided for such response under Paragraph III.42.b. and/or 42.c. elapses.

e. For each omnibus account with a provisional distribution less than $1,000 for which Respondents do not obtain records for the underlying accounts, the amount of Settlement Funds allocated to that omnibus account will remain in the Settlement Funds. In each instance where the Respondents' Outreach Process to an omnibus or non-disclosed account intermediary does not yield the data necessary to make a distribution to the investors who held Ultra Fund shares in the associated omnibus or non-disclosed account within 70 days of the request for such data (or such later date agreed to between Respondents and the omnibus account intermediary), the Respondents shall have the discretion, with the approval of the Commission staff, to consider and implement other means of distribution to the underlying shareholders. If the Commission staff and Respondents are unable to agree on an alternative means of distribution for any such omnibus account within 250 days of the entry of the Order, the amount of Settlement Funds allocated to the associated omnibus or non-disclosed account will remain in the Settlement Funds.

f. Retirement Plans:

"Retirement Plan" as used in this Order means an employee benefit plan, as such plans are defined in section 3(3) of ERISA, 29 U.S.C. § 1002(3), which is not an Individual Retirement Account (IRA), whether or not the plan is subject to Title I of ERISA.

Assets of Retirement Plans are held in trust by a trustee, and the trust is the legal owner of the assets. Plan fiduciaries and intermediaries, as defined in Department of Labor Field Assistance Bulletin No. 2006-01, April 19, 2006 (the "Field Assistance Bulletin"), of Retirement Plans are to distribute the monies received in accordance with their legal, fiduciary, and contractual obligations and consistent with guidance issued by the Department of Labor, including, but not limited to, the Field Assistance Bulletin.

For the purposes of this Order, each Retirement Plan itself (and not the individual plan participants) shall be treated as the shareholder to receive the distribution, if any, of the Settlement Funds from Respondents.

The fiduciary of a Retirement Plan receiving a distribution may distribute it pursuant to one of the following four alternatives: (1) Retirement Plan fiduciaries may allocate the distribution to current and former participants in the Retirement Plan using the methodology referenced in paragraphs Paragraphs III.42.g. and

III.42.h. of this Order. Respondents will provide a description of the methodology to Retirement Plan fiduciaries that wish to utilize this option; (2) Retirement Plan fiduciaries may allocate the distribution pro rata (based on total account balance) among the accounts of all persons who are currently participants in the Retirement Plan (whether or not they are currently employees); (3) Retirement Plan fiduciaries may allocate the distribution per capita among the accounts of all persons who are currently participants in the Retirement Plan (whether or not they are currently employees); (4) To the extent that none of the three preceding alternatives is administratively feasible because the costs of effecting the allocation exceed the amount of the distribution, Retirement Plan fiduciaries may, to the extent permitted by the Retirement Plan, use the distribution amount to pay the reasonable expenses of administering the plan.

In view of, among other things, alternative methodologies available to Retirement Plans, plan fiduciaries and/or intermediaries will not be reimbursed the costs and expenses associated with administering the distribution received pursuant to this Order.

g. Within 270 days of the date of this Order, Respondents shall cause the distribution of the portion of the Settlement Funds that is necessary to compensate those Ultra Fund shareholders who were harmed as a result of the mispricing of the Ultra Fund's NAV from February 2007 through June 18, 2008, utilizing the methodology that has been reviewed and approved by the Commission staff. However, any material changes, additions or adjustments to that methodology must be reviewed and approved by the staff.

h. Within 280 days of the date of this Order, Respondents shall cause any remaining amount of the Settlement Funds to be distributed according to the following methodology: (1) all Ultra Fund shareholders who redeemed their shares on June 18, 2008, shall receive a pro rata share of the remaining amount of the Settlement Funds up to an amount equal to \$0.17 per share; and, if Settlement Funds remain, (2) all Ultra Fund shareholders who redeemed their shares on June 17, 2008 or June 18, 2008, shall receive a pro rata share of the remaining amount of the Settlement Funds up to an amount equal to \$0.29 per share; and, if Settlement Funds remain, (3) all Ultra Fund shareholders who redeemed their shares on June 16, 2008, June 17, 2008 or June 18, 2008, shall receive a pro rata share of the remaining amount of the Settlement Funds. Respondents shall not be required to make any disbursement to any Ultra Fund shareholder if that shareholder is due less than \$10 pursuant to the method approved by the Commission staff. Furthermore, Respondents shall not pay any Ultra Fund shareholder pursuant to this methodology any amount in excess of the difference between the Fund's reported NAV on June 13, 2008 and the actual NAV at which the shareholder redeemed his or her shares.

i. Respondents shall not be required to make any disbursement to any Ultra Fund shareholder if that shareholder is due less than \$10 in the aggregate under Paragraphs III.42.g. and III.42.h. above. In order to implement this de minimis distribution amount, Respondents will apply the Gross-Up Formula. The Gross-Up Formula requires that the distributions be ranked in descending order of the size of the provisional distribution. Respondents will then calculate the total amount of the distributions that were calculated to be less than $10 (the "de minimis distribution"). Respondent will then redistribute the de minimis distribution in sequence to the accounts with the largest distributions less than $10, sequentially assigning a distribution of $10 to each account until the de minimis distribution is depleted.

j. All distribution checks shall bear a stale date of 90 days and shall be voided thereafter.

k. Any excess amounts, and any amounts Respondents are unable, due to factors beyond their control, to pay to any affected Ultra Fund shareholder, and any sums that are not paid to any Ultra Fund shareholder who is due less than $10, shall be transferred to the Securities and Exchange Commission. Such payment shall be made when the final accounting is submitted and shall be: (i) made by United States postal money order, certified check, bank cashier's check or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) 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 (iv) submitted under cover letter that identifies the Evergreen Adviser and the Evergreen Distributor as the 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 John T. Dugan, Associate Director, Division of Enforcement, Securities and Exchange Commission, 33 Arch Street, 23rd Floor, Boston, MA 02110.

l. Respondents may pay for any tax liabilities of the Settlement Funds from the Settlements Funds. Respondents agree to be responsible for all tax compliance responsibilities associated with the Settlement Funds and may retain any professional services necessary. The costs and expenses of any such professional services shall be borne by Respondents and shall not be paid out of the Settlement Funds. Respondents shall also retain the services of and be exclusively responsible for the compensation and expenses of an independent third party not unacceptable to the Commission's staff. The independent third party shall, at least 15 business days prior to the date Respondents make any distribution described in Paragraphs III.42.g. and/or III.42.h. above to the Ultra Fund shareholders who are due $10 or more, submit for the Commission staff's review an initial accounting and certification of the payments to be made to shareholders pursuant to this Order. The initial accounting and certification shall be in a form not unacceptable to the Commission's staff, and shall include: (i) each payee's name and address; (ii) the amount to be paid to each payee; and (iii) the expected date of each payment.

m. Within 180 days of the date Respondents effect the distributions described above, Respondents shall submit to the Commission staff for the Commission's approval a final accounting and certification of the disposition of the monies paid pursuant to and referenced in this Order. The final accounting and certification shall be in a form not unacceptable to the Commission's staff, and shall include: (i) each payee's name and address; (ii) the amount paid to each payee; (iii) the date of each payment; (iv) the check number or other identifier of money transferred; (v) the date and amount of any returned payment; (vi) a description of any effort to locate a prospective payee whose payment was returned, or to whom payment was not made due to factors beyond Respondents' control; (vii) any amounts to be paid to the Commission with respect to any prospective payee who Respondents were unable to pay due to factors beyond their control, or who would be entitled to less than $10 under the method set forth above; and (viii) a final statement totaling all payments and anticipated payment to the Commission, which shall reconcile with the amounts ordered under Paragraph IV.H. and Paragraph IV.I below plus the payment referenced in Paragraph III.39. above. Any and all supporting documentation for the accounting and certification shall be provided to the Commission's staff upon request. Respondents shall cooperate with reasonable requests for information in connection with the accounting and certification.

n. After Respondents have submitted the final accounting to the Commission staff, the staff shall submit the final accounting to the Commission for approval and shall request Commission approval to send the remaining residual amount to the United States Treasury.

43. Certification. No later than 24 months after the date of entry of the Order, the chief executive officer of Respondents shall each certify to the Commission, in writing, that Respondent has fully adopted and complied in all material respects with the undertakings set forth in this section and with the recommendations of the Independent Compliance Consultant or, in the event of material non-adoption or non-compliance, shall describe such material non-adoption and non-compliance.

44. Recordkeeping. Respondents shall each preserve for a period 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 Respondent's compliance with the undertakings set forth above.

45. Deadlines. For good cause shown, the Commission's staff may extend any of the procedural dates set forth above.

Respondents' Cooperation and Remedial Acts

46. In determining to accept the Respondents' Offer, the Commission considered the cooperation afforded to the Commission staff and the remedial acts undertaken by Respondents. In determining whether to accept the Offer, the Commission has further considered the undertakings set forth in Paragraph III.39., Paragraph III.40., and Paragraph III.41. above.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in the Respondents' Offer. It is hereby ORDERED that:

A. Pursuant to Section 203(e) of the Advisers Act, the Evergreen Adviser is hereby censured. Pursuant to Section 15(b)(4) of the Exchange Act, the Evergreen Distributor is hereby censured.

B. Pursuant to Section 203(k) of the Advisers Act, the Evergreen Adviser shall cease and desist from committing or causing any violations and any future violations of Sections 204A and 206(2) of the Advisers Act.

C. Pursuant to Section 9(f) of the Investment Company Act, the Evergreen Adviser shall cease and desist from committing or causing any violations and any future violations of Sections 17(a) and 34(b) of the Investment Company Act, and Rule 22c-1 promulgated pursuant to Section 22(c) of the Investment Company Act.

D. Pursuant to Section 21C of the Exchange Act, the Evergreen Distributor shall cease and desist from committing or causing any violations and any future violations of Sections 15(f) and 17(a) of the Exchange Act and Rule 17a-4 thereunder.

E. Pursuant to Section 203(k) of the Advisers Act, the Evergreen Distributor shall cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act.

F. Pursuant to Section 9(f) of the Investment Company Act, the Evergreen Distributor shall cease and desist from committing or causing any violations and any future violations of Rule 22c-1 promulgated pursuant to Section 22(c) of the Investment Company Act.

G. The Evergreen Adviser and the Evergreen Distributor shall comply with the undertakings set forth in Paragraph III.38., Paragraph III.42., Paragraph III.43., and Paragraph III.44. above.

H. IT IS FURTHER ORDERED that Respondent Evergreen Adviser shall, within ten business days of the entry of this Order, pay: (1) disgorgement in the total amount of $2,860,000 plus prejudgment interest thereon in the amount of $265,000; and (2) pursuant to Sections 203(e) and 203(i) of the Advisers Act and Sections 9(b) and 9(d) of the Investment Company Act, a civil penalty in the amount of $2,000,000 into an account opened in the name of the Ultra Short Opportunities Fund Qualified Settlement Fund consistent with the provisions of Paragraph III.42. above.

I. IT IS FURTHER ORDERED that Respondent Evergreen Distributor shall, within ten business days of the entry of this Order, pay: (1) disgorgement in the amount of $1; and (2), pursuant to Section 21B(a) of the Exchange Act and Section 203(i) of the Advisers Act, a civil penalty in the amount of $2,000,000 into the same account opened in the name of the Ultra Short Opportunities Fund Qualified Settlement Fund referenced in Paragraph IV.H. above and consistent with the provisions of Paragraph III.42. above.

J. There shall be, pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, a Fair Fund established for the funds described in paragraphs IV.H. and IV.I. Regardless of whether any distribution is made from such Fair Fund, 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 penalties, Respondents Evergreen Adviser and Evergreen Distributor agree that they shall not, after offset or reduction in any Related Investor Action based on the Respondents' payment of disgorgement in this action and the payment described in Paragraph III.39. above, further benefit by offset or reduction of any part of the Evergreen Adviser or the Evergreen Distributor's payment of civil penalties in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, the Evergreen Adviser and the Evergreen Distributor agree that they shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the United States Treasury or to a Fair Fund, as the Commission directs. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalties imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against the Evergreen Adviser, the Evergreen Distributor or their affiliates, or all of them, 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.

K. The obligations to pay prejudgment interest, disgorgement, and penalty are not fully satisfied until all funds are disbursed and the final accounting is approved by the Commission and any residual has been transferred to the Commission for disbursement to the United States Treasury. In the event the Commission must enforce these obligations to pay, additional interest shall accrue on the ordered amounts pursuant to Rule 600 of the Commission's Rules of Practice, 17 C.F.R. § 201.600, and/or 31 U.S.C. § 3717 until the obligations are paid in full.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey and
Commissioner Paredes
Disapproved

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60071 / June 8, 2009

INVESTMENT ADVISERS ACT OF 1940
Release No. 2889 / June 8, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13356

In the Matter of Michael A. Callaway, Respondent.	ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b)(6) OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTIONS 203(f) AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940 AND IMPOSING A CEASE-AND-DESIST ORDER

I.

On January 30, 2009, the Securities and Exchange Commission ("Commission") instituted public administrative and cease-and-desist proceedings pursuant to Section 15(b)(6) of the Securities Exchange Act of 1934 ("Exchange Act") and Sections 203(f) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") against Respondent Michael A. Callaway ("Callaway" or "Respondent").

II.

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 Making Findings and Imposing Remedial Sanctions Pursuant to Section 15(b)(6) of the Securities Exchange Act of 1934 and Sections 203(f) and 203(k) of the Investment Advisers Act of 1940 and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

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

A. SUMMARY

From at least 2000 through 2005 (the "relevant period"), Merrill Lynch, Pierce, Fenner & Smith Inc. ("Merrill Lynch"), through its pension consulting services advisory program, breached its fiduciary duty to certain of the firm's pension fund clients and prospective clients by omitting to disclose material information. During this time period, Respondent was an investment adviser representative for Merrill Lynch, and in that capacity owed a fiduciary duty to the firm's pension fund clients to whom Respondent provided advice. Those clients included public pension funds seeking advice in developing appropriate investment strategies and in selecting investment managers to manage the assets entrusted to their care. In providing such advice, Respondent omitted to disclose to some of the firm's pension consulting clients that certain managers included in search results had not been vetted and approved in advance by Merrill Lynch Consulting Services in New Jersey. Respondent also failed to disclose material facts involving a conflict of interest inherent in clients' use of Merrill Lynch's transition management group. In addition, up to and including 2003, Respondent failed to disclose fully when entering into an arrangement for directed brokerage the facts creating a material conflict of interest inherent in recommending the use of directed brokerage to pay hard dollar fees. Respondent's fee disclosure policies were consistent with those of Merrill Lynch and Merrill Lynch Consulting Services at the time and, after 2003, in some instances exceeded those policies. Moreover, Respondent's conduct described herein was known to Merrill Lynch and to Merrill Lynch Consulting Services, which never directed Respondent to make further disclosures. However, by omitting to disclose the aforesaid facts to his clients, Respondent aided and abetted and caused Merrill Lynch's violation of Section 206(2) of the Advisers Act.

B. RESPONDENT AND OTHER RELEVANT ENTITIES

Michael A. Callaway, age 57, of Ponte Vedra, Florida, during the relevant period was a Senior Vice President and Financial Advisor at Merrill Lynch, an investment adviser representative, and head of Merrill Lynch's Ponte Vedra, Florida office. Callaway was employed by Merrill Lynch from 1976 until his retirement in September of 2008. During the relevant period, Callaway and a team of approximately ten Merrill Lynch employees, including three other investment adviser representatives in Merrill Lynch's Ponte Vedra, Florida office (the "Ponte Vedra office"), provided advisory services to close to 100 public pension fund clients in Florida. During the relevant time period, Callaway was licensed with FINRA and was a registered representative associated with Merrill Lynch's broker-dealer as well as an associated person of Merrill Lynch's investment adviser.

[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.

Merrill Lynch, Pierce, Fenner & Smith Inc. ("Merrill Lynch") is the wholly-owned principal operating subsidiary of the holding company, Merrill Lynch & Co. Merrill Lynch has been registered with the Commission as a broker-dealer since March 12, 1959, and as an investment adviser since December 8, 1978.

Merrill Lynch Consulting Services is an advisory program offered under the auspices of Merrill Lynch's Global Wealth Management Group, and provides advisory services to high net worth and institutional clients, including public pension funds.

C. FACTS

From at least 2000 through 2005, Merrill Lynch, through its Consulting Services program, provided advisory services to high net worth and institutional clients, including public pension funds. As an integral part of these services, it assisted clients in developing appropriate investment policies and in identifying asset allocations to meet their individual needs. Merrill Lynch also monitored clients' existing money managers to provide information to clients on whether the managers' performances remained consistent with the clients' investment objectives. It also helped clients to identify and evaluate new money managers so that the clients could select one or more such managers for the discretionary management of their accounts.

During the relevant period, Respondent, as part of the Merrill Lynch Consulting Services program, worked with a team of approximately ten Merrill Lynch employees that provided advisory services to close to 100 public pension fund clients in Florida, including many municipal employees, police and firefighters' pension funds. The headquarters for Merrill Lynch Consulting Services was located in Jersey City, New Jersey, and provided support to this office and to other investment adviser representatives throughout the country who provided advisory services. During the relevant period, Respondent breached his fiduciary duty to the firm's pension fund clients and prospective clients by failing to disclose the material information described below.

The Manager Identification Process

During the relevant period, Respondent failed to inform some clients that certain managers included in search results given to clients were not vetted and approved in advance by Merrill Lynch Consulting Services in New Jersey.

Written and oral communications that Respondent provided to his clients, taken together with various Merrill Lynch documents of which Respondent was or should have been aware, described the typical procedure for identifying new money managers for Respondent's clients as based upon extensive research by a team of experienced researchers at Merrill Lynch Consulting Services headquarters in New Jersey. Respondent's clients were further informed that these researchers would identify suitable money managers for the client based upon the client's specific investment objectives and risk tolerance for the portfolio intended to be managed by the new manager. Respondent further represented to clients that managers presented to them in search results had been fully vetted by Merrill Lynch Consulting Services in New Jersey. The documents provided by Merrill Lynch Consulting Services to Respondent's clients regarding this service repeatedly referred to Merrill Lynch's large research staff and capabilities, giving the impression that those resources were deployed for every client's money manager search.

The Ponte Vedra office's procedures for performing manager searches, however, deviated from these descriptions with respect to some clients. Contrary to Merrill Lynch's disclosures, certain money managers were included in search results provided to some clients of Respondent's office even though they were not vetted and approved in advance by Merrill Lynch Consulting Services. Respondent was responsible for placing these managers on the Ponte Vedra list, thereby allowing them to be included in search results presented to those clients. Merrill Lynch Consulting Services was aware that Respondent recommended real estate managers who had not been vetted, because Merrill Lynch did not offer its research service for real estate managers. On occasion, Respondent and other consultants in his office also recommended some money managers without Merrill Lynch's written prior approval. In both types of recommendations, Respondent's identification process deviated from disclosures clients received about that process.

Based on the above, Respondent, at a minimum, recklessly omitted to disclose relevant information to some Merrill Lynch Consulting Services clients.

Transition Management

During the relevant period, Respondent also failed to inform clients that Merrill Lynch Consulting Services, and consequently, Respondent, received compensation from their use of Merrill Lynch's transition management desk. Transition management was a service offered by Merrill Lynch's Transition Management group, a separate unit of Merrill Lynch, to clients in the process of terminating one money manager and hiring another. Without the services of a transition manager, the money manager being terminated would sell the shares held by the fund that the new money manager did not want in its portfolio and transfer the proceeds from those sales to the client's account. The new money manager would then use these proceeds to purchase securities for its portfolio on behalf of the client. Merrill Lynch's transition management desk represented that it could manage a transition more efficiently and cost-effectively by offering cross trades and reduced commission costs. Merrill Lynch was engaged to provide transition management services to approximately ten clients of Respondent between July 2000 and the end of 2005.

Respondent failed to disclose, however, that Merrill Lynch Consulting Services and thus he received a portion of the commissions for the transitioned shares. Because prior to November 2005 they were not explicitly made aware that Merrill Lynch Consulting Services and Respondent received a portion of these commissions, clients were unable to evaluate whether Respondent's recommendation of Merrill Lynch's transition management services was disinterested.

Based on the above, Respondent negligently failed to ensure that the conflicts of interest inherent in the recommendation of transition management were disclosed to the Consulting Services clients he served.

Directed Brokerage

During the relevant period, Merrill Lynch Consulting Services charged for its services on a fixed fee basis, with the amount charged to each client set forth in a written agreement. Clients could pay in cash (referred to as "hard dollars") or through "directed brokerage." Directed brokerage was a contractual arrangement whereby the clients directed money managers to execute trades through Merrill Lynch's institutional trading desk, consistent with the money managers' best execution obligations. In return, these clients received credit for a portion of the commissions generated by these trades against the hard dollar fee owed to Merrill Lynch Consulting Services. Portions of the commissions generated by such trades were paid to Merrill Lynch Consulting Services and, therefore, to Respondent.

Under Merrill Lynch's standard directed brokerage relationship, Merrill Lynch Consulting Services and Respondent potentially could receive and, in fact, often did receive significantly more revenues from the directed brokerage commissions than the fees they would have received if clients had elected to pay only with hard dollars. Portions of the commissions generated by such trades were received by Merrill Lynch Consulting Services, and, consequently, increased Respondent's own compensation. Up to and including 2003, Respondent failed fully to disclose when entering into an arrangement for directed brokerage the fact that Merrill Lynch Consulting Services, and therefore, Respondent himself would receive a financial benefit if his clients entered into a directed brokerage relationship. In some circumstances, Respondent brought to a client's attention compensation to Merrill Lynch Consulting Services over and above the hard dollar fee, and offered to renegotiate fees with the client, even though Merrill Lynch Consulting Services did not require that he do so. However, he failed to make such disclosures on a routine basis at the outset of a directed brokerage arrangement. Beginning in 2004, Respondent voluntarily initiated disclosure of the amount of each client's hard dollar fee and the amount of directed brokerage commissions generated by the client on a quarterly basis, even though Merrill Lynch Consulting Services did not require these disclosures.

Based on the above, Respondent negligently failed to ensure that the conflicts of interest inherent in the recommendation of directed brokerage were routinely disclosed to the Consulting Services clients he served.

D. DISCUSSION

By making materially misleading misrepresentations and failing to disclose material facts to some of the firm's pension consulting clients, as discussed above, Merrill Lynch violated Section 206(2) of the Advisers Act, which provides that "[i]t shall be unlawful for any investment adviser, by 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."[2] As a result of the conduct described above, principally constituting non-disclosures, Respondent willfully[3] aided and abetted and caused Merrill Lynch's violation of Section 206(2) of the Advisers Act.

IV.

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

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

A. Respondent Callaway cease and desist from committing or causing any violations and any future violations of Section 206(2) of the Advisers Act;

B. Respondent is hereby censured; and

C. Respondent shall, within 90 days of the entry of this Order, pay a civil money penalty in the amount of $20,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Such payment shall be: (A) made by United States postal money order, certified check, bank cashiers 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 Michael A. Callaway as a Respondent in these proceedings, the file number of these

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2 Proof of scienter is not required to establish a violation of Section 206(2) of the Advisers Act. SEC v. Capital Gains Research Bureau, 375 U.S. 180, 195 (1963).

3 A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting Hughes v. SEC, 174 F.2d 969, 977 (D.C. Cir. 1949)).

proceedings, a copy of which cover letter and money order or check shall be sent to Laura B. Josephs, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9038 / June 8, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13507

In the Matter of Evergreen Investment Management Company, LLC, and Evergreen Investment Services, Inc. Respondents.	ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE RULE 602(c)(3) DISQUALIFICATION PROVISION

I.

Evergreen Investment Management Company, LLC ("EIMCO"), and Evergreen Investment Services, Inc. ("EIS") (collectively, "Respondents") have submitted a letter, dated May 21, 2009, requesting a waiver of the Rule 602(c)(3) disqualification from the exemption from registration under Regulation E arising from Respondents' settlement of an administrative proceeding commenced by the Commission.

II.

On June 8, 2009, pursuant to Respondents' Offer of Settlement, the Commission issued an Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b)(4) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"), and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act"), Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order") against Respondents. The Order found, among other things, that: (1) from February 2007 through June 18, 2008, the Evergreen Ultra Short Opportunities Fund (the "Fund") overstated its net asset value ("NAV") by as much as 17% and, as a result, certain shareholders redeemed their shares at prices higher than they should have received – to the detriment of remaining shareholders – and certain shareholders purchased shares at higher prices than they should have paid; (2) from June 13, 2008 through June 17, 2008, EIS, with EIMCO's knowledge, disclosed to select Fund select Fund shareholders, including shareholders who were brokerage customers of an affiliate, that recent significant decreases in the Fund's NAV were caused by the downward re-pricing of certain securities owned by the Fund that resulted not from market-related events but rather from a change in the way the Fund valued those securities and that the re-pricings may continue – information these shareholders were then able to use in deciding whether to redeem their shares before further potential re-pricings of the securities held by the Fund; (3) from as early as January 2008, EIMCO caused the Fund to engage in prohibited securities transactions with other mutual funds in the Evergreen family of mutual funds; and (4) EIS failed to preserve certain business-related electronic communications as required by federal securities laws and in violation of a Commission Order entered against it on September 19, 2007, in a separate enforcement action. The Order found that, as a result of the conduct described therein, EIMCO willfully violated Sections 204A and 206(2) of the Advisers Act and Section 34(b) of the Investment Company Act and willfully aided and abetted and caused violations of Section 17(a)(2) of the Investment Company Act and Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act; and EIS willfully violated Sections 15(f) and 17(a) of the Exchange Act and Rule 17a-4(b)(4) thereunder, and Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act, and willfully aided and abetted and caused EIMCO's violations of Section 206(2) of the Advisers Act. The Order censures the Respondents and requires them to, among other things: (1) pay a total of approximately $7,125,000 in disgorgement plus prejudgment interest and civil penalties (and acknowledges the Respondents' undertaking to make a payment of an additional $33,000,000 to compensate shareholders for harm caused by the conduct set forth in the Order); (2) cease and desist from committing or causing violations of various provisions of the federal securities laws; and (3) comply with certain undertakings concerning compliance oversight.

III.

Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if any investment adviser or underwriter for the securities to be offered is subject to an order of the Commission entered pursuant to Section 15(b) of the Exchange Act or Section 203(e) of the Advisers Act. 17 C.F.R. § 230.602(c)(3). Rule 602(e) of the Securities Act of 1933 ("Securities Act") provides, however, that the disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in Respondents' request, the Commission has determined that, pursuant to Rule 602(e) under the Securities Act, a showing of good cause has been made and 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 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.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

3

Commissioner Casey
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9039 / June 8, 2009

SECURITIES EXCHANGE ACT OF 1934
Release No. 60060 / June 8, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13507

In the Matter of

Evergreen Investment Management Company, LLC and Evergreen Investment Services, Inc.

Respondents.

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

Evergreen Investment Management Company, LLC ("EIMCO") and Evergreen Investment Services, Inc. ("EIS") (collectively, "Respondents") have submitted a letter, dated May 22, 2009, on behalf of themselves and their affiliates, including Wells Fargo and Company, whose stock is traded on the New York Stock Exchange, 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 Respondents' settlement of an administrative proceeding instituted by the Commission.

On June 8, 2009, pursuant to the Respondents' Offer of Settlement, the Commission issued an Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b)(4) and 21C of the Exchange Act, Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"), and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act"), Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order") against Respondents.

The Order finds that, as a result of the conduct described therein: EIMCO willfully violated Sections 204A and 206(2) of the Advisers Act and Section 34(b) of the Investment Company Act, and willfully aided and abetted and caused violations of Section 17(a)(2) of the

Investment Company Act and Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act thereunder; and EIS willfully violated Sections 15(f) and 17(a) of the Exchange Act and Rule 17a-4(b)(4) thereunder, and Rule 22c-1(a) promulgated pursuant to Section 22(c) of the Investment Company Act, and willfully aided and abetted and caused EIMCO's violations of Section 206(2) of the Advisers Act. The Order censures the Respondents and requires them to, among other things: (1) pay a total of approximately $7,125,000 in disgorgement plus prejudgment interest and civil penalties (and acknowledges the Respondents' undertaking to make a payment of an additional $33,000,000 to compensate shareholders for harm caused by the conduct set forth in the Order); (2) cease and desist from committing or causing violations of various provisions of the federal securities laws; and (3) comply with certain undertakings concerning compliance oversight.

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 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 Respondents' 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 as to EIMCO and EIS and their affiliates resulting from the entry of the Order is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9040 / June 9, 2009

SECURITIES EXCHANGE ACT OF 1934
Release No. 60078 / June 9, 2009

In the Matter of **Deutsche Bank Securities, 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 EXCHANGE ACT OF 1934**

Deutsche Bank Securities, Inc. ("DBSI") has submitted a letter, on behalf of itself and any of its current or future affiliates, dated May 21, 2009, 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 DBSI's settlement of an injunctive action filed by the Commission.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York, charging DBSI, a registered broker-dealer, with violations of the broker-dealer anti-fraud provisions. In its complaint, the Commission alleged that DBSI misled its customers regarding the fundamental nature and increasing risks associated with auction rate securities ("ARS") that DBSI underwrote, marketed and sold. On June 9, 2009, pursuant to DBSI's Consent, the Court entered a Judgment permanently enjoining DBSI from violating Section 15(c) of the Exchange Act. The Judgment provides that DBSI will, among other things, offer buy back at par certain ARS from certain customers.

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 date on which the statement was first made . . . has been made the subject of a judicial or 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 upon the representations set forth in DBSI's letter, the Commission has determined that, under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Judgment 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 waivers 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 DBSI and any current or future affiliates resulting from the entry of the Judgment are hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9041 / June 9, 2009

In the Matter of **RBC Capital Markets Corp.** **Respondent.**	**ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE RULE 602(b)(4) and 602(c)(2) DISQUALIFICATION PROVISIONS**

I.

Respondent RBC Capital Markets Corp. ("RBC") has submitted a letter, dated May 1, 2009, requesting a waiver of the Rule 602(b)(4) and 602(c)(2) disqualifications from the exemption from registration under Regulation E arising from RBC's settlement of an injunctive action commenced by the Commission.

II.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York, charging RBC, a registered broker-dealer, with violations of the broker-dealer anti-fraud provisions. In its complaint, the Commission alleged that RBC misled its customers regarding the liquidity and increasing risks associated with auction rate securities ("ARS") that RBC underwrote, marketed and sold. On June 9, 2009, pursuant to RBC's Consent, the Court entered a Judgment permanently enjoining RBC from violating Section 15(c) of the Securities Exchange Act of 1934. The Judgment provides that RBC will, among other things, offer to purchase at par certain ARS from certain customers.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if the issuer or any of its affiliates is subject to any order, judgment, or decree of a court "temporarily or permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities." *See* Rule 602(b)(4) of the Securities Act of 1933 ("Securities Act"). The Regulation E exemption is also not available for the securities of an issuer if an investment adviser or underwriter of the securities to be offered is "temporarily or permanently restrained or enjoined by any court from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser." *See* Rule 602(c)(2). Rule 602(e) of the Securities Act provides, however, that the disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in Respondent'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 Judgment.

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(b)(4) and 602(c)(2) under the Securities Act resulting from the entry of the Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9042 / June 9, 2009

SECURITIES EXCHANGE ACT OF 1934
Release No. 60079 / June 9, 2009

In the Matter of **RBC Capital Markets Corp.,** **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 AS TO RBC CAPITAL MARKETS CORP. AND ITS AFFILIATES**

RBC Capital Markets Corp. ("RBC") has submitted a letter on behalf of itself and any of its current and future affiliates, dated May 5, 2009, 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 injunctive action filed by the Commission.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York, charging RBC, a registered broker-dealer, with violations of the broker-dealer anti-fraud provisions. In its complaint, the Commission alleged that RBC misled its customers regarding the liquidity and increasing risks associated with auction rate securities ("ARS") that RBC underwrote, marketed and sold. On June 9, 2009, pursuant to RBC's Consent, the Court entered a Judgment permanently enjoining RBC from violating Section 15(c) of the Exchange Act. The Judgment provides that RBC will, among other things, offer to purchase at par certain ARS from certain customers.

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 date on which the statement was first made . . . has been made the subject of a judicial or 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 RBC's letter, the Commission has determined that, under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Judgment 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 as to RBC and any current or future affiliates resulting from the entry of the Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9043A / June 9, 2009

SECURITIES EXCHANGE ACT OF 1934
Release No. 60081A / June 9, 2009

In the Matter of

Banc of America Securities, LLC and
Banc of America Investment Services, Inc.

Respondents.

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 AS TO BANC OF AMERICA SECURITIES LLC, BANC OF AMERICA INVESTMENT SERVICES, INC., BANK OF AMERICA CORPORATION AND THEIR AFFILIATES

Banc of America Securities, LLC ("BAS"), Banc of America Investment Services, Inc. ("BAI"), and Bank of America Corporation ("BAC" and collectively with BAS and BAI, "BOA") have submitted a letter on behalf of themselves and any of their current and future affiliates, dated May 14, 2009, 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 their settlement of an injunctive action filed by the Commission.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York, charging BAS and BAI, both registered broker-dealers, with violations of the broker-dealer anti-fraud provisions. In its complaint, the Commission alleged that BAS and BAI misled their customers regarding the liquidity and increasing risks associated with auction rate securities ("ARS") that BAS underwrote, marketed and sold. On June 9, 2009, pursuant to BAS and BAI's Consent, the Court entered a Judgment permanently enjoining BAS and BAI from violating Section 15(c) of the Exchange Act. The

Judgment provides that BOA will, among other things, offer to purchase at par certain ARS from certain customers.

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 date on which the statement was first made . . . has been made the subject of a judicial or 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 BOA's letter, the Commission has determined that, under the circumstances, the request for a waiver of the disqualifications resulting from the entry of the Judgment 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 as to BOA and any current or future affiliates resulting from the entry of the Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9044 / June 9, 2009

In the Matter of Banc of America Securities, LLC, and Banc of America Investment Services, Inc., Respondents.	**ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE RULE 602(b)(4) AND 602(c)(2) DISQUALIFICATION PROVISIONS**

I.

Banc of America Securities LLC ("BAS") and Banc of America Investment Services, Inc. ("BAI" collectively with BAS, "BOA" or "Respondents") have submitted a letter, dated May 29, 2009, requesting a waiver of the Rule 602(b)(4) and 602(c)(2) disqualification from the exemption from registration under Regulation E arising from Respondents' settlement of an injunctive action commenced by the Commission.

II.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York , charging BAS and BAI, both registered broker-dealers, with violations of the broker-dealer anti-fraud provisions of the Securities Exchange Act of 1934 ("Exchange Act"). In its complaint, the Commission alleged that BAS and BAI misled thousands of their customers regarding the fundamental nature and increasing risks associated with auction rate securities that BAS underwrote, marketed and sold. On June 9, 2009, pursuant to BOA's consent, the Court entered a Judgment permanently enjoining Respondents from violating Section 15(c) of the Exchange Act.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if the issuer or any of its affiliates is subject to any order, judgment, or decree of a court "temporarily or permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities." *See* Rule 602(b)(4) of the Securities Act of 1933 ("Securities Act"). The Regulation E exemption is also not available for the securities of an issuer if an investment adviser or underwriter of the securities to be offered is "temporarily or permanently restrained or enjoined by any court from engaging or continuing any conduct or practice in connection with the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser." *See* Rule 602(c)(2). Rule 602(e) of the Securities Act provides, however, that the disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in Respondents' 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 Judgment.

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(b)(4) and 602(c)(2) under the Securities Act resulting from the entry of the Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9045 / June 9, 2009

In the Matter of **Deutsche Bank Securities, Inc.** **Respondent.**	**ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE RULE 602(b)(4) and 602(c)(2) DISQUALIFICATION PROVISIONS**

I.

Deutsche Bank Securities, Inc. ("DBSI") has submitted a letter, on behalf of Deutsche Bank AG and its affiliates, dated May 22, 2009, requesting a waiver of the Rule 602(b)(4) and 602(c)(2) disqualification from the exemption from registration under Regulation E arising from DSBI's settlement of an injunctive action commenced by the Commission.

II.

On June 3, 2009, the Commission filed a civil injunctive action in the United States District Court for the Southern District of New York, charging DBSI, a registered broker-dealer, with violations of the broker-dealer anti-fraud provisions of the Securities Exchange Act of 1934 ("Exchange Act"). In its complaint, the Commission alleged that DBSI misled its customers regarding the fundamental nature and increasing risks associated with auction rate securities that DBSI underwrote, marketed and sold. On June 9, 2009, pursuant to DBSI's consent, the Court entered a Judgment permanently enjoining DBSI from violating Section 15(c) of the Exchange Act.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if the issuer or any of its affiliates is subject to any order, judgment, or decree of a court "temporarily or permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities." *See* Rule 602(b)(4) of the Securities Act of 1933 ("Securities Act"). The Regulation E exemption is also not available for the securities of an issuer if an investment adviser or underwriter of the securities to be offered is "temporarily or permanently restrained or enjoined by any court from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser." *See* Rule 602(c)(2). Rule 602(e) of the Securities Act provides, however, that the disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in DBSI'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 Judgment.

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(b)(4) and 602(c)(2) under the Securities Act resulting from the entry of the Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC- 28764; File No. 812-13662]

Banc of America Securities LLC, et al.; Notice of Application and Temporary Order

June 9, 2009

Agency: Securities and Exchange Commission ("Commission").

Action: Temporary order and notice of application for a permanent order under section 9(c) of the Investment Company Act of 1940 ("Act").

Summary of Application: Applicants have received a temporary order exempting them from section 9(a) of the Act, with respect to an injunction entered against Banc of America Securities LLC ("BAS") and Banc of America Investment Services, Inc. ("BAI") on June 9, 2009 by the United States District Court for the Southern District of New York ("Injunction") until the Commission takes final action on an application for a permanent order. Applicants also have applied for a permanent order.

Applicants: BAS, BAI, Columbia Management Advisors, LLC ("CMA"), Columbia Wanger Asset Management, LP ("CWAM"), Columbia Management Distributors, Inc. ("CMDI"), Banc of America Investment Advisors, Inc. ("BAIA"), Bank of America Capital Advisors LLC ("BACA"), U.S. Trust Hedge Fund Management, Inc. ("USTHFM"), Merrill Lynch, Pierce, Fenner & Smith, Incorporated ("MLPFS"), IQ Investment Advisors LLC ("IQ"), Roszel Advisors, LLC ("Roszel"), Nuveen Asset Management ("NAM"), Nuveen Investments Advisers Inc. ("NIA"), Nuveen Investments Institutional Services Group, LLC ("ISG"), Nuveen HydePark Group, LLC ("Nuveen HydePark"), NWQ Investment Management Company LLC ("NWQ"), Nuveen Investment Solutions, Inc. ("NIS"), Santa Barbara Asset Management, LLC ("Santa Barbara"), Symphony Asset Management LLC ("Symphony"), Tradewinds Global Investors, LLC ("Tradewinds") and Winslow Capital Management, Inc. ("Winslow", together with NAM, NIA, ISG, Nuveen HydePark, NWQ, NIS, Santa Barbara, Symphony and Tradewinds, the "Nuveen Advisers"), Nuveen Investments, LLC ("Nuveen Investments"), KECALP Inc. ("KECALP") and Merrill Lynch Ventures, LLC ("Ventures") (collectively, "Applicants").[1]

Filing Date: The application was filed on June 3, 2009. Applicants have agreed to file an amendment during the notice period, the substance of which is reflected in this notice.

Hearing or Notification of Hearing: An order granting the application will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on July 6, 2009, and should be accompanied by proof of service on applicants, in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

Addresses: Secretary, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090; Applicants: BAS, One Bryant Park, New York, NY 10036; BAI, CMA, BAIA, BACA, 100 Federal Street, Boston, MA 02110; CWAM, 227 West Monroe Street, Suite 3000, Chicago, IL 60606; CMDI, One Financial Center, Boston, MA 02110; USTHFM, 225 High Ridge Road, West Building, Stamford, CT 06905; MLPFS, IQ, KECALP, Ventures, North Tower, 4 World Financial Center, New York, NY 10080; Roszel, 1700 Merrill Lynch Drive, Pennington, NJ 08534; and the Nuveen Advisers and Nuveen Investments, 333 West Wacker Drive, Chicago, IL 60606.

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[1] Applicants request that any relief granted pursuant to the application also apply to any other company of which BAS or BAI is or may become an affiliated person (together with the Applicants, the "Covered Persons").

For Further Information Contact: Emerson S. Davis, Senior Counsel, at 202-551-6868, or Julia Kim Gilmer, Branch Chief, at 202-551-6821 (Division of Investment Management, Office of Investment Company Regulation).

Supplementary Information: The following is a temporary order and a summary of the application. The complete application may be obtained via the Commission's Web site by searching for the file number, or an applicant using the Company name box, at http://www.sec.gov/search/search.htm or by calling (202) 551-8090.

Applicants' Representations:

1. BAS, an indirect wholly owned subsidiary of Bank of America Corporation ("BAC"), is a full service U.S. investment bank and brokerage firm that provides a wide range of investment banking, and financial advisory services to corporate, institutional and individual clients. BAS is registered as an investment adviser under the Investment Advisers Act of 1940 ("Advisers Act") and is registered as a broker-dealer under the Securities Exchange Act of 1934 ("Exchange Act"). BAI is a wholly owned subsidiary of Bank of America, N.A. and also an indirect subsidiary of BAC. BAI is registered as an investment adviser under the Advisers Act and is registered as a broker-dealer under the Exchange Act. While BAS and BAI do not currently serve, and no existing company of which BAS or BAI is an affiliated person (other than the Applicants) currently serves, as investment adviser, depositor or principal underwriter for a registered investment company ("RIC"), or principal underwriter for any registered open-end investment company, registered investment trust ("UIT") or face amount certificate company or employees' securities companies ("ESC", and together with RICs, the "Funds," and such services, the "Fund Servicing Activities"), each may do so in the future. CMA, CWAM, BAIA, BACA, USTHFM, IQ, Roszel, the Nuveen Advisers and KECALP are registered as investment

advisers under the Advisers Act and provide investment advisory or subadvisory services to Funds. Ventures provides investment advisory services to an ESC. CMDI, MLPFS and Nuveen Investments are registered as broker-dealers under the Exchange Act and serve as principal underwriters for certain Funds. Nuveen Investments also serves as depositor to certain UITs.

2. On June 9, 2009, the United States District Court for the Southern District of New York entered a judgment, which included the Injunction, against BAS and BAI ("Judgment") in a matter brought by the Commission.[2] The Commission alleged in the complaint ("Complaint") that BAS and BAI violated section 15(c) of the Exchange Act in connection with the marketing and sale of auction rate securities ("ARS"). The Complaint alleged that BAS and BAI misled customers regarding the fundamental nature and increasing risk associated with ARS that they underwrote, marketed and sold. Without admitting or denying any of the allegations in the Complaint, except as to jurisdiction, BAS and BAI consented to the entry of the Judgment that included, among other things, the entry of the Injunction and certain undertakings to take various remedial actions for the benefit of purchasers of certain ARS.

Applicants' Legal Analysis:

1. Section 9(a)(2) of the Act, in relevant part, prohibits a person who has been enjoined from engaging in or continuing any conduct or practice in connection with the purchase or sale of a security, or in connection with activities as an underwriter, broker or dealer, from acting, among other things, as an investment adviser or depositor of any registered investment company or a principal underwriter for any registered open-end investment company, registered unit investment trust, or registered face-amount certificate company. Section 9(a)(3) of the Act

[2] Securities and Exchange Commission v. Banc of America Securities LLC and Banc of America Investment Services, Inc., Judgment against Banc of America Securities LLC and Banc of America Investment Services, Inc., 09 CIV 5170 (S.D.N.Y., entered June 9, 2009).

makes the prohibition in section 9(a)(2) applicable to a company, any affiliated person of which has been disqualified under the provisions of section 9(a)(2). Section 2(a)(3) of the Act defines "affiliated person" to include, among others, any person directly or indirectly controlling, controlled by, or under common control, with the other person. Applicants state that BAS and BAI are or may be considered affiliated persons of each of the other Applicants within the meaning of section 2(a)(3). Applicants state that, as a result of the Injunction, they would be subject to the prohibitions of section 9(a).

2. Section 9(c) of the Act provides that the Commission shall grant an application for exemption from the disqualification provisions of section 9(a) of the Act if it is established that these provisions, as applied to Applicants, are unduly or disproportionately severe or that the conduct of the Applicants has been such as not to make it against the public interest or the protection of investors to grant the exemption. Applicants have filed an application pursuant to section 9(c) seeking a temporary and permanent order exempting the Applicants and the other Covered Persons from the disqualification provisions of section 9(a).

3. Applicants believe they meet the standards for exemption specified in section 9(c). Applicants state that the prohibitions of section 9(a) as applied to them would be unduly and disproportionately severe and that the conduct of Applicants has been such as not to make it against the public interest or the protection of investors to grant the requested exemption from section 9(a).

4. Applicants state that the conduct alleged in the Complaint did not involve any of the Applicants acting in their capacity as investment adviser, sub-adviser, depositor or principal underwriter for any of the Funds. Applicants also state that to the best of their knowledge, none of the current directors and officers of the Applicants (other than BAS and BAI) or their

employees that engage in Fund Servicing Activities (or any other persons in such roles during the time period covered by the Complaint) participated in the conduct alleged in the Complaint to have constituted the violations that provide a basis for the Injunction. Applicants further state that any personnel at BAS and BAI who participated in the conduct alleged in the Complaint to have constituted the violations that provide a basis for the Injunction have had no, and will not have any future involvement in the Applicants' Fund Servicing Activities.

5. Applicants state that the inability of the Applicants to engage in Fund Servicing Activities would result in potentially severe financial hardships for the Funds they serve and the Funds' shareholders or unitholders. Applicants state that they will distribute written materials, including an offer to meet in person to discuss the materials, to the boards of directors of the Funds (the "Boards"), including the directors who are not "interested persons," as defined in section 2(a)(19) of the Act, of the Funds and their independent legal counsel as defined in rule 0-1(a)(6) under the Act, if any, regarding the Injunction, any impact on the Funds, and the application. Applicants state that they will provide the Boards with all information concerning the Injunction and the application that is necessary for the Funds to fulfill their disclosure and other obligations under the federal securities laws.

6. Applicants also state that, if they were barred from providing Fund Servicing Activities to the Funds, the effect on their businesses and employees would be severe. Applicants state that they have committed substantial capital and resources to establishing an expertise in providing Fund Servicing Activities. Applicants further state that prohibiting them from providing Fund Servicing Activities would not only adversely affect their businesses (except for BAI and BAS) but would also adversely affect their employees who are involved in Fund Servicing Activities. Applicants also state that disqualifying KECALP and Ventures from

continuing to provide investment advisory services to ESCs is not in the public interest or in furtherance of the protection of investors and would frustrate the expectations of eligible employees who invest in ESCs. Applicants state that it would not be consistent with the purposes of the ESC provisions of the Act to require another entity not affiliated with Merrill Lynch & Co., Inc., or BAC to manage the ESCs.

7. Applicants state that several Applicants and certain of their affiliates have previously received orders under section 9(c), as described in greater detail in the application.

Applicants' Condition:

Applicants agree that any order granting the requested relief will be subject to the following condition:

Any temporary exemption granted pursuant to the application shall be without prejudice to, and shall not limit the Commission's rights in any manner with respect to, any Commission investigation of, or administrative proceedings involving or against, Covered Persons, including without limitation, the consideration by the Commission of a permanent exemption from section 9(a) of the Act requested pursuant to the application or the revocation or removal of any temporary exemptions granted under the Act in connection with the application.

Temporary Order:

The Commission has considered the matter and finds that the Applicants have made the necessary showing to justify granting a temporary exemption.

Accordingly,

IT IS HEREBY ORDERED, pursuant to section 9(c) of the Act, that Applicants and any other Covered Persons are granted a temporary exemption from the provisions of section 9(a), solely with respect to the Injunction, subject to the condition in the application, from June 9, 2009, until the Commission takes final action on their application for a permanent order.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC- 28762; File No. 812-13663]

RBC Capital Markets Corporation, et al.; Notice of Application and Temporary Order

June 9, 2009

Agency: Securities and Exchange Commission ("Commission").

Action: Temporary order and notice of application for a permanent order under section 9(c) of the Investment Company Act of 1940 ("Act").

Summary of Application: Applicants have received a temporary order exempting them from section 9(a) of the Act, with respect to an injunction entered against RBC Capital Markets Corporation ("RBC") on June 9, 2009 by the United States District Court for the Southern District of New York ("Injunction"), until the Commission takes final action on an application for a permanent order. Applicants also have applied for a permanent order.

Applicants: RBC, Voyageur Asset Management Inc. ("Voyageur"), Tamarack Distributors Inc. ("Tamarack"), and Sky Investment Counsel Inc. ("Sky") (collectively, other than RBC, the "Fund Servicing Applicants" and together with RBC, the "Applicants").[1]

Filing Date: The application was filed on June 3, 2009. Applicants have agreed to file an amendment during the notice period, the substance of which is reflected in this notice.

Hearing or Notification of Hearing: An order granting the application will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving Applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on

[1] Applicants request that any relief granted pursuant to the application also apply to any other company of which RBC is or may become an affiliated person (together with the Applicants, the "Covered Persons").

July 6, 2009, and should be accompanied by proof of service on Applicants, in the form of an affidavit, or for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

Addresses: Secretary, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090; Applicants: RBC, One Liberty Plaza, 165 Broadway, New York, NY 10006; Voyageur and Tamarack, 100 South Fifth Street, Suite 2300, Minneapolis, MN 55402; and Sky, 1 Adelaide Street East, Suite 2310, Toronto, ON, Canada M5C 2V9.

For Further Information Contact: Jaea F. Hahn, Senior Counsel, at (202) 551-6870, or Julia Kim Gilmer, Branch Chief, at (202) 551-6821, (Division of Investment Management, Office of Investment Company Regulation).

Supplementary Information: The following is a temporary order and a summary of the application. The complete application may be obtained via the Commission's Web site by searching for the file number, or an applicant using the Company name box, at http://www.sec.gov/search/search.htm or by calling (202) 551-8090.

Applicants' Representations:

1. RBC is a full service investment banking firm engaged in securities underwriting, sales and trading, investment banking, financial advisory services and investment research services. RBC is registered with the Commission as a broker-dealer under the Securities Exchange Act of 1934, as amended ("Exchange Act") and as an investment adviser under the Investment Advisers Act of 1940, as amended ("Advisers

Act"). RBC is an indirect, wholly owned subsidiary of Royal Bank of Canada ("Royal Bank"), a Canada-based global financial services firm.

2. Voyaguer and Sky are registered as investment advisers under the Advisers Act and provide investment advisory or subadvisory services to registered investment companies ("Funds"). Voyageur is an indirect, wholly owned subsidiary of Royal Bank. Royal Bank indirectly owns a controlling interest in Sky. Tamarack is a broker-dealer registered under the Exchange Act and serves as principal underwriter to open-end Funds. None of the Applicants serve as depositor to any Fund.

3. On June 9, 2009, the United States District Court for the Southern District of New York entered a judgment against RBC ("Judgment") in a matter brought by the Commission.[2] The Commission alleged in the complaint ("Complaint") that RBC violated section 15(c) of the Exchange Act by misrepresenting to many of its customers that auction rate securities were safe, highly liquid investments that were substitutes for cash or money market funds. The Complaint further alleges that on February 11, 2008, RBC determined not to place bids in most of its auctions, as it had historically done, resulting in failed auctions. Without admitting or denying the allegations in the Complaint, except as to jurisdiction, RBC consented to the entry of the Injunction and other equitable relief including undertakings to take various remedial actions for the benefit of purchasers of certain auction rate securities.

Applicants' Legal Analysis:

1. Section 9(a)(2) of the Act, in relevant part, prohibits a person who has been enjoined from, among other things, engaging in or continuing any conduct or practice in

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2 Securities and Exchange Commission v. RBC Capital Markets Corporation, Judgment as to Defendant RBC Capital Markets Corporation, 09-cv-5172 (S.D.N.Y., June 9, 2009).

connection with the purchase or sale of a security, or in connection with activities as an underwriter, broker or dealer, from acting, among other things, as an investment adviser or depositor of any registered investment company or a principal underwriter for any registered open-end investment company, registered unit investment trust or registered face-amount certificate company. Section 9(a)(3) of the Act makes the prohibition in section 9(a)(2) applicable to a company, any affiliated person of which has been disqualified under the provisions of section 9(a)(2). Section 2(a)(3) of the Act defines "affiliated person" to include, among others, any person directly or indirectly controlling, controlled by, or under common control with, the other person. Applicants state that RBC is an affiliated person of each of the other Applicants within the meaning of section 2(a)(3) of the Act. Applicants state that the entry of the Injunction results in Applicants being subject to the disqualification provisions of section 9(a) of the Act.

2. Section 9(c) of the Act provides that the Commission shall grant an application for exemption from the disqualification provisions of section 9(a) if it is established that these provisions, as applied to the Applicants, are unduly or disproportionately severe or that the Applicants' conduct has been such as not to make it against the public interest or the protection of investors to grant the exemption. Applicants have filed an application pursuant to section 9(c) seeking a temporary and permanent order exempting them and Covered Persons from the disqualification provisions of section 9(a) of the Act.

3. Applicants believe they meet the standards for exemption specified in section 9(c). Applicants state that the prohibitions of section 9(a) as applied to them would be unduly and disproportionately severe and that the conduct of the Applicants has been

such as not to make it against the public interest or the protection of investors to grant the exemption from section 9(a).

4. Applicants state that the alleged conduct giving rise to the Injunction did not involve any of the Applicants acting in the capacity of investment adviser or subadviser to any Fund or in the capacity of principal underwriter for any open-end Fund. Applicants also state that none of the current or former directors, officers, or employees of the Fund Servicing Applicants had any knowledge of, or had any involvement in, the conduct alleged in the Complaint. Applicants further state that the personnel at RBC who were involved in the violations alleged in the Complaint have had no involvement in providing investment advisory, subadvisory or principal underwriting services to Funds and will not have any future involvement in such activities.

5. Applicants state that the inability to continue to provide investment advisory and subadvisory services to Funds and principal underwriting services to open-end Funds would result in potential hardship for the Funds and their shareholders. Applicants state that they will, as soon as reasonably practical, distribute written materials, including an offer to meet in person to discuss the materials, to the boards of directors of the Funds ("Boards") for which the Applicants serve as investment adviser, investment subadviser or principal underwriter, including the directors who are not "interested persons," as defined in section 2(a)(19) of the Act, of such Funds, and their independent legal counsel as defined in rule 0-1(a)(6) under the Act, relating to the circumstances that led to the Injunction, any impact on the Funds, and the application. Applicants state they will provide the Boards with all information concerning the Injunction and the application

that is necessary for the Funds to fulfill their disclosure and other obligations under the federal securities laws.

6. Applicants also state that, if they were barred from providing services to Funds, the effect on their businesses and employees would be severe. Applicants state that they have committed substantial resources to establish an expertise in providing advisory and distribution services to Funds. Applicants further state that prohibiting them from providing such services would not only adversely affect their businesses, but would also adversely affect approximately 35 employees who are involved in those activities.

7. Applicants have not previously received an exemption under section 9(c) as the result of conduct that triggered section 9(a).

Applicants' Condition:

Applicants agree that any order granting the requested relief will be subject to the following condition:

Any temporary exemption granted pursuant to the application shall be without prejudice to, and shall not limit the Commission's rights in any manner with respect to, any Commission investigation of, or administrative proceedings involving or against, Covered Persons, including, without limitation, the consideration by the Commission of a permanent exemption from section 9(a) of the Act requested pursuant to the application or the revocation or removal of any temporary exemptions granted under the Act in connection with the application.

Temporary Order:

The Commission has considered the matter and finds that Applicants have made the necessary showing to justify granting a temporary exemption.

Accordingly,

IT IS HEREBY ORDERED, pursuant to section 9(c) of the Act, that Applicants and any other Covered Persons are granted a temporary exemption from the provisions of section 9(a), solely with respect to the Injunction, subject to the condition in the application, from June 9, 2009, until the Commission takes final action on their application for a permanent order.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Walter not participating

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC-28763; File No. 812-13664]

Deutsche Bank Securities Inc., et al.; Notice of Application and Temporary Order

June 9, 2009

Agency: Securities and Exchange Commission ("Commission").

Action: Temporary order and notice of application for a permanent order under section 9(c) of the Investment Company Act of 1940 ("Act").

Summary of Application: Applicants have received a temporary order exempting them from section 9(a) of the Act, with respect to an injunction entered against Deutsche Bank Securities Inc. ("DBSI") on June 9, 2009 by the United States District Court for the Southern District of New York ("Injunction"), until the Commission takes final action on an application for a permanent order. Applicants also have applied for a permanent order.

Applicants: DBSI, Deutsche Investment Management Americas, Inc. ("DIMA"), Deutsche Asset Management (Hong Kong) Limited ("DeAM (HK)"), Deutsche Asset Management International GmbH ("DeAMI"), Deutsche Asset Management (Japan) Limited ("DeAMJ"), Deutsche Investments Australia Limited ("DIAL"), RREEF America L.L.C. ("RREEF"), RREEF Global Advisors Limited ("RREEF (G)"), and DWS Investments Distributors, Inc. ("DIDI") (collectively, other than DBSI, the "Fund Servicing Applicants" and together with DBSI, the "Applicants").[1]

Filing Date: The application was filed on June 9, 2009.

Hearing or Notification of Hearing: An order granting the application will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to

[1] Applicants request that any relief granted pursuant to the application also apply to any other company of which DBSI is or may become an affiliated person (together with the Applicants, the "Covered Persons").

the Commission's Secretary and serving Applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on July 6, 2009, and should be accompanied by proof of service on Applicants, in the form of an affidavit, or for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

Addresses: Secretary, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090; Applicants: DBSI, 60 Wall Street, New York, NY 10005; DIMA, 345 Park Avenue, New York, NY 10154; DeAM (HK), 48/F Cheung Kong Centre, 2 Queen's Road Central, Hong Kong, China; DeAMI, Mainzer Landstrasse 178-190, Frankfurt AM Main, 60327; DeAMJ, Sanno Park Tower, 2-11-1, Nagata-Cho, Chiyoda-Ku, Tokyo, 100-6173; DIAL, Deutsche Bank Place, Level 16, CNR Hunter and Phillip Streets, Sydney, NSW 2000; RREEF, 875 N. Michigan Avenue, 41st Floor, Chicago, IL 60611; RREEF (G), Winchester House, 1 Great Winchester Street, London, United Kingdom EC2N 2DB; and DIDI, 222 South Riverside Plaza, Chicago, IL 60606.

For Further Information Contact: Steven I. Amchan, Senior Counsel, at (202) 551-6826, or Julia Kim Gilmer, Branch Chief, at (202) 551-6821, (Division of Investment Management, Office of Investment Company Regulation).

Supplementary Information: The following is a temporary order and a summary of the application. The complete application may be obtained via the Commission's Web site by searching for the file number, or an applicant using the Company name box, at http://www.sec.gov/search/search.htm or by calling (202) 551-8090.

Applicants' Representations:

1. Deutsche Bank AG ("DB") is a stock corporation organized under the laws of the Federal Republic of Germany. DBSI is an indirect wholly-owned subsidiary of DB, and an affiliated person of each Fund Servicing Applicant within the meaning of section 2(a)(3) of the Act (by virtue of being under common control with the Fund Servicing Applicants). DBSI provides securities brokerage and investment advisory services to private clients and institutions and correspondent clearing services to broker-dealers. DBSI also provides a variety of capital raising, market making, and brokerage services for its government, financial institution, and corporate clients, including fixed income and equity sales and trading, emerging markets activities, and equity market research and investment banking.

2. DIMA, DeAM (HK), DeAMI, DeAMJ, DIAL, RREEF, and RREEF (G) are registered as investment advisers under the Investment Advisers Act of 1940, as amended ("Advisers Act") and provide investment advisory or subadvisory services to registered investment companies ("Funds"). DIDI is a broker-dealer registered under the Securities Exchange Act of 1934 ("Exchange Act") and serves as principal underwriter to Funds.

3. On June 9, 2009, the United States District Court for the Southern District of New York entered a judgment against DBSI ("Judgment") in a matter brought by the Commission.[2] The Commission alleged in the complaint ("Complaint") that DBSI violated section 15(c) of the Exchange Act by marketing auction rate securities as highly liquid investments comparable to cash or money market instruments and by selling auction rate securities to its customers without adequately disclosing the risks involved in

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[2] Securities and Exchange Commission v. Deutsche Bank Securities Inc., Judgment on Consent Against Defendant Deutsche Bank Securities Inc., 09 Civ. 5174 (S.D.N.Y. June 9, 2009).

purchasing such securities. Without admitting or denying the allegations in the Complaint, except as to jurisdiction, DBSI consented to the entry of the Judgment that included, among other things, the entry of the Injunction and other equitable relief including undertakings to take various remedial actions for the benefit of purchasers of certain auction rate securities.

Applicants' Legal Analysis:

1. Section 9(a)(2) of the Act, in relevant part, prohibits a person who has been enjoined from, among other things, engaging in or continuing any conduct or practice in connection with the purchase or sale of a security, or in connection with activities as an underwriter, broker or dealer, from acting, among other things, as an investment adviser or depositor of any registered investment company or a principal underwriter for any registered open-end investment company, registered unit investment trust or registered face-amount certificate company. Section 9(a)(3) of the Act makes the prohibition in section 9(a)(2) applicable to a company, any affiliated person of which has been disqualified under the provisions of section 9(a)(2). Section 2(a)(3) of the Act defines "affiliated person" to include, among others, any person directly or indirectly controlling, controlled by, or under common control with, the other person. Applicants state that DBSI is an affiliated person of each of the other Applicants within the meaning of section 2(a)(3) of the Act. Applicants state that the entry of the Injunction results in Applicants being subject to the disqualification provisions of section 9(a) of the Act.

2. Section 9(c) of the Act provides that the Commission shall grant an application for exemption from the disqualification provisions of section 9(a) if it is established that these provisions, as applied to the Applicants, are unduly or

disproportionately severe or that the Applicants' conduct has been such as not to make it against the public interest or the protection of investors to grant the exemption. Applicants have filed an application pursuant to section 9(c) seeking a temporary and permanent order exempting them and Covered Persons from the disqualification provisions of section 9(a) of the Act.

3. Applicants believe they meet the standard for exemption specified in section 9(c). Applicants state that the prohibitions of section 9(a) as applied to them would be unduly and disproportionately severe and that the conduct of the Applicants has been such as not to make it against the public interest or the protection of investors to grant the exemption from section 9(a).

4. Applicants state that the alleged conduct giving rise to the Injunction did not involve any of the Applicants acting in the capacity of investment adviser, subadviser or depositor to any Fund or in the capacity of principal underwriter for any open-end Fund, UIT, or registered face-amount certificate company. Applicants also state that none of the current or former directors, officers, or employees of the Fund Servicing Applicants had any responsibility for, or had any involvement in, the conduct alleged in the Complaint. Applicants further state that the personnel at DBSI who were involved in the violations alleged in the Complaint have had no and will not have any future involvement in providing investment advisory, subadvisory, depository or underwriting services to Funds.

5. Applicants state that their inability to continue to provide investment advisory, subadvisory and underwriting services to Funds would result in potential hardship for the Funds and their shareholders. Applicants state that they will, as soon as reasonably practicable, distribute written materials, including an offer to meet in person to

discuss the materials, to the boards of directors ("Boards") of the Funds for which the Applicants serve as investment adviser, investment subadviser or principal underwriter, including the directors who are not "interested persons," as defined in section 2(a)(19) of the Act, of such Funds, and their independent legal counsel as defined in rule 0-1(a)(6) under the Act, relating to the circumstances that led to the Injunction, any impact on the Funds, and the application. Applicants state they will provide the Boards of the Funds with all information concerning the Injunction and the application that is necessary for the Funds to fulfill their disclosure and other obligations under the federal securities laws.

6. Applicants also state that, if the Fund Servicing Applicants were barred from providing services to the Funds, the effect on their businesses and employees would be severe. Applicants state that they have committed substantial resources to establish an expertise in providing advisory and principal underwriting services to Funds. Applicants further state that prohibiting the Fund Servicing Applicants from providing such services would not only adversely affect their businesses, but would also adversely affect over 500 employees who are involved in those activities.

7. Applicants previously have received exemptions under section 9(c) as the result of conduct that triggered section 9(a) as described in greater detail in the application.

Applicants' Condition:

Applicants agree that any order granting the requested relief will be subject to the following condition:

Any temporary exemption granted pursuant to the application shall be without prejudice to, and shall not limit the Commission's rights in any manner with respect to, any Commission investigation of, or administrative proceedings involving or against, Covered Persons, including, without limitation, the consideration by the Commission of a permanent exemption from section 9(a) of the Act requested pursuant to the application or the revocation or removal of any temporary exemptions granted under the Act in connection with the application.

Temporary Order:

The Commission has considered the matter and finds that Applicants have made the necessary showing to justify granting a temporary exemption.

Accordingly,

IT IS HEREBY ORDERED, pursuant to section 9(c) of the Act, that Applicants and any other Covered Persons are granted a temporary exemption from the provisions of section 9(a), solely with respect to the Injunction, subject to the condition in the application, from June 9, 2009, until the Commission takes final action on their application for a permanent order.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Chairman Schapiro
not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60074 / June 9, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2986 / June 9, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13508

In the Matter of MICHAEL BEAULIEU (CPA), Respondent.	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Michael Beaulieu ("Respondent" or "Beaulieu") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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,

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[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order,...suspend from appearing or practicing before it any....accountant...who has been by name...permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

paragraph 3, below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Beaulieu, age 51, is a certified public accountant and was licensed to practice in the State of Massachusetts. He served as controller of Cardinal Health, Inc. ("Cardinal") from 1998 until January 2001, as the senior vice president of finance for Cardinal's Pharmaceutical Distribution and Provider Services and Medical Products and Services segments from January 2001 through January 2003, as Cardinal's chief financial officer of Healthcare Products and Services from January 2003 to January 2004, and as senior vice president of finance for Pharmaceutical Distribution and Provider Services from February 2004 until his resignation in March 2006.

2. Cardinal was, at all relevant times, an Ohio corporation with its principal place of business in Dublin, Ohio. Cardinal was, and continues to be, engaged in the business of developing and distributing health care and pharmaceutical products and services. At all relevant times, Cardinal's common stock was registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the New York Stock Exchange.

3. On May 27, 2009, the Commission filed a complaint against Beaulieu in SEC v. Michael Beaulieu, et al., Civil Action No. 09-CV-4945, in the United States District Court for the Southern District of New York. On May 29, 2009, the court entered an order permanently enjoining Beaulieu, by consent, from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5 and 13b2-1 thereunder, and aiding and abetting violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder. Beaulieu was also ordered to pay a $50,000 civil money penalty.

4. The Commission's complaint alleged, among other things, that, at different times from at least September 2000 through at least March 2004, Beaulieu and other former senior accounting and finance officers of Cardinal engaged in a fraudulent earnings and revenue management scheme to inflate Cardinal's publicly reported operating revenue, earnings and growth trends. The Complaint alleged that Beaulieu engaged in a number of improper accounting and disclosure practices that materially misrepresented Cardinal's publicly reported revenue, earnings, and growth trends. These practices included, among other things: misclassifying bulk sales as operating revenue to overstate reported operating revenue; overstating quarterly earnings by selectively accelerating the recognition of cash discount income; and improperly establishing and/or

using a general reserve account and directing or approving the adjustment of various reserve accounts in a departure from generally accepted accounting principles ("GAAP").

On October 26, 2004, as described in the Complaint, Cardinal restated its financial results for fiscal years 2000 to 2003 and for the first three quarters of fiscal year 2004. In its restatement, Cardinal disclosed, among other things, that it had improperly classified $1.2 billion of bulk revenue as operating revenue and that Cardinal had an undisclosed practice of accelerating payment of vendor invoices at the end of certain reporting periods, which improved operating results for those periods. The restatement (as subsequently corrected) also reduced Cardinal's net earnings by a cumulative total of $65.9 million, due to Cardinal's adjustments to reserves and other accruals, which were restated as a result of misapplications of GAAP, other errors or an absence of substantiation. In addition, Cardinal reversed, reclassified and recognized in a later period the $22 million of expected litigation settlement proceeds it had previously recognized during the second quarter of fiscal year 2001 and the first quarter of fiscal year 2002.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately that:

A. Beaulieu is suspended from appearing or practicing before the Commission as an accountant.

B. After three years from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Schapiro
not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60075 / June 9, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2987 / June 9, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13509

In the Matter of **GARY JENSEN (CPA),** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Gary Jensen ("Respondent" or "Jensen") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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,

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

The Commission, with due regard to the public interest and without preliminary hearing, may, by order,...suspend from appearing or practicing before it any....accountant...who has been by name...permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

paragraph 3, below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Jensen, age 54, is a certified public accountant and was licensed to practice in the State of Missouri. He served as senior vice president and corporate controller of Cardinal Health, Inc. ("Cardinal") from August 2002 until his resignation in February 2005. From January 2003 until October 2004, Jensen also served as Cardinal's principal accounting officer.

2. Cardinal was, at all relevant times, an Ohio corporation with its principal place of business in Dublin, Ohio. Cardinal was, and continues to be, engaged in the business of developing and distributing health care and pharmaceutical products and services. At all relevant times, Cardinal's common stock was registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the New York Stock Exchange.

3. On May 27, 2009, the Commission filed a complaint against Jensen in SEC v. Gary Jensen, et al., Civil Action No. 09-CV-4945, in the United States District Court for the Southern District of New York. On May 29, 2009, the court entered an order permanently enjoining Jensen, by consent, from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5, 13b2-1, and 13b2-2 thereunder, and aiding and abetting violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder. Jensen was also ordered to pay a $75,000 civil money penalty.

4. The Commission's complaint alleged, among other things, that, at different times from at least September 2000 through at least March 2004, Jensen and other former senior accounting and finance officers of Cardinal engaged in a fraudulent earnings and revenue management scheme to inflate Cardinal's publicly reported operating revenue, earnings and growth trends. The Complaint alleged that Jensen engaged in a number of improper accounting and disclosure practices that materially misrepresented Cardinal's publicly reported revenue, earnings, and growth trends. These practices included, among other things: misclassifying bulk sales as operating revenue to overstate reported operating revenue; overstating quarterly earnings by selectively accelerating the recognition of cash discount income; and improperly establishing and/or using a general reserve account and directing or approving the adjustment of various reserve accounts in a departure from generally accepted accounting principles ("GAAP"). In addition, the Complaint alleged that Jensen signed at least one materially false and misleading management representation letter to Cardinal's external auditor.

On October 26, 2004, as described in the Complaint, Cardinal restated its financial results for fiscal years 2000 to 2003 and for the first three quarters of fiscal year 2004. In its restatement, Cardinal disclosed, among other things, that it had improperly classified \$1.2 billion of bulk revenue as operating revenue and that Cardinal had an undisclosed practice of accelerating payment of vendor invoices at the end of certain reporting periods, which improved operating results for those periods. The restatement (as subsequently corrected) also reduced Cardinal's net earnings by a cumulative total of \$65.9 million, due to Cardinal's adjustments to reserves and other accruals, which were restated as a result of misapplications of GAAP, other errors or an absence of substantiation. In addition, Cardinal reversed, reclassified and recognized in a later period the \$22 million of expected litigation settlement proceeds it had previously recognized during the second quarter of fiscal year 2001 and the first quarter of fiscal year 2002.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately that:

A. Jensen is suspended from appearing or practicing before the Commission as an accountant.

B. After three years from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Schapiro
not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60076 / June 9, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2988 / June 9, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13510

In the Matter of **RICHARD MILLER (CPA),** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Richard Miller ("Respondent" or "Miller") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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,

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order,...suspend from appearing or practicing before it any....accountant...who has been by name...permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

paragraph 3, below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Miller, age 52, is and has been a certified public accountant licensed to practice in the State of Ohio. He served as Chief Financial Officer of Cardinal Health, Inc. ("Cardinal") from 1998 until his resignation in July 2004.

2. Cardinal was, at all relevant times, an Ohio corporation with its principal place of business in Dublin, Ohio. Cardinal was, and continues to be, engaged in the business of developing and distributing health care and pharmaceutical products and services. At all relevant times, Cardinal's common stock was registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the New York Stock Exchange.

3. On May 27, 2009, the Commission filed a complaint against Miller in SEC v. Richard Miller, et al., Civil Action No. 09-CV-4945, in the United States District Court for the Southern District of New York. On May 29, 2009, the court entered an order permanently enjoining Miller, by consent, from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5, 13b2-1, 13b2-2, and 13a-14 thereunder, and aiding and abetting violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder. Miller was also ordered to pay a $120,000 civil money penalty.

4. The Commission's complaint alleged, among other things, that, at different times from at least September 2000 through at least March 2004, Miller and other former senior accounting and finance officers of Cardinal engaged in a fraudulent earnings and revenue management scheme to inflate Cardinal's publicly reported operating revenue, earnings and growth trends. The Complaint alleged that Miller engaged in a number of improper accounting and disclosure practices that materially misrepresented Cardinal's publicly reported revenue, earnings, and growth trends. These practices included, among other things: misclassifying bulk sales as operating revenue to overstate reported operating revenue; overstating quarterly earnings by selectively accelerating the recognition of cash discount income; improperly establishing and/or using a general reserve account and directing or approving the adjustment of various reserve accounts to meet earnings projections in a departure from generally accepted accounting principles ("GAAP"); and improperly classifying expected litigation settlement proceeds to inflate earnings, in a further departure from GAAP. In addition, the Complaint alleged that Miller signed at least one materially false and misleading management representation letter to Cardinal's external auditor and signed certifications

falsely certifying the accuracy of the financial statements and disclosures in Cardinal's periodic filings.

On October 26, 2004, as described in the Complaint, Cardinal restated its financial results for fiscal years 2000 to 2003 and for the first three quarters of fiscal year 2004. In its restatement, Cardinal disclosed, among other things, that it had improperly classified $1.2 billion of bulk revenue as operating revenue and that Cardinal had an undisclosed practice of accelerating payment of vendor invoices at the end of certain reporting periods, which improved operating results for those periods. The restatement (as subsequently corrected) also reduced Cardinal's net earnings by a cumulative total of $65.9 million due to Cardinal's adjustments to reserves and other accruals, which were restated as a result of misapplications of GAAP, other errors or an absence of substantiation. In addition, Cardinal reversed, reclassified and recognized in a later period the $22 million of expected litigation settlement proceeds it had previously recognized during the second quarter of fiscal year 2001 and the first quarter of fiscal year 2002.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately that:

A. Miller is suspended from appearing or practicing before the Commission as an accountant.

B. After five years from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey, and
Commissioner Paredes
Disapproved

SECURITIES AND EXCHANGE COMMISSION

17 CFR PARTS 200, 232, 240, 249 and 274

[Release Nos. 33-9046; 34-60089; IC-28765; File No. S7-10-09]

RIN 3235-AK27

FACILITATING SHAREHOLDER DIRECTOR NOMINATIONS

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: We are proposing changes to the federal proxy rules to remove impediments to the exercise of shareholders' rights to nominate and elect directors to company boards of directors. The new rules would require, under certain circumstances, a company to include in the company's proxy materials a shareholder's, or group of shareholders', nominees for director. The proposal includes certain requirements, key among which are a requirement that use of the new procedures be in accordance with state law, and provisions regarding the disclosures required to be made concerning nominating shareholders or groups and their nominees. In addition, the new rules would require companies to include in their proxy materials, under certain circumstances, shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with the Commission's disclosure rules – including the proposed new rules. We also are proposing changes to certain of our other rules and regulations – including the existing exemptions from our proxy rules and the beneficial ownership reporting requirements – that may be affected by the new proposed procedures.

DATES: Comments should be received on or before [insert date 60 days after publication in the Federal Register].

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.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-10-09 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 Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-10-09. 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/final.shtml). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. 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: Lillian Brown, Tamara Brightwell, or Eduardo Aleman, Division of Corporation Finance, at (202) 551-3200, or, with regard to investment companies, Kieran G. Brown, Division of Investment Management, at (202) 551-6784, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

SUPPLEMENTARY INFORMATION: We are proposing new Rule 82a of Part 200 Subpart D – Information and Requests,[1] and new Rules 14a-11,[2] 14a-18,[3] and 14a-19,[4] new Regulation 14N[5] and Schedule 14N,[6] and amendments to Rule 13[7] of Regulation S-T,[8] Rules 13a-11,[9] 13d-1,[10] 14a-2,[11] 14a-4,[12] 14a-6,[13] 14a-8,[14] 14a-9,[15] 14a-12,[16] and 15d-11,[17] Schedule 14A,[18] and

1 17 CFR 200.82a.

2 17 CFR 240.14a-11.

3 17 CFR 240.14a-18.

4 17 CFR 240.14a-19.

5 17 CFR 240.14n et seq.

6 17 CFR 240.14n-101.

7 17 CFR 232.13.

8 17 CFR 232.10 et seq.

9 17 CFR 240.13a-11.

10 17 CFR 240.13d-1.

11 17 CFR 240.14a-2.

12 17 CFR 240.14a-4.

13 17 CFR 240.14a-6.

14 17 CFR 240.14a-8.

15 17 CFR 240.14a-9.

16 17 CFR 240.14a-12.

17 17 CFR 240.15d-11.

18 17 CFR 240.14a-101.

Form 8-K,[19] under the Securities Exchange Act of 1934.[20] Although we are not proposing amendments to Schedule 14C[21] under the Exchange Act, the proposed amendments would affect the disclosure provided in Schedule 14C, as Schedule 14C requires disclosure of some items of Schedule 14A.

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[19] 17 CFR 249.308.

[20] 15 U.S.C. 78a et seq.

[21] 17 CFR 240.14c-101.

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I. THE NEED FOR REFORMS TO THE FEDERAL PROXY RULES

A. Overview

The nation and the markets have recently experienced, and remain in the midst of, one of the most serious economic crises of the past century. This crisis has led many to raise serious concerns about the accountability and responsiveness of some companies and boards of directors to the interests of shareholders, and has resulted in a loss of investor confidence. These concerns have included questions about whether boards are exercising appropriate oversight of management, whether boards are appropriately focused on shareholder interests, and whether boards need to be more accountable for their decisions regarding such issues as compensation structures and risk management. In light of the current economic crisis and these continuing concerns, the Commission has determined to revisit whether and how the federal proxy rules may be impeding the ability of shareholders to hold boards accountable through the exercise of their fundamental right to nominate and elect members to company boards of directors.

Regulation of the proxy process and disclosure is a core function of the Commission and is one of the original responsibilities that Congress assigned to the Commission in 1934. Section 14(a) of the Exchange Act[22] stemmed from a Congressional belief that "[f]air corporate suffrage is an important right that should attach to every equity security bought on a public exchange."[23] The Congressional committees recommending passage of Section 14(a) proposed that "the solicitation and issuance of proxies be left to regulation by the Commission"[24] and explained that Section 14(a) would give the Commission the "power to control the conditions under which

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22 15 U.S.C. 78n(a)

23 H. R. Rep. No. 1383, 73d Cong., 2d Sess., 13. See also Mills v. Electric Auto-Lite Co., 396 U.S. 375, 381 (1970); J. I. Case Co. v. Borak, 377 U.S. 426, 431 (1964).

24 S. Rep. No. 792, 73d Cong., 2d Sess., 12 (1934).

proxies may be solicited."[25] Congress thus recognized a federal interest in the way public corporations handle the proxy process, and granted the Commission authority to prescribe rules to regulate the solicitation of proxies "as necessary or appropriate in the public interest or for the protection of investors."[26]

Responding to the Commission's mandate from Congress, the Commission has actively overseen the development of the proxy process since 1934. The Commission has monitored the process and has considered changes when it appeared that the process was not functioning in a manner that adequately protected the interests of investors.[27] At the same time, the Commission has been mindful of the traditional role of the states in regulating corporate governance. For example, Exchange Act Rule 14a-8,[28] the shareholder proposal rule, explicitly provides that a company is permitted to exclude a shareholder proposal if it "is not a proper subject for action by shareholders under the laws of the jurisdiction of the company's organization"[29] or "[i]f the

25 H.R. Rep. No. 1383, 73d Cong., 2d Sess., 14 (1934). The same report demonstrated a congressional intent to prevent frustration of the "free exercise of the voting rights of stockholders." Id. Courts have found that the relevant legislative history also demonstrates an "intent to bolster the intelligent exercise of shareholder rights granted by state corporate law." Roosevelt v. E.I. Du Pont de Nemours & Co., 958 F.2d 416, 421 (D.C. Cir. 1992); see Borak, 377 U.S. at 431.

26 15 U.S.C. 78n(a).

27 For example, as discussed in further detail below, the Commission has considered changes to the proxy rules in recent years. See Security Holder Director Nominations, Release No. 34-48626 (October 14, 2003) [68 FR 60784] ("2003 Proposal"); Shareholder Proposals, Release No. 34-56160 (July 27, 2007) [72 FR 43466] ("Shareholder Proposals Proposing Release"); Shareholder Proposals Relating to the Election of Directors, Release No. 34-56161 (July 27, 2007) [72 FR 43488] ("Election of Directors Proposing Release"); and Shareholder Proposals Relating to the Election of Directors, Release No. 34-56914 (December 6, 2007) [72 FR 70450] (Election of Directors Adopting Release"). When we refer to the "2007 Proposals" and the comments received in 2007, we are referring to the Shareholder Proposals Proposing Release and the Election of Directors Proposing Release and the comments received on those proposals, unless otherwise specified.

28 17 CFR 240.14a-8.

29 17 CFR 240.14a-8(i)(1).

proposal would, if implemented, cause the company to violate any state, federal, or foreign law to which it is subject."[30]

In identifying the rights that the proxy process should protect, the Commission has sought to take as a touchstone the rights of shareholders under state corporate law. As Chairman Ganson Purcell explained to a committee of the House of Representatives in 1943:

> The rights that we are endeavoring to assure to the stockholders are those rights that he has traditionally had under State law, to appear at the meeting; to make a proposal; to speak on that proposal at appropriate length; and to have his proposal voted on.[31]

This principle has given rise to a shorthand that explains much of the Commission's activity in regulating the proxy process. The proxy rules seek to improve the corporate proxy process so that it functions, as nearly as possible, as a replacement for an actual in-person meeting of shareholders.

Refining the proxy process so that it replicates, as nearly as possible, the annual meeting is particularly important given that the proxy process has become the primary way for shareholders to learn about the matters to be decided by the shareholders and to make their views known to company management.[32] Our recent examinations of the proxy process and the

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30 17 CFR 240.14a-8(i)(2).

31 Securit[ies] and Exchange Commission Proxy Rules: Hearings on H.R. 1493, H.R. 1821, and H.R. 2019 before the House Committee on Interstate and Foreign Commerce, 78th Cong., 1st Sess. 172 (1943) (statement of SEC Chairman Ganson Purcell).

32 See, e.g., Securit[ies] and Exchange Commission Proxy Rules: Hearings on H.R. 1493, H.R. 1821, and H.R. 2019 Before the House Comm. on Interstate and Foreign Commerce, 78th Cong., 1st Sess., at 17-19 (1943) (Statement of the Honorable Ganson Purcell, Chairman, Securities and Exchange Commission) (Explaining the initial Commission rules requiring the inclusion of shareholder proposals in the company proxy materials: "We give [a stockholder] the right in the rules to put his proposal before all of his fellow stockholders along with all other proposals … so that they can see then what they are and vote accordingly. … The rights that we are endeavoring to assure to the stockholders are those rights that he has traditionally had under State law, to appear at the meeting; to make a proposal; to speak on that proposal at appropriate

comments that we have received in the course of these examinations suggest that the director nomination and shareholder proposal processes are two areas in which our current proxy rules pose impediments to the exercise of shareholders' rights.[33] These proposed amendments are intended to remove impediments so shareholders may more effectively exercise their rights under state law to nominate and elect directors at meetings of shareholders.

There are many competing policy arguments about the effect that shareholder-nominated directors or shareholder-proposed nomination procedures might have on a company and its governance. Some commenters believe that the presence of shareholder-nominated directors would make boards more accountable to the shareholders who own the company and that this accountability would improve corporate governance and make companies more responsive to shareholder concerns.[34] Some commenters further express the belief that, absent an effective way for shareholders to exercise rights to nominate and elect directors that state corporate law presumes shareholders have, the election of directors is a self-sustaining process of the board

length; and to have his proposal voted on. But those rights have been rendered largely meaningless through the process of dispersion of security ownership through[out] the country. ... [T]he assurance of these fundamental rights under State laws which have been, as I say, completely ineffective ... because of the very dispersion of the stockholders' interests throughout the country[;] whereas formerly.... a stockholder might appear at the meeting and address his fellow stockholders[, t]oday he can only address the assembled proxies which are lying at the head of the table. The only opportunity that the stockholder has today of expressing his judgment comes at the time he considers the execution of his proxy form, and we believe ... that this is the time when he should have the full information before him and ability to take action as he sees fit."); see also S. Rep. 792. 73d Cong., 2d Sess., 12 (1934) ("[I]t is essential that [the stockholder] be enlightened not only as to the financial condition of the corporation, but also as to the major questions of policy, which are decided at stockholders' meetings.").

33 See, e.g., Unofficial Transcript of the Roundtable Discussion on Proposals for Shareholders, May 25, 2007, comments of Leo E. Strine Jr., Vice Chancellor, Court of Chancery of the State of Delaware (Vice Chancellor Strine), at 112, available at: http://www.sec.gov/news/openmeetings/2007/openmtg_trans052507.pdf (observing that it is "a little bit perverse" that "a bylaw dealing with the election process that might well have been viable under state law was kept off the ballot when you could have something that was precatory mandated to be on the ballot").

34 See, e.g., comment letters on the 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from James McRitchie, Corporate Governance (October 1, 2007) ("McRitchie 2007"); and Stephen Abrecht, Executive Director, SEIU Master Trust (October 1, 2007) ("SEIU").

determining its members, with little actual input from shareholders.[35] Commenters have noted that without competition for director elections, directors are effectively unaccountable to shareholders and may lose sight of their proper role as representatives of the company.[36]

Similarly, foreign investors have noted the lack of accountability of directors in the United States compared with other countries, stating among other things that "[t]he harsh reality is that U.S. corporate governance practices are on a relative decline compared to other leading markets."[37] In that vein, the Committee on Capital Markets Regulation has observed that this "difference creates an important potential competitiveness problem for U.S. companies."[38] Other commenters have expressed concern that the relative inability of shareholders of U.S. companies to participate in the selection of directors compared with shareholders of their foreign competitors creates a competitiveness problem for U.S. companies.[39]

Academic literature also has highlighted the roles of boards of directors at companies that have demonstrated corporate governance failings. Such literature points to a link between board

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35 See, e.g., 2004 Roundtable Submission of Lucian Bebchuk: Lucian Arye Bebchuk, The Case for Shareholder Access to the Ballot, 59 The Business Lawyer 43, 49 (2003) ("Bebchuk 2003 Article") ("Suppose that there is a widespread concern among shareholders that a board with a majority of independent directors is failing to serve shareholder interests. It is precisely under such circumstances that the nominating committee cannot be relied on to make desirable replacements of members of the board or even of members of the committee itself – at least not unless shareholders have adequate means of applying pressure on the committee.").

36 See, e.g., comment letter on 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from William Apfel, et al., Walden Asset Management (September 11, 2007).

37 Comment letter on 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from Michael O'Sullivan, President, Australian Council of Super Investors, et al. (October 2, 2007). See also Michelle Edkins, Acting Chairman, International Corporate Governance Network Shareholder Rights Committee (October 2, 2007) and Knut Kjer, CEO, Norges Bank Investment Management, et al. (September 28, 2007).

38 Committee on Capital Markets Regulation, Interim Report (November 30, 2006) at 109, available at: http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf.

39 See comment letter on 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from Carl Levin, United States Senator, (September 27, 2007) at page 6.

accountability and company performance.[40] In recognition of this link, Congress passed the Sarbanes-Oxley Act of 2002 to help strengthen corporate governance at public companies.[41] Commenters additionally have argued that competition for board seats might lead companies to nominate directors who are better qualified and more independent.[42]

On the other side of the debate, some commenters have raised concerns that shareholder-nominated directors could impede the proper functioning of companies and cause inefficiencies. For example, some argue that a shareholder-nominated director may be beholden to and focused solely on the concerns of the nominating shareholder or group, with the potential result being that a small number of shareholders could impose their unique concerns on the company and the rest of shareholders.[43] Additionally, some commenters have suggested that the presence of a shareholder-nominated director could disrupt the functioning of the board and could even lead to the company moving in a direction that does not reflect the interests of its shareholders overall.[44] Others have raised concerns that the possibility of a contested election could deter qualified

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40 See, e.g., Michael E. Murphy, The Nominating Process for Corporate Boards of Directors – A Decision-Making Analysis, 5 BERKELEY BUS. L.J. 131 (2008).

41 See, e.g., Section 301 of the Sarbanes-Oxley Act of 2002, inserting Section 10A(m) to the Exchange Act, which directed the Commission to promulgate rules requiring the national securities exchanges to "prohibit the listing of any security of an issuer that is not in compliance" with the Act's audit committee provisions. As a consequence, listed companies are now required to have audit committees composed solely of independent directors.

42 See generally Bebchuk 2003 Article. See also In re Oracle Corp. Derivative Litigation, 824 A.2d 917, 941 (Del. Ch. 2003) ("The recent reforms enacted by Congress and by the stock exchanges reflect a narrower conception of who they believe can be an independent director. These definitions, however, are blanket labels that do not take into account the decision at issue. Nonetheless, the definitions recognize that factors other than the ones explicitly identified in the new exchange rules might compromise a director's independence, depending on the circumstances.").

43 See, e.g., comment letters on 2007 Proposals from Thomas Wilson, President, The Allstate Corporation (October 2, 2007) and David T. Hirschmann, Senior Vice President, U.S. Chamber of Commerce (October 2, 2007).

44 See, e.g., comment letter on 2007 Proposals from Anne M. Mulcahy, Chairman, Business Roundtable Corporate Governance Task Force, Business Roundtable (October 1, 2007) ("Mulcahy, BRT").

candidates from seeking to serve as members of a board.[45]

We recognize that there are long-held and deeply felt views on both sides of these issues. The action we take today is focused on removing burdens that the federal proxy process currently places on the ability of shareholders to exercise their basic rights to nominate and elect directors. If we adopted rules to remove those burdens, we believe that these rules would facilitate shareholders' ability to participate more fully in the debates surrounding these issues. To the extent shareholders have the right to nominate directors at meetings of shareholders, the federal proxy rules should not impose unnecessary barriers to the exercise of this right.[46] The SEC's mission is investor protection, and we believe that investors are best protected when they can exercise the rights they have as shareholders, without unnecessary obstacles imposed by the federal proxy rules.

Based on the staff's and Commission's review of the proxy solicitation process and the extensive public input that we have received over the past several years on the topic of shareholders' ability to meaningfully exercise their rights to vote for and nominate directors of the companies in which they invest, we have decided to propose changes to the current proxy rules relating to the nomination of directors. First, we believe that we can and should structure the proxy rules to better facilitate the exercise of shareholders' rights to nominate and elect directors. The right to nominate is inextricably linked to, and essential to the vitality of, a right

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45 Id.

46 See, e.g., Unofficial Transcript of the Roundtable on the Federal Proxy Rules and State Corporation Law (May 7, 2007), comments of R. Franklin Balotti, Director, Richards, Layton & Finger, P.A., at 14-17, available at: http://www.sec.gov/spotlight/proxyprocess/proxy-transcript050707.pdf; Unofficial Transcript of the Roundtable on the Federal Proxy Rules and State Corporation Law (May 7, 2007), comments of Vice Chancellor Strine, at 18-23; and Unofficial Transcript of the Roundtable on the Federal Proxy Rules and State Corporation Law (May 7, 2007), comments of Stanley Keller, Edwards Angell Palmer & Dodge LLP, at 142-143.

to vote for a nominee.[47] The failure of the proxy process to adequately facilitate shareholder nomination rights has a direct and practical effect on the right to elect directors.[48] As noted, the proxy rules have been designed to improve the proxy process so that it functions, as nearly as possible, as a replacement for an in-person meeting of shareholders. This is important because the proxy process today represents shareholders' principal means of participating effectively at an annual or special meeting of shareholders.[49] Based on the feedback we have received over the last few years, it appears that the federal proxy process may not be adequately replicating the conditions of the shareholder meeting. Second, we believe that parts of the federal proxy process may unintentionally frustrate voting rights arising under state law, and thereby fail to provide fair corporate suffrage. These two potential shortcomings in our regulations provide compelling

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47 See, e.g., Durkin v. Nat'l Bank of Olyphant, 772 F.2d 55, 59 (3d Cir. 1985) (stating that "the unadorned right to cast a ballot in a contest for office, a vehicle for participatory decisionmaking and the exercise of choice, is meaningless without the right to participate in selecting the contestants. As the nominating process circumscribes the range of the choice to be made, it is a fundamental and outcome-determinative step in the election of officeholders. To allow for voting while maintaining a closed candidate selection process thus renders the former an empty exercise. This is as true in the corporate suffrage context as it is in civic elections, where federal law recognizes that access to the candidate selection process is a component of constitutionally-mandated voting rights. See United States v. Classic, 313 U.S. 299, 316-317, 85 L.Ed. 1368, 61 S.Ct. 1031 (1941) (article I, section 2 right to choose congressional representatives includes the right to participate in primary elections); Smith v. Allwright, 321 U.S. 649, 661-662, 88 L.Ed. 987, 64 S.Ct. 757 (1944) (fifteenth amendment prohibition of race-based abridgement of voting rights applies to primary as well as general elections). Banks do not exist for the purpose of creating an aristocracy of directors and officers which can continue in office indefinitely, immune from the wishes of the shareholder-owners of the corporation. And there is no more justification for precluding shareholders from nominating candidates for their board of directors than there would be for public officials to deny citizens the right to vote because of their race, poverty or sex. Cf. U.S. Const. amends. XV, XXIV, and XIX." id. at 59 (emphasis added)); and Hubbard v. Hollywood Park Realty Enterprises, Inc., 1991 Del. Ch. LEXIS 9 (Del. Ch. Jan. 14, 1991) (quoting Durkin).

48 Shoen v. Amerco, 885 F.Supp. 1332, 1342 (D. Nev. 1994) ("unadorned right to cast a ballot in a contest for office, after all, is meaningless without the right to participate in selecting the contestants" (internal quotation marks omitted)).

49 Historically, a shareholder's voting rights generally were exercised at a shareholder meeting. As discussed above, in passing the Securities Exchange Act, Congress understood that many companies had become held nationwide through dispersed ownership, at least in part facilitated by stock exchange listing of shares. Although voting rights in public companies technically continued to be exercised at a meeting, the votes cast at the meeting were by proxy and the voting decision was made during the proxy solicitation process. This structure persists to this day.

reasons for us to reform the proxy process and our disclosure requirements relating to director nominations.[50] The comments received on the Commission's recent proposals on this topic in 2003 and in 2007, as well as the Roundtables held by the Commission in 2004 and 2007, helped form the basis for our beliefs.[51]

B. Shareholder Participation in the Nomination and Election Process

1. Existing Shareholder Options

Many commenters have noted that current procedures available for director nominations afford little practical ability for shareholders to participate effectively in the nomination process and, through that process, exercise their rights and responsibilities as owners of their companies.[52] If shareholders are dissatisfied with their company's performance and believe that the problem lies with the ineffectiveness of the company's board of directors, the existing proxy process provides shareholders with three principal options to attempt to effect change.[53] First, shareholders can mount a proxy contest in accordance with our proxy rules. Second,

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50 The Commission's proxy rules have required shareholder proposals on certain matters to be included in company proxy materials since 1940 (see Release No. 34-2376 (January 12, 1940)), subject to amendment from time to time pursuant to the Commission's dynamic regulation of the proxy process.

51 See 2003 Proposal; Shareholder Proposals Proposing Release; Election of Directors Proposing Release; and Election of Directors Adopting Release. See also, Section II, below, regarding the Commission's consideration of the proxy rules.

52 See, e.g., 2003 Staff Report and summary of comments in response to the Commission's May 1, 2003 solicitation of comments.

53 Commenters on the 2003 Proposal discussed the range of options currently available. See, e.g., comment letters from Ashland, Inc. (December 17, 2003) ("Ashland"); Conoco-Phillips (December 31, 2003); Delphi Corporation (December 10, 2003); Emerson Electric Co. (December 15, 2003); Financial Services Roundtable (December 22, 2003); Kerr-McGee Corporation (December 22, 2003) ("Kerr-McGee"); Independent Community Bankers of America (December 22, 2003); Letter Type D; Malcom S. Morris (November 6, 2003) ("Morris"); Office Depot, Inc. (December 22, 2003) ("Office Depot"); Valero Energy Corporation (December 18, 2003) ("Valero"); and Wachtell Lipton Rosen & Katz (November 14, 2003) ("Wachtell"). Cf. Blasius, 564 A.2d at 659 ("Generally, shareholders have only two protections against perceived inadequate business performance. They may sell their stock (which, if done in sufficient numbers, may so affect security prices as to create an incentive for altered managerial performance), or they may vote to replace incumbent board members.").

shareholders can use the shareholder proposal procedure in Rule 14a-8 to submit proposals and have a vote on topics that are important to them. Third, shareholders can conduct a "withhold vote" or "vote no" campaign against one or more directors.[54]

Shareholders also can use options that exist outside of the proxy process. For example, shareholders can sell their shares (sometimes referred to as the "Wall Street Walk"); they can engage in a dialogue with management (including recommending a candidate to the nominating committee); or they can propose a board nominee at a shareholder meeting. Each of these options has drawbacks that limit its effectiveness.[55]

a. Options Using the Proxy Process

Shareholders' existing options under the proxy rules to exercise their ownership rights are often criticized. The chief complaint from shareholders about the existing options is the high cost involved in mounting a proxy contest under the Commission's proxy rules. Because this cost must be borne by the shareholders undertaking the contest, the option generally is not used outside the corporate-control context, where the cost may be better justified.[56] A shareholder or group of shareholders that is dissatisfied with the leadership of a company generally, but is not

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54 In the case of plurality voting, shareholders may vote in the election of directors for, or withhold authority to vote for, each nominee rather than vote for, against or abstain, as is the case for other matters to be voted on by shareholders. See Exchange Act Rule 14a-4(b)(2).

55 See, e.g., comment letter on the 2003 Proposal from The Corporate Library (December 22, 2003) ("Corporate Library") ("Shareholders can sell the stock at what they perceive to be a substantial discount. Or they can run their own slate of candidates, paying 100 percent of the costs, which may come to hundreds of thousands or even millions of dollars, for only a pro rata share of any increase in shareholder value as a result of the contested election. Meanwhile, management will spend the shareholders' money to fight them. This is not a level playing field. It is close to perpendicular.").

56 See, e.g., Corporate Library. See also Bebchuk 2003 Article at 46. Surveying data from contested elections from 1996 to 2002, Professor Bebchuk concludes that "the safety valve of potential ouster via the ballot is currently not working. In the absence of an attempt to acquire the company, the prospect of being removed in a proxy contest is far too remote to provide directors with incentives to serve shareholders." The principal reason the costs could be better justified in the corporate control context is because benefits that are expected to arise from a successful contest are internalized by the shareholder undertaking the contest.

seeking a change in control must, as a result of our proxy rules, nevertheless undertake a proxy contest, along with its related expenses and other burdens, to put nominees before the shareholders for a vote. The shareholder proposal process in Rule 14a-8, under which a company may be required to include a shareholder proposal in the company proxy materials, also has been criticized as an ineffective tool for exercising ownership rights, as Rule 14a-8 is not available for proposals that relate to director elections.[57] With regard to withhold vote and vote no campaigns, because some companies use plurality voting for board elections and therefore candidates can be elected regardless of whether they receive more than 50% of the shareholder vote, withhold vote campaigns may be limited in their effectiveness. In addition, restrictions under the proxy rules may limit the effectiveness of withhold vote and vote no campaigns because shareholders cannot solicit proxy authority through these campaigns.

Further, in any vote for the election of directors, customary election processes may serve to amplify the practical effect that the proxy rules have in impeding shareholder nominees.[58] In particular, as noted with regard to withhold vote campaigns, for companies using plurality rather than majority voting for board elections, nominees generally can be elected as director regardless of whether they receive a majority of the shareholder vote.[59] Therefore, in an election in which there are the same number of nominees as there are board positions open, each nominee

[57] Exchange Act Rule 14a-8(i)(8).

[58] See, e.g., Unofficial Transcript of the Security Holder Director Nominations Roundtable (March 10, 2004) ("2004 Roundtable Transcript"), comments of Ira M. Millstein, Weil, Gotshal & Manges, available at: http://www.sec.gov/spotlight/dir-nominations/transcript03102004.txt.

[59] Under plurality voting, the nominee with the greatest number of votes is elected. But see footnote 69, below (noting that some companies using a plurality standard have adopted policies requiring incumbent directors to resign if they receive less than majority support). Shareholders at companies using majority voting, or some other voting method other than plurality voting, may be better able to express dissatisfaction with a company's nominee or nominees. As discussed, in recent years, many companies have adopted a majority voting standard.

receiving even a single vote will be elected, regardless of the number of votes withheld from a nominee.

b. Options Outside the Proxy Process

Shareholders also are critical of the options available to them outside the proxy process. The "Wall Street Walk" is not an optimal solution because it may not be practical for large institutional shareholders and others who follow a passive management or indexing strategy, and it may require investors to lock in a loss.[60] Selling shares may be very costly for these types of investors because they may face liquidity issues as a result of the size of their holdings and may be forced to sell their holdings in a manner that results in capital gains and therefore is not tax efficient. In addition, while selling shares may depress the stock price, leading to higher cost of capital for the firm and thus may ultimately spur management changes,[61] the investor who sold its shares will not benefit from any improvement that follows the management change.

Engaging management in a dialogue also may not be an effective option for shareholders because company management may be unresponsive to investor concerns.[62] While shareholders can recommend an individual for nomination as director to a company's nominating committee,

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60 See 2003 Summary of Comments, text at notes 9-10. Although the AFL-CIO noted that active managers of mutual funds can sell their shares in a company with an "ineffective or unresponsive board," pension fund managers, including the AFL-CIO and Amalgamated Bank Longview Fund, noted that the issue of director accountability is more important to them because they may manage index funds that are necessarily long-term investors who cannot easily sell. See comment letters from American Federation of Labor and Congress of Industrial Organizations (December 19, 2003) ("AFL-CIO") and Amalgamated Bank LongView Funds (December 21, 2003) ("LongView"). See also 2004 Roundtable Transcript, comments of Richard H. Moore, Treasurer of North Carolina.

61 See 2004 Roundtable Transcript, comments of Peter J. Wallison, American Enterprise Institute.

62 See, e.g., comment letters on the 2003 Proposal from Lucian A. Bebchuk (December 22, 2003) ("Bebchuk"); California Public Employees' Retirement System ("CalPERS"); California State Teachers' Retirement System ("CalSTRS") (December 4, 2003); Charles Capito (October 20, 2003); Council of Institutional Investors ("CII") (December 12, 2003); Creative Investment Research ("CIR") (December 22, 2003); Corporate Library; and Aaron Rosenthal (October 20, 2003).

we understand these recommendations are rarely accepted by nominating committees.[63] Moreover, in some cases, shareholders may not be able to exercise their state law rights effectively because they have had difficulty gaining access to members of company boards and their committees.[64]

Finally, given the near universal use of proxy voting and the inability of shareholders to use the company proxy to vote for shareholder nominees, it can be futile to nominate a director in person at a shareholder meeting.[65]

2. Recent Corporate Governance and Other Reforms

Over the past several years there have been a number of changes in corporate governance practices and the federal securities laws that may have mitigated some of the concerns expressed by commenters in 2003 and 2007 but, in our view, have not sufficiently addressed the central problem that we are seeking to solve – shareholders' limited ability to exercise their rights to nominate directors and have the nominations disclosed to and considered by the shareholders. For example, some commenters on the 2003 Proposal urged the Commission to defer action in

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63 See, e.g., Division of Corporation Finance, U.S. Securities and Exchange Commission, Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors (July 15, 2003), available at: http://www.sec.gov/news/studies/proxyreport.pdf; see also, comment letter on the 2003 Proposal from CII; and Michael E. Murphy, The Nominating Process for Corporate Boards of Directors – A Decision-Making Analysis, 5 BERKELEY BUS. L.J. 131 (2008).

64 See, e.g., comment letter on the 2003 Proposal from CII; comment letter on 2007 Proposals from SEIU. See also Michael E. Murphy, The Nominating Process for Corporate Boards of Directors – A Decision-Making Analysis, 5 BERKELEY BUS. L.J. 131 (2008). See also Division of Corporation Finance, U.S. Securities and Exchange Commission, Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors (July 15, 2003), available at: http://www.sec.gov/news/studies/proxyreport.pdf.

65 See Unofficial Transcript of the Roundtable Discussion Regarding the Federal Proxy Rules and State Corporation Law (May 7, 2007), comments of Vice Chancellor Strine at 79 (commenting that "this annual meeting thing could be a fix" where the most active shareholder institutions gain representation on the board through other means such as through litigation settlement); see generally, 5 Fletcher Cyclopedia of Corporations § 2049.10 (Perm. Ed.) ("In large corporations, the shareholders' meeting is now only a necessary formality; the shareholders' expression can only be had by the statutory device of proxies and solicitation of proxies.").

order to assess the effectiveness of the then recently-enacted Sarbanes-Oxley Act of 2002 and other reforms, including enhanced director independence requirements and expansion of the nominating committee function at public companies.[66] Other commenters, while praising these reforms, doubted that they would be sufficient to address the problems that they hoped would be remedied through reform of the proxy process itself.[67] In particular, commenters in 2003 argued that objective independence standards for directors and the use of independent nominating committees, without more, may not counteract the perceived tendency of some boards to defer to management, given factors such as the significant personal relationships that can exist between directors and officers.[68] Therefore, shareholders may still want, but currently may not be able, to effectively nominate and elect directors that satisfy independence concerns specific to the companies in which they invest.

Since the 2003 Proposal, a number of other changes in the governance landscape have occurred, including a significant movement by larger companies toward majority voting rather than plurality voting in director elections,[69] and changes in state law to more expressly indicate that corporate governing documents may set out shareholders' right to nominate directors.[70] The

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66 See, e.g., comment letter from American Bar Association (January 7, 2004) ("ABA").

67 2004 Roundtable Transcript, comments of Nell Minow and Ralph V. Whitworth.

68 See generally, Bebchuk. See also In re Oracle Corp., 824 A.2d at 941. See footnote 42, above.

69 The Corporate Library reports that as of December 2008, 49.5 percent of companies in the S&P 500 had made the switch to majority voting for director elections and another 18.4 percent had, while retaining a plurality standard, adopted a policy requiring that a director that does not receive majority support must submit his or her resignation. On the other hand, the plurality voting standard is still the standard at the majority of smaller companies in the Russell 1000 and 3000 indices, with 54.5 percent of companies in the Russell 1000 and 74.9 percent of the companies in the Russell 3000 still using a straight plurality voting standard. The Corporate Library Analyst Alert, December 2008. See also Broadridge letter dated March 27, 2009 and attached analysis in response to File No. SR-NYSE-2006-92 (stating that in calendar year 2007, 373 NYSE-listed companies had a majority vote standard for the election of directors).

70 In CA, Inc. v. AFSCME, 953 A.2d 227 (Del. 2008), the Delaware Supreme Court held that shareholders can propose and adopt a bylaw regulating the process by which directors are elected. In light of this ruling, Delaware recently amended the Delaware General Corporation Law to add new Section 112, effective

Commission also has adopted changes to our rules, including enhanced disclosure requirements concerning nominating committees[71] and changes to our proxy rules to facilitate the use of electronic shareholder forums.[72] While these and other changes have been significant, after considering the views discussed throughout the release, we believe the federal proxy process could still be improved to further remove impediments to the exercise of shareholders' rights under state law to nominate directors.

II. RECENT COMMISSION CONSIDERATION OF THE PROXY RULES AND REGULATIONS ADDRESSING THE ELECTION OF DIRECTORS[73]

A. 2003 Review of the Proxy Process and Subsequent Rulemaking

In April 2003, the Commission directed the Division of Corporation Finance to review the proxy rules and regulations and interpretations regarding procedures for the nomination and

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August 1, 2009, clarifying that the bylaws of a Delaware corporation may provide that, if the corporation solicits proxies with respect to an election of directors, the corporation may be required to include in its solicitation materials one or more individuals nominated by a stockholder in addition to the individuals nominated by the board of directors. The obligation of the corporation to include such stockholder nominees will be subject to the procedures and conditions set forth in the bylaw adopted under Section 112. Delaware also added new Section 113, which will allow a Delaware corporation's bylaws to include a provision that the corporation, under certain circumstances, will reimburse a stockholder for the expenses incurred in soliciting proxies in connection with an election of directors. In addition, the American Bar Association's Committee on Corporate Laws, which is responsible for the Model Business Corporation Act, is considering similar changes to the Model Act. See American Bar Association, Section of Business Law, "Corporate Laws Committee To Address Current Governance Issues," April 29, 2009 (noting that Delaware's recent statutory amendments "are being actively considered by the Committee") (available at: http://www.abanet.org/abanet/media/release/news_release.cfm?releaseid=662). Thirty states have adopted all or substantially all of the Model Act as their general corporation statute.

Also, in 2007, North Dakota amended its corporate code to permit five percent shareholders to provide a company notice of intent to nominate directors and require the company to include each such shareholder nominee in its proxy statement and form of proxy. N.D. Cent. Code § 10-35-08 (2009); see North Dakota Publicly Traded Corporations Act, N.D. Cent. Code §10-35 et al. (2007).

71 See Disclosure Regarding Nominating Committee Functions and Communications Between Security Holders and Boards of Directors, Release No. 33-8340 (December 11, 2003) [68 FR 69204].

72 See Electronic Shareholder Forums, Release No. 34-57172 (January 18, 2008) [73 FR 4450] ("Electronic Shareholder Forums Release").

73 The Commission also has considered the topic on at least three earlier occasions – in 1942, 1977, and 1992. For a discussion, see 2003 Proposal.

election of corporate directors[74] and on May 1, 2003, the Commission solicited public input with respect to the Division's review.[75] Commenters generally supported the Commission's decision to review the proxy rules and regulations with respect to director nominations and elections and, in July 2003, the Division of Corporation Finance provided to the Commission its report and recommended changes to the proxy rules related to the nomination and election of directors.[76]

The Division recommended proposed changes in two areas: (1) disclosure related to nominating committee functions and shareholder communications with boards of directors; and (2) enhanced shareholder access to the proxy process relating to the nomination of directors.[77] The Commission proposed and adopted the recommended disclosure requirements concerning nominating committee functions and shareholder communications with boards of directors.[78] In addition, in October 2003, the Commission proposed rules that would have created a mechanism for nominees of long-term shareholders, or groups of long-term shareholders, with significant shareholdings to be included in company proxy materials.[79] The proposed new rules were intended to address perceived inadequacies in the proxy process with respect to director nominations and elections.[80] The proposal generated significant public comment, with

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74 See Press Release No. 2003-46 (April 14, 2003).

75 See Release No. 34-47778 (May 1, 2003) [68 FR 24530] and comment file number S7-10-03.

76 See Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors, Division of Corporation Finance (July 15, 2003) ("2003 Staff Report"), available at http://www.sec.gov/news/studies/proxyrpt.htm. See also Summary of Comments in Response to the Commission's Solicitation of Public Views Regarding Possible Changes to the Proxy Rules (July 15, 2003), attached as Appendix A to the Staff Report.

77 See 2003 Staff Report.

78 Disclosure Regarding Nominating Committee Functions and Communications Between Security Holders and Boards of Directors, Release No. 33-8340 (December 11, 2003) [68 FR 69204].

79 See 2003 Proposal. The proposal would have required shareholders to have held the requisite amount of securities to meet the ownership threshold for two years as of the date of the nomination.

80 See 2003 Proposal (explaining that the proposal would "apply only in those instances where criteria suggest

shareholders generally supporting adoption of rules that would facilitate their right to nominate directors and companies and their advisors generally opposing such rules because of concerns that a requirement to include shareholder director nominees in the company's proxy materials would impede the proper functioning of boards and cause inefficiencies.[81] The Commission did not adopt final rules based on the proposal.

B. 2007 Rulemaking Concerning Shareholder Proposals Seeking to Establish Bylaw Procedures for Shareholder Director Nominations

One of the means that shareholders use to express their views on the management and affairs of a company is through shareholder proposals, which are addressed in Rule 14a-8. Rule 14a-8 provides shareholders with an opportunity to place a proposal in a company's proxy materials for a vote at an annual or special meeting of shareholders. Under this rule, a company generally is required to include the proposal unless the shareholder has not complied with the rule's procedural requirements or the proposal falls within one of the rule's 13 substantive bases for exclusion. One of the substantive bases that a company may rely on in excluding a shareholder proposal is Rule 14a-8(i)(8), which addresses shareholder proposals concerning director elections.[82] This provision frequently is referred to as the "election exclusion." In interpreting this provision, the Commission took the position in 2007 that Rule 14a-8(i)(8) permits exclusion of a proposal that would establish a procedure that may result in contested elections to the board.[83]

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that the company has been unresponsive to security holder concerns as they relate to the proxy process").

81 See 2003 Summary of Comments.

82 Rule 14a-8(i)(8) provides that a company need not include a proposal that "relates to a nomination or an election for membership on the company's board of directors or analogous governing body or a procedure for such nomination or election[.]"

83 See Election of Directors Adopting Release (citing Commission statements made in Release No. 34-12598 (July 7, 1976) ("[T]he principal purpose of [Rule 14a-8(i)(8)] is to make clear, with respect to corporate

In 2006, the U.S. Court of Appeals for the Second Circuit, in American Federation of State, County and Municipal Employees, Employees Pension Plan v. American International Group, Inc.,[84] held that AIG could not rely on Rule 14a-8(i)(8) to exclude a shareholder proposal that, if adopted, would have amended AIG's bylaws to require the company, under specified circumstances, to include shareholder nominees for director in the company's proxy materials at subsequent meetings. The Second Circuit interpreted the language of the rule[85] and the Commission's statements in adopting the rule in 1976 as limiting the election exclusion "to shareholder proposals used to oppose solicitations dealing with an identified board seat in an upcoming election and reject[ing] the somewhat broader interpretation that the election exclusion applies to shareholder proposals that would institute procedures making such election contests more likely."[86] The effect of the AFSCME decision was to permit the bylaw proposal to be included in company proxy materials and, had the bylaw been approved by shareholders, for subsequent election contests conducted under it to take place in the company's proxy materials without compliance with the disclosure requirements applicable to election contests under the Commission's other proxy rules.[87] The Commission was concerned that the Second Circuit's

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elections, that Rule 14a-8 is not the proper means for conducting campaigns or effecting reforms in elections of that nature, since other proxy rules, including Rule 14a-[12], are applicable thereto.")). See also Division of Corporation Finance no-action letters to Citigroup, Inc. (January 31, 2003) and AOL Time Warner (February 29, 2003). As noted in the Election of Directors Proposing Release, in each of 1993 and 1995, the Division issued one letter that took a contrary view. See Dravo Corp. (February 21, 1995); and Pinnacle West Capital Corp. (March 26, 1993) (not permitting exclusion under Rule 14a-8(i)(8) of proposals seeking to include qualified nominees in the company's proxy statement).

84 462 F.3d 121 (2d Cir. 2006) (AFSCME).

85 At the time of the AFSCME decision, Rule 14a-8(i)(8) provided that a company need not include a proposal that "relates to an election for membership on the company's board of directors or analogous governing body." See id. at 125. This language was amended in 2007. See Election of Directors Adopting Release.

86 462 F.3d at 128.

87 Exchange Act Rule 14a-12(c) [17 CFR 240.14a-12(c)] defines an election contest as "[s]olicitations by any person or group of persons for the purposes of opposing a solicitation subject to this regulation by any other

decision resulted in uncertainty and confusion with respect to the appropriate application of Rule 14a-8(i)(8), and that it could lead to contested elections for directors without the disclosure otherwise required under the proxy rules for contested elections.[88] This concern led the Commission to reopen the issue of shareholder involvement in the nomination and election process.[89]

In May 2007, the Commission hosted three roundtables on the proxy process during which a number of individuals and representatives from the public and private sector focused on the relationship between the proxy rules and state corporate law,[90] proxy voting mechanics,[91] and

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person or group of persons with respect to the election or removal of directors at any annual or special meeting of security holders ...." Items 4(b) and 5(b) of Exchange Act Schedule 14A set out special disclosure requirements for solicitations subject to Rule 14a-12(c).

88 See Election of Directors Proposing Release. In this regard, the Commission was concerned that shareholders and companies would be unable to know with certainty whether a proposal that could result in an election contest may be excluded under Rule 14a-8(i)(8), depending on where the company was incorporated or conducting business, and that the staff would be severely limited in their ability to interpret Rule 14a-8 in responding to companies' notices of intent to exclude shareholder proposals.

89 Although the Second Circuit's decision was binding only within that Circuit, it created uncertainty elsewhere about the continuing validity of the interpretation of Rule 14a-8(i)(8). After the AFSCME decision and prior to the Commission's codification of the interpretation in December 2007, the staff of the Division of Corporation Finance received three no-action requests seeking to exclude similar proposals under Rule 14a-8(i)(8). In Hewlett-Packard (January 22, 2007), the staff took a position of "no view" on the company's request for no-action relief. A second request for no-action relief was submitted by Reliant Energy. Subsequent to the staff of the Division of Corporation Finance taking a "no view" position on Hewlett-Packard's request, Reliant Energy filed a complaint in the U.S. District Court for the Southern District of Texas seeking a declaratory judgment that the company could properly omit a similar proposal that it had received for inclusion in its proxy materials. During the pendency of this litigation and prior to the staff's response to Reliant's no-action request, the shareholder withdrew the proposal and the company therefore withdrew its no-action request. (See Reliant Energy, Inc. (February 23, 2007)). A third request for no-action relief from UnitedHealth Group, Inc. was withdrawn after the company agreed to include the proposal in its proxy materials. (See UnitedHealth Group, Inc. (March 29, 2007)).

90 Roundtable on the Federal Proxy Rules and State Corporation Law (May 7, 2007). Materials related to the roundtable, including an archived broadcast and a transcript of the roundtable, are available at: http://www.sec.gov/spotlight/proxyprocess.htm.

91 Roundtable on Proxy Voting Mechanics (May 24, 2007). Materials related to the roundtable, including an archived broadcast and a transcript of the roundtable, are available at: http://www.sec.gov/spotlight/proxyprocess.htm.

shareholder proposals.[92] Following the roundtables, in July 2007, the Commission published for comment two alternative proposals addressing the election exclusion in Rule 14a-8. The first would have amended Rule 14a-8 to enable shareholders to include proposals on shareholder director nomination bylaws in company proxy materials where certain conditions were met.[93] The conditions that could be included in such a proposal would not have been limited under the rule proposal so long as they complied with applicable state law and governing corporate documents. As noted in the proposing release, the goal underlying the proposal was to better align the proxy rules with shareholders' rights under state law, in particular the right to nominate directors. The Commission's alternative proposal sought to amend Rule 14a-8 so that a shareholder nomination bylaw proposal could be excluded by a company.[94] The Commission adopted this proposal in December 2007 to provide certainty to companies and shareholders in light of the AFSCME decision.[95] The Commission did not take final action on the first proposal, with the exception of the portion of the first proposal intended to facilitate the creation and use of electronic shareholder forums, which the Commission adopted in January 2008.[96]

III. PROPOSED CHANGES TO THE PROXY RULES

A. Introduction

We are proposing amendments to the proxy rules to require companies to include disclosures about shareholder nominees for director in the companies' proxy materials, under

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92 Roundtable on Proposals of Shareholders (May 25, 2007). Materials related to the roundtable, including an archived broadcast and a transcript of the roundtable, are available at: http://www.sec.gov/spotlight/proxyprocess.htm.

93 See Shareholder Proposals Proposing Release.

94 See Election of Directors Proposing Release.

95 See Election of Directors Adopting Release.

96 See Electronic Shareholder Forums Release.

certain circumstances, so long as the shareholders are not seeking to change the control[97] of the issuer or to gain more than a limited number of seats on the board. These proposed amendments build on the Commission's 2003 and 2007 proposals. They also reflect our experience with, and continued consideration of, the issue of shareholder involvement in the proxy process, the interaction between the proxy rules and state law, and the extensive comment that we have received over the past six years on these topics. As stated previously, due to dispersed ownership, director elections are largely conducted by proxy rather than in person and, as a result, impediments that the federal proxy rules create to shareholders nominating directors through the proxy process translate into the inability of shareholders to effectively exercise their rights to nominate and to elect those directors. We believe the proposed rule changes will provide shareholders with a greater voice and an avenue to exercise the rights they have to effect change on the boards of the companies in which they invest that they no longer can exercise effectively through attending a shareholder meeting in person.

The Commission's proposals would provide shareholders with two ways to more fully exercise their rights to nominate directors. First, we are proposing a new proxy rule (Exchange Act Rule 14a-11) that would, under certain circumstances, require companies to include shareholder nominees for director in the companies' proxy materials. This requirement would apply unless state law or a company's governing documents[98] prohibits shareholders from nominating directors.[99] In this regard, state law or a company's governing documents may

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97 A change in control could include any number of extraordinary transactions, including a sale of substantially all of the company's assets. See, e.g., Item 14(a) of Schedule 14A.

98 Under state law, a company's governing documents may have various names. When we refer to governing documents throughout the release, we generally are referring to a company's charter, articles of incorporation, certificate of incorporation, and/or bylaws, as applicable.

99 We are not aware of any law in any state or in the District of Columbia that prohibits shareholders from nominating directors. Nonetheless, should any such law be enacted in the future, then this condition would

provide for nomination or disclosure rights in addition to those provided pursuant to Rule 14a-11 (e.g., a company could choose to provide a right for shareholders to have their nominees disclosed in the company's proxy materials regardless of share ownership – in that instance, the company's provision would apply for certain shareholders who would not otherwise have their nominees included in the company's proxy materials pursuant to Rule 14a-11). Second, we are proposing an amendment to Exchange Act Rule 14a-8(i)(8), the election exclusion, to preclude companies from relying on Rule 14a-8(i)(8) to exclude from their proxy materials shareholder proposals by qualifying shareholders that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11.

Request for Comment

A.1. Does the Commission need to facilitate shareholder director nominations or remove impediments to help make the proxy process better reflect the rights a shareholder would have at a shareholder meeting?

A.2. Should the Commission adopt revisions to the proxy rules to facilitate the inclusion of shareholder nominees in company proxy materials, or are the existing means that are available to shareholders to exercise their rights to nominate directors adequate? How have changes in corporate governance over the past six years, including the move by many companies away from plurality voting to majority voting, affected a shareholder's ability to place nominees in company proxy materials? How have other developments, as well as ongoing developments such as some states adopting statutes allowing companies to

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not be satisfied.

reimburse shareholders who conduct director election contests and enabling companies to include in their bylaws provisions for inclusion of shareholder director nominees in company proxy materials, affected a shareholder's ability to nominate directors? Have other changes in law or practice created a greater or lesser need for such a rule?

A.3. Would the proposed amendments enable shareholders to effect change in a company's board of directors? Please explain and provide any empirical data in support of any arguments or analyses.

A.4. What would be the costs and benefits to companies and shareholders if the Commission adopted new proxy rules that would facilitate the inclusion of shareholder director nominees in company proxy materials? What would be the costs and benefits to companies if the Commission adopted the proposed amendment to Rule 14a-8(i)(8)?

A.5. What direct or indirect effect, if any, would the proposed changes to the proxy rules have on companies' corporate governance policies relating to the election of directors?

A.6. Could the proposed amendments to the proxy rules be modified to better meet the Commission's stated intent? If so, how? Please explain and provide empirical data or other specific information in support of any arguments or analyses. Please identify and discuss any other rules that would need to be amended.

A.7. We note concerns regarding investor confidence. Would amending the proxy rules as proposed help restore investor confidence? Why or why not? Please explain and provide empirical data or other specific information in support of any arguments or analyses.

A.8. We also note concerns about board accountability and shareholder participation in the proxy process. Would the proposed amendments to the proxy rules address concerns about board accountability and shareholder participation on the one hand, and board dynamics, on the other? If so, how? If not, why not? Please explain and provide empirical data in support of any arguments or analyses.

A.9. Would adoption of only proposed Rule 14a-11 meet the Commission's stated objectives? If so, why? If not, why not? What modifications to the proposed rule and related disclosure requirements would be necessary, if any?

A.10. Would adoption of only the proposed amendment to Rule 14a-8(i)(8) and the related disclosure requirements meet the Commission's stated objectives? If so, why? If not, why not? What modifications to the proposed rule amendment and related disclosure requirements would be necessary, if any?

A.11. Would other revisions to our proxy rules achieve the same or similar objectives as the Commission's proposal? For example, regardless of what other action the Commission may take in this area, should we adopt new disclosure requirements and liability provisions to address recent changes in some state laws concerning the inclusion of shareholder nominees for director in company proxy materials pursuant to a company's governing documents?

A.12. Are there any states that prohibit, or permit companies to prohibit, shareholders from nominating a candidate or candidates for election as director?

B. Proposed Exchange Act Rule 14a-11

1. Overview

As discussed, currently, a shareholder or group of shareholders must undertake a proxy contest and incur the related expenses to have any reasonable chance at successfully putting director nominees before the shareholders for a vote. A board's nominees, on the other hand, are listed in the company's proxy materials, which are funded out of corporate assets.

We believe it is an appropriate time for us to revisit whether and how the federal proxy rules may be impeding the ability of shareholders to exercise their fundamental rights to nominate and elect board members. As mentioned above, we are aware of the concerns and questions about the accountability and responsiveness of some companies and boards of directors to the interests of shareholders, particularly in the current market environment. Additionally, based on the comments received in response to our solicitation of public input on the topic in prior releases and roundtables, we have learned that shareholders face significant obstacles to efficiently exercising their right to determine the leadership of the companies in which they invest. Much of the public input that we have received suggests that including shareholder nominees for director in company proxy materials would be the most direct and effective method of facilitating shareholders' rights in connection with the nomination and election of directors.[100]

On the other hand, the business community and many of its legal advisors have expressed concern that mandating shareholder access to company proxy materials could turn every election of directors into a contest, which would be costly and disruptive to companies and could discourage some qualified board candidates from agreeing to appear on a company's slate of nominees. Because the composition of the board of directors is fundamental to a company's

[100] See 2003 Summary of Comments.

governance, the current filing and other requirements applicable to shareholders who wish to propose an alternate slate are, in the view of these commenters, more appropriate than including shareholder nominees for director in company proxy materials.[101]

In light of the erosion of investor confidence that has taken place over the past several months, and after further consideration of the issue, we have determined to propose a rule that would require companies to include disclosure about shareholder nominees for director in company proxy materials under specified conditions.[102] These nominees would then also be included on a company's form of proxy in accordance with the requirements of Rule 14a-4.[103] Rule 14a-11 would not apply where shareholders relying on the rule are seeking to change the control of the issuer or to gain more than a limited number of seats on the board of directors. In this regard, we believe that shareholders who are seeking such a change should continue to use the procedures currently available for election contests.

2. Application of Exchange Act Rule 14a-11

Proposed Rule 14a-11 would apply to all companies subject to the Exchange Act proxy rules[104] (including investment companies registered under Section 8 of the Investment Company Act of 1940),[105] other than companies that are subject to the proxy rules solely because they have

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101 See id.

102 See proposed Exchange Act Rule 14a-11.

103 See proposed amendment to Rule 14a-4.

104 Exchange Act Rule 3a12-3 [17 CFR 240.3a12-3] exempts foreign private issuers from the Commission's proxy rules. As such, the proposed rule would not apply to foreign private issuers.

105 15 U.S.C. 80a et seq. Investment companies currently are required to comply with the proxy rules under the Exchange Act when soliciting proxies, including proxies relating to the election of directors. See Investment Company Act Rule 20a-1 [17 CFR 270.20a-1] (requiring registered investment companies to comply with regulations adopted pursuant to Section 14(a) of the Exchange Act that would be applicable to a proxy solicitation if it were made in respect of a security registered pursuant to Section 12 of the Exchange Act).

a class of debt registered under Section 12 of the Exchange Act. As proposed, a company would be subject to Rule 14a-11 unless applicable state law or a company's governing documents prohibits shareholders from nominating candidates for the board of directors. When a company's governing documents do prohibit nomination rights, shareholders who want to amend the provision may seek to do so by submitting a shareholder proposal.[106]

In the 2003 Proposal, the Commission proposed to make the new requirement concerning shareholder director nominations operative for a company only after the occurrence of one or both of two possible triggering events. The first triggering event was that at least one of the company's nominees for the board of directors for whom the company solicited proxies received withhold votes from more than 35% of the votes cast at an annual meeting of shareholders at which directors were elected (provided, that this triggering event could not occur in a contested election to which Rule 14a-12(c) would apply or an election to which the proposed shareholder nomination procedure would have applied). The second proposed triggering event was that a shareholder proposal submitted under Rule 14a-8 providing that the company become subject to the proposed shareholder nomination procedure was submitted for a vote of shareholders at an annual meeting by a shareholder or group of shareholders that (1) held more than 1% of the company's securities entitled to vote on the proposal and (2) held those securities for one year as of the date the proposal was submitted, and the proposal received more than 50% of the votes cast on that proposal at that meeting.[107]

Today's proposal does not require a triggering event. Instead, Rule 14a-11 would apply to all companies subject to Exchange Act Section 14(a), other than companies that are subject to

106 A company generally would not be permitted to exclude such a shareholder proposal under our proposed amendment to Rule 14a-8(i)(8), discussed in Section III.C., below.

107 Only votes for and against a proposal would have been included in the calculation of the shareholder vote.

the proxy rules solely because they have a class of debt registered under Exchange Act Section 12. Accordingly, a company would be required to disclose the nominee or nominees of any shareholder or shareholder group meeting the proposed eligibility standards and other conditions in Rule 14a-11, discussed below. Our decision not to include triggering events in the current proposal reflects our concern that the federal proxy rules may be impeding the exercise of shareholders' ability under state law to nominate directors at all companies, not just those with demonstrated governance issues. In addition, we note that many commenters on the 2003 Proposal expressed concern about that proposal's complexity[108] and indicated that the multi-year process created by the trigger requirement could make it more difficult for shareholders to efficiently effect change in the composition of boards of directors.[109] Finally, in light of our concerns about restoring investor confidence to the greatest number of shareholders as quickly as possible, we do not want to add a layer of complexity and delay to the operation of the proposed rule that would frustrate our stated objectives.

Request for Comment

B.1. Would adoption of Rule 14a-11 conflict with any state law, federal law, or rule of a national securities exchange or national securities association? To the extent you indicate that the rule would conflict with any of these provisions, please be specific in your discussion of those provisions that you believe would conflict. How should the Commission address these conflicts? Should the rule also address conflicts with a company's country of incorporation where the company is organized in a non-U.S. jurisdiction but does not meet the definition of foreign

[108] See 2003 Summary of Comments and Letter Type I from 5,858 individuals or entities.

[109] See 2003 Summary of Comments; see also comment letter from American Federation of State, County, and Municipal Employees (September 24, 2003) ("AFSCME 2003").

private issuer? Should the rule also explicitly refer to conflicts with laws of U.S. possessions or territories?

B.2. Should Rule 14a-11 apply as proposed? Is it appropriate for proposed Rule 14a-11 to be unavailable where state law or a company's governing documents prohibit shareholders from nominating candidates for director? Would the proposed rule effectively facilitate shareholders' basic rights, particularly the right to nominate directors?

B.3. As proposed, Rule 14a-11 would apply to all companies subject to the proxy rules, other than companies that are subject to the proxy rules solely because they have a class of debt registered under Exchange Act Section 12. What effect, if any, will this application have on any particular group of companies (e.g., on smaller reporting companies)? Are there modifications that would accommodate the needs of a particular group of companies (e.g., smaller reporting companies) while accomplishing the goals of the proposal? Would it instead be more appropriate to exclude from operation of the procedure smaller reporting companies, either on a temporary basis through staggered compliance dates based on company size, or on a permanent basis? Should any other groups of companies be excluded from operation of the rule (e.g., companies subject to the proxy rules for less than a specified period of time (e.g., one year, two years, or three years))? If so, for what period of time should the companies be excluded from operation of the rule (e.g., one year, two years, three years, permanently)?

B.4. Should proposed Rule 14a-11 apply to registered investment companies? Are there any aspects of the proposed nomination procedure that should be modified in the case of registered investment companies?

B.5. Should companies that are subject to the proxy rules solely because they have a class of debt registered under Exchange Act Section 12 be excluded from application of Rule 14a-11, as proposed? Please explain why or why not.

B.6. As proposed, Rule 14a-11 would apply to companies that have voluntarily registered a class of equity securities pursuant to Exchange Act Section 12(g). Should companies that have registered on a voluntary basis be subject to Rule 14a-11? If so, should nominating shareholders of these companies be subject to the same ownership eligibility thresholds as those shareholders of companies that were required to register a class of equity securities pursuant to Section 12? Should we adjust any other aspects of Rule 14a-11 for companies that have voluntarily registered a class of equity securities pursuant to Section 12(g)?

B.7. Should proposed Rule 14a-11 be inapplicable to a company that has or adopts a provision in its governing documents that provides for or prohibits the inclusion of shareholder director nominees in the company proxy materials? Should the Commission's rules respond to variations in shareholder director nomination disclosures and procedures adopted, for example, under state corporate laws that specify that a company's governing documents may address the use of a company's proxy materials for shareholder nominees to the board of directors? Would it be more appropriate to only permit companies to comply with governing document provisions or state laws where those provisions or laws provide shareholders with greater nomination or proxy disclosure rights than those provided under proposed Rule 14a-11? Should Rule 14a-11 provide that a company's governing documents may render the rule inapplicable to a company only if the shareholders have approved, as contrasted to the board implementing without shareholder approval, a provision in the company's governing documents addressing the inclusion of shareholder nominees in company proxy materials? Should Rule 14a-11 be inapplicable if such shareholder-approved provisions are more restrictive than Rule 14a-11? Should Rule 14a-11 be inapplicable if such shareholder-approved provisions are less restrictive than Rule 14a-11? Or both?

B.8. The New York Stock Exchange has filed with the Commission a proposed rule change to amend NYSE Rule 452 and corresponding Section 402.08 of the Listed Company Manual to eliminate broker discretionary voting for the election of directors. The Commission published the proposed rule change, as amended on February 26, 2009, for comment in the Federal Register on March 6, 2009.[110] If the amendment to Rule 452 is approved, what would be its effect on operation of proposed Rule 14a-11? Would any changes to Rule 14a-11 be required? Please be specific in your response.

B.9. Should proposed Rule 14a-11 exempt companies where state law or the company's governing documents require that directors be elected by a majority of shares present in person or represented by proxy at the meeting and entitled to vote? What specific issues would arise in an election where state law or the company's governing documents provided for other than plurality voting (e.g.,

[110] See Release No. 34-59464 (February 26, 2009) [74 FR 9864].

majority voting)? What specific issues would arise in an election that is conducted by cumulative voting? Would these issues need to be addressed in revisions to the proposed rule text? If so, how?

B.10. Should companies be able to take specified steps or actions, such as adopting a majority vote standard or bylaw specifying procedures for the inclusion of shareholder nominees in company proxy materials, to prevent application of proposed Rule 14a-11 where it otherwise would apply? If so, what such steps or actions would be appropriate and why would they be appropriate? For example, should companies that agree with a shareholder proponent not to exclude a shareholder proposal submitted by an eligible shareholder pursuant to Rule 14a-8 be exempted from application of the proposed rule for a specified period of time? Should a company that implements any shareholder proposals that receive a majority of votes cast in a given year be exempted?

B.11. Should companies subject to Rule 14a-11 be permitted to exclude certain shareholder proposals that they otherwise would be required to include? If so, what categories of proposals? For example, should the company be able to exclude proposals that are non-binding, proposals that relate to corporate governance matters generally, proposals that relate to the structure or composition of boards of directors, or other proposals?

B.12. One concern that has been raised about the effectiveness of the present proxy rules is the high cost to a shareholder to conduct a solicitation to nominate a director. Should the proposed rule provide that it does not apply to a company whose governing documents include a provision for reimbursement of expenses incurred by a participant or participants in the course of a solicitation in opposition as defined in Rule 14a-12(c)? If so, should the rule specify what manner of reimbursement would be sufficient for proposed Rule 14a-11 not to apply?

B.13. Should Rule 14a-11 be widely available, as proposed, or should application of the rule be limited to companies where specific events have occurred to trigger operation of the rule? If so, what events should trigger operation of the rule?

B.14. If the Commission were to include triggering events in Rule 14a-11, would either of the triggering events proposed in 2003 and described above be appropriate? In responding, please discuss how any changes in corporate governance practices over the past six years have affected the usefulness of the triggering events proposed in 2003. For example, over the past six years many companies have adopted majority voting. If the triggering events proposed in 2003 are not appropriate, are there alternative events that the Commission should consider in place of, or in addition to, the above events? For example, should application of Rule 14a-11 be triggered by other factors such as economic performance (e.g., lagging a peer index for a specified number of consecutive years), being delisted by an exchange, being sanctioned by the Commission or other regulators, being indicted on criminal charges, having to restate earnings, having to restate earnings more than once in a specified period, or failing to take action on a shareholder proposal that received a majority shareholder vote?

B.15. In the 2003 Proposal, the rule proposed would have been triggered by withhold votes for one or more directors of more than 35% of the votes cast. Is it appropriate to apply such a trigger to current proposed Rule 14a-11? If so, what would be an appropriate percentage and why? Would it be appropriate to base this trigger on votes cast rather than votes outstanding? Please provide a basis for any alternate recommendations, including numeric data, where available. Is the percentage of withhold votes the appropriate standard in all cases? For example, what standard is appropriate for companies that do not use plurality voting? If your comments are based upon data with regard to withhold votes for individual directors, please provide such data in your response.

B.16. If the Commission were to include a triggering event requirement, for what period of time after a triggering event should Rule 14a-11 apply (e.g., one year, two years, three years, or permanently)? Should there be a means other than the adoption of a provision in the company's governing documents for the company or shareholders to terminate application of the requirement at a company? If so, what other means would be appropriate?

B.17. What would be the possible consequences of the use of triggering events? Would the withhold vote trigger result in more campaigns seeking withhold votes? How would any such consequences affect the operation and governance of companies?

B.18. If the proposed requirement applied only after a specified triggering event, how would the company make shareholders aware when a triggering event has occurred? If the rule became operative based on the occurrence of triggering events, should the rule require additional disclosures in a company's Exchange

Act Form 10-Q,[111] 10-K,[112] or 8-K[113] or, in the case of a registered investment company, Form N-CSR?[114] For example, the rule could require the following:

- A company would be required to disclose the shareholder vote with regard to the directors receiving a withhold vote or a shareholder proposal, either of which may result in a triggering event, in its quarterly report on Form 10-Q for the period in which the matter was submitted to a vote of shareholders or, where the triggering event occurred during the fourth quarter of the fiscal year, on Form 10-K;[115] and
- A company would be required to include in that Form 10-Q or 10-K information disclosing that it would be subject to Rule 14a-11 as a result of such vote, if applicable.

B.19. Should the company's disclosure regarding the applicability of Rule 14a-11 be filed or made public in some other manner? If so, what manner would be appropriate?

B.20. Should companies be exempted from complying with Rule 14a-11 for any election of directors in which another party commences or evidences its intent to commence a solicitation in opposition subject to Rule 14a-12(c) prior to the

111 17 CFR 249.308a.

112 17 CFR 249.310.

113 17 CFR 249.308.

114 17 CFR 249.331 and 17 CFR 274.128.

115 Item 4 of Part II to Exchange Act Form 10-Q and Item 4 of Part I to Exchange Act Form 10-K currently require that companies disclose the results of the voting on all matters submitted to a vote of shareholders during the period covered by the report. We could add a provision to these items that would require disclosure of specific information relating to the application of Rule 14a-11 or a shareholder director nomination process provided for under applicable state law or in a company's governing documents.

company mailing its proxy materials? What should be the effect if another party commences a solicitation in opposition after the company has mailed its proxy materials?

B.21. If a triggering event is required and companies are exempted from complying with Rule 14a-11 because another party has commenced or evidenced its intent to commence a solicitation in opposition subject to Rule 14a-12(c), should the period in which Rule 14a-11 applies be extended to the next year? What should be the effect if another party commences a solicitation in opposition after the company has mailed its proxy materials?

B.22. What provisions, if any, would the Commission need to make for the transition period after adoption of a rule based on this proposal? Would it be necessary to adjust the timing requirements of the rule depending on the effective date of the rule (e.g., if the rules are adopted shortly before a proxy season)?

B.23. Should the Commission consider rulemaking under Section 19(c) of the Exchange Act to amend the listing standards of registered exchanges to require that shareholders have access to the company's proxy materials to nominate directors under the requirements and procedures described in connection with proposed Rule 14a-11 to reflect, for example, changes the Sarbanes-Oxley Act made to director and independence requirements, among other matters?

3. Eligibility to Use Exchange Act Rule 14a-11

In seeking to balance shareholders' ability to participate more fully in the nomination and election process against the potential cost and disruption to companies subject to the proposed new rule, we are proposing that only holders of a significant, long-term interest in a company be able to rely on Rule 14a-11 to have disclosure about their nominees for director included in company proxy materials. We are proposing that the requirement for a company to include a shareholder's nominee or nominees for director in the company's proxy materials and on its form of proxy be based on a minimum ownership threshold, which would be tiered according to company size. Assuming the other conditions of proposed Rule 14a-11 are met, companies would not be able to exclude a shareholder nominee or nominees if the nominating shareholder or group:

- Beneficially owns, as of the date of the shareholder notice on Schedule 14N, either individually or in the aggregate:[116]
    - For large accelerated filers as defined in Exchange Act Rule 12b-2,[117] and registered investment companies with net assets of $700 million or more, at least 1% of the company's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders);[118]
    - For accelerated filers as defined in Rule 12b-2, and registered investment companies with net assets of $75 million or more but less than $700 million, at least 3% of the company's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders);[119] and

116 The manner in which a nominating shareholder or group would establish its eligibility to use proposed Rule 14a-11 is discussed further, below.

117 17 CFR 240.12b-2.

118 See proposed Rule 14a-11(b)(1)(i).

119 See proposed Rule 14a-11(b)(1)(ii).

- For non-accelerated filers as defined in Rule 12b-2, and registered investment companies with net assets of less than $75 million, at least 5% of the company's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders);[120]

- Has beneficially owned the securities that are used for purposes of determining the ownership threshold continuously for at least one year as of the date of the shareholder notice on Schedule 14N (in the case of a shareholder group, each member of the group must have held the securities that are used for purposes of determining the ownership threshold for at least one year as of the date of the shareholder notice on Schedule 14N);[121] and
- Represents that it intends to continue to own those securities through the date of the annual or special meeting.[122]

The issue of the appropriate eligibility ownership threshold generated a great deal of comment when proposed in the 2003 Proposal.[123] While some commenters believed that all shareholders, regardless of the amount of shares owned, should be able to include nominees in the company proxy materials for the purpose of nominating one or more directors, others

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120 See proposed Rule 14a-11(b)(1)(iii).

121 See proposed Rule 14a-11(b)(2). The one-year holding period requirement applies only to the securities that are used for purposes of determining the ownership threshold.

122 Id. Pursuant to proposed Rule 14a-18(b), the nominating shareholder or group would be required to include in its notice to the company of the intent to nominate a representation that the nominating shareholder or group satisfies the conditions in Rule 14a-11(b).

123 See 2003 Summary of Comments; comment letter on the Shareholder Proposals Proposing Release from California Public Employees' Retirement System (September 26, 2007) ("CalPERS 2007") (noting that a 2003 analysis of the holdings of three of the largest public pension funds showed that their combined ownership exceeded 2% in only one instance, and exceeded 1.5% in only 12 instances).

advocated share ownership thresholds ranging from the $2,000 threshold required to submit a Rule 14a-8 proposal to share ownership percentages such as 3%, 5% or 10% of a company's outstanding common stock.[124] Those who advocated no threshold or a nominal dollar amount argued that the imposition of a threshold would discriminate against smaller investors or unfairly advantage larger shareholders who already may have the resources to run their own slates using the existing rules for contested elections.[125] Those who advocated a larger share ownership threshold argued that a nominating shareholder should have a substantial, long-term stake in the company in order to require the use of company funds to nominate a candidate.[126] In addition, advocates of a larger share ownership threshold pointed out that the composition of the board of directors is critical to a corporation's functions and, accordingly, shareholders should have to evidence a significant financial interest by satisfying a substantial ownership threshold in order to require a company to include in its proxy materials a shareholder director nominee or nominees.[127]

The tiered beneficial ownership thresholds that we are proposing represent an effort to balance the varying considerations and address the possibility that certain companies could be impacted disproportionately based on their size.[128] In determining the proposed ownership thresholds, we considered two different samples of data on security ownership as an indicator of the ownership of securities that are entitled to be voted on the election of directors. First, we

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124 See 2003 Summary of Comments.

125 See id.

126 See id.

127 See id.

128 In this regard, we believe that the relative resource requirement for larger issuers to fund and administer the process would be smaller. Therefore, the thresholds we are proposing will more likely result in more large accelerated and accelerated filers receiving qualifying nominations than non-accelerated filers.

considered the current ownership make-up of a sample provided by an outside source of 5,327 companies that have held meetings between January 1, 2008 and April 15, 2009.[129] In this sample, roughly 26% of the firms are classified as large accelerated filers, 35% are classified as accelerated filers, and 38% are classified as non-accelerated filers. The second sample is derived from CDA Spectrum and is based on filings of Forms 13F in the third quarter of 2008.[130] In this sample, roughly 26% of the firms are classified as large accelerated filers, 33% are classified as accelerated filers, and 40% are classified as non-accelerated filers.[131]

In the first sample, nearly all (above 99%) of large accelerated filers have at least one shareholder that could meet the 1% threshold individually, while a somewhat greater number of large accelerated filers (also above 99%) have two or more shareholders that each have held at least 0.5% of the shares outstanding for the appropriate period and, thus, could more easily aggregate their securities in order to meet the 1% ownership requirement. In the CDA sample, 98% of large accelerated filers have at least one shareholder that could meet the 1% threshold individually, while 99% of large accelerated filers have two or more shareholders that each have held at least 0.5% of the shares outstanding for the appropriate period. By contrast, based on the first sample, using an ownership threshold of 3% would reduce the number of large accelerated

129 The staff received beneficial ownership information for these companies aggregated at various thresholds and matched the information on market value of the float (obtained from Datastream). The sample excludes mutual funds.

130 Institutional investment managers who exercise investment discretion over $100 million or more in Section 13(f) securities must report their holdings on Form 13F with the SEC. The sample includes 6,700 companies that are referenced in the Form 13F form that have common equity and are traded on NYSE, NYSE Amex Equities, or NASDAQ. Of these we were able to match the information on the market value of float (obtained from Datastream) for 5,877 observations.

131 Under Rule 12b-2, a large accelerated filer must have an aggregate worldwide market value of the voting and non-voting common equity held by its non-affiliates of $700 million or more, and an accelerated filer must have an aggregate worldwide market value of the voting and non-voting common equity held by its non-affiliates of $75 million or more but less than $700 million. Filers that do not meet the criteria for accelerated or large accelerated filer status are classified as non-accelerated filers.

filers where a single shareholder could make a nomination to 77% of large accelerated filers and reduce the number of large accelerated filers that have two or more shareholders that have held at least 1.5% of the shares for the appropriate period to 89%. Using the CDA sample these numbers would drop to 96% and 97% respectively.

With regard to accelerated filers, roughly 85% of filers have at least one shareholder that could meet the 3% threshold individually, while roughly 92% of accelerated filers have two or more shareholders that each have held at least 1.5% of the shares outstanding for the appropriate period and, thus, could more easily aggregate their securities in order to meet the 3% ownership requirement. In the CDA sample, 91% of accelerated filers have at least one shareholder that could meet the 3% threshold individually, while 93% of accelerated filers have two or more shareholders that each have held at least 1.5% of the shares outstanding for the appropriate period. By contrast, based on the first sample, using an ownership threshold of 5% would reduce the number of accelerated filers where a single shareholder could make a nomination to 58% of accelerated filers. Further, 78% of accelerated filers have two or more shareholders that have held at least 2.5% of the shares for the appropriate period. Using the CDA sample these numbers would drop to 66% and 88% respectively.

With regard to non-accelerated filers, roughly 59% of filers in the first sample have at least one shareholder that could meet the 5% threshold individually, while roughly 71% of non-accelerated filers have two or more shareholders that each have held at least 2.5% of the shares outstanding for the appropriate period and, thus, could more easily aggregate their securities in order to meet the 5% ownership requirement. In the CDA sample, 41% of non-accelerated filers have at least one shareholder that could meet the 5% threshold individually, while 49% of non-accelerated filers have two or more shareholders that each have held at least 2.5% of the shares outstanding for the appropriate period. By contrast, based on the first sample, using an ownership threshold of 7% would reduce the number of non-accelerated filers where a single shareholder could make a nomination to 41% of non-accelerated filers. Further, only 43% of non-accelerated filers have two or more shareholders that have held at least 4% and 62% have two or more shareholders that have held at least 3% of the shares for the appropriate period.[132] Using the CDA sample these numbers would drop to 33%, 37% and 45% respectively.

With regard to registered investment companies, we are proposing tiered thresholds based on the net assets of the companies.[133] Consistent with our approach to reporting companies (other than registered investment companies), the tiered beneficial ownership thresholds that we are proposing represent an effort to balance the various competing views and address the possibility that certain registered investment companies could be impacted disproportionately based on their size. Because registered investment companies are not classified as large accelerated filers, accelerated filers, and non-accelerated filers, we propose to base the tiers on the net assets of the companies.[134] In particular, we are proposing tiers for registered investment companies that are based on the worldwide market value levels used by reporting companies

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132 The staff did not have information regarding the beneficial ownership for the 3.5% threshold.

133 In the case of a registered investment company, in determining the securities that are entitled to be voted on the election of directors for purposes of establishing whether the applicable threshold has been met, the nominating shareholder or group may rely on information set forth in the following documents, unless the nominating shareholder or group knows or has reason to know that the information contained therein is inaccurate: (1) in the case of a series company, a Form 8-K that would be required to be filed in connection with the meeting where directors are to be elected (for a further discussion of Form 8-K filing requirements for registered investment companies, see footnote 138, below, and accompanying text); or (2) in the case of other registered investment companies, the company's most recent annual or semi-annual report filed with the Commission on Form N-CSR. See Instruction 1 to proposed Rule 14a-11(b).

134 See Instruction 2 to proposed Rule 14a-11(b). For registered investment companies that are organized in series form, we are proposing that the net assets thresholds apply to the company as a whole, and not on a series by series basis, because directors are elected for the company by the shareholders of all series rather than separately for each series of the company. See Investment Company Act Rule 18f-2(g) [17 CFR 270.18f-2(g)].

(other than registered investment companies) to determine filing status.[135] Under the proposal, the amount of net assets of a registered investment company for these purposes would be the amount of net assets of the company as of the end of the company's second fiscal quarter in the fiscal year immediately preceding the fiscal year of the meeting, as disclosed in the company's Form N-CSR filed with the Commission, except that, for a series investment company the amount of net assets would be the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting, as disclosed in a Form 8-K filed in connection with the meeting where directors are to be elected.[136]

The requirement that the net asset determination for investment companies other than series investment companies be made as of the end of the company's second fiscal quarter in the fiscal year immediately preceding the fiscal year of the meeting is similar to the requirements for reporting companies (other than registered investment companies), which determine large accelerated filer, accelerated filer, and non-accelerated filer status as of the end of the fiscal year, using the market value of the issuer's common equity as of the last business day of the immediately preceding second fiscal quarter.[137] However, we have chosen a single date, June 30 of the calendar year immediately preceding the calendar year of the meeting, for series investment companies, due to the fact that different series of a series company may have different fiscal year and semi-annual period ending dates. Moreover, although registered investment companies generally are not required to file Form 8-K, we are proposing to require a registered investment company that is a series company to file Form 8-K within four business

135 See footnote 131, above.

136 See Instructions 2 and 3 to proposed Rule 14a-11(b).

137 See Rule 12b-2.

days after the company determines the anticipated meeting date, disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of the company's shares that are entitled to vote for the election of directors (or if votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.[138] Registered investment companies, including series investment companies, currently disclose net asset and outstanding share information in their annual and semi-annual reports filed on Form N-CSR, but we believe that the additional Form 8-K filing is necessary for series companies because a series company may file multiple Form N-CSRs with respect to different series covering different fiscal year and semi-annual period ending dates and is required to disclose net asset and outstanding share information on a series by series basis, rather than for the company as a whole.

The purpose of the proposed rule would be to remove impediments the federal proxy rules create to shareholders' exercise of their rights to nominate and elect members of boards of directors. At the same time, we recognize that there are competing concerns that also need to be taken into account, such as the potential cost and disruption to the company of a rule with no shareholder eligibility requirements. To balance those interests, we are proposing a rule that includes shareholder eligibility requirements. In particular, we are proposing eligibility requirements based on the duration of ownership and minimum ownership levels.

With respect to duration of ownership eligibility criteria, we believe that long-term shareholders are more likely to have interests that are better aligned with other shareholders and

[138] See proposed General Instruction B.1 and proposed Item 5.07(b) of Form 8-K; proposed Rules 13a-11(b)(3) and 15d-11(b)(3); and Instruction 3 to proposed Rule 14a-11(b).

are less likely to use the rule solely for short-term gain. We are proposing a one year holding requirement for each nominating shareholder or member of a nominating group rather than the two year requirement proposed in 2003. The holding period generated less comment in 2003 than the ownership threshold, with the majority of commenters that addressed the topic supporting the proposed holding period.[139] Some commenters, however, advocated either lowering the holding period to one year,[140] or raising it (e.g., to 5 years).[141] Some of these commenters suggested that the two year holding period was too onerous.[142] After further consideration, we believe that a one year holding requirement would be sufficient to appropriately limit use of Rule 14a-11 to long-term shareholders without placing an undue burden on shareholders seeking to use the rule. In addition, a one year requirement is consistent with the existing eligibility requirement for shareholders to submit proposals under Rule 14a-8.

With regard to a minimum ownership level as a shareholder eligibility requirement, we believe it is important that any shareholder or group that intends to submit a nominee to a company for inclusion in the company's proxy materials continue to have a significant economic

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139 See 2003 Summary of Comments; see also comment letters from AFL-CIO; Alliance Capital Management L.P. (December 15, 2003) ("Alliance Capital"); American Society of Corporate Secretaries (December 22, 2003) ("ASCS"); Henry A. McKinnell, Chairman, The Business Roundtable (December 22, 2003) ("McKinnell, BRT"); United States Chamber of Commerce (December 19, 2003) ("Chamber"); Carl T. Hagberg (December 22, 2003); Committee on Securities Regulation, New York State Bar Association (December 22, 2003) ("NYS Bar"); State Teachers Retirement System of Ohio (December 18, 2003) ("STRS Ohio"); Sullivan & Cromwell LLP (December 22, 2003) ("Sullivan"); T. Rowe Price Associates, Inc. (December 24, 2003) ("T. Rowe"); Valero; and Wachtell.

140 See 2003 Summary of Comments; see also comment letters from CalPERS; CIR; Gary K. Duberstein (December 22, 2003) ("Duberstein"); Gary Tannahill (December 6, 2003) ("Tannahill"); and Wolf Haldenstein Adler Freeman & Herz LLP (December 19, 2003) ("Wolf Haldenstein").

141 See 2003 Summary of Comments; see also letters from Compass Bancshares, Inc. (December 22, 2003) ("Compass"); and W. Paul Fitzgerald, Director, EMC Corporation (December 19, 2003), Gail Deegan, Director, EMC Corporation (December 22, 2003), and Alfred Zeien, Director, EMC Corporation (December 22, 2003) (collectively, "EMC Corporation").

142 See 2003 Summary of Comments; see also comment letters from CalPERS; CIR; Duberstein; Tannahill; and Wolf Haldenstein.

interest in the company. Therefore, we have proposed the requirement that a nominating shareholder or group provide a statement as to the nominating shareholder's or group's intent to continue to hold the requisite amount of securities through the date of the meeting. Commenters in 2003 generally supported a holding requirement through the date of the meeting,[143] with some suggesting an even longer holding period (e.g., through the term of the nominee's service on the board, if elected).[144] We continue to believe that a requirement to hold the securities through the date of the meeting is appropriate to demonstrate the nominating shareholder's commitment to the director nominee and the election process; however, we also have proposed a disclosure requirement under which a nominating shareholder or group would state their intent with respect to continued ownership of their shares after the election.[145]

In addition, to rely on proposed Rule 14a-11 to have disclosure about their nominee or nominees included in the company proxy materials, a nominating shareholder or group must:

- Not acquire or hold the securities for the purpose of or with the effect of changing control of the company or to gain more than a limited number of seats on the board;
- Provide and file with the Commission a notice to the company on proposed new Schedule 14N[146] of the nominating shareholder's or group's intent to require that the company include that nominating shareholder's or group's nominee in the company's

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143 See 2003 Summary of Comments; see also comment letters from America's Community Bankers (December 18, 2003) ("ACB"); Alliance Capital; ASCS; Blackwell Sanders Peper Martin LLP (December 22, 2003) ("Blackwell Sanders"); McKinnell, BRT; CalPERS; Chamber; CIR; Compass; FedEx Corporation (December 19, 2003) ("FedEx"); Intel Corporation (December 22, 2003) ("Intel"); International Paper Company (December 22, 2003) ("International Paper"); Peter O. Clauss and J. Peter Wolf of Pepper Hamilton, LLP (December 16, 2003) ("Clauss & Wolf"); Sullivan; Tannahill; Valero; Wachtell; and Wells Fargo & Company (December 19, 2003) ("Wells Fargo").

144 See 2003 Summary of Comments; see also comment letters from ACB; McKinnell, BRT; Chamber; Compass; FedEx; Intel; International Paper; Clauss & Wolf; Sullivan; Valero; Wachtell; and Wells Fargo.

145 See proposed Rule 14a-18(f) and proposed Item 5(b) of Schedule 14N.

146 See Section III.B.6. for a discussion of Schedule 14N and the disclosure required to be filed.

proxy materials by the date specified by the company's advance notice provision or, where no such provision is in place, no later than 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting,[147] except that if the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 days from the prior year, then the nominating shareholder or group must provide notice a reasonable time before the company mails its proxy materials, as specified by the company in a Form 8-K filed within four business days after the company determines the anticipated meeting date pursuant to proposed Item 5.07;[148] and

- Include in the shareholder notice on Schedule 14N disclosure about the amount and percentage of securities owned by the nominating shareholder or group, length of ownership of such securities, and the nominating shareholder's or group's intent to continue to hold the securities through the date of the meeting as well as intent with respect to continued ownership after the election, a certification that the nominating shareholder or group is not seeking to change the control of the company or to gain more than a limited number of seats on the board of directors, and disclosure meeting the requirements of Rule 14a-18.[149]

Request for Comment

C.1. Are the proposed shareholder eligibility criteria for Rule 14a-11 necessary or

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147 This date would be calculated by determining the release date disclosed in the previous year's proxy statement, increasing the year by one, and counting back 120 calendar days.

148 See proposed Instruction 2 to paragraph (a) of Rule 14a-11 and proposed General Instruction B.1. to Form 8-K. A late filing of such form would result in the registrant losing eligibility to file on Form S-3.

149 See proposed Exchange Act Rules 14a-18 and 14n-1. See discussion in Section III.B.5. regarding proposed Rule 14a-11(d), which limits the number of nominees a company would be required to include in its proxy materials.

appropriate? If not, why not? Should there be any restrictions regarding which shareholders can use proposed Rule 14a-11 to nominate directors for inclusion in company proxy materials? Should those restrictions be consistent with the requirements of Rule 14a-8 or should they be more extensive than the minimum requirements in Rule 14a-8?

C.2. The proposed eligibility threshold is based on the percentage of securities owned and entitled to vote on the election of directors. This threshold is based on current Rule 14a-8 and reflects our intent to focus on those shareholders eligible to vote for directors. Is the proposed threshold appropriate or could it be better focused to accomplish our objective? For example, should eligibility instead be based on record ownership? Should eligibility be based on the value of shares owned? If so, on what date should the value be measured? What would be an appropriate value amount? Is there another standard or criteria? Is submission of the nomination the correct date on which to make these eligibility determinations? If not, what date should be used?

C.3. For companies that have more than one class of securities entitled to vote on the election of directors, does the rule provide adequate guidance on how to determine whether a shareholder meets the requisite ownership thresholds? Should the rule specifically address how to make this determination if one class of securities has greater voting rights than another class?

C.4. What other criteria or alternatives should the Commission consider to determine the eligibility standards for shareholders to nominate directors?

C.5. Is it appropriate to use a tiered approach to the ownership threshold for reporting companies (other than registered investment companies)? If so, is it appropriate and workable to use large accelerated filer, accelerated filer, and non-accelerated filer to define the three tiers? Are there aspects of the definitions of these groups that do not work with the proposed rule? Should we instead define the tiers strictly by public float or strictly by market capitalization? If so, what should the public float or market capitalization thresholds be (e.g., 5% for companies with less than $75,000,000 in public float; 3% for companies with more than $75,000,000 but less than $700,000,000 in public float; 1% for companies with greater than $700,000,000 in public float)?

C.6. Is the 1% standard that we have proposed for large accelerated filers appropriate? Should the standard be lower (e.g., $2,000 or 0.5%) or higher (e.g., 2%, 3%, 4%, 5%, 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)? Is the 3% standard that we have proposed for accelerated filers appropriate? Should the standard be lower (e.g., 1% or 2%) or higher (e.g., 4%, 5%, 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)? Is the 5% standard that we have proposed for non-accelerated filers appropriate? Should the standard be lower (e.g., 1%, 2%, 3%, or 4%) or higher (e.g., 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)?

C.7. Should groups of shareholders composed of a large number of beneficial holders, but who collectively own a percentage of shares below the proposed thresholds, be permitted to have a nominee included in the company proxy materials? If so, what would be a sufficiently large group? Would a group composed of over 1%, 3%, 5% or 10% of the number of beneficial holders be sufficient? Should there be different disclosure requirements for a large shareholder group?

C.8. Is it appropriate to use a tiered approach to the ownership threshold for registered investment companies? Should the tiers and ownership percentages for registered investment companies be similar to those for reporting companies other than registered investment companies, as proposed, or should they be different? Is it appropriate and workable to base the tiers on a registered investment company's net assets? Should another measure be used instead? Should the determination of which tier a series investment company belongs to be made on a series by series basis, rather than for the company as a whole? Should the levels of net assets for each category be higher or lower? If so, why?

C.9. Should the determination of which tier a series investment company is in be based on the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting, as disclosed in a Form 8-K filed in connection with the meeting at which directors are to be elected? Should the determination of which tier other registered investment companies are in be based on the net assets of the company as of the end of the company's second fiscal quarter in the fiscal year immediately preceding the fiscal year of the meeting, as disclosed in the company's Form N-CSR? If not, as of what date should net assets be determined for these purposes? Should all registered investment companies use a single date for purposes of making this determination?

C.10. Should a registered investment company that is a series company be required to file a Form 8-K disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of shares of the company that are entitled to vote for the election of directors (or if votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter? If not, how should shareholders of a series company determine whether they meet the applicable ownership threshold?

C.11. Is the 1% standard that we have proposed for registered investment companies with net assets of $700 million or more appropriate? Should the standard be lower (e.g., $2,000 or 0.5%) or higher (e.g., 2%, 3%, 4%, 5%, 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)? Is the 3% standard that we have proposed for registered investment companies with net assets of $75 million or more, but less than $700 million, appropriate? Should the standard be lower (e.g., 1% or 2%) or higher (e.g., 4%, 5%, 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)? Is the 5% standard that we have proposed for registered investment companies with net assets of less than $75 million appropriate? Should the standard be lower (e.g., 1%, 2%, 3%, or 4%) or higher (e.g., 6%, 7%, 8%, 9%, 10%, 15%, 20%, or 25%)? Should the determination of whether a shareholder or shareholder group beneficially owns a sufficient percentage of a series company's securities to nominate a director be made on a series by series basis, rather than for the company as a whole (i.e., should a shareholder be permitted to take advantage of the nomination process contained in proposed Rule 14a-11 if he or she owns the applicable percentage of shares of a series of the company, but does not own the applicable percentage of the company as a whole)? Should closed-end investment companies be subject to the same standards as open-end investment companies? As proposed, business development companies would be treated in the same manner as reporting companies (other than registered investment companies).[150] Should business development companies be subject to the same tiered approach as reporting companies (other than registered investment companies)? Why or why not?

C.12. In determining the securities that are entitled to be voted on the election of directors of a registered investment company for purposes of establishing whether the applicable threshold has been met, should the nominating shareholder or group be permitted to rely on information set forth in a Form 8-K filed in connection with the meeting where directors are to be elected (in the case of a series company) or the company's most recent annual or semi-annual report filed with the Commission on Form N-CSR (in the case of other investment companies), unless the nominating shareholder or group knows or has reason to know that the information contained therein is inaccurate?

C.13. Voting rights for some registered investment companies are based on the net asset value of the shareholder's securities rather than the number of securities. Does the rule provide adequate guidance on how to determine whether a shareholder meets the requisite ownership threshold in such a case? Should the rule specifically address how to make the ownership threshold determination in cases where different securities of the same investment company have different voting rights on a per share basis?

150 Business development companies are a category of closed-end investment company that are not registered under the Investment Company Act, but are subject to certain provisions of that Act. See Sections 2(a)(48) and 54-65 of the Investment Company Act [15 U.S.C. 80a-2(a)(48) and 80a-53-64].

C.14. Should there be a restriction on shareholder eligibility that is based on the length of time securities have been held? If so, is one year the proper standard? Should the standard be longer (e.g., two years, three years, four years, or five years)? Should the standard be shorter (e.g., six months)? Should the standard be measured by a different date (e.g., one year as of the date of the meeting, rather than the date of the notice)?

C.15. Should eligibility be conditioned on meeting the required ownership threshold by holding a net long position for the required time period? If the Commission were to adopt such a requirement, would this require other modifications to the proposal?

C.16. As proposed, a nominating shareholder would be required to represent its intent to hold the securities until the date of the election of directors. Is it appropriate to include such a requirement? What should be the remedy if the nominating shareholder or group represents its intent to hold the securities through the date of the meeting for the election of directors and fails to do so? Should the company be permitted to exclude any nominations from that nominating shareholder or member of a group for some period of time afterward (e.g., one year, two years, three years)? If the nominating shareholder or group fails to hold the securities through the date of the meeting, what, if anything, should the effect be on the election? Should the nominee submitted by the shareholder or group be disqualified?

C.17. We are proposing that a nominating shareholder represent an intent to hold through the date of the meeting because we believe it is important that the nominating shareholder or group have a significant economic interest in the company. Is it appropriate to require the shareholder to provide a statement regarding its intent with regard to continued ownership of the securities beyond the election of directors? Should a nominating shareholder be required to represent that it will hold the securities beyond the election if the nominating shareholder's nominee is elected (e.g., for six months after the election, one year after the election, or two years after the election)? Would the answer be different if the nominating shareholder's nominee is not elected?

C.18. In the 2003 Proposal the Commission solicited comment on whether the rule should include a provision that would deny eligibility for any nominating shareholder or group that has had a nominee included in the company materials where that nominee did not receive a sufficient percentage of the votes. Commenters were mixed in their responses[151] so we have not proposed a requirement in this regard, but are again requesting comment as to whether the rule should include a provision denying eligibility for any nominating shareholder or group who has had a nominee included in the company materials where that nominee did not receive a sufficient percentage of the votes (e.g., 5%, 10%, 15%, 25%, or 35%) within a specified period of time in the past (e.g., one year, two years, three years, four years, five years). If there should be such an eligibility standard, how long should the prohibition last (e.g., one year, two years, three years)? Similarly, we are again requesting comment (see also Request for

[151] See 2003 Summary of Comments; see also comment letters from CalPERS, CII, and CIR (objecting to resubmission standards); and comment letters from ASCS, Blackwell Sanders, Investment Company Institute (December 22, 2003) ("ICI"), The New York City Bar Association (December 22, 2003) ("NYC Bar"), and Wells Fargo (expressing support for a resubmission standard).

Comment D.16.) as to whether the rule should include a provision that would deny eligibility for any nominee that has been included in the company proxy materials within a specified period of time in the past (e.g., one year, two years, three year, four years, five years) where that nominee did not receive at least a specified percentage of the votes (e.g., 5%, 10%, 15%, 25%, or 35%). How long should any such prohibition last (e.g., one year, two years, three years)?

C.19. As proposed, shareholders may aggregate their holdings in order to meet the ownership eligibility requirement. The shares held by each member of a group that are used to satisfy the ownership threshold must meet the minimum holding period. Should shareholders be allowed to aggregate their holdings in order to meet the ownership eligibility requirement to nominate directors?

C.20. If shareholders should be able to aggregate their holdings, is it appropriate to require that all members of a nominating shareholder group whose shares are used to satisfy the ownership threshold to meet the minimum holding period individually? If aggregation is not appropriate, what ownership threshold would be appropriate for an individual shareholder?

C.21. If a nominating shareholder sells any shares of the company that are in excess of the amount needed to satisfy the ownership threshold, should that shareholder not be eligible under the rule? Would it matter when the nominating shareholder sold the shares in relation to the nomination process?

C.22. Would shareholder groups effectively be able to form to satisfy the ownership thresholds? If not, what impediments exist? What, if anything, would be appropriate to lessen or eliminate such impediments?

C.23. What would be an appropriate method of establishing the beneficial ownership level of a nominating shareholder or group? What would be sufficient evidence of ownership? For example, if the nominating shareholder is not the registered holder of the securities, should the nominating shareholder be required to provide a written statement from the "record" holder of the securities (usually a broker or bank), verifying that at the time the nominating shareholder submitted its notice to the company, the nominating shareholder continuously held the securities for at least one year?

C.24. Should the Commission limit use of the rule, as proposed, to shareholders that are not seeking to change the control of the company or to gain more than a limited number of seats on the board of directors? Why or why not? Would it be appropriate to require the shareholder to represent that it will not seek to change the control of a company or to gain more than a limited number of seats on the board for a period of time beyond the election of directors? How should the rules address the possibility that a nominating shareholder's or group's intent may change over time?

4. Shareholder Nominee Requirements

a. The nomination must be consistent with applicable law and regulation

A company would not be required to include a shareholder nominee in its proxy materials if the nominee's candidacy or, if elected, board membership would violate controlling state law,[152] federal law,[153] or rules of a national securities exchange or national securities association

[152] Rule 14a-11, as proposed, would permit a company to exclude a shareholder nominee from its proxy materials if the nominee's candidacy or, if elected, board membership would violate controlling state or federal law. If a company's governing documents permit the inclusion of shareholder nominees in the

(other than rules of a national securities exchange or national securities association that set forth requirements regarding the independence of directors), and such violation could not be cured.[154] Because compliance with independence standards can depend on the overall make-up of a board, we have excluded independence standards from this requirement and have, instead, proposed a separate provision addressing independence standards. The nominating shareholder or group would be required to make a representation that the shareholder nominee is in compliance with the generally applicable independence requirements of a national securities exchange or national securities association that set forth objective standards.[155] The representation would not be required in instances where a company is not subject to the requirements of a national securities exchange or a national securities association. We recognize that exchange rules regarding director independence generally include some standards that depend on an objective determination of facts and other standards that depend on subjective determinations.[156] As

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company's proxy materials but impose more restrictive eligibility standards or mandate more extensive disclosures than those required by Rule 14a-11, the company could not exclude a nominee submitted by a shareholder in compliance with Rule 14a-11 on the grounds that the shareholder or the nominee fails to meet the more restrictive standards included in the company's governing documents. In other words, companies may not opt out of Rule 14a-11 by adopting alternate requirements for inclusion of shareholder nominees for director in the company's proxy materials.

153 For example, in response to our 2003 Proposal, one commenter noted that without such a requirement, a shareholder could nominate and have elected a director who was employed by a company's competitor thereby "potentially causing the company to violate Section 8 of the Clayton Act of 1914." See 2003 Summary of Comments; see also comment letter from McKinnell, BRT.

154 This requirement is set forth in proposed Exchange Act Rule 14a-11(a)(2). Pursuant to proposed Exchange Act Rule 14a-18(a), the notice to the company by the nominating shareholder or group would be required to include a representation that, to the knowledge of the nominating shareholder or group, the nominee's candidacy or, if elected, board membership would not violate any of the specified provisions.

155 Compliance with these existing independence standards would be established through the inclusion in the notice to the company by the nominating shareholder or group of a representation that the nominee satisfies the existing standard. This representation is required in proposed Exchange Act Rule 14a-18(c). In the case of a registered investment company or a business development company, a nominating shareholder or group would be required to represent that its nominee is not an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act. [15 U.S.C. 80a-2(a)(19)].

156 See proposed Rule 14a-18(c) and the Instruction to paragraph (c). For example, the NYSE listing standards include both subjective and objective components in defining an "independent director." As an example of

proposed, however, to comply with Rule 14a-11 the nominating shareholder or group would only be required to represent that the nominee meets the objective criteria for "independence" in any generally applicable national securities exchange or national securities association rules.[157] For this purpose, the nominee would be required to meet the definition of "independent" that is applicable to directors of the company generally and not any particular definition of independence applicable to members of the audit committee of the company's board of directors. To the extent a rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board (for example, requiring that the board of directors or any group or committee of the board of directors make a determination that the nominee has no material relationship with the listed company), this element of an independence standard would not have to be satisfied.

Specifically, as proposed, each nominating shareholder or each member of the nominating shareholder group would be required to represent in its notice to the company on Schedule 14N[158] that, to the knowledge of the nominating shareholder or group, the nominee, in the case of a registrant other than an investment company, satisfies the standards of a national securities exchange or national securities association regarding director independence that apply

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a subjective determination, Section 303A.02(a) of the NYSE Listed Company Manual provides that no director will qualify as "independent" unless the board of directors "affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company)." Section 303A.02(b) of the NYSE Listed Company Manual provides that a director is not independent if the director has any of several specified relationships with the company. On the other hand, Section 303A.02(b) provides that a director is not independent if he or she has any of several specified relationships with the company that can be determined by a "bright-line" objective test. For example, a director is not independent if "the director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $120,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service)."

157 See Instruction to proposed Rule 14a-18(c).

158 See proposed Rule 14n-101.

to the company, if any, except that, where a rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board, this element of an independence standard would not have to be satisfied.[159] Where a company is not subject to the standards of a national securities exchange or national securities association, the representation would not be required.

The proposals would require any nominating shareholder or group of shareholders of a registered investment company or a business development company to represent that its nominee to the board of the company is not an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act,[160] rather than representing that the nominee satisfies the generally applicable objective standards of a national securities exchange or national securities association regarding director independence.[161] We are proposing to incorporate the Section 2(a)(19) test rather than the test applied to other companies because the Section 2(a)(19) test is tailored to capture the broad range of affiliations with investment advisers, principal underwriters, and others that are relevant to "independence" in the case of investment companies.

Some commenters on the 2003 Proposal stated that nominating committees should be able to apply their own director qualifications criteria to shareholder nominees;[162] however, a

159 See proposed Rule 14a-18(a). We note that our proposal addresses only the requirements under Rule 14a-11 to be included in a company's proxy materials – the proposal would not preclude a nominee from ultimately being subject to the subjective determination test of independence for board committee positions. A company could include disclosure in its proxy materials advising shareholders that the shareholder nominee for director would not meet the company's subjective criteria, as appropriate.

160 15 U.S.C. 80a-2(a)(19).

161 See proposed Rule 14a-18(c).

162 See 2003 Summary of Comments; see also comment letters from ABA; Agilent Technologies, Inc. (December 19, 2003) ("Agilent"); McKinnell, BRT; Chamber; Richard Hall (December 22, 2003) ("Hall"); ICI; Intel; NYC Bar; Software & Information Industry Association (December 22, 2003) ("SIIA"); Sullivan; Valero; and Wells Fargo.

nominee required to be included by the company pursuant to Exchange Act Rule 14a-11 would be, notwithstanding the conditions in the proposal, the nominating shareholder's or group's nominee, not the company's nominee. Therefore, we do not believe it is appropriate that shareholder nominees be required to meet the nominating committee's or board's criteria.

b. Relationships between the nominee, the nominating shareholder or group, and the company

We recognize that a shareholder nomination process presents the potential risk of nominating shareholders or groups acting merely as a surrogate for the company or its management in order to block usage of the rule by another nominating shareholder or group. To balance the benefits of the new rule against these concerns, we propose that the nominating shareholder or group be required to represent that no relationships or agreements between the nominee and the company and its management, and between the nominating shareholder or group and the company and its management exist.[163] Specifically, as proposed, each nominating shareholder or each member of the nominating shareholder group would be required to represent in its notice to the company on Schedule 14N that neither the nominee nor the nominating shareholder (or any member of the nominating shareholder group, if applicable) has an agreement with the company regarding the nomination of the nominee.[164] This representation, along with the required disclosure, would provide some assurance to shareholders that certain shareholders or groups are not receiving special treatment by the company or acting on the

163 This representation would be required in the nominating shareholder's notice to the company on Schedule 14N, pursuant to proposed Exchange Act Rule 14a-18(d). Instruction 2 to proposed Exchange Act Rule 14a-11(d) clarifies that if a nominee, nominating shareholder or any member of a nominating group has an agreement with the company or an affiliate of the company regarding the nomination of a candidate for election, any nominee or nominees from such shareholder or group shall not be counted in calculating the number of shareholder nominees for purposes of proposed Rule 14a-11(d).

164 See proposed Rule 14a-18(d).

company's behalf.[165] This proposed requirement also was included in the 2003 proposal. Commenters generally supported the proposed requirement,[166] though some suggested that the Commission provide an exception for negotiations and other communications between the nominating shareholder or group and the company regarding potential nominees.[167] Accordingly, we have proposed a clarifying instruction to proposed Rule 14a-18(d), which states that negotiations with the nominating committee of the company to have the nominee included on the company's proxy card as a management nominee, where those negotiations are unsuccessful, or negotiations that are limited to whether the company is required to include the shareholder nominee for director on the company's proxy card in accordance with Rule 14a-11, would not be considered a direct or indirect agreement with the company for purposes of the rule.[168]

The Commission also recognizes that some commenters feel that inclusion of shareholder nominees for director in company proxy materials could have a disruptive effect on board dynamics and board operation.[169] For example, we have heard from some commenters concerns about the possibility of "special interest" or "single issue" directors that would advance the interests of the nominating shareholder over the interests of shareholders as a group.[170] In

165 The nominating shareholder and each member of the nominating shareholder group would be subject to liability pursuant to a proposed amendment to Rule 14a-9 with respect to the representation and disclosure included in the company's proxy materials.

166 See 2003 Summary of Comments; see also comment letters from McKinnell, BRT; CalPERS; CII; CIR; and Wells Fargo.

167 See 2003 Summary of Comments; see also comment letters from McKinnell, BRT and Wells Fargo.

168 See proposed Instruction 1 to Rule 14a-18(d).

169 See, e.g., comment letter on 2007 Proposals from Mulcahy, BRT.

170 See comment letters on 2007 Proposals from Keith F. Higgins, Committee Chair, American Bar Association, Section of Business Law (October 2, 2007) ("ABA 2007"); and Mulcahy, BRT. See also 2003 Summary of Comments and comment letters from ABA; ASCS; McKinnell, BRT; Blackwell

response to this concern, in 2003, the Commission proposed a limitation on relationships between a nominating shareholder or group and the director nominee that is included in company proxy materials. For example, where the nominating shareholder or members of the nominating shareholder group were natural persons, the nominating shareholder or group would not have been able to nominate themselves or any member of the nominating shareholder group, or any member of the immediate family of the nominating shareholder or any member of the group. In addition, a nominating shareholder would not have been able to nominate an individual who had been employed by, or whose immediate family member had been employed by, the nominating shareholder or any member of the nominating shareholder group, or who had accepted consulting, advisory, or other compensatory fees from the nominating shareholder or any member of the nominating shareholder group. A number of commenters expressed concern about these requirements,[171] and questioned the fairness and wisdom of the limitations.[172] These commenters did not believe that it was fair to subject shareholder nominees for director to a different standard than board nominees[173] and felt that the requirements would inhibit significant

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Sanders; Sullivan; and Valero.

171 See 2003 Summary of Comments; see also comment letters from BellTel Retirees Inc. (January 12, 2004); AFL-CIO; Association for Investment Management and Research (December 22, 2003); Association of US West Retirees (January 13, 2004); CalPERS; CalSTRS; CII; CIR; Corporate Library; Domini Social Investments LLC (December 22, 2003); Duberstein; State Board of Administration of Florida (December 19, 2003); Mark S. Gardiner (December 22, 2003); Hermes Pensions Management Limited (December 22, 2003); Alan G. Hevesi, Comptroller, State of New York (December 19, 2003) ("Hevesi"); Institutional Shareholder Services (December 18, 2003); Lawndale Capital Management, LLC (December 22, 2003) ("Lawndale"); LongView; LSV Asset Management (December 22, 2003); James McRitchie, Editor, Corporate Governance (November 16, 2003, December 22, 2003, and March 29, 2004) ("McRitchie 2003"); State Retirement and Pension System of Maryland (December 16, 2003); STRS Ohio; Ohio Public Employees Retirement System (December 22, 2003); Relational Investors LLC (December 21, 2003) ("Relational"); Kurt Schacht, J.D., CFA, Wyser-Pratte & Co. (November 13, 2003); San Diego City Employees' Retirement System (December 17, 2003); Social Investment Forum Ltd. (December 22, 2003); and Tannahill.

172 See 2003 Summary of Comments; see also comment letters from CalPERS; CII; Hevesi; Lawndale; and Relational.

173 See id.

holders from seeking seats on boards,[174] thus excluding particularly desirable director candidates from being nominated under the rule.[175] While some commenters supported the proposed limitations (e.g., to address the special interest concern),[176] others noted that any nominees that were included in the company's proxy materials would still have to be elected by the shareholders and, if elected, would be subject to state law fiduciary duties.[177]

After further consideration and review of the comments on the 2003 Proposal, we have determined not to propose limitations on the relationships between a nominating shareholder or group and their director nominee or nominees. We agree with those commenters that opposed the proposed limitations and believe that such limitations may not be appropriate or necessary. Rather, we believe that Rule 14a-11, as proposed, should facilitate exercises of state law rights and afford a shareholder or group meeting the proposed standards the ability to propose a nominee for director that, in the nominating shareholder's view, better represents the interests of shareholders than those put forward by the nominating committee or board. We note that once a nominee is elected to the board of directors, that director will be subject to state law fiduciary duties and owe the same duty to the corporation as any other director on the board.

c. Nominating shareholder or group will not be deemed affiliates of the company

It is our view that the mere use of proposed Rule 14a-11, by itself, should not be deemed

174 See 2003 Summary of Comments; see also comment letters from CalPERS; CII; Lawndale; McRitchie 2003; and Relational.

175 See 2003 Summary of Comments; see also comment letter from Richard Moore, North Carolina Treasurer; Sean Harrigan, President, CalPERS; and Alan G. Hevesi, New York State Comptroller, on behalf of National Coalition for Corporate Reform (December 18, 2003) ("NCCR").

176 See 2003 Summary of Comments; see also comment letters from ABA; ASCS; Blackwell Sanders; Hall; and Sullivan.

177 See 2003 Summary of Comments; see also comment letters from CalPERS and NCCR.

to establish a relationship between the nominating shareholder or group and the company that would result in that holder or group being deemed an "affiliate" of the company for purposes of the federal securities laws. Accordingly, proposed Rule 14a-11(a) would include an instruction making clear that a nominating shareholder will not be deemed an "affiliate" of the company under the Securities Act of 1933[178] or the Exchange Act solely as a result of nominating a director or soliciting for the election of such a director nominee or against a company nominee pursuant to Rule 14a-11.[179] In addition, where a shareholder nominee is elected, and the nominating shareholder or group does not have an agreement or relationship with that director, other than relating to the nomination, the nominating shareholder or group would not be deemed an affiliate solely by virtue of having nominated that director under the proposed rules.[180]

Request for Comment

D.1. Is it appropriate to use compliance with state law, federal law, and listing standards as a condition for eligibility?

D.2. Should there be any other or additional limitations regarding nominee eligibility? Would any such limitations undercut the stated purposes of the proposed rule? Are any such limitations necessary? If so, why?

D.3. Should there be requirements regarding independence of the nominee and nominating shareholder or group and the company and its management? If so, are the proposed limitations appropriate? What other or additional limitations would

178 15 U.S.C. 77a et seq.

179 This safe harbor is set forth in Instruction 1 to proposed Rule 14a-11(a). The safe harbor is intended to operate such that the determination of whether a shareholder or group is an "affiliate" of the company would continue to be made based upon all of the facts and circumstances regarding the relationship of the shareholder or group to the company, but a shareholder or group will not be deemed an affiliate "solely" by virtue of having nominated that director.

180 See Instruction 1 to proposed Rule 14a-11(a).

be appropriate? If these limitations generally are appropriate, are there instances where they should not apply? Should the fact that the nominee is being nominated by a shareholder or group, combined with the absence of any agreement with the company or its management, be a sufficient independence requirement?

D.4. How should any independence standards be applied? Should the nominee and the nominating shareholder or group have the full burden of determining the effect of the nominee's election on the company's compliance with any independence requirements, even though those consequences may depend on the outcome of any election and may relate to the outcome of the election with regard to nominees other than shareholder nominees? Should the rules specify that the nominating shareholder or group may rely on information disclosed in the company's Commission filings in making this determination? How should the independence standards be applied when the entity is not a corporation – for example, a limited partnership?

D.5. Where a company is subject to an independence standard of a national securities exchange or national securities association that includes a subjective component (e.g., subjective determinations by a board of directors or a group or committee of the board of directors), should the shareholder nominee be subject to those same requirements as a condition to nomination?

D.6. As proposed, a nominating shareholder or group would be required to represent that the shareholder nominee satisfies generally applicable objective standards of a national securities exchange or national securities association that are applicable to directors of the company generally and not any particular definition of independence applicable to members of the audit committee of the company's board of directors. Should the proposal clarify that the nominee must meet the applicable objective standards of the company's primary listing exchange?

D.7. Should the company or its nominating committee have any role in determining whether a shareholder nominee satisfies the generally applicable objective standards for director independence of any exchange on which the company's securities are listed?

D.8. If a company has more stringent independence requirements than the listing standards applicable to the company, should the company's requirements apply? Or should the listing standards apply?

D.9. If a company is not subject to an independence standard, should shareholder nominees to the board of directors under Rule 14a-11 be required to provide disclosure concerning whether they would be independent? If so, what standard should apply? Should the nominating shareholder or group be able to select the standard?

D.10. Should we apply the "interested person" standard of Section 2(a)(19) of the Investment Company Act with respect to the representation that a shareholder nominee be independent from a company that is a registered investment company? Should the "interested person" standard also apply to shareholder nominees for election to the board of directors of a business development company? Should we instead apply a different independence standard to registered investment companies or business development companies, such as the definition of independence in Exchange Act Rule 10A-3?[181]

D.11. As proposed, the rule includes a safe harbor providing that nominating shareholders will not be deemed "affiliates" solely as a result of using Rule 14a-11. This safe harbor would apply not only to the nomination of a candidate, but also where that candidate is elected, provided that the nominating shareholder or group does not have an agreement or relationship with that director otherwise than relating to the nomination. Is it appropriate to provide such a safe harbor for shareholder nominations? Should the safe harbor continue to apply where the nominee is elected? If so, should the nomination and election of the shareholder's nominee be a consideration in determining whether the shareholder is an affiliate, or should the safe harbor be "absolute"?

D.12. Should the Commission include a similar safe harbor provision for nominating shareholders that submit a nominee for inclusion in a company's proxy materials pursuant to an applicable state law provision or a company's governing documents rather than using proposed Rule 14a-11? Why or why not?

D.13. Should the eligibility criteria include a prohibition on any affiliation between nominees and nominating shareholders or groups? If so, what limitations would be appropriate? For example, should there be a prohibition on the nominee being the nominating shareholder or a member of the nominating shareholder group, a member of the immediate family of the nominating shareholder or any member of the nominating shareholder group, or an employee of the nominating shareholder or any member of the nominating shareholder group? Would such a limitation unnecessarily restrict access by shareholders to the proxy process?

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181 17 CFR 240.10A-3.

D.14. Should eligibility criteria include a prohibition on agreements between companies and its management and nominating shareholders, as proposed? Would such a prohibition inhibit desirable negotiations between shareholders and boards or nominating committees regarding nominees for directors? Should the prohibition provide an exception to permit such negotiations, as proposed? If so, what should the relevant limitations be?

D.15. Should the nominee be required to make any of the representations (e.g., the independence representation), either in addition to or instead of, the nominating shareholder or group? If so, should these representations be included in the shareholder notice on Schedule 14N or in some other document?

D.16. Should there be a nominee eligibility criterion that would exclude an otherwise eligible nominee where that nominee has been included in the company's proxy materials as a candidate for election as director but received a minimal percentage of the vote? If so, what would be the appropriate percentage (e.g., 5%, 10%, 15%, 25%, or 35%)? If so, for how long should the nominee be excluded (e.g., 1 year, 2 years, 3 years, 4 years, 5 years, permanently)?

5. Maximum Number of Shareholder Nominees to Be Included in Company Proxy Materials

We do not intend for proposed Rule 14a-11 to be available for any shareholder or group that is seeking to change the control of the issuer or to gain more than a limited number of seats on the board. The existing procedures regarding contested elections of directors are intended to continue to fulfill that purpose.[182] We also note that by allowing shareholder nominees to be included in a company's proxy materials, the cost of the solicitation is essentially shifted from

182 See, e.g., Exchange Act Rule 14a-12(c).

the individual shareholder or group to the company and thus, all of the shareholders. We do not believe that an election contest conducted by a shareholder to change the control of the issuer or to gain more than a limited number of seats should be funded out of corporate assets. Further, extensive changes in board membership, or the possibility of such changes as a result of additional nominees being included in the proxy statement, have the potential to be disruptive to the board, while also potentially being confusing to shareholders. Amending our rules to provide for the inclusion of shareholder nominees for directors in a company's proxy materials is a significant change. Given the novelty of such a change, we believe it is appropriate to take an incremental approach as a first step and reassess at a later time to determine whether additional changes would be appropriate.

As proposed, a company would be required to include no more than one shareholder nominee or the number of nominees that represents 25 percent of the company's board of directors, whichever is greater.[183] Where a company has a director (or directors) currently serving on its board of directors who was elected as a shareholder nominee pursuant to Rule 14a-11, and the term of that director extends past the date of the meeting of shareholders for which the company is soliciting proxies for the election of directors, the company would not be required to include in its proxy materials more shareholder nominees than could result in the total number of directors serving on the board that were elected as shareholder nominees being greater than one shareholder nominee or 25 percent of the company's board of directors, whichever is greater.[184] We believe this limitation is appropriate to reduce the possibility of a

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183 See proposed Rule 14a-11(d)(1). According to information from RiskMetrics, based on a sample of 1,431 public companies, in 2007, the median board size was 9, with boards ranging in size from 4 to 23 members. Approximately 40% of the boards in the sample had 8 or fewer directors, approximately 60% had between 9 and 19 directors, and less than 1% had 20 or more directors.

184 See proposed Rule 14a-11(d)(2). Depending on board size, 25% of the board may not result in a whole number. In those instances, the maximum number of shareholder nominees for director that a registrant

nominating shareholder or group using the proposed new rule as a means to effect a change in control of a company or to gain more than a limited number of seats on the board by repeatedly nominating additional candidates for director. We note that in the 2003 Proposal, the Commission proposed to require companies to include a set number of nominees, rather than a percentage of the board, as proposed today.[185] We believe that using a percentage in the rule will promote ease of use and alleviate any concerns that a company may increase its board size in an effort to reduce the effect of a shareholder nominee elected to the board.

Proposed Rule 14a-11(d)(3) would address situations where more than one shareholder or group would be eligible to have its nominees included in the company's form of proxy and disclosed in its proxy statement pursuant to the proposed rule. In those situations, the company would be required to include in its proxy statement and form of proxy the nominee or nominees of the first nominating shareholder or group from which it receives timely notice of intent to nominate a director pursuant to the rule, up to and including the total number of shareholder nominees required to be included by the company.[186] Where the first nominating shareholder or group from which the company receives timely notice does not nominate the maximum number of directors allowed under the rule, the nominee or nominees of the next nominating shareholder or group from which the company receives timely notice of intent to nominate a director pursuant to the rule would be included in the company's proxy materials, up to and including the total number of shareholder nominees required to be included by the company.

will be required to include in its proxy materials will be the closest whole number below 25%. See Instruction 1 to paragraph (d).

185 Comments on the 2003 Proposal provided a range of views regarding the appropriate number of shareholder nominees. Commenters that supported the use of a percentage, or combination of a set number and a percentage, to determine the number of shareholder nominees suggested percentages ranging from 20% to 35%. See 2003 Summary of Comments.

186 This requirement is set forth in proposed Rule 14a-11(d)(3).

Although in 2003 we proposed a standard under which the largest shareholder or group would have their nominee or nominees included in the company proxy materials and the limited number of shareholders that commented did not generally object to such a standard,[187] after further consideration we believe that such a standard might be difficult for companies to administer because it would lack certainty. By using a first-in standard, a company would be able to begin preparing its materials and coordinating with the nominating shareholder or group immediately upon receiving an eligible nomination rather than waiting to see whether another nomination from a larger nominating shareholder or group is submitted before the notice deadline. This approach also may be fairer to the shareholder whose notice is received first and may provide certainty to the shareholder because it eliminates the possibility that the shareholder's nominee will be excluded as a result of a larger shareholder subsequently submitting a nominee.

Request for Comment

E.1. Is it appropriate to include a limitation on the number of shareholder director nominees? If not, how would the proposed rules be consistent with our intention not to allow Rule 14a-11 to become a vehicle for changes in control?

E.2. If there should be a limitation, is the proposed maximum percentage of shareholder nominees for director that we have proposed appropriate? If not, should the maximum percentage be higher (e.g., 30%, 35%, 40%, or 45%) or lower (e.g., 10%, 15%, or 20%)? Should the percentage vary depending on the size of the board? Should the limitation be the greater or lesser of a specified number of nominees or percentage of the total number of directors on the board? Is it appropriate to permit more than one shareholder nominee regardless of the

[187] See 2003 Summary of Comments.

size of the company's board of directors?

E.3. In instances where 25% of the board does not result in a whole number, the maximum number of shareholder nominees for director that a registrant will be required to include in its proxy materials will be the closest whole number below 25%. Is it appropriate to round down in this instance? Should we instead round up to the nearest whole number above 25%? Is a rounding rule necessary?

E.4. Should the proposed rule address situations where the governing documents provide a range for the number of directors on the board rather than a fixed number of board seats? If so, what changes to the rule would be necessary?

E.5. The proposal contemplates taking into account incumbent directors who were nominated pursuant to proposed Rule 14a-11 for purposes of determining the maximum number of shareholder nominees. Is that appropriate? Should there be a different means to account for such incumbent directors?

E.6. Should the procedure address situations in which, due to a staggered board, fewer director positions are up for election than the maximum permitted number of shareholder nominees? If so, how? Should the maximum number be based on the number of directors to be elected rather than to the overall board size?

E.7. Should any limitation on shareholder nominees take into account incumbent directors who were nominated outside of the Rule 14a-11 process, such as pursuant to an applicable state law provision, a company's governing documents, or a proxy contest? If so, should such directors be counted as "shareholder nominees" for purposes of determining the 25%?

E.8. Should any limitation on shareholder nominees take into account shareholder nominees for director that a company includes in its proxy materials other than pursuant to Rule 14a-11 (e.g., voluntarily)?

E.9. Should Rule 14a-11 provide an exception for controlled companies or companies with a contractual obligation that permits a certain shareholder or group of shareholders to appoint a set number of directors? Should a nominating shareholder or group only be permitted to submit nominees for director based upon the number of director seats the nominating shareholder is entitled to vote on? For example, if a board consists of 10 directors and the company is contractually obligated to permit a certain shareholder or shareholders to appoint five directors to the board, should shareholders entitled to vote on the remaining five director slots be limited to submitting nominees based on a board size of five rather than 10, meaning that a nominating shareholder may submit one nominee for inclusion in the company's proxy materials?

E.10. We have proposed a limitation that permits the nominating shareholder or group that first provides notice to the company to include its nominee or nominees in the company's proxy materials where there is more than one eligible nominating shareholder or group. Is this appropriate? If not, should there be different criteria for selecting the shareholder nominees (e.g., largest beneficial ownership, length of security ownership, random drawing, allocation among eligible nominating shareholders or groups, etc.)? Rather than using criteria such as that proposed, should companies have the ability to select among eligible nominating shareholders or groups? If so, what criteria should the company be required to use in doing so?

E.11. If the Commission adopts a "first-in" approach, should the first shareholder or group get to nominate up to the total number of nominees required to be included by the company or, where there is more than one nominating shareholder or group and more than one slot for nominees, should the slots be allocated among proposing shareholders according to, for example, the order in which the shareholder or group provided notice to the company?

E.12. Under the proposal, where the first nominating shareholder or group to deliver timely notice to the company does not nominate the maximum number of directors allowed under the rule, the nominee or nominees of the next nominating shareholder or group to deliver timely notice of intent to nominate a director pursuant to the rule would be included in the company's proxy materials, up to and including the total number of shareholder nominees required to be included by the company. Should the rule specify how to determine which of a second nominating shareholder's or group's nominees are to be selected where there are more nominees than available spots under the rule? Should Rule 14a-11 provide that only one nominating shareholder or group may have their nominee or nominees included in the company proxy materials, regardless of whether they nominate the maximum number allowed under the rule?

E.13. Would the "first-in" approach result in an undue advantage to the first shareholder or group to submit a nomination? Would such an approach result in a race to be the first in?

6. Notice and Disclosure Requirements

To submit a nominee for inclusion in the company's proxy statement and form of proxy, proposed Rule 14a-11 would require that the nominating shareholder or group provide a notice on Schedule 14N to the company of its intent to require that the company include that shareholder's or group's nominee or nominees in the company's proxy materials.[188] The shareholder notice on Schedule 14N would also be required to be filed with the Commission.

The notice would be required to be provided to the company and filed by the date specified by the company's advance notice provision or, where no such provision is in place, no later than 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting. We are proposing 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting as the standard where a company does not have an advance notice provision because we believe that 120 days would provide adequate time for companies to take the steps necessary to include or, where appropriate, to exclude a shareholder nominee for director that is submitted pursuant to Rule 14a-11. If the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, however, then the nominating shareholder must provide notice a reasonable time before the company mails its proxy materials. The company would be required to disclose the date by which the shareholder must submit the required notice in a Form 8-K filed pursuant to proposed Item 5.07 within four business days after the company determines the anticipated meeting date.[189]

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188 See proposed Rule 14a-11(c), Rule 14a-18 and Rule 14n-1.

189 See proposed Instruction 2 to Rule 14a-11(a) and proposed Rule 14a-18. This would be similar to the requirement currently included in Rule 14a-5(f), which specifies that, where the date of the next annual meeting is advanced or delayed by more than 30 calendar days from the date of the annual meeting to which the proxy statement relates, the company must disclose the new meeting date in the company's earliest possible quarterly report on Form 10-Q. Although registered investment companies generally are not required to file Form 8-K, we are proposing to require them to file a Form 8-K disclosing the date by which the shareholder notice must be provided if the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year. See proposed Exchange Act Rules 13a-11(b)(2) and 15d-11(b)(2).

The notice would be filed with the Commission on proposed new Exchange Act Schedule 14N on the date the notice is sent to the company.[190] The new Schedule 14N would require:[191]

- The name and address of the nominating shareholder or each member of the nominating shareholder group;
- Information regarding the amount and percentage of securities beneficially owned and entitled to vote at the meeting;
- A written statement from the "record" holder of the shares beneficially owned by the nominating shareholder or each member of the nominating shareholder group (usually a broker or bank) verifying that, as of the date of the shareholder notice on Schedule 14N, the shareholder continuously held the securities for at least one year;[192]
- A written statement of the nominating shareholder's or group's intent to continue to own the requisite shares through the shareholder meeting at which directors are elected. Additionally, the nominating shareholder or group would provide a written statement regarding the nominating shareholder's or group's intent with respect to continued ownership after the election;[193] and

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190 In this regard, we propose to amend Rule 13(a)(4) of Regulation S-T to provide that a Schedule 14N will be deemed to be filed on the same business day if it is filed on or before 10 p.m. Eastern Standard Time or Eastern Daylight Saving Time, whichever is currently in effect. This will allow nominating shareholders additional time to file the notice on Schedule 14N and transmit the notice to the company.

191 In the 2003 Proposal, the Commission proposed to rely on disclosure obtained in a Schedule 13G. The Schedule 13G filing requirement is triggered when a shareholder or group owns more than 5% of the company's securities. In the current proposal, we are proposing ownership thresholds for many companies that are different from the more than 5% threshold proposed in 2003. We nevertheless believe uniform disclosure for all companies, regardless of size, would be appropriate. Therefore, we are proposing a new filing requirement on Schedule 14N, to require certain disclosures regarding the nominating shareholder and nominee that would not otherwise be required to be filed.

192 This requirement would be applicable only where the nominating shareholder is not the registered holder of the shares and where the shareholder has not filed a Schedule 13D, Schedule 13G, Form 3, Form 4, and/or Form 5, or amendments to those documents. <u>See</u> Item 5(a) to proposed Schedule 14N.

193 <u>See</u> proposed Rule 14a-18(f), proposed Item 5(b) of Schedule 14N, proposed Item 7(e) of Schedule 14A, and proposed Item 22(b)(18) of Schedule 14A.

- A certification that to the best of the nominating shareholder's or group's knowledge and belief, the securities are not held for the purpose of, or with the effect of, changing the control of the issuer or gaining more than a limited number of seats on the board of directors.[194]

We believe that these disclosures would assist shareholders in making an informed voting decision with regard to any nominee or nominees put forth by the nominating shareholder or group, in that the disclosures would enable shareholders to gauge the nominating shareholder's or group's interest in the company, longevity of ownership, and intent with regard to continued ownership in the company. These disclosures also would be important to the company in determining whether the nominating shareholder or group is eligible to rely on Rule 14a-11 to include a nominee or nominees in the company's proxy materials.

The shareholder notice on Schedule 14N also would include representations concerning the nominating shareholder's or group's eligibility to use Rule 14a-11, as well as disclosure about the nominating shareholder or group and the nominee for director. The disclosure provided by the nominating shareholder or group would be similar to the disclosure currently required in a contested election and would be included by the company in its proxy materials. This disclosure would be required pursuant to proposed new Exchange Act Rule 14a-18. Specifically, the shareholder notice on Schedule 14N would be required to include:

- A representation that the nominating shareholder or group is eligible to submit a nominee under Rule 14a-11;[195]

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194 See Item 8 of proposed Schedule 14N.

195 The eligibility standards for nominating shareholders are set forth in proposed Rule 14a-11(b). Pursuant to Rule 14a-18(b), the nominating shareholder would be required to include a representation in the notice that the nominating shareholder or group satisfies the conditions in Rule 14a-11(b).

- A representation that, to the knowledge of the nominating shareholder or group, the candidate's nomination or initial service on the board, if elected, would not violate controlling state law, federal law, or applicable listing standards (other than a standard relating to independence);[196]
- A representation that, to the knowledge of the nominating shareholder or group, the nominee meets the objective criteria for independence from the company that are set forth in applicable rules of a national securities exchange or national securities association[197] or, in the case of a registered investment company or business development company, that the nominee to the board is not an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act;[198]
- A representation that neither the nominee nor the nominating shareholder (or any member of the nominating shareholder group, if applicable) has an agreement with the company regarding the nomination of the nominee;[199]
- A statement from the nominee that the nominee consents to be named in the company's proxy statement and to serve on the board if elected, for inclusion in the company's proxy statement;[200]

196 Proposed Rule 14a-11(a)(2) requires that the nomination and initial board service not violate these standards. This representation would be included in the nominating shareholder's notice pursuant to proposed Rule 14a-18(a).

197 The representation is not required if the company is not subject to the rules of a national securities exchange or national securities association.

198 This representation would be included in the nominating shareholder's notice pursuant to proposed Rule 14a-18(c). The criteria for independence would be those generally applicable to directors, and not particular independence requirements, such as the requirements for audit committee members. See the Instruction to Rule 14a-18(c).

199 This representation would be included in the nominating shareholder's notice pursuant to proposed Rule 14a-18(d).

200 This statement would be included in the nominating shareholder's notice pursuant to proposed

- A statement that the nominating shareholder or each member of the nominating shareholder group intends to continue to own the requisite amount of securities through the date of the meeting;[201]
- Disclosure about the nominee complying with the requirements of Item 4(b), Item 5(b), and Items 7(a), (b) and (c) and, for investment companies, Item 22(b) of Exchange Act Schedule 14A, for inclusion in the company's proxy statement;[202]
- Disclosure about the nominating shareholder or members of a nominating shareholder group consistent with the disclosure currently required pursuant to Item 4(b) and Item 5(b) of Schedule 14A in a contested election;[203]
- Disclosure about whether the nominating shareholder or member of a nominating shareholder group has been involved in any legal proceeding during the past five years, as specified in Item 401(f) of Regulation S-K. Disclosure pursuant to this section need not be provided if provided in response to Items 4(b) and 5(b) of

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Rule 14a-18(e).

201 See proposed Rule 14a-18(f).

202 This information would be included in the nominating shareholder's notice pursuant to proposed Rule 14a-18(g). This information would identify the nominee, describe certain legal proceedings, if any, related to the nominee, and describe certain of the nominee's transactions and relationships with the company. See Items 7(a), (b), and (c) of Schedule 14A. This information also would include biographical information and disclosure about certain interests of the nominee. See Item 5(b) of Schedule 14A. With respect to a nominee for director of a registered investment company or business development company, the disclosure would include certain basic information about the nominee and any arrangement or understanding between the nominee and any other person pursuant to which he was selected as a nominee; information about the positions, interests, and transactions and relationships of the nominee and his immediate family members with the company and persons related to the company; information about the amount of equity securities of funds in a fund complex owned by the nominee; and information describing certain legal proceedings related to the nominee, including legal proceedings in which the nominee is a party adverse to, or has a material interest adverse to, the company or any of its affiliated persons. See paragraph (b) of Item 22 of Schedule 14A.

203 This information would be submitted in the nominating shareholder's notice pursuant to proposed Rule 14a-18(h).

Schedule 14A;[204]

- The following disclosure regarding the nature and extent of the relationships between the nominating shareholder or group and nominee and the company or any affiliate of the company:
  - Any direct or indirect material interest in any contract or agreement between the nominating shareholder or group or the nominee and the company or any affiliate of the company (including any employment agreement, collective bargaining agreement, or consulting agreement);
  - Any material pending or threatened litigation in which the nominating shareholder or group or nominee is a party or a material participant and that involves the company, any of its officers or directors, or any affiliate of the company; and
  - Any other material relationship between the nominating shareholder or group or the nominee and the company or any affiliate of the company not otherwise disclosed;[205]
- Disclosure of any website address on which the nominating shareholder or group may publish soliciting materials;[206] and
- If desired to be included in the company's proxy statement, any statement in support of the shareholder nominee or nominees, which may not exceed 500 words.[207]

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204 See proposed Rule 14a-18(i). Similar information is required for a nominee in response to Items 4(b) and 5(b) of Schedule 14A. We believe that it is appropriate to require similar disclosure of information from the nominating shareholder or group.

205 See proposed Rule 14a-18(j).

206 This information would be included in the nominating shareholder's notice pursuant to proposed Rule 14a-18(k).

207 See proposed Rule 14a-18(l). The 500 words would be counted in the same manner as words are counted under Rule 14a-8. Any statements that are, in effect, arguments in support of the nomination would

We note that the disclosure requirements we have proposed here are substantially similar to the requirements the Commission proposed in the 2003 Proposal. In both cases, the requirements focus on obtaining disclosure similar to what would be obtained in an election contest. In the 2003 Proposal, because the Commission proposed a 5% ownership threshold, nominating shareholders or groups would have been required to file a Schedule 13G, so the Commission also proposed to require certain disclosures and representations from the nominating shareholder and nominee on Schedule 13G rather than create a new schedule. Under the tiered ownership threshold we are proposing, a nominating shareholder or group may hold less than 5% of the company's securities and would not be required to file a Schedule 13G. Accordingly, because we believe that uniform disclosure regardless of company size would be appropriate, we are proposing a new Schedule 14N that would require the same disclosures and representations from the nominating shareholder and nominee regardless of the percentage of the company's securities held by the nominating shareholder or group.

The Schedule 14N would be filed with the Commission in the following manner:[208]

- The filing would include a cover page in the form set forth in proposed Schedule 14N with the appropriate box on the cover page marked to specify that the filing relates to

constitute part of the supporting statement. Accordingly, any "title" or "heading" that meets this test would be counted toward the 500-word limitation. Inclusion of a website address in the supporting statement would not violate the 500-word limitation; rather, the website address would be counted as one word for purposes of the 500-word limitation. We note that in the 2003 Proposal the Commission proposed that a company would be required to include a nominating shareholder's or group's supporting statement in the company's proxy materials in instances where the company made a statement opposing the nominating shareholder's nominee or nominees and/or supporting company nominees. Most commenters thought that a nominating shareholder's or group's supporting statement should be included in company proxy materials irrespective of whether the company includes its own supporting statement or statement in opposition to a shareholder nominee. See 2003 Summary of Comments.

208 The requirement to file a Schedule 14N with the Commission is set forth in proposed Rule 14n-1 and proposed Rule 14a-18.

a Rule 14a-11 nomination;[209]

- The filing would be made under the subject company's Exchange Act file number (or in the case of a registered investment company, under the subject company's Investment Company Act file number); and
- The filing would be made on the date the notice is first transmitted to the company.

In order to file the Schedule 14N on EDGAR, a nominating shareholder or group and any nominee that does not already have EDGAR filing codes, and to which the Commission has not previously assigned a user identification number, which we call a "Central Index Key (CIK)" code, would need to obtain the codes by filing electronically a Form ID[210] at https://www/filermanagement.edgarfiling.sec.gov. The applicant also would be required to submit a notarized authenticating document. If the authenticating document is prepared before the applicant makes the Form ID filing, the authenticating document may be uploaded as a Portable Document Format (PDF) attachment to the electronic filing. An applicant also may submit the authenticating document by faxing it to the Commission within two business days before or after electronically filing the Form ID.[211]

The Schedule 14N would be required to be amended promptly for any material change in the facts set forth in the originally-filed Schedule 14N. In this regard, we would view withdrawal of a nominating shareholder or group, or of a director nominee, and the reasons for

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209 The Schedule 14N also would be used for disclosure concerning the inclusion of shareholder nominees in company proxy materials when made pursuant to an applicable state law provision or a company's governing documents, as set out in proposed Rule 14a-19.

210 17 CFR 239.63; 249.446; and 274.402.

211 The authenticating document would need to be manually signed by the applicant over the applicant's typed signature, include the information contained in the Form ID, and confirm the authenticity of the Form ID. If the authenticating document is filed after electronically filing the Form ID, it would need to include the accession number assigned to the electronically filed Form ID as a result of its filing. See 17 CFR 232.10(b)(2).

any such withdrawal, as a material change. For example, such a withdrawal could be material because it may result in a group no longer meeting the required ownership threshold under Rule 14a-11. The nominating shareholder or group also would be required to file a final amendment to the Schedule disclosing within 10 days of the final results of the election being announced by the company the nominating shareholder's or group's intention with regard to continued ownership of their shares. The nominating shareholder would previously have disclosed their intent with regard to continued ownership of the company's securities in its original notice on Schedule 14N. Filing of the amendment to the Schedule 14N would provide shareholders with information as to whether the outcome of the election may have altered the intent of the shareholder and what further plans with regard to the company the nominating shareholder may have.

The Schedule 14N, as filed with the Commission, as well as any amendments to the Schedule 14N, would be subject to the liability provisions of Exchange Act Rule 14a-9 pursuant to proposed new paragraph (c) to the rule.[212]

In a traditional proxy contest, shareholders would receive the disclosure required by Items 4(b), 5(b), and Item 7 (or Item 22, as applicable) of Schedule 14A as discussed above. The proposed Schedule 14N disclosure requirements are somewhat more expansive in that they also would include the disclosures concerning ownership amount, length of ownership, intent to continue holding the shares through the date of the meeting, and a certification that the nominating shareholder or group is not seeking to change the control of the issuer or to gain more than a limited number of seats on the board of directors. In addition, the proposed disclosure requirements would include representations concerning the nominating shareholder's or group's eligibility to rely on Rule 14a-11 to include a nominee or nominees in the company's

212 For further discussion, see Section III.E.

proxy statement, as well as representations concerning the nominee's eligibility, and disclosure regarding the nature and extent of the relationships between the nominating shareholder or group and nominee and the company or any affiliate of the company. Today's proposed disclosure requirements are not as extensive, however, as those in the Shareholder Proposals Proposing Release that were not adopted. In that instance, a shareholder that was relying on a company bylaw to include a nominee for director in a company's proxy materials would have had to provide the following disclosures in addition to what we are proposing today:

- a description of the following items that occurred during the 12 months prior to the formation of any plans or proposals, or during the pendency of any proposal or nomination:
  - any material transaction of the shareholder with the company or any of its affiliates, and
  - any discussion regarding the proposal between the shareholder and a proxy advisory firm;
- any holdings of more than 5% of the securities of any competitor of the company (i.e., any enterprise with the same SIC code); and
- any meetings or contacts, including direct or indirect communication by the shareholder, with the management or directors of the company that occurred during the 12-month period prior to the formation of any plans or proposals, or during the pendency of the proposal.[213]

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213 These disclosures would have applied to either a shareholder proponent of a proposal to amend a company's bylaws to establish procedures for inclusion in the company's proxy materials of shareholder nominees for director or to a nominating shareholder under such an adopted bylaw. A shareholder proponent of a bylaw proposal would also have been required to disclose background information about the proposing shareholder including qualifications and background relevant to the plans or proposals, and any interests or relationships of such shareholder proponent that are not shared generally by the other

Based on the comments we received on the Shareholder Proposals Proposing Release, we believe that requiring such extensive disclosure may be impractical and may serve as a deterrent to shareholders' exercise of their right to nominate directors. We believe that the disclosure we propose today would provide transparency and facilitate shareholders' ability to make an informed voting decision on a shareholder director nominee or nominees without being unnecessarily burdensome on nominating shareholders or groups. We believe that the proposed disclosure would be particularly important because the nominating shareholder or group would not be bound by the same fiduciary duties applicable to the members of a board's nominating committee in selecting director nominees.

Request for Comment

F.1. Are the proposed content requirements of the shareholder notice on Schedule 14N appropriate? Are there matters included in the notice that should be eliminated (e.g., should the nominating shareholder be required to provide disclosure of its intention with regard to continued ownership of the shares after the election, as is proposed)?

F.2. Are there additional matters that should be included? For example, is there additional information that should be included with regard to the nominating shareholder or group or with regard to the shareholder nominee?

F.3. Are the required representations appropriate? Should there be additional representations (e.g., should the nominee be required to make a representation concerning their understanding of their duties under state law if elected and their

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shareholders of the company and that could have influenced the decision by such proponent to submit a proposal.

ability to act in the best interest of the company and all shareholders)? Should any of the proposed representations be eliminated?

F.4. Is five years a sufficient time period for information about whether the nominating shareholder or member of a nominating shareholder group has been involved in any legal proceeding? Should it instead be ten years?

F.5. What should be the consequence of a nominating shareholder or group including materially false information or a materially false representation in the nominating shareholder's or group's notice on Schedule 14N to the company, whether before inclusion of a nominee in the company's proxy materials, after inclusion of a nominee in the company's proxy materials but before the election, or after a nominee has been included in the company's proxy materials and elected? Should it make a difference whether the false information or representation was provided knowingly? Should it make a difference whether the false information or representation was material?

F.6. What should be the consequence to the nominating shareholder or group of submitting the notice on Schedule 14N to the company after the deadline? What should be the consequence of filing the notice on Schedule 14N with the Commission after the deadline? Should a late submission to the company or late filing with the Commission render the nominating shareholder or group ineligible to have a nominee included in the company's proxy materials under Rule 14a-11 with respect to the upcoming meeting, as is currently proposed?

F.7. The proposed instructions to Rule 14a-11 address how to provide disclosure where the nominating shareholder is a "general or limited partnership, syndicate or other group." Is this sufficiently broad to address any nominating shareholders that may use the rule?

F.8. Should a company's advance notice provision govern the timing of the submission of shareholder nominations for directors? If not, should the Commission adopt a specific deadline instead? Should the Commission make no reference to advance notice provisions as they may apply to proxy solicitations and adopt a generally applicable federal standard? Would such an approach better enable consistent exercise by shareholders of their voting and nominating rights across public companies? If the Commission were to establish a federal standard, would 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting be appropriate? Should it be longer (e.g., 150 or 180 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting), or shorter (e.g., 90 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting)?

F.9. In the absence of an advance notice provision, the nominating shareholder or group would be required to submit the notice to the company and file with the Commission no later than 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting. Is this deadline appropriate and workable? If not, what should be the deadline (e.g., 80, 90, 100, 150, or 180 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting)?

F.10. Should there be a specified range of time in which a shareholder is permitted to submit a nominee (e.g., no earlier than 150 days before and no later than 120 days before the date the company mailed its proxy materials the previous year)? Should a different range be used (e.g., should the submission of nominations be limited to no earlier than 120 days and no later than 90 days; no earlier than 180 days and no later than 150 days; or no earlier than 180 days and no later than 120 days before the date the company mailed its proxy statement the previous year)? Does permitting submission of a nominee at any time prior to 120 days before the company mailed its proxy materials the previous year skew the process in favor of certain shareholders? If so, why? If not, why? If a different date range would be more workable, please tell us the range and why.

F.11. The proposed notice requirements address both regularly scheduled annual meetings and circumstances where a company may not have held an annual meeting in the prior year or has moved the date of the meeting more than 30 days from the prior year. Under these circumstances, what is the appropriate date by which a nominating shareholder must submit the notice to the company? Should the Commission adopt a specific deadline for non-regularly scheduled meetings, or rely on a "reasonable time" standard? If a "reasonable time" standard is adopted, should the company be required to file the Form 8-K announcing the deadline any minimum number of days in advance of the deadline? If so, how many days notice should the company provide and why? What deadline should apply when a company holds a special meeting in lieu of an annual meeting?

F.12. As proposed, an instruction to Form 8-K would specify that a company would be required to file a report pursuant to Item 5.07 within four business days of determining the anticipated meeting date if the company did not hold an annual meeting the previous year or if the annual meeting has been changed by more than 30 calendar days from the date of the previous year's meeting. Is such an instruction necessary? Should the company be required to file the Item 5.07 Form 8-K in less than four business days (e.g., two business days) or more than four business days (e.g., seven business days, 10 business days)?

F.13. Should a registered investment company be required to disclose on Form 8-K the date by which a shareholder or shareholder group must submit the notice to the company of its intent to require its nominees on the company's proxy card? Should this date also be required to be disclosed on the company's Web site, if it has one? Should registered investment companies instead be permitted to provide this disclosure in a different manner?

F.14. As proposed, a shareholder's or group's notice of intent to submit a nomination for director is required to be filed with the Commission on Schedule 14N. Is such a filing appropriate? Should additional or lesser information be filed with the Commission? Should a shareholder or group be required to send the notice to the company without filing the notice on Schedule 14N?

F.15. When should the notice on Schedule 14N be filed with the Commission? Is it sufficient to require the Schedule 14N to be filed at the time it is provided to the company? Should an abbreviated version of the Schedule 14N be filed sooner, before the nominating shareholder or group provides notice to the company, such as at the time a shareholder or group first decides to make a nomination, when the nominating shareholder first identifies a nominee for director, or some other time? Should it be filed later?

F.16. The notice on Schedule 14N would be required to be amended promptly for any material change in the facts set forth in the originally-filed Schedule 14N. Should the nominating shareholder or group be required to amend the Schedule 14N for any material change in the facts? Why or why not?

F.17. The nominating shareholder or group would be required to file a final amendment to the Schedule disclosing, within 10 days of the final results of the election being announced by the company, the nominating shareholder's or group's intention with regard to continued ownership of their shares. Should the nominating shareholder or group be required to amend the Schedule 14N to disclose their intent regarding continued ownership? Why or why not?

F.18. In situations where a nominating shareholder or group beneficially owns more than 5% of the company's securities, should we permit a combined Schedule 13G/Schedule 14N filing? Should we permit a combined Schedule 13D/Schedule 14N filing? Why or why not?

F.19. Should a nominating shareholder or group be required to file Schedule 14N on EDGAR, as proposed?

F.20. Should the notice be required to include a description of the following items that occurred during the 12 months prior to the formation of any plans or proposals with respect to the nomination, or during the pendency of any nomination: (i) any material transaction of the shareholder with the company or any of its affiliates, and (ii) any discussion regarding the nomination between the shareholder and a proxy advisory firm?

F.21. Should the nominating shareholder or group and/or nominee be required to disclose any holdings of more than 5% of the securities of any competitor of the company (i.e., any enterprise with the same SIC code)?

F.22. Should the nominating shareholder or group and/or nominee be required to disclose any meetings or contacts, including direct or indirect communication by the shareholder, with the management or directors of the company that occurred during the 12-month period prior to the formation of any plans or proposals with respect to a nomination?

7. Requirements for a Company That Receives a Notice from a Nominating Shareholder or Group

a. Inclusion of a Shareholder Director Nominee

Upon receipt of a shareholder's or group's notice of its intent to require the company to include in its proxy materials a shareholder nominee or nominees pursuant to Rule 14a-11, the company would determine whether any of the events permitting exclusion of the shareholder nominee or nominees has occurred.[214] If not, the company would notify in writing the nominating shareholder or group no later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the Commission that it will include the nominee or nominees. The company would be required to provide this notice in a manner that provides evidence of timely receipt by the nominating shareholder or group.

The company would then include disclosure regarding the shareholder nominee or

[214] See proposed Rule 14a-11(f).

nominees and the nominating shareholder or group in the company's proxy statement[215] and include the name of the nominee on the company's form of proxy that is included with the proxy statement.[216] With regard to the company's form of proxy, the company could identify any shareholder nominees as such and recommend how shareholders should vote for, against, or withhold votes on those nominees and management nominees on the form of proxy.[217] The company would otherwise be required to present the nominees in an impartial manner in accordance with Rule 14a-4. Under the current rules, a company may provide shareholders with the option to vote for or withhold authority to vote for the company's nominees as a group, provided that shareholders also are given a means to withhold authority for specific nominees in the group. In our view, this option would not be appropriate where the company's form of proxy includes shareholder nominees, as grouping the company's nominees may make it easier to vote for all of the company's nominees than to vote for the shareholder nominees in addition to some of the company nominees. Accordingly, when a shareholder nominee is included, the proposed rules would not permit a company to provide shareholders the option of voting for or withholding authority to vote for the company nominees as a group, but would instead require

215 Under the proposed rules, inclusion of a shareholder nominee in the company's proxy materials would not require the company to file a preliminary proxy statement provided that the company was otherwise qualified to file directly in definitive form. In this regard, the proposed rules make clear that inclusion of a shareholder nominee would not be deemed a solicitation in opposition. See proposed revisions to Rule 14a-6(a)(4) and Note 3 to that rule.

216 These requirements are set forth in proposed Rule 14a-11(a), proposed Rule 14a-18(g)-(l) and proposed amendments to Rule 14a-4(b)(2). In addition, we are proposing to add paragraph (e) to Item 7 of Schedule 14A (and, for registered investment companies and business development companies, paragraph (18) to Item 22(b) of Schedule 14A) to state that the registrant must include the disclosure required from the nominating shareholder under proposed Rule 14a-11(a).

217 This would be similar to the current practice with regard to shareholder proposals submitted pursuant to Rule 14a-8 where companies identify the shareholder proposals and provide a recommendation to shareholders as to how they should vote on those proposals.

that each nominee be voted on separately.[218]

A company also would be required to include in its proxy statement, if desired by the nominating shareholder or group, a statement by the nominating shareholder or group in support of the shareholder nominee or nominees. In this regard, we believe that not only should a company be able to include a statement in support of the company nominees in its proxy statement, provided that it complies with Rule 14a-9, we also are of the view that a nominating shareholder or group should be afforded a similar opportunity. Accordingly, we are proposing to require a company to include a nominating shareholder's or group's statement of support for the shareholder nominee or nominees, so long as the statement of support does not exceed 500 words.[219] This statement must be provided to the company in the shareholder notice on Schedule 14N.[220]

In addition, both the company and the nominating shareholder or group would be able to solicit in favor of their nominees outside the proxy statement (for example, on a designated website), provided that such solicitations were made within the parameters of the applicable proxy rules. Any written soliciting materials published, sent or given by the nominating shareholder or group outside the company's proxy statement would be required to be filed with the Commission in accordance with proposed Rule 14a-2(b)(7) or (b)(8) on the date of first use.

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218 See proposed Rule 14a-4(b)(2)(iv). We anticipate that companies would continue to be able to solicit discretionary authority to vote a shareholder's shares for the company nominees, as well as to cumulate votes for the company nominees in accordance with applicable state law, where such state law provides for cumulative voting.

219 See proposed Rule 14a-11(a). In counting the 500 words, any statements that are, in effect, arguments in support of the proposal would be viewed as part of the supporting statement. Accordingly, any "title" or "heading" that meets this test would be counted toward the 500-word limitation. Inclusion of a website address in the supporting statement would not violate the 500-word limitation; rather, the website address would be counted as one word for purposes of the 500-word limitation.

220 See proposed Rule 14a-18(l).

b. Excluding a Shareholder Director Nomination That Does Not Comply with the Requirements of Rule 14a-11

A company may determine that it is not required under proposed Rule 14a-11 to include a nominee from a nominating shareholder or group in its proxy materials if it determines any of the following:

- Proposed Rule 14a-11 is not applicable to the company;
- The nominating shareholder or group has not complied with the requirements of Rule 14a-11;
- The nominee does not meet the requirements of Rule 14a-11;
- Any representation required to be included in the notice to the company is false or misleading in any material respect; or
- The company has received more nominees than it is required to include by proposed Rule 14a-11 and the nominating shareholder or group is not entitled to have its nominee included under the criteria proposed in Rule 14a-11(d)(3).[221]

The nominating shareholder or group would need to be notified of the company's determination not to include the shareholder nominee in sufficient time to consider the validity of any determination to exclude the nominee.[222] In this regard, we note the time-sensitive nature of Rule 14a-11 and the interpretive issues that may arise in applying the new rule. Accordingly, the rules that we are proposing, which set out the process by which a company would determine whether to include a shareholder nominee and notify the nominating shareholder or group, include a proposed procedure by which companies would send a notice to the Commission where the company intends not to include a shareholder nominee in its proxy materials, and could seek

221 See proposed Rule 14a-11(a).

222 See proposed Rule 14a-11(f).

staff advice – through a no-action request – with respect to that determination.[223] This procedure is modeled after the staff no-action process used in connection with shareholder proposals under Rule 14a-8.

In addition, we have proposed a process by which a nominating shareholder or group may remedy certain eligibility or procedural deficiencies in a nomination.[224] The various time deadlines set out in the proposed process were determined by considering the appropriate balance between companies' needs in meeting printing and filing deadlines for their shareholder meetings with shareholders' need for adequate time to satisfy the requirements of the rule. In doing so, we considered the timing requirements and deadlines in Rule 14a-8 when crafting the requirements and deadlines for Rule 14a-11; however, due to the potential complexity of the nomination process, we determined that it would be appropriate to provide additional time for the process. For example, once a nominating shareholder submits a nominee pursuant to Rule 14a-11, the company must consider the nominee submitted and make a determination as to whether to include the nominee or submit a no-action request pursuant to Rule 14a-11(f). A nominating shareholder will be afforded time to respond to the no-action request, and the staff will need time to process the request. In addition, a company may need time after receipt of the no-action response from the staff to finalize the proxy materials.

The following process would apply when a company receives a shareholder nomination under Rule 14a-11:

- Upon receipt of a shareholder's or shareholder group's notice of intent to nominate a

223 See proposed Rule 14a-11(f)(7) – (14). As is the case with regard to the Rule 14a-8 staff no-action process, we encourage companies and shareholders to attempt to resolve disputes independently. To the extent that a company and nominating shareholder or group are able to resolve an issue at any point during the staff no-action process, the company would withdraw its request for a no-action position from the staff.

224 See proposed Rule 14a-11(f)(3) – (6).

director or directors, the company would determine whether any of the eligibility requirements have not been satisfied by the nominating shareholder or group or nominee or nominees and whether the company will seek to exclude the shareholder nominee or nominees;[225]

- If the company determines that the eligibility requirements have not been satisfied by the nominating shareholder or group or nominee or nominees and it seeks to exclude the shareholder nominee or nominees, the company would notify in writing the nominating shareholder or group of this determination, at the business address, facsimile number and/or e-mail address provided in the nominating shareholder's or group's notice to the company. This notice must be postmarked or transmitted electronically no later than 14 calendar days after it receives the shareholder notice of intent to nominate. The company should provide this notice in a manner that provides evidence of receipt by the nominating shareholder or group;[226]
- The company's notice to the nominating shareholder or group that it has determined that the company may exclude a shareholder nominee or nominees would be required to include an explanation of the company's basis for determining that it may exclude the nominee or nominees;[227]

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225 See proposed Rule 14a-11(f)(1)-(3). See also proposed Rule 14a-11(a) detailing circumstances permitting exclusion of shareholder nominee or nominees. Where a company receives more than one nominee from an eligible nominating shareholder or group and some of those nominees are eligible to be placed in the company's proxy materials, the company's determination that one or more of the nominating shareholder's or group's nominees are not eligible will not affect the company's obligation to place the eligible nominee or nominees in its proxy materials.

226 See proposed Rule 14a-11(f)(3).

227 See proposed Rule 14a-11(f)(4).

- The nominating shareholder or group would have 14 calendar days after receipt of the written notice of deficiency to respond to that notice and correct any eligibility or procedural deficiencies identified in that notice. The nominating shareholder's or group's response must be postmarked, or transmitted electronically, no later than 14 calendar days from the date the shareholder received the company's notice. As with the company's notice, the nominating shareholder or group should provide the response in a manner that provides evidence of its receipt by the company;[228]
- Neither the composition of a nominating shareholder group nor a shareholder nominee could be changed as a means to correct a deficiency identified in the company's notice to the nominating shareholder or group – those matters would be required to remain as they were described in the notice to the company (we believe that to allow otherwise could serve to undermine the purpose of the notice deadline provided for in the rule); however, where a nominating shareholder or group inadvertently submits a number of nominees that exceeds the maximum number required to be included by the company, the nominating shareholder or group may specify which nominee or nominees are not to be included in the company's proxy materials;[229]
- If, upon review of the nominating shareholder's response, the company determines that the company still may exclude a shareholder nominee or nominees, after providing the requisite notice of and time for the nominating shareholder or group to

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228 See proposed Rule 14a-11(f)(5). We believe it is necessary to impose a time limit for a nominating shareholder's response to a notice of deficiency due to the potential time-sensitive nature of the nomination process and a company's preparation of its proxy materials for filing.

229 See proposed Rule 14a-11(f)(6).

remedy any eligibility or procedural deficiencies in the nomination, the company would be required to provide notice of the basis for its determination to the Commission no later than 80 calendar days before it files its definitive proxy statement and form of proxy with the Commission. The Commission staff could permit the company to make its submission later than 80 days before the company files its definitive proxy statement and form of proxy if the company demonstrates good cause for missing the deadline;[230]

- The company's notice to the Commission would include: (a) identification of the nominating shareholder or each member of the nominating shareholder group, as applicable; (b) the name of the nominee or nominees; (c) an explanation of the company's basis for determining that it may exclude the nominee or nominees; and (d) a supporting opinion of counsel when the company's basis for excluding a nominee or nominees relies on a matter of state law;[231]
- Unless otherwise provided in Rule 14a-11 (e.g., the nominating shareholder's or group's obligation to demonstrate that it responded to a company's notice of deficiency, where applicable, within 14 calendar days after receipt of the notice of deficiency), the burden would be on the company to demonstrate that it may exclude a nominee or nominees;[232]
- The company would be required to file its notice of its intent to exclude with the Commission and simultaneously provide a copy to the nominating shareholder or

230 See proposed Rule 14a-11(f)(7). This would be similar to the procedures the company must follow if it intends to exclude a shareholder proposal under Rule 14a-8. See Rule 14a-8(j). Given the similarities in the processes, we are proposing an 80-day deadline for Rule 14a-11(f).

231 See proposed Rule 14a-11(f)(8).

232 See proposed Rule 14a-11(f)(9).

each member of the nominating shareholder group;[233]

- The nominating shareholder or group could submit a response to the company's notice to the Commission. This response would be postmarked or transmitted electronically no later than 14 calendar days after the nominating shareholder's or group's receipt of the company's notice to the Commission. The nominating shareholder or group would be required to provide a copy of its response to the Commission simultaneously to the company;[234]
- The Commission staff would, at its discretion, provide an informal statement of its views (a no-action letter) to the company and the nominating shareholder or group;[235]
- The company would provide the nominating shareholder or group with notice, no later than 30 calendar days before it files its definitive proxy statement and form of proxy with the Commission, of whether it will include or exclude the shareholder nominee or nominees;[236]
- All materials submitted to the Commission in relation to Rule 14a-11(f) would be publicly available upon submission;[237] and

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233 See proposed Rule 14a-11(f)(10).

234 See proposed Rule 14a-11(f)(11). A nominating shareholder group may, but is not required to, respond to a company's notice to the staff.

235 See proposed Rule 14a-11(f)(12). The staff's no-action responses to submissions made pursuant to proposed Rule 14a-11(f) would reflect only informal views. The staff determinations reached in these no-action letters would not, and cannot, adjudicate the merits of a company's position with respect to exclusion of a shareholder nominee under Rule 14a-11. Accordingly, a discretionary staff determination would not preclude an interested person from pursuing a judicial determination regarding the application of Rule 14a-11.

236 See proposed Rule 14a-11(f)(13).

237 See proposed Rule 82a, which would state that materials filed with the Commission pursuant to proposed Rule 14a-11(f), written communications related thereto received from any person, and each related no-action letter or other written communication issued by the staff of the Commission, shall be made available to any person upon request for inspection or copying. This rule would be similar to Rule 82, which applies to no-action requests related to shareholder proposals.

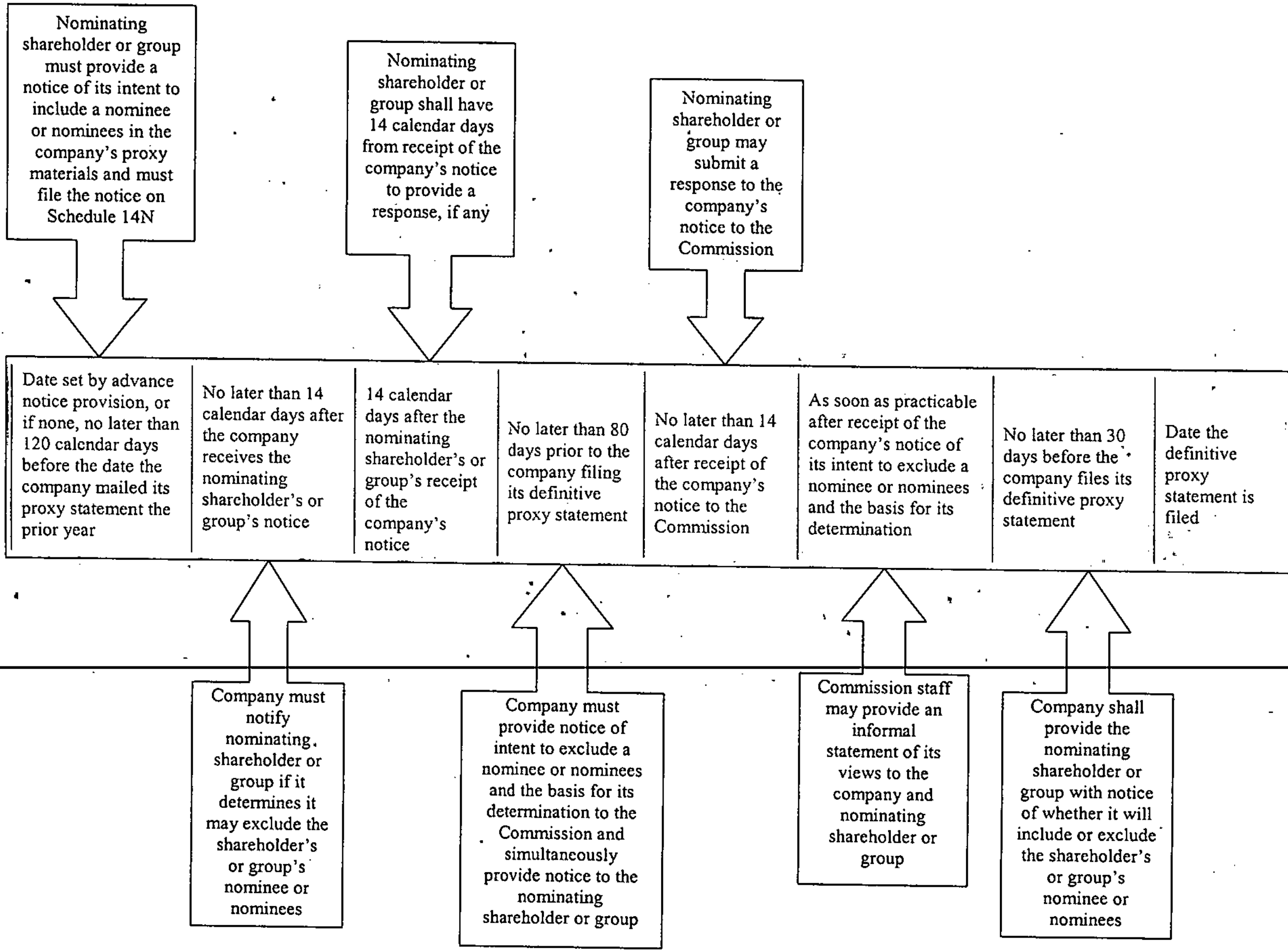
- The company or any nominating shareholder or group could request that the staff seek the Commission's views with respect to a determination of the staff under Rule 14a-11(f). The staff, upon such a request or on its own motion, would generally present questions to the Commission that involve matters of substantial importance and where the issues are novel or highly complex, although the granting of a request for an informal statement by the Commission is entirely within its discretion.[238]

The process generally would operate as follows:

Due Date	**Action Required**
Date set by company's advance notice provision or, in the absence of such a provision, 120 days before the anniversary of the date that the company mailed the prior year's proxy materials	Nominating shareholder or group must provide and file notice on Schedule 14N
Within 14 calendar days after the company's receipt of the nominating shareholder's or group's notice on Schedule 14N	Company must notify the nominating shareholder or group of any determination not to include the nominee or nominees
Within 14 calendar days after the nominating shareholder's or group's receipt of the company's deficiency notice	Nominating shareholder must respond to the company's deficiency notice
No later than 80 calendar days before the company files its definitive proxy statement and form of proxy with the Commission	Company must provide notice of its intent to exclude the nominating shareholder's or group's nominee or nominees and the basis for its determination to the Commission
Within 14 calendar days of the nominating shareholder's or group's receipt of the company's notice to the Commission	Nominating shareholder or group could submit a response to the company's notice to the Commission staff
As soon as practicable	Commission staff would, at its discretion, provide an informal statement of its views to the company and the nominating shareholder or group
No later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the Commission	Company must provide the nominating shareholder or group with notice of whether it will include or exclude the shareholder's nominee or nominees

238 See Commission Rules of Informal and Other Procedures Rule 202.1(d).

Rule 14a-11 deadlines



Request for Comment

G.1. Under proposed Rule 14a-11(a) a company would not be required to include a shareholder nominee where: (1) applicable state law or the company's governing documents prohibit the company's shareholders from nominating a candidate for director; (2) the nominee's candidacy or, if elected, board membership, would violate controlling state law, federal law or rules of a national securities exchange or national securities association; (3) the nominating shareholder or group does not meet the rule's eligibility requirements; (4) the nominating shareholder's or group's notice is deficient, (5) any representation in the nominating shareholder's or group's notice is false in any material respect, or (6) the nominee is not required to be included in the company's proxy materials due to the proposed limitation on the number of nominees required to be included. Proposed Rule 14a-11(f)(1) provides that the company shall determine whether any of these events have occurred. Will companies be able to make this determination? Why or why not?

G.2. As proposed, neither the composition of a nominating shareholder group nor a shareholder nominee could be changed as a means to correct a deficiency identified in the company's notice to the nominating shareholder or group. Should we permit the nominating shareholder group to change its composition to correct an identified deficiency, such as a failure of the group to meet the requisite ownership threshold? Should the nominating shareholder or group be permitted to submit a replacement shareholder nominee in the event that it is determined that a nominee does not meet the eligibility criteria?

G.3. As proposed, inclusion of a shareholder nominee in the company's proxy materials would not require the company to file a preliminary proxy statement provided that the company was otherwise qualified to file directly in definitive form. In this regard, the proposed rules make clear that inclusion of a shareholder nominee would not be deemed a "solicitation in opposition." Is this appropriate or should the inclusion of a nominee instead be viewed as a solicitation in opposition that would require a company to file its proxy statement in preliminary form? Should we view inclusion of a shareholder nominee as a solicitation in opposition for other purposes (e.g., expanded disclosure obligations)?

G.4. Under the proposal, companies would not be able to provide shareholders the option of voting for the company's slate of nominees as a whole. Should we allow companies to provide that option to shareholders? Are any other revisions to the form of proxy appropriate? Would a single ballot or "universal ballot" that includes both company nominees and shareholder nominees be confusing? Would a universal ballot result in logistical difficulties? If so, please specify.

G.5. Is it appropriate to require that the company include in its proxy statement a supporting statement by the nominating shareholder or group? If so, should this requirement be limited to instances where the company wishes to make a statement opposing the nominating shareholder's nominee or nominees or supporting company nominees? Is it appropriate to limit the nominating shareholder's or group's supporting statement to 500 words? If not, what limit, if any, is more appropriate (e.g., 250, 750, or 1000 words)? Should the limit be 500 words per nominee, or some other number (e.g., 250, 750, or 1000 words)?

Should the company's supporting statement be similarly limited? Why or why not?

G.6. Should the rule explicitly state that the nominating shareholder's or group's supporting statement may contain statements opposing the company's nominees? Would it be appropriate to require a company to include a nominating shareholder's or group's statement of opposition in its proxy materials?

G.7. Is the 14-day time period for the company to respond to a nominating shareholder's notice or for the nominating shareholder to respond to a company's notice of deficiency sufficient? Should the time period be longer (e.g., 20 days, 25 days, 30 days) or shorter (e.g., 10 days, 7 days, 5 days)? Should the rule explicitly set out the effect of a company providing the notice late (e.g., the company may not exclude the nominee) or of a shareholder responding to this notice late (e.g., the nominee may be excluded)?

G.8. Is the 80-day requirement for submission of the company's notice to the Commission sufficient? If not, should the requirement be increased (e.g., 90 days, 100 days, 120 days, or more) or decreased (e.g., 75 days, 60 days, or less)? Is the proposed provision under which the staff could permit the company to make its submission later than 80 days before filing its definitive proxy statement where the company demonstrates good cause appropriate? If not, why not? Should the rule more explicitly discuss the effect of such a late filing?

G.9. Is the 14-day time period for the nominating shareholder to respond to the receipt of a company's notice to the Commission of its intent to exclude the nominee sufficient? Should it be longer (e.g., 20 days, 25 days, 30 days) or shorter (e.g., 10 days, 7 days, 5 days)? Should the rule explicitly set out the effect of a shareholder responding to the company's notice late (e.g., the nominee may be excluded)?

G.10. Is the requirement that the company notify the nominating shareholder or group of whether it will include or exclude the nominating shareholder's or group's nominee or nominees no later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the Commission appropriate and workable? If not, what should the deadline be (e.g., 40 calendar days before filing definitive proxy materials, 35 days before filing definitive proxy materials, 25 calendar days before filing definitive proxy materials, 20 calendar days before filing definitive proxy materials)? Should the rule explicitly set out the effect of a company sending this notice late?

G.11. Would the timing requirements overall allow a company to comply with the requirements of e-proxy?

G.12. Do the proposed timing requirements, in the aggregate, allow sufficient time for the informal staff review process? How far in advance of filing definitive proxy materials do companies typically begin printing those materials? If the proposed timing requirements do not allow sufficient time for the informal staff review process, please tell us specifically which timing requirements pose a problem and suggest a specific alternative time that would be sufficient.

G.13. What should happen if one of the deadlines specified in the proposed process in Rule 14a-11(f) falls on a Saturday, Sunday, or federal holiday? Should the deadline be counted from the preceding or succeeding federal work day?

G.14. Should the informal staff review process be the same for reporting companies (other than registered investment companies), registered investment companies, and business development companies? Should there be unique procedures for different types of entities? If so, what is unique to a particular type of entity that would require a unique process?

G.15. Should there be a method for a company to obtain follow-up information after a nominating shareholder or group submits an initial response to the company's notice of determination? If so, should that follow-up method have similar time frames as those related to the initial request and response? What adjustments to timing might be required for the nominating shareholder or group to respond to any such follow-up request?

G.16. The proposed requirement for a legal opinion regarding state law is modeled on the requirement in Rule 14a-8. Is such a requirement necessary and appropriate in the context of proposed Rule 14a-11? Should it be changed in any way (e.g., should it be revised to require a legal opinion regarding foreign law for those instances where there may be a conflict with a company's country of incorporation where the company is organized in a non-U.S. jurisdiction but does not meet the definition of foreign private issuer)?

G.17. What process would be appropriate for addressing disputes concerning a company's determination? Is the proposed staff review process an appropriate means to address disputes concerning the company's determination? If not, by what other means should a company's determination be subject to review? Exclusively by the courts? Are there other processes we should consider?

G.18. In the absence of a staff review process, what would be the potential litigation cost associated with the resolution of disputes concerning company determinations? Would shareholder meetings be delayed due to such litigation or threat of litigation?

G.19. Are there certain types of company determinations that should or should not be subject to the staff review process (e.g., whether a nominating shareholder or group meets the required ownership threshold)? Please provide specific examples in your response.

G.20. How should we address the situation where a nominating shareholder qualifies, provides its notice, and submits all of the nominees a company is required to include, then becomes ineligible under the rule? Under what circumstances should a second shareholder or group be able to nominate directors? If the second nominating shareholder or group provided a notice before the first shareholder became ineligible? Should it matter whether a company had notified the second nominating shareholder or group that it intended to exclude their nominee or nominees?

8. Application of the Other Proxy Rules to Solicitations By the Nominating Shareholder or Group

As proposed, Rule 14a-11 would permit shareholders to aggregate their securities with other shareholders in order to meet the applicable minimum ownership threshold to nominate a director. Accordingly, we anticipate that shareholders would, in many instances, engage in communications with other shareholders in an effort to form a nominating shareholder group that would be deemed solicitations under the proxy rules. In 2003 we proposed an exemption from certain of the proxy rules to enable shareholders to communicate for the limited purpose of forming a nominating shareholder group without filing and disseminating a proxy statement. To qualify for the exemption, shareholders would have had two options. The communications would either have been made to a limited number of shareholders or, in the alternative, to an unlimited number of shareholders, provided that the communication was limited in content and filed with the Commission. Some commenters supported adoption of limited exemptions,[239] while others stated that the exemptions were unnecessary or duplicative of existing exemptions from the proxy rules. In particular, commenters expressed concerns about the exemption for solicitations not involving more than 30 persons in connection with the formation of a nominating security holder group.[240] These commenters believed the 30-person exemption might be used for undeclared control purposes and believed that there was no reason to replace the 10-person exemption set forth in Exchange Act Rule 14a-2(b)(2), which permits limited testing of the waters before application of the notice and filing requirements of the proxy rules.[241]

After considering further the need for an exemption, and in particular the comments received on the 2003 Proposal, we are proposing an exemption from the proxy rules for communications made in connection with using proposed Rule 14a-11[242] that are limited in

[239] See 2003 Summary of Comments; see also comment letters from CalPERS; CIR; ICI; and Clauss & Wolf.

[240] See 2003 Summary of Comments; see also comment letters from ABA; NYC Bar; and Sullivan.

[241] Id.

[242] The proposed exemption would not apply to solicitations made when seeking to have a nominee included in a company's proxy materials pursuant to a procedure specified in the company's governing documents. In this instance, companies and/or shareholders would have determined the parameters of the shareholder's or group's access to the company's proxy materials. Given the range of possible criteria companies and/or shareholders could establish for nominations, we are not proposing to extend the exemption to those circumstances. A shareholder would need to determine whether one of the existing exemptions applies to their solicitation conducted in connection with a nomination made pursuant to a company's governing documents. The proposed exemption also would not apply to nominations made pursuant to applicable state law provisions, again because state law could establish any number of possible criteria for nominations.

content and filed with the Commission.[243] We believe this limited exemption will facilitate shareholders' use of proposed Rule 14a-11 and remove concerns shareholders seeking to use the rule may have regarding certain communications with other shareholders regarding their intent to submit a nomination pursuant to the rule. The exemption would not apply to oral communications because such communications could not easily satisfy the filing requirement, which we believe is important in determining compliance with the content restriction in the proposed exemption. As proposed, Exchange Act Rules 14a-3 to 14a-6 (other than paragraphs 14a-6(g) and 14a-6(p)), 14a-8, 14a-10, and 14a-12 to 14a-15 would not apply to any solicitation by or on behalf of any shareholder in connection with the formation of a nominating shareholder group, provided that:

- Each written communication includes no more than:
  - A statement of the shareholder's intent to form a nominating shareholder group in order to nominate a director under the proposed rule;
  - Identification of, and a brief statement regarding, the potential nominee or nominees or, where no nominee or nominees have been identified, the characteristics of the nominee or nominees that the shareholder intends to nominate, if any;
  - The percentage of securities that the shareholder beneficially owns or the aggregate percentage owned by any group to which the shareholder belongs; and
  - The means by which shareholders may contact the soliciting party;[244] and
- Any written soliciting material published, sent or given to shareholders in accordance

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[243] See proposed Rule 14a-2(b)(7)(i).

[244] See id.

with the terms of this provision is filed with the Commission by the nominating shareholder, under the company's Exchange Act file number (or in the case of a registered investment company, under the company's Investment Company Act file number), no later than the date the material is first published, sent or given to shareholders. The soliciting material would be required to include a cover page in the form set forth in Schedule 14A, with the appropriate box on the cover page marked.[245]

In this regard, we note that shareholders also would have the option to structure their solicitations, whether written or oral, to comply with an existing exemption from the proxy rules, including the exemption for solicitations of no more than 10 shareholders,[246] and the exemption for certain communications that take place in an electronic shareholder forum.[247]

Both the nominating shareholder or group and the company may wish to solicit in favor of their nominees for director by various means, including orally, by U.S. mail, electronic mail, and website postings. While the company ultimately would file a proxy statement and therefore could rely on the existing proxy rules to solicit outside the proxy statement,[248] shareholders could be limited in their soliciting activities under the current proxy rules. Accordingly, we are proposing a new exemption to the proxy rules providing that solicitations by or on behalf of a nominating shareholder or group in support of a nominee included in the company's proxy statement and form of proxy in accordance with the proposed rule, would not be subject to

245 See proposed Rule 14a-2(b)(7)(ii). We note that written communications include electronic communications, such as e-mails and website postings.

246 Exchange Act Rule 14a-2(b)(2).

247 Exchange Act Rule 14a-2(b)(6).

248 See Exchange Act Rule 14a-12.

Exchange Act Rules 14a-3 to 14a-6 (other than paragraphs 14a-6(g) and 14a-6(p)), 14a-8, 14a-10, and 14a-12 to 14a-15, provided that:

- The soliciting party does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as proxy for a shareholder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization;[249]
- Each written communication includes:
  - The identity of the nominating shareholder or group and a description of his or her direct or indirect interests, by security holdings or otherwise;
  - A prominent legend in clear, plain language advising shareholders that a shareholder nominee is or will be included in the company's proxy statement and to read the company's proxy statement when it becomes available because it includes important information. The legend also must explain to shareholders that they can find the proxy statement, other soliciting material and any other relevant documents, at no charge on the Commission's website; and
  - Any soliciting material published, sent or given to shareholders in accordance with this paragraph must be filed by the nominating shareholder or group with the Commission, under the company's Exchange Act file number, no later than the date the material is first published, sent or given to shareholders.[250] Three copies of the material would at the same time be filed with, or mailed for filing to, each

249 See proposed Rule 14a-2(b)(8)(i).

250 For a registered investment company, the filing would be made under the subject company's Investment Company Act file number.

national securities exchange upon which any class of securities of the company is listed and registered. The soliciting material would be required to include a cover page in the form set forth in Schedule 14A, with the appropriate box on the cover page marked.[251]

Request for Comment

H.1. Should the Commission provide a new exemption for soliciting activities undertaken by shareholders seeking to form a nominating shareholder group pursuant to Rule 14a-11? If so, is the proposed exemption appropriate? If not, why not? What specific changes to the exemption would be appropriate? Should the rule require that a shareholder meet any of the requirements of Rule 14a-11 to rely on the exemption (e.g., have held the securities they seek to aggregate for the required holding period)? Is it appropriate to require filing with the Commission on the date of first use, as proposed?

H.2. Should the Commission expand the proposed exemption for soliciting activities undertaken by shareholders seeking to form a nominating shareholder group pursuant to Rule 14a-11 to apply also to oral communications? If so, what amendments to the proposed exemption would be necessary?

H.3. What requirements should apply to soliciting activities conducted by a nominating shareholder or group? In particular, what filing requirements and specific parameters should apply to any such solicitations? For example, we have proposed a limited content exemption for certain solicitations by shareholders seeking to form a nominating shareholder group. Is this content-based limitation appropriate? Should shareholders, for example, also be permitted to explain their

[251] See proposed Rule 14a-2(b)(8)(iii).

reasons for forming a nominating shareholder group? Should shareholders be permitted to identify any potential nominee, as proposed, and why that person was chosen? If not, what, if any, limitations would be more appropriate? For example, should an exemption for certain solicitations by shareholders seeking to form a nominating shareholder group be limited to no more than a specified number of shareholders, but not limited in content (e.g., fewer than 10 shareholders, 10 shareholders, 20 shareholders, 30 shareholders, 40 shareholders, more than 40 shareholders)?

H.4. Should communications made to form a group be permitted to identify a possible or proposed nominee or nominees, as proposed?

H.5. Is the requirement that the nominating shareholder or group provide a description of his or her direct or indirect interests, by security holdings or otherwise, sufficiently clear? Do we need to provide additional guidance as to what interests would be required to be disclosed?

H.6. Should all written soliciting materials be filed with the Commission on the date of first use? If not, how much later should they be filed (e.g., two business days after first use; four business days after first use, some other date)? Should the materials be filed before the date of first use?

H.7. Should we provide a similar exemption for soliciting activities undertaken by shareholders seeking to form a nominating shareholder group other than in connection with Rule 14a-11 (e.g., in connection with a nomination under applicable state law provisions or a company's governing documents)?

H.8. Should solicitations by or on behalf of a nominating shareholder or group in support of a nominee included in the company's proxy statement and form of proxy pursuant to Rule 14a-11 be exempt? Why or why not?

H.9. Should the exemption be conditioned on the soliciting materials including a legend about the shareholder's nominee being included in company proxy materials and a statement about where shareholders can find the proxy statement, soliciting material, and other relevant documents, as proposed? Should any other conditions be included in the exemption?

H.10. Should a nominating shareholder or group be required to file any soliciting material published, sent or given to shareholders in accordance with the exemption no later than the date the material is first published, sent or given to shareholders, as proposed?

H.11. Should solicitations by the nominating shareholder or group be limited or prohibited? If so, why?

H.12. Should we provide a similar exemption for soliciting activities undertaken by a nominating shareholder or group in support of their nominee or nominees, where those nominees are included in a company's proxy materials pursuant to applicable state law provisions or a company's governing documents?

C. Amendments to Exchange Act Rule 14a-8(i)(8)

1. Background

Currently, Rule 14a-8(i)(8) allows a company to exclude from its proxy statement a shareholder proposal that relates to a nomination or an election for membership on the company's board of directors or a procedure for such nomination or election. As noted, the

Commission amended this provision in 2007 to expressly permit the exclusion of a proposal that would result in an immediate election contest or would set up a process for shareholders to conduct an election contest in the future by requiring the company to include shareholders' director nominees in the company's proxy materials for subsequent meetings. The Commission adopted this proposal in December 2007 to provide certainty to companies and shareholders in light of the AFSCME decision.[252] In the adopting release, the Commission noted the many disclosures that are required for election contests that would not have been provided for in Rule 14a-8.[253] In this regard, several Commission rules, including Exchange Act Rule 14a-12, regulate contested proxy solicitations to assure that investors receive disclosure to enable them to make informed voting decisions in elections. The requirements to provide these disclosures to shareholders from whom proxy authority is sought are grounded in Rule 14a-3, which requires that any party conducting a proxy solicitation file with the Commission, and furnish to each person solicited, a proxy statement containing the information in Schedule 14A. Items 4(b) and 5(b) of Schedule 14A require numerous specified disclosures if the solicitation is subject to Rule 14a-12(c), and Item 7 of Schedule 14A also requires important specified disclosures for any director nominee. Finally, all of these disclosures are covered by the prohibition on the making of a solicitation containing false or misleading statements or omissions that is found in Rule 14a-9.

The Commission's action in 2007 provided certainty to shareholders and companies regarding the application of Rule 14a-8(i)(8) in the wake of the AFSCME decision that had caused confusion about what disclosure and liability rules might apply to any resulting election

252 See Election of Directors Adopting Release. See also footnotes 88 and 89, above.

253 See Election of Directors Adopting Release.

contest. As noted in Section II., at that time, the Commission did not take any action with respect to the alternative proposal published in 2007.[254] Since that time, we have continued to consider whether the proxy process can be improved and we have concluded that the proxy rules, including Rule 14a-8(i)(8), can be amended to further facilitate shareholders' rights to nominate directors and promote fair corporate suffrage, while still providing appropriate disclosure and liability protections.

2. Proposed Amendment to Rule 14a-8(i)(8)

We are proposing an amendment to Rule 14a-8(i)(8), the election exclusion, to enable shareholders, under certain circumstances, to require companies to include in company proxy materials proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11.[255] The proposal would have to meet the procedural requirements of Rule 14a-8 and not be subject to one of the substantive exclusions other than the election exclusion (e.g., the proposal could be excluded if the

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254 Under the alternative proposal, Rule 14a-8(i)(8) would have been amended with certain conditions to permit a qualifying shareholder who makes full disclosure in connection with a bylaw proposal relating to director nominations procedures to have that proposal included in a company's proxy materials.

255 A proposal would continue to be subject to exclusion under Rule 14a-8(i)(2) if its implementation would cause the company to violate any state, federal, or foreign law to which it is subject, or under Rule 14a-8(i)(3), if the proposal or supporting statement was contrary to any of the Commission's proxy rules. As proposed to be amended, Rule 14a-8(i)(8) would allow shareholders to propose additional means, other than Rule 14a-11, for disclosure of shareholder nominees in company proxy materials. Therefore, a shareholder proposal that seeks to provide an additional means for including shareholder nominees in the company's proxy materials pursuant to the company's governing documents would not be deemed to conflict with Rule 14a-11 simply because it would establish different eligibility thresholds or require more extensive disclosures about a nominee or nominating shareholder than would be required under Rule 14a-11. A shareholder proposal would conflict with Rule 14a-11, however, to the extent that the proposal would purport to prevent a shareholder or shareholder group that met the requirements of proposed Rule 14a-11 from having their nominee for director included in the company's proxy materials. A shareholder proposal would also be subject to exclusion under Rule 14a-8(i)(2) or Rule 14a-8(i)(3) to the extent that it would affirmatively excuse nominating shareholders or their nominees from compliance with the liability provisions of Rule 14a-9(c) or the proposed Rule 14a-19 disclosure requirements applicable to shareholder nominations submitted pursuant to an applicable state law provision or a company's governing documents.

shareholder proponent did not meet the ownership threshold under Rule 14a-8).[256]

As proposed, except as provided below in the codification of staff positions, revised Rule 14a-8(i)(8) would not restrict the types of amendments that a shareholder could propose to a company's governing documents to address the company's provisions regarding nomination procedures or disclosures related to shareholder nominations, although any such proposals that conflict with proposed Rule 14a-11 or state law could be excluded.[257] We recognize that the proposed amendments to Rule 14a-8(i)(8) could result in shareholders proposing amendments that would establish procedures for nominating directors and disclosures related to such nominations that require a different ownership threshold, holding period, or other qualifications or representations than those proposed in Rule 14a-11. The amendments proposed by shareholders through Rule 14a-8 would be permitted unless they would conflict with Rule 14a-11 (i.e., proposals that would preclude nominations by shareholders who would qualify under proposed Rule 14a-11 to have their nominee for director included in the company's proxy materials) or applicable state law. We considered whether this would create confusion or lack of certainty for companies and their shareholders, but believe that this possibility is outweighed by the importance of facilitating shareholders' ability to exercise their rights to determine their own additional shareholder nomination proxy disclosure and related procedures.

3. Disclosure Requirements

We are not proposing any new disclosure requirements for a shareholder that submits a

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256 Currently, Rule 14a-8 requires that a shareholder proponent have continuously held at least $2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting for a period of one year prior to submitting the proposal. See Rule 14a-8(b). These requirements would remain the same. The proposal may be subject to exclusion if the procedural requirements of the rule are not met or it falls within one of the other substantive bases for exclusion included in Rule 14a-8.

257 In this regard, the proposed revision to Rule 14a-8(i)(8) would not make a distinction between binding and non-binding proposals.

proposal that would amend, or that requests an amendment to, a company's governing documents to address the company's nomination procedures or procedures for inclusion of shareholder nominees in company proxy materials or disclosures related to those shareholder provisions.[258] New disclosures would not be required from a shareholder simply submitting such a proposal to amend, or requesting an amendment to, a company's governing documents because the Commission believes that a shareholder may simply want to amend the company's procedures for nominating directors, but may not intend to nominate any particular individual.[259]

As noted, the proposed amendments to Rule 14a-8(i)(8) could result in shareholders proposing amendments that would establish procedures for nominating directors and disclosures related to such nominations that require a different ownership threshold, holding period, or other qualifications or representations than those proposed in Rule 14a-11. In addition, a state could set forth in its corporate code[260] or a company may choose to amend its governing documents, to provide for nomination or disclosure rights in addition to those provided pursuant to Rule 14a-11 (e.g., a company could choose to provide a right for shareholders to have their nominees disclosed in the company's proxy materials regardless of ownership – in that instance, the company's provision would apply for certain shareholders who would not otherwise have their nominees included in the company's proxy materials pursuant to Rule 14a-11). Accordingly, we are proposing amendments to our proxy rules to address the disclosure requirements when a

258 Shareholders submitting a proposal to amend a company's governing documents to address nomination procedures for inclusion of shareholder nominees in company proxy materials or disclosures related those shareholder nomination provisions would be subject to the rule's current requirements. See footnote 256, above.

259 This approach is different from the disclosure requirements the Commission proposed in the Shareholder Proposals Release in 2007; however, it is consistent with the overall requirements relating to the submission of shareholder proposals – generally, shareholder proponents are not required to provide any type of disclosure along with their proposal.

260 See discussion of North Dakota Publicly Traded Corporations Act, N.D. Cent. Code §10-35 et al., in footnote 70, above.

nomination is made pursuant to such a provision.[261] We believe the proposed additional disclosure requirements are necessary to provide shareholders with full and fair disclosure of information that is material when a choice among directors to be elected is presented.

Proposed Rule 14a-19 would apply to a shareholder nomination for director for inclusion in the company's proxy materials made pursuant to procedures established pursuant to state law or by a company's governing documents. The proposed rule would require a nominating shareholder or group to include in its shareholder notice on Schedule 14N (which also would be filed with the Commission on the date provided to the company) disclosures about the nominating shareholder or group and their nominee that are similar to what would be required in an election contest.[262]

Specifically, the shareholder notice on Schedule 14N would be required to include:

- A statement from the nominee that the nominee consents to be named in the company's proxy statement and to serve on the board if elected, for inclusion in the company's proxy statement;[263]
- Disclosure about the nominee complying with the requirements of Item 4(b), Item 5(b), and Items 7(a), (b) and (c) and, for investment companies, Item 22(b) of Exchange Act Schedule 14A, for inclusion in the company's proxy statement;[264]

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261 See proposed Rule 14a-19.

262 See proposed Rule 14a-19.

263 See proposed Rule 14a-19(a).

264 See proposed Rule 14a-19(b). This information would identify the nominee, describe certain legal proceedings, if any, related to the nominee, and describe certain of the nominee's transactions and relationships with the company. See Items 7(a), (b), and (c) of Schedule 14A. This information also would include biographical information and information concerning interests of the nominee. See Item 5(b) of Schedule 14A. With respect to a nominee for director of an investment company, the disclosure would include certain basic information about the nominee and any arrangement or understanding between the nominee and any other person pursuant to which he was selected as a nominee; information about the positions, interests, and transactions and relationships of the nominee and his immediate family members

- Disclosure about the nominating shareholder or members of a nominating shareholder group consistent with the disclosure currently required pursuant to Item 4(b) and Item 5(b) of Schedule 14A;[265]
- Disclosure about whether the nominating shareholder or member of a nominating shareholder group has been involved in any legal proceeding during the past five years, as specified in Item 401(f) of Regulation S-K. Disclosure pursuant to this section need not be provided if provided in response to Items 4(b) and 5(b) of Schedule 14A;[266]
- The following disclosure regarding the nature and extent of the relationships between the nominating shareholder or group and nominee and the company or any affiliate of the company:
  - Any material direct or indirect interest in any contract or agreement between the nominating shareholder or group or the nominee and the company or any affiliate of the company (including any employment agreement, collective bargaining agreement, or consulting agreement);
  - Any material pending or threatened litigation in which the nominating shareholder or group or nominee is a party or a material participant, and that involves the company, any of its officers or directors, or any affiliate of the company; and
  - Any other material relationship between the nominating shareholder or group or

with the company and persons related to the company; information about the amount of equity securities of funds in a fund complex owned by the nominee; and information describing certain legal proceedings related to the nominee, including legal proceedings in which the nominee is a party adverse to, or has a material interest adverse to, the company or any of its affiliated persons. See paragraph (b) of Item 22 of Schedule 14A.

265 See proposed Rule 14a-19(c).

266 See proposed Rule 14a-19(d).

the nominee and the company or any affiliate of the company not otherwise disclosed;[267] and

- Disclosure of any website address on which the nominating shareholder or group may publish soliciting materials.[268]

These disclosures would then be included in the company's proxy materials pursuant to proposed new Item 7(f) of Schedule 14A. Proposed Item 22(b)(19) of Schedule 14A would require investment companies to include in their proxy materials disclosures from the nominating shareholder or shareholder group with regard to the nominee and nominating shareholder or shareholder group that are similar to those required for reporting companies (other than registered investment companies).

In addition, the nominating shareholder or group would be required to identify the shareholder or group making the nomination and the amount of their ownership in the company on Schedule 14N. The filing would be required to include, among other disclosures:

- The name and address of the nominating shareholder or each member of the nominating shareholder group; and
- Information regarding the aggregate number and percentage of the securities entitled to be voted, including the amount beneficially owned and the number of shares over which the nominating shareholder or each member of the nominating shareholder group has or shares voting or disposition power.

We believe that these disclosures would assist shareholders in making an informed voting decision with regard to any nominee or nominees put forth by the nominating shareholder or group, in that the disclosures would enable shareholders to gauge the nominating shareholder's

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267 See proposed Rule 14a-19(e).

268 See proposed Rule 14a-19(f).

or group's interest in the company. Depending on the requirements of the state law provisions or the company's governing documents, these disclosures also may be important to the company in determining whether the nominating shareholder or group meets any ownership threshold, where applicable. The nominating shareholder or group would be liable for any false or misleading statements in these disclosures pursuant to proposed new paragraph (c) of Rule 14a-9.[269]

The disclosure requirements we are proposing differ from the approach proposed in the alternative proposal in 2007.[270] In that release, the Commission proposed requiring significant new disclosures from shareholder proponents of bylaw proposals to be made on Schedule 13G. Commenters expressed concern that the proposed disclosure requirements were too onerous and should not be required to submit a shareholder proposal.[271] Upon further consideration, we believe that it is appropriate to allow the submission of proposals to amend, or that request an amendment to, a company's governing documents to address the company's nomination procedures or disclosures related to shareholder nominations without requiring extensive disclosure regarding the shareholder proponent. As noted above, we acknowledge that some shareholders may simply desire to amend or establish the company's procedure for nominating directors, but may not contemplate nominating any particular individual. In addition, we do not

269 See proposed Rule 14a-9(c).

270 See Shareholder Proposals Proposing Release.

271 See, e.g., comment letters from American Federation of Labor and Congress of Industrial Organizations (August 2, 2007) ("AFL-CIO 2007"); Amalgamated Bank LongView Funds (October 2, 2007); Australian Council of Super-Investors (October 2, 2007); Robert Balopole, CFA, President, Balopole Investment Management Corp.; CalPERS 2007; California State Teachers' Retirement System (November 16, 2007) ("CalSTERS 2007"); Council of Institutional Investors (September 18, 2007) ("CII"); Public Employees' Retirement Association of Colorado (October 1, 2007) ("CO Retirement"); McRitchie 2007; F&C Management Limited (October 1, 2007); State Board of Administration of Florida (October 3, 2007); ICGN Shareholder Rights Committee (October 2, 2007); State Universities Retirement System of Illinois (October 1, 2007); Investment Management Association (October 2, 20007); KLD Research & Analytics, Inc. (October 2, 2007); Brett McDonnell (September 27, 2007); Treasurer, State of North Carolina (October 2, 2007); Ohio Public Employees Retirement System (October 2, 2007); SEIU; International Brotherhood of Teamsters (August 30, 2007); UK Local Authority Pension Fund Forum (October 2, 2007); and United Church Foundation (September 27, 2007).

require additional disclosure from proponents of other types of shareholder proposals submitted under Rule 14a-8. We are soliciting comment, however, on whether additional disclosure from a shareholder submitting a bylaw proposal would be appropriate.

4. Codification of Prior Staff Interpretations

Although we are proposing to amend Rule 14a-8(i)(8), we continue to believe that under certain circumstances companies should have the right to exclude proposals related to particular elections and nominations for director from company proxy materials where those proposals could result in an election contest between company and shareholder nominees without the important protections provided by the disclosure and liability provisions otherwise provided for in the proxy rules. Rule 14a-8(i)(8) should not, however, be read so broadly such that the provision could be used to permit the exclusion of proposals regarding the qualifications of directors, shareholder voting procedures, board nomination procedures and other election matters of importance to shareholders that would not directly result in an election contest between management and shareholder nominees, and that do not present significant conflicts with the Commission's other proxy rules. Therefore, we propose to amend Rule 14a-8(i)(8) to codify certain prior staff interpretations with respect to the type of proposals that would continue to be excludable.[272]

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[272] In limited circumstances, the staff may permit proponents to make minor revisions to a proposal to cure a deficiency under Rule 14a-8. Under existing staff interpretations, the staff may permit revisions to proposals that would disqualify board nominees from standing for election at the upcoming meeting or that would remove a director from office before his or her term expires. In contrast, where the proposal or supporting statement questions the competence or business judgment of one or more directors that will stand for reelection at the upcoming meeting, the staff will generally not permit the proponent to revise the proposal to cure such a deficiency. The proposed codification of existing staff interpretations under Rule 14a-8(i)(8) is not intended to alter the staff's historical approach (see Staff Legal Bulletin No. 14 (July 13, 2001)) to permitting revisions to cure deficiencies under Rule 14a-8(i)(8).

A company would be permitted to exclude a proposal under Rule 14a-8(i)(8) if it:

- Would disqualify a nominee who is standing for election;[273]
- Would remove a director from office before his or her term expired;[274]
- Questions the competence, business judgment, or character of one or more nominees or directors;[275]
- Nominates a specific individual for election to the board of directors,[276] other than pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents; or
- Otherwise could affect the outcome of the upcoming election of directors.

With regard to the language "otherwise could affect the outcome of the upcoming election of directors," we are seeking to address the fact that the proposed new language of the exclusion specifically addresses the particular types of proposals that we have traditionally seen in this area and that we believe are clearly excludable under the policy underlying the rule. With the broader proposed language, we are seeking to address new proposals that may be developed over time that are comparable to the four specified categories and would undermine the purpose of the exclusion. This broader language is generally consistent with the language of the other bases for exclusion in Rule 14a-8.[277]

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273 See, e.g., Dollar Tree Stores, Inc. (March 7, 2008) and Waddell and Reed Financial, Inc. (February 23, 2001).

274 See, e.g., TVI Corporation (April 2, 2008) and First Energy Corp. (March 17, 2003).

275 See, e.g., Exxon Mobil Corporation (March 20, 2002) and AT&T Corp. (February 12, 2001).

276 See, e.g., N-Viro International Corporation (March 8, 2007) and Dow Jones & Company, Inc. (January 31, 1996).

277 See, e.g., Rule 14a-8(i)(7) addressing proposals that "deal[] with a matter relating to the company's ordinary business operations," and Rule 14a-8(i)(10) addressing proposals that have been "substantially implemented" already by the company.

Request for Comment

I.1. Should the Commission amend Rule 14a-8(i)(8), as proposed, to allow proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11? Should the rule instead require such proposals to be included only in particular circumstances? For example, should inclusion of such proposals be required only when a company already has a provision in place regarding the inclusion of shareholder director nominees, or disclosure about those nominees, in company proxy materials?

I.2. Should the Commission amend Rule 14a-8(i)(8) to allow proposals that would amend, or that request an amendment to, a company's governing documents to provide for or prohibit inclusion of shareholder nominees for director in company proxy materials? Should such an amendment operate separately from proposed Rule 14a-11? Should such an amendment be adopted regardless of whether proposed Rule 14a-11 is adopted? If so, under what circumstances should such proposals be permitted? For example, should shareholder proposals be included where they propose or request amendments to provisions in the company's governing documents to address the inclusion of shareholder nominees for director in the company's proxy materials so long as such amendments are not prohibited under state law? Should such proposals instead be included only if the law of the company's state of incorporation explicitly authorizes a company to have a provision in its governing documents that permits the inclusion of shareholder nominees in the company's proxy materials? Should such proposals instead be limited under Rule 14a-8 to instances when a company already has a provision in its governing documents that addresses the inclusion of shareholder nominees in the company's proxy materials?

I.3. Should companies be required to include non-binding proposals regarding procedures to include shareholder nominees for director in company proxy materials, as proposed? Should the requirements instead be limited to binding proposals?

I.4. Should proposed Rule 14a-8(i)(8) operate independently, even if proposed Rule 14a-11 were not adopted or not in effect? Why or why not? Are there changes or additions to Rule 14a-8(i)(8) as proposed that can or should be made so that it would be better suited or able to operate independently? Please give specific recommendations.

I.5. Is it sufficiently clear that shareholders would have the ability under proposed Rule 14a-8(i)(8) to propose nomination procedures that are different from proposed Rule 14a-11 provided that such procedures would serve as additional methods of accessing the proxy and would not preclude a shareholder or group or shareholders who satisfied the Rule 14a-11 requirements from using the Rule 14a-11 method? If not, what clarification should be made?

I.6. As proposed, a shareholder proposal under Rule 14a-8(i)(8) would supplement proposed Rule 14a-11, not replace it. Should shareholders instead be permitted under Rule 14a-8(i)(8) to propose governing document amendments that would conflict with proposed Rule 14a-11? Please explain how and why. Are there different limitations on such proposals that we should consider? If so, what are they?

I.7. What would be the costs to companies if Rule 14a-8(i)(8) were amended as proposed?

I.8. Rule 14a-8 currently requires that a shareholder proponent have held continuously at least $2,000 in market value or 1% of the company's securities entitled to be voted on the proposal at the meeting for at least one year as of the date of submission of the proposal. Are these thresholds appropriate? Should the minimum ownership threshold be higher than $2,000 in market value of the company's securities entitled to be voted on the proposal? Should the minimum ownership threshold be periodically adjusted for inflation? Should these eligibility determinations be made on the date of submission of the proposal, as proposed? If not, what date should be used?

I.9. Are there alternative thresholds that would be more appropriate for purposes of submitting a proposal under Rule 14a-8(i)(8) (e.g., 1%, 2%, 3%, 4%, or 5% of the company's securities)? If so, please explain.

I.10. We are not proposing any requirements to disclose information about a shareholder proponent who submits a proposal that seeks to establish a procedure for nominating one or more directors. Should the rule require disclosure about a shareholder proponent who submits a proposal that relates to procedures for nominating directors but does not nominate a director? If so, what disclosures would be appropriate? The disclosures required in a contested election? Disclosure about the proponent's motives and interactions with the company leading up to the proposal? With respect to requiring disclosure from shareholder proponents, should our rules make a distinction between a proposal relating to a procedure for nominating directors and other proposals on other unrelated subjects?

I.11. Should disclosure consistent with that required in an election contest as defined in Rule 14a-12 be required for shareholder nominations pursuant to applicable state law provisions or a company's governing documents, as proposed? Why or why not? What additional disclosures should be required, if any? Which of the proposed disclosure requirements, if any, should be deleted or revised?

I.12. As proposed, the disclosures required for a nomination pursuant to an applicable state law provision or a company's governing documents do not include all of the disclosures that would be required for a Rule 14a-11 nomination. Would any of the additional disclosures required under Rule 14a-11 be appropriate with regard to a nomination under an applicable state law provision or a company's governing documents? If so, which ones in particular? Should a nominating shareholder or group submitting a nomination pursuant to an applicable state law provision or a company's governing documents be required to provide a statement regarding the nominating shareholder's or group's intent to continue to hold the securities through the date of the meeting? Should the rules require a statement regarding the nominating shareholder's or group's intent with respect to continued ownership of the shares after the election?

I.13. Should Rule 14a-8(i)(8) be amended to codify the prior staff interpretations of the election exclusion, as proposed? Why or why not? Does the proposed new language best describe the category of proposals that companies should be permitted to exclude? Are there other examples or categories or proposals that should be included in the revised rule (that do not restrict the ability of shareholders to propose nomination procedures)?

I.14. Is the proposed new language of Rule 14a-8(i)(8) sufficiently clear? In particular, would the proposed language "or otherwise could affect the outcome of the upcoming election of directors," achieve its goal? Would there be unintended consequences of revising the language as proposed?

D. Other Rule Changes

1. Beneficial Ownership Reporting Requirements

The proposed rules would enable shareholders to engage in limited solicitations to form nominating shareholder groups and engage in solicitations in support of their nominees without disseminating a proxy statement. Although the minimum amount of securities a shareholder or group of shareholders must beneficially hold to be eligible to submit a nomination pursuant to proposed Rule 14a-11 is 1% for large accelerated filers, 3% for accelerated filers, and 5% for non-accelerated filers, the Commission anticipates that some shareholders or groups of shareholders may beneficially own in the aggregate more than 5% of the company's securities that are eligible to vote for the election of directors. Therefore, nominating shareholders will need to consider whether they have formed a group under Exchange Act Section 13(d)(3) and Rule 13d-5(b)(1) that is required to file beneficial ownership reports.[278] Any person who is directly or indirectly the beneficial owner of more than 5% of a class of equity securities

[278] Nominating shareholders that have formed a group under Exchange Act Section 13(d)(3) and Rule 13d-5(b) would need to reassess whether group status and the obligation of the group to file beneficial ownership reports continue after the election of directors.

registered under Exchange Act Section 12 must report that ownership by filing an Exchange Act Schedule 13D with the Commission.[279] There are exceptions to this requirement, however, that permit such a person to report that ownership on Schedule 13G rather than Schedule 13D.[280] One exception permits filings on Schedule 13G for a specified list of qualified institutional investors who have acquired the securities in the ordinary course of their business and with neither the purpose nor the effect of changing or influencing control of the company. A second exception applies to persons who are not specified in the first exception. These beneficial owners of more than 5% of a subject class of securities may file on Schedule 13G if they acquired the securities with neither the purpose nor the effect of changing or influencing control of the company and they are not directly or indirectly the beneficial owner of 20% or more of the subject class of securities.

Central to Schedule 13G eligibility is that the shareholder be a passive investor that has acquired the securities without the purpose, or the effect, of changing or influencing control of the company. In addition, shareholders who are filing as qualified institutional investors must have acquired the securities in the ordinary course of their business. We believe that the formation of a shareholder group solely for the purpose of nominating one or more directors pursuant to proposed Rule 14a-11, the nomination of one or more directors pursuant to proposed Rule 14a-11, soliciting activities in connection with such a nomination (including soliciting in opposition to a company's nominees), or the election of such a nominee as a director under proposed Rule 14a-11, should not result in a nominating shareholder or nominating shareholder group losing its eligibility to file on Schedule 13G. In such circumstances, a nominating shareholder or nominating shareholder group could report on Schedule 13G, rather than

279 See Exchange Act Rule 13d-1.

280 See, e.g., Exchange Act Rules 13d-1(b) and 13d-1(c).

Schedule 13D. Accordingly, we are proposing to revise the requirement that the first and second categories of persons who may report their ownership on Schedule 13G have acquired the securities without the purpose or effect of changing or influencing control of the registrant to provide an exception for activities solely in connection with a nomination under Rule 14a-11.[281] Any activity other than those provided for under Rule 14a-11 would make these instructions inapplicable. These rule changes would not apply to nominating shareholders or groups that submit a nomination pursuant to an applicable state law provision or a company's governing documents because in those instances the applicable provisions may not limit the number of board seats for which a shareholder or group could nominate candidates or include a requirement that the nominating shareholder or group lack intent to change the control of the issuer or to gain more than a limited number of seats on the board (as is the case under proposed Rule 14a-11). Accordingly, we do not believe it would be appropriate to make any determination as to whether a nominating shareholder or group under an applicable state law provision or a company's governing documents would be eligible to file on Schedule 13G.

Request for Comment

J.1. The proposal would provide that a shareholder or shareholder group[282] would not, solely by virtue of nominating one or more directors under proposed Rule 14a-11, soliciting on behalf of that nominee or nominees, or having that nominee or nominees elected, lose their eligibility to file as a passive or qualified institutional

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281 This exception would only be available for purposes of the nomination. After the election of directors, a nominating shareholder or group would need to reassess its eligibility to continue to report on Schedule 13G as a passive or qualified institutional investor. For example, if a nominating shareholder is the nominee, and is successful in being elected to the board of a company, the shareholder would most likely be ineligible to continue filing on Schedule 13G because of its ability as a director to directly or indirectly influence the management and policies of the company.

282 A group may file on Schedule 13G so long as each member qualifies to do so individually.

investor. This provision would then permit those shareholders or groups to report their ownership on Schedule 13G, rather than Schedule 13D. Is this approach appropriate? Should other conditions be required to be satisfied? If so, what other conditions? For example, should a nominating shareholder or group cease to qualify as a passive or qualified institutional investor where the nominee is the nominating shareholder or a member of the group, a member of the immediate family of the nominating shareholder or any member of the group, an employee of the nominating shareholder or any member of the group, or is in any way controlled by the nominating shareholder or any member of the group?

J.2. Should nominating shareholders or groups be required to comply with the additional Schedule 13D filing and disclosure requirements under the Exchange Act beneficial ownership reporting standards?

J.3. Should we provide a similar provision for nominating shareholders or groups submitting a nomination pursuant to an applicable state law provision or a company's governing documents? Why or why not?

2. Exchange Act Section 16

Exchange Act Section 16[283] applies to every person who is the beneficial owner of more than 10% of any class of equity security registered under Exchange Act Section 12 ("10% owners"), and each officer and director (collectively with 10% owners, "insiders") of the issuer of such security. Generally:

- Section 16(a) requires an insider to file an initial report with the Commission disclosing his or her beneficial ownership of all equity securities of the issuer upon

[283] 15 U.S.C. 78p.

becoming an insider. To keep this information current, Section 16(a) also requires insiders to report changes in such holdings, in most cases within two business days following the transaction.[284]

- Section 16(b) provides the issuer (or shareholders suing on behalf of the issuer) a private right of action to recover from an insider any profit realized by the insider from any purchase and sale (or sale and purchase) of any equity security of the issuer within any period of less than six months.[285]
- Section 16(c) makes it unlawful for an insider to sell any equity security of the issuer if the insider: (1) does not own the security sold; or (2) owns the security, but does not deliver it against the sale within specified time periods.[286]

In 2003 the Commission proposed that a group formed solely for the purpose of nominating a director pursuant to proposed Rule 14a-11, soliciting in connection with the election of that nominee, or having that nominee elected as a director should not be viewed as being aggregated together for purposes of the 10% ownership determination under Section 16.[287] We are not proposing such an exclusion today and instead believe it would be appropriate to apply the existing analysis of whether a group has formed[288] and whether Section 16 applies.[289] In this regard, because the ownership thresholds for proposed Rule 14a-11 are significantly lower than 10%, and are generally lower than what was proposed in 2003, we do not believe that the

284 Exchange Act Section 16(a) [15 U.S.C. 78p(a)].

285 Exchange Act Section 16(b) [15 U.S.C. 78p(b)].

286 Exchange Act Section 16(c) [15 U.S.C. 78p(c)].

287 Commenters on the 2003 Proposal generally supported the proposed exception. See 2003 Summary of Comments; see also comment letters from CalPERS, CIR; ICI; NYC Bar; and NYS Bar.

288 See Exchange Act Rule 13d-5(b) [17 CFR 240.13d-5(b)].

289 See Exchange Act Rule 16a-1(a)(1) [17 CFR 240.16a-1(a)(1)].

lack of an exclusion would have a deterrent effect on the formation of groups, and therefore an exclusion may be unnecessary under the current proposal. Rather, a group formed for the purpose of nominating a director pursuant to proposed Rule 14a-11, soliciting in connection with the election of that nominee, or having that nominee elected as a director, would be analyzed the same way as any other group for purposes of determining whether group members are 10% owners subject to Section 16.

Some shareholders, particularly institutions and other entities, may be concerned that successful use of proposed Rule 14a-11 to include a director nominee in company proxy materials may result in the nominating person also being deemed a director under the "deputization" theory developed by courts in Section 16(b) short-swing profit recovery cases.[290] Under this theory it is possible for a person to be deemed a director subject to Section 16, even though the issuer has not formally elected or otherwise named that person a director. We have not proposed standards for establishing the independence of the nominee from the nominating shareholder, or members of the nominating shareholder group.

Request for Comment

K.1. Would it be a disincentive to using proposed Rule 14a-11 if shareholders forming a group to nominate a director could become subject to Section 16 once the group's ownership exceeds 10% of the company's equity securities? Why or why not?

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290 See Feder v. Martin Marietta, 406 F.2d 260 (2d Cir.), cert. denied, 396 U.S. 1036 (1970); Blau v. Lehman, 368 U.S. 403 (1962); and Rattner v. Lehman, 193 F.2d 564 (2d Cir. 1952). The judicial decisions in which this theory was applied do not establish precise standards for determining when "deputization" may exist. However, the express purpose of Section 16(b) is to prevent the unfair use of information by insiders through their relationships to the issuer. Accordingly, one factor that courts may consider in determining if Section 16(b) liability applies is whether, by virtue of the "deputization" relationship, the "deputizing" entity's transactions in issuer securities may benefit from the deputized director's access to inside information.

K.2. Are there any specific reasons why shareholders forming a group solely to nominate a director pursuant to proposed Rule 14a-11 should not be subject to Section 16 once the group's ownership exceeds 10% of the company's equity securities? If so, should the Commission adopt an exclusion from Section 16? Why, or why not?

K.3. If we should amend Rule 16a-1(a)(1), the rule that defines who is a 10% owner for Exchange Act Section 16 purposes, to exclude a Rule 14a-11 nominating shareholder group from the definition, how should such an exclusion be structured? For example, these groups could remain subject to the general condition of the rule that they not have the purpose or effect of changing or influencing control of the issuer, but a note to Rule 16a-1(a)(1) could provide an exception for members of nominating shareholder groups formed solely for the purpose of using proposed Rule 14a-11.[291] Should these conditions or other conditions apply?

K.4. Should the Commission consider providing an exclusion to the existing Rule 13d-5 definition of "group" that applies to both the Section 13(d) beneficial ownership reporting requirements and the Section 16 reporting requirements?

K.5. If the Commission adopts any such exclusion, should it be based on additional or different conditions? For example, should the Commission provide an exclusion from the definition of "group" in Rule 13d-5(b) for shareholders that agree to act together solely for the purpose of holding their securities in accordance with

291 Rule 16a-1(a)(1) also contains a general condition that the securities be held for the benefit of third parties or in customer or fiduciary accounts in the ordinary course of business, but this condition would not be applicable to nominating shareholder groups under the exclusion contemplated by this comment request.

proposed Rule 14a-11(b)(2)?

K.6. Are there reasons that members of nominating shareholder groups formed under proposed Rule 14a-11 should be treated differently than shareholder groups permitted to form and formed to nominate directors under an applicable state law provision, or under provisions in a company's governing documents? If so, why? What distinctions ought to be drawn between groups formed under proposed Rule 14a-11 and an applicable state law provision or a company's governing documents in terms of Rule 13d-5(b) and Rule 16a-1(a)(1)?

K.7. Should there be a prohibition on any affiliation between nominees and nominating shareholders or groups? If so, what limitations would be appropriate? Would any such prohibitions or limitations make it less likely that in Section 16(b) cases courts would find nominating shareholders to be "deputized" directors in circumstances where liability should not apply? Would the lack of any such prohibitions or limitations increase the likelihood that courts would find nominating shareholders to be "deputized" directors?

E. Application of the Liability Provisions in the Federal Securities Laws to Statements Made By a Nominating Shareholder or Nominating Shareholder Group

It is our intent that a nominating shareholder or group relying on Rule 14a-11, an applicable state law provision, or a company's governing documents to include a nominee in company proxy materials be liable for any materially false or misleading statements in information provided by the nominating shareholder or group to the company (in its shareholder notice on Schedule 14N) that is then included in the company's proxy materials. To this end we have amended Rule 14a-9 to add a new paragraph (c), to specifically address these situations.

Proposed new paragraph (c) states that "no nominee, nominating shareholder or nominating shareholder group, or any member thereof, shall cause to be included in a registrant's proxy materials, either pursuant to the federal proxy rules, an applicable state law provision, or a registrant's governing documents as they relate to including shareholder nominees for director in registrant proxy materials, any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading."

In addition, proposed new Rule 14a-11(e) contains express language providing that the company would not be responsible for information that is provided by the nominating shareholder or group under Rule 14a-11 and then repeated by the company in its proxy statement, except where the company knows or has reason to know that the information is false or misleading. A similar provision is included in proposed Rule 14a-19 with regard to information that is provided by the nominating shareholder or group in connection with a nomination made pursuant to an applicable state law provision or the company's governing documents.[292]

Also, as proposed, any information that is provided to the company in the notice from the nominating shareholder or group under Rule 14a-11 (and, as required, filed with the Commission by the nominating shareholder or group) and then included in the company's proxy materials would not be incorporated by reference into any filing under the Securities Act, the Exchange

[292] See Note to proposed Rule 14a-19.

Act, or the Investment Company Act unless the company determines to incorporate that information by reference specifically into that filing.[293] A similar provision would apply to information that is provided by the nominating shareholder or group in connection with a nomination made pursuant to an applicable state law provision or the company's governing documents.[294]

To the extent the company does incorporate that information by reference or otherwise adopt the information as its own, however, we would consider the company's disclosure of that information as the company's own statement for purposes of the antifraud and civil liability provisions of the Securities Act, the Exchange Act, or the Investment Company Act, as applicable.

Request for Comment

L.1. Is an amendment to Rule 14a-9 the appropriate means to assign liability for materially false or misleading information provided by the nominating shareholder or group to the company that is included in the company's proxy materials? If not, what would be a more appropriate means? Should we characterize the disclosure provided to the company by the nominating shareholder or group and included in the company's proxy materials as soliciting material of the nominating shareholder or group, as we proposed in 2003? Why or why not? Is it appropriate for proposed Rule 14a-9(c) to apply to nominations made pursuant to Rule 14a-11, an applicable state law provision, and a company's governing documents?

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293 See the Instruction to proposed Item 7(c) of Schedule 14A; Instruction to proposed Item 22(b)(18) of Schedule 14A.

294 See the Instruction to proposed Item 7(f) of Schedule 14A; Instruction to proposed Item 22(b)(19) of Schedule 14A.

L.2. Does the language of proposed new paragraph (c) of Rule 14a-9 make clear that the nominating shareholder or group would be liable for any information included in its Schedule 14N or notice to the company that is included in the company's proxy materials? If not, what specific changes should be made to the proposed rule text?

L.3. Does the proposal make clear the company's responsibilities when it includes such information in its proxy materials? Should the proposal include language otherwise addressing a company's responsibility for repeating statements that it knows or has reason to know are not accurate? Are there situations where a company should be responsible for repeating statements of the nominating shareholder or group? Should the proposal treat disclosure provided in connection with a nomination pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents differently?

L.4. Should information provided by nominating shareholders or groups be deemed incorporated by reference into Securities Act, Exchange Act, or Investment Company Act filings? Why or why not?

L.5. Should information, if incorporated by reference into Securities Act or Exchange Act filings, still be treated as the responsibility of the nominee rather than the company? As proposed, are we creating a disincentive to incorporation by reference?

F. General Request for Comment

We request and encourage any interested person to submit comments regarding:

- the proposed amendments that are the subject of this release;

- additional or different changes; or
- other matters that may have an effect on the proposals contained in this release.

We request comment from the point of view of companies, investors and other market participants. With regard to any comments, we note that such comments are of great assistance to our rulemaking initiative if accompanied by supporting data and analysis of the issues addressed in those comments.

IV. PAPERWORK REDUCTION ACT

A. Background

The proposed amendments contain "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995.[295] We are submitting the proposal to the Office of Management and Budget for review in accordance with the PRA.[296] The titles for the collections of information are:

(1) "Form ID" (OMB Control No. 3235-0328);

(2) "Proxy Statements – Regulation 14A (Commission Rules 14a-1 through 14a-19 and Schedule 14A)" (OMB Control No. 3235-0059);

(3) "Information Statements – Regulation 14C (Commission Rules 14c-1 through 14c-7 and Schedule 14C)"[297] (OMB Control No. 3235-0057);

(4) "Schedule 14N";

(5) "Securities Ownership – Regulation 13D and 13G (Commission Rules 13d-1 through 13d-7 and Schedules 13D and 13G)" (OMB Control No. 3235-0145);

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295 44 U.S.C. 3501 et seq.

296 44 U.S.C. 3507(d) and 5 CFR 1320.11.

297 Exchange Act Schedule 14C requires disclosure of some items of Exchange Act Schedule 14A. Therefore, while we are not proposing to amend the text of Schedule 14C, the proposed amendments to Schedule 14A also must be reflected in the PRA burdens for Schedule 14C.

(6) "Form 8-K" (OMB Control No. 3235-0060); and

(7) "Rule 20a-1 under the Investment Company Act of 1940, Solicitations of Proxies, Consents, and Authorizations" (OMB Control No. 3235-0158).

These regulations, rules and forms were adopted pursuant to the Exchange Act and the Investment Company Act and set forth the disclosure requirements for securities ownership reports filed by investors, proxy and information statements,[298] and current reports filed by companies to ensure that investors are informed and can make informed voting or investing decisions. The hours and costs associated with preparing, filing, and sending these schedules and forms constitute reporting and cost burdens imposed by each collection of information. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

B. Summary of Proposed Amendments

The Commission's proposals would provide shareholders with two ways to more fully exercise their rights to nominate directors. First, we are proposing a new rule – Rule 14a-11 – that would, under certain circumstances, require companies to include in their proxy materials shareholder nominees for director submitted by long-term shareholders or groups of shareholders with significant holdings. Under the rule, a company would not be required to include a shareholder nominee or nominees for director in the company proxy materials where the nominating shareholder or group is seeking to change the control of the issuer or to obtain more

[298] The proxy rules apply only to domestic companies with securities registered under Section 12 of the Exchange Act and to investment companies registered under the Investment Company Act. The number of annual reports by reporting companies may differ from the number of proxy and information statements filed with the Commission in any given year. This is because some companies are subject to reporting requirements by virtue of Section 15(d) of the Exchange Act, and therefore are not covered by the proxy rules. Also, some companies are subject to the proxy rules only because they have a class of debt registered under Section 12. These companies generally are not required to hold annual meetings for the election of directors. In addition, companies that are not listed on a national securities exchange may not hold annual meetings and therefore would not be required to file a proxy or information statement.

than a limited number of seats on the board. Proposed Rule 14a-11 would not apply where state law or a company's governing documents prohibit shareholders from nominating directors.

For purposes of the PRA, we estimate the total annual incremental paperwork burden resulting from proposed Rule 14a-11 and the related rule changes for reporting companies (other than registered investment companies), and registered investment companies to be approximately 17,149 hours of internal company or shareholder time and a cost of approximately $2,796,320 for the services of outside professionals.[299] For purposes of the PRA, we estimate the total annual incremental paperwork burden to nominating shareholders and groups from proposed Schedule 14N to be approximately 28,565 hours of shareholder personnel time, and $3,808,600 for services of outside professionals. As discussed further, below, these total costs include all additional disclosure burdens associated with the proposed rules including burdens related to the notice and disclosure requirements.

Second, under the proposed amendment to Rule 14a-8(i)(8), the "election exclusion," a company would not be permitted to exclude a shareholder proposal that would amend, or that requests an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11.

For purposes of the PRA, we estimate the total annual incremental paperwork burden resulting from the proposed amendment to Rule 14a-8(i)(8) and the related rule changes for reporting companies (other than registered investment companies), registered investment companies, and shareholders to be approximately 7,692 hours of internal company or

299 For convenience, the estimated PRA hour burdens have been rounded to the nearest whole number. We estimate an hourly cost of $400 per hour for the service of outside professionals based on our consultations with several registrants and law firms and other persons who regularly assist registrants in preparing and filing proxy statements and related disclosures with the Commission.

shareholder time and a cost of approximately $1,025,500 for the services of outside professionals.

In connection with proposed Rule 14a-11 and the proposed amendment to Rule 14a-8(i)(8), we also are proposing new rules that would require a notice to be filed with the Commission on proposed new Schedule 14N, and provided to the company, when a shareholder seeks to submit a nomination to a company pursuant to Rule 14a-11 or pursuant to an applicable state law provision or the company's governing documents. The Schedule 14N would include disclosure similar to the disclosure currently required in a proxy contest. The nominating shareholder or group would provide the disclosure specified in Rule 14a-18 or Rule 14a-19, as applicable, in the Schedule 14N. The company would be required to include the disclosure provided by the nominating shareholder in its proxy materials.

We also are proposing a new exemption from the proxy rules for communications by nominating shareholders or groups that are soliciting in favor of a shareholder nominee for director included pursuant to Rule 14a-11. This exemption would require inclusion in the written soliciting materials of a legend advising shareholders to look at the company's proxy statement when it becomes available and advising shareholders how to find the company's proxy statement. The burden hours resulting from the proposed exemption are included in the above totals related to proposed Rule 14a-11.

Compliance with the proposed disclosure requirements would be mandatory. There would be no mandatory retention period for the information disclosed, and responses to the disclosure requirements would not be kept confidential.

C. Paperwork Reduction Act Burden Estimates

The proposed amendments would, if adopted, require additional disclosure on Schedules

14A and 14C and new Schedule 14N, as well as Form 8-K. Schedule 14A prescribes the information that a company and/or a soliciting shareholder must include in its proxy statement to provide shareholders with material information relating to voting decisions. Schedule 14C prescribes the information that a company that is registered under Exchange Act Section 12 must include in its information statement in advance of a shareholders' meeting when it is not soliciting proxies from its shareholders, including when it takes corporate action by written authorization or consent of shareholders. When filed in connection with Rule 14a-11, Schedule 14N would require disclosure about the amount and percentage of securities entitled to be voted on the election of directors by the nominating shareholder or group, the length of ownership of such securities, and the nominating shareholder's or group's intent to continue to hold the securities through the date of the meeting. Schedule 14N would also require a certification that the nominating shareholder or group is not seeking to change the control of the company or to gain more than a limited number of seats on the board, as well as disclosure similar to the disclosure currently required for a contested election and certain representations required for use of Rule 14a-11, including that the nominee meets the generally applicable objective criteria for "independence" in any applicable national securities exchange or national securities association rules. When filed in connection with a nomination pursuant to an applicable state law provision or the company's governing documents, the Schedule 14N would include similar but more limited disclosures and representations. Exchange Act Rule 14a-8 requires the company to include a shareholder proposal in its Schedule 14A or 14C unless the shareholder has not complied with the procedural requirements in Rule 14a-8 or the proposal falls within one of the 13 substantive bases for exclusion in Rule 14a-8. Investment Company Act Rule 20a-1 requires registered investment companies to comply with Exchange Act Regulation 14A or 14C, as applicable.[300]

1. Proposed Rule 14a-11

Proposed Rule 14a-11 would require any subject company to include disclosure about a nominating shareholder's or group's nominee or nominees for election as director in the company's proxy materials when the conditions of the rule are met. The proposed rule would apply unless state law or a company's governing documents prohibit shareholders from nominating a candidate or candidates for election as director. A nominating shareholder or group would be required to file proposed Schedule 14N to disclose information about the nominating shareholder or group and the nominee or nominees, and the company would be required to include certain information regarding the nominating shareholder or group and nominee or nominees in the company's proxy statement unless the company determines that it is not required to include the nominee or nominees in its proxy materials.[301] Nominating shareholders also would be afforded the opportunity to include in the company's proxy statement a statement of support for its nominee or nominees of a length not to exceed 500 words. The nominee or nominees also would be included on the company's form of proxy in accordance with Exchange Act

Rule 14a-4.

Under the proposed rule, shareholders or groups beneficially owning at least 1%, 3%, or 5% of a company's securities entitled to be voted on the election of directors, for large accelerated, accelerated, and non-accelerated filers, respectively, would be eligible to submit a

300 The annual responses to Investment Company Act Rule 20a-1 reflect the number of proxy and information statements that are filed by registered investment companies.

301 The burdens associated with Schedule 14N and the disclosure requirements of Rule 14a-18 and Rule 14a-19 are discussed in Section IV.C.3. below.

nominee for election as director to be included in the company's proxy materials subject to certain limitations on the overall number of shareholder nominees for director.

We estimate that 4,163 reporting companies (other than registered investment companies) are likely to have at least one shareholder that could meet the above thresholds.[302] For purposes of this analysis, we estimate that 5% of companies with shareholders eligible to submit nominees pursuant to Rule 14a-11 will receive nominees from shareholders for inclusion in their proxy materials, which would result in 208 companies with shareholders meeting the applicable eligibility threshold receiving nominees annually.[303] We further estimate that 61 registered investment companies will receive nominees from shareholders pursuant to Rule 14a-11 annually.[304] For purposes of the PRA, we estimate that the incremental disclosure burden will be

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302 We estimate that 1,385 large accelerated filers have at least one shareholder that meets the 1% threshold; 1,584 accelerated filers have at least one shareholder meeting the 3% threshold; and 1,194 non-accelerated filers have at least one shareholder meeting the 5% threshold. See Section II.B.3., above.

Shareholders would be permitted to aggregate holdings for purposes of meeting the eligibility thresholds in Rule 14a-11 and therefore the Commission anticipates that some groups of shareholders may beneficially own in the aggregate more than 5% of the company's securities that are eligible to vote for the election of directors. In these circumstances, nominating shareholders will need to consider whether they have formed a group under Exchange Act Section 13(d)(3) and Rule 13d-5(b)(1) that is required to file beneficial ownership reports. To the extent nominating shareholder groups exceed the 5% threshold and file a Schedule 13G this would result in an increased number of Schedule 13G filings. We estimate that 25% of the nominees will be from shareholders who individually meet the eligibility thresholds (52), and 75% will be from shareholder groups (156). Were each of these groups to exceed 5%, we estimate that an additional 156 Schedule 13G filings will be made annually as a result of the proposed rule. The total burden associated with this increase in the number of filings is 1935 burden hours (156 additional Schedule 13Gs x 12.4 hours/schedule). This burden corresponds to 484 hours of shareholder time (156 additional Schedule 13Gs x 12.4 hours/Schedule x .25) and $580,320 for services of outside professionals (156 additional Schedule 13Gs x 12.4 hours/Schedule x .75 x $400).

303 In this regard, we note that in 2008 there were at least 32 contested elections. See RiskMetrics Group, 2008 Postseason Report Summary, Weathering the Storm: Investors Respond to the Global Credit Crisis, October 2008. In addition, approximately 118 Rule 14a-8 shareholder proposals related to board issues were submitted to shareholders for a vote in the 2008-2009 proxy season. See RiskMetrics 2009 Proxy Season Scorecard, May 15, 2009. We believe these two numbers, or 150 shareholders in total, provide some indication of the number of shareholders that may be interested in using Rule 14a-11. Based upon this information, we believe it is reasonable to use 208 (based on 5% of the companies that have at least one shareholder that meets the ownership threshold) as the estimate for the number of companies that may receive nominees.

304 We estimate that approximately 1,225 registered investment companies will hold a shareholder meeting in a given year, based on the number of responses to Rule 20a-1, and that 5% of such companies will receive

95 hours per nominee for each reporting company (other than registered investment companies) and registered investment company to comply with the requirements of Rule 14a-11 and Items 7(e) and (f) and 22(b)(18) and (19) of Schedule 14A.[305] As discussed, we estimate for PRA purposes that each company that receives nominees pursuant to Rule 14a-11 will receive two nominees from shareholders or groups. Thus, for reporting companies (other than registered investment companies) we estimate 13,015 total company burden hours which corresponds to 9,761 hours of company time, and a cost of approximately $1,301,500 for the services of outside professionals. In the case of registered investment companies, we estimate the total annual incremental paperwork burden to prepare the disclosure that would be required under this portion of the proposed rules to be approximately 3,805 burden hours, which corresponds to 2,854 hours of company time and a cost of approximately $380,500 for the services of outside professionals. In each case, this estimate includes:

- if the company determines that it will include a shareholder nominee, the company's preparation of a written notice to the nominating shareholder or group (five burden hours per notice);

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nominees from shareholders for inclusion in their proxy materials. We believe that using the 5% estimate for registered investment companies is reasonable because we estimate that shareholders of registered closed-end and open-end investment companies will on balance submit nominees at the same rate as other companies.

305 The actual burden hours will depend on the number of shareholder nominees submitted to a company for inclusion in its proxy materials. For purposes of the PRA, in the case of reporting companies (other than registered investment companies) we assume each shareholder or group would submit two nominees. As discussed in footnote 183 above, the median board size based on a 2007 sample of public companies was nine. Approximately 60% of the boards sampled had between nine and 19 directors. In the case of registered investment companies, we estimate that the median board size is eight. See Investment Company Institute and Independent Directors Council, Overview of Fund Governance Practices 1994-2006, at 6-7 (November 2007), available at: http://www.ici.org/issues/dir/1rpt_07_fund_gov_practices.pdf (noting that the median number of independent directors per fund complex in 2006 was six and that independent directors held 75% or more of board seats in 88% of fund complexes). Thus, although some shareholders or groups could nominate fewer than two nominees and others would be permitted to nominate more than two nominees, depending on the size of the board, we assume for purposes of the PRA that each shareholder or group would submit two nominees.

- the company's inclusion in its proxy statement and form of proxy of the name of, and other related disclosures concerning, a person or persons nominated by a shareholder or shareholder group (five burden hours per nominee);[306]
- the company's preparation of its own statement regarding the shareholder nominee or nominees (20 burden hours per nominee); and
- if a company determines that it may exclude a shareholder nominee submitted pursuant to the proposed rule, the company's preparation of a written notice to the nominating shareholder or group followed by written notice of the basis for its determination to exclude the nominee to the Commission staff (65 burden hours per notice).

For purposes of this analysis, we assume that approximately 187 (or 90% of) reporting companies (other than registered investment companies) and 55 (or 90% of) registered investment companies that have a shareholder or group and receives a shareholder nominee for director would be required to include the nominee in its proxy materials. In the other 10% of cases we assume that the company would be able to exclude the shareholder nominee (after providing notice of its reasons to the Commission). If a company determines to include a shareholder nominee, it must provide written notice to the nominating shareholder or group. We estimate the burden associated with preparing this notice to be five hours. For reporting companies (other than registered investment companies), this would result in 935 aggregate burden hours (187 companies x 5 hours/company), which corresponds to 701 burden hours of company time (187 companies x 5 hours/company x .75) and $93,500 in services of outside professionals (187 companies x 5 hours/company x .25 x $400). For registered investment companies, this would result in 275 aggregate burden hours (55 companies x 5 hours/company),

306 The requirement is in proposed amended Rule 14a-4.

which corresponds to 206 burden hours of company time (55 companies x 5 hours/company x .75), and $27,500 for services of outside professionals (55 companies x 5 hours/company x .25 x $400).

We estimate the annual disclosure burden for companies to include nominees on their form of proxy and proxy materials to be 5 burden hours per nominee, for a total of 1,870 aggregate burden hours (187 responses x 5 hours/response x 2 nominees) for reporting companies (other than registered investment companies), and 550 aggregate burden hours (55 responses x 5 hours/response x 2 nominees) for registered investment companies. For reporting companies (other than registered investment companies), this corresponds to 1,403 burden hours of company time, and $187,000 for services of outside professionals.[307] For registered investment companies, this corresponds to 413 hours of company time, and $55,000 for services of outside professionals.[308]

We estimate that 187 reporting companies (other than registered investment companies) and 55 registered investment companies would include a statement with regard to the shareholder nominees.[309] We anticipate that the burden to include a statement would include time spent to research the nominee's background, preparation of the statement, and company time for review of the statement by, among others, the nominating committee and legal counsel. We estimate that this burden would be approximately 20 hours per nominee. For reporting companies (other than registered investment companies), this would result in 7,480 aggregate

307 The calculations for these numbers are: 1,870 burden hours x .75 = 1,402 burden hours of company time and 1,870 burden hours x .25 x $400 = $187,000 for services of outside professionals.

308 The calculations for these numbers are: 550 burden hours x .75 = 413 hours of company time and 550 burden hours x .25 x $400 = $55,000 for services of outside professionals.

309 We estimate that each company that includes a shareholder nominee in its proxy materials would include such a statement.

burden hours (187 statements x 20 hours/statement x 2 nominees). This corresponds to 5,610 hours of company time (187 statements x 20 hours/statement x 2 nominees x .75) and $748,000 for services of outside professionals (187 statements x 20 hours/statement x 2 nominees x .25 x $400) for reporting companies (other than registered investment companies). For registered investment companies, this would result in 2,200 aggregate burden hours (55 statements x 20 hours/statement x 2 nominees). This corresponds to 1,650 hours of company time (55 statements x 20 hours/statement x 2 nominees x .75) and $220,000 for services of outside professionals (55 statements x 20 hours/statement x 2 nominees x .25 x $400).

Further, for purposes of this analysis, we assume that approximately 42 (or 20% of) reporting companies (other than registered investment companies) and 12 (or 20% of) registered investment companies who receive a shareholder nominee for director for inclusion in their proxy materials would make a determination that they are not required to include a nominee in their proxy materials because the nominee is ineligible under proposed Rule 14a-11 and would file a notice of intent to exclude that nominee.[310] We estimate that the burden hours associated with preparing and submitting the company's notification to the nominating shareholder or group and the Commission regarding its intent to exclude a shareholder nominee, and its reasons for doing so, would be 65 hours per notification.[311] In the case of reporting companies (other than

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310 We assume that 21 of these nominees (or 50% of those sought to be excluded by companies) would ultimately be excludable under the rule.

311 This estimate is based on data provided by the American Society of Corporate Secretaries in its comment letter on the 2003 Proposal. In its letter, the ASCS provided data from a survey of its own, as well as the Business Roundtable's, members indicating that the average burden associated with preparing and submitting a no-action request to the staff in connection with a shareholder proposal was approximately 30 hours and associated costs of $13,896. Although the letter did not specify as much, assuming these costs correspond to legal fees, which we estimate at an hourly cost of $400, we estimate that this cost is equivalent to approximately 35 hours ($13,896/$400). For purposes of the PRA, we assume that submitting the notice and reasons for excluding a shareholder nominee to the staff will be comparable to preparing a no-action request to exclude a proposal under Rule 14a-8. Thus, we estimate that the burden to submit the notice and reasons for excluding a shareholder nominee would be approximately 65 hours.

registered investment companies), we estimate that this would result in an aggregate burden of 2,730 (42 notices x 65 hours/notice), corresponding to 2,048 hours of company time (42 notices x 65 hours/notice x .75) and $273,000 for the services of outside professionals (42 responses x 65 hours/notice x .25 x $400). In the case of registered investment companies, we estimate that this would result in 780 aggregate burden hours (12 notices x 65 hours/notice), which would correspond to 585 hours of company time (12 notices x 65 hours/notice x .75) and $78,000 for the services of outside professionals (12 notices x 65 hours/notice x .25 x $400). These burdens would be added to the PRA burdens of Schedules 14A and 14C or, in the case of registered investment companies, Rule 20a-1.

We also estimate that the annual incremental burden for the nominating shareholder's or group's participation in the Rule 14a-11 exclusion process would average 30 hours per nomination.[312] For nominating shareholders or groups of reporting companies (other than registered investment companies), this would result in 1,260 total burden hours (42 responses x 30 hours/response). This would correspond to 945 hours of shareholder time (42 responses x 30 hours/response x .75) and $126,000 for services of outside professionals (42 responses x 30 hours/response x .25 x $400). For nominating shareholders or groups of registered investment companies, this would result in 360 total burden hours (12 responses x 30 hours/response). This would correspond to 270 hours of shareholder time (12 responses x 30 hours/response x .75) and $36,000 for services of outside professionals (12 responses x 30 hours/response x .25 x $400). This burden would be added to the PRA burden of Schedule 14N.

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312 As noted in footnote 311, above, we estimate that the average burden to a company associated with preparing and submitting a no-action request to the staff is approximately 65 burden hours. We believe that the average burden for a shareholder proponent to respond to a company's no-action request is likely to be less than a company's burden; therefore, we estimate 30 burden hours for a nominating shareholder to respond to a company's notice of intent to exclude to the Commission.

We also are proposing a new exemption from the proxy rules for communications by nominating shareholders or groups that are soliciting in favor of a shareholder nominee for director. Although nominating shareholders or groups would not be required to engage in written solicitations, the exemption would require inclusion in any written soliciting materials of a legend advising shareholders to look at the company's proxy statement when it becomes available and advising shareholders how to find the company's proxy statement. For purposes of this analysis, we assume that 50% of nominating shareholders or groups would solicit in favor of their nominee or nominees outside the company's proxy statement. In the case of reporting companies (other than registered investment companies), this would result in an aggregate burden of 104 hours (104 solicitations x 1 hour/solicitation), which corresponds to 78 hours of shareholder time (104 solicitations x 1 hour/solicitation x .75) and $10,400 for services of outside professionals (104 solicitations x 1 hour/solicitation x .25 x $400). These burden hours would be added to the PRA burden of Schedule 14A.[313]

2. Proposed Amendment to Rule 14a-8(i)(8)

Our proposed amendment to Rule 14a-8(i)(8), the election exclusion, would enable shareholders to submit proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11. As proposed, revised Rule 14a-8(i)(8) would not restrict the types of amendments that a shareholder could propose to a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, although any such proposals that conflict with

313 In the case of registered investment companies, this would result in an aggregate burden of 31 hours (31 solicitations x 1 hour/solicitation), which corresponds to 23 hours of shareholder time (31 solicitations x 1 hour/solicitation x .75) and $3,100 for services of outside professionals (31 solicitations x 1 hour/solicitation x .25 x $400). These burden hours would be added to the PRA burden of Rule 20a-1.

proposed Rule 14a-11 or state law could be excluded. The proposal would have to meet the procedural requirements of Rule 14a-8 and not be subject to one of the substantive exclusions other than the election exclusion (e.g., the proposal could be excluded if the shareholder proponent did not meet the ownership threshold under Rule 14a-8).

Historically, shareholders have made relatively few proposals relating to shareholder access to company proxy materials. The staff received 368 no-action requests from companies seeking to exclude shareholder proposals during the 2006-2007 proxy season. Of these requests, only three (or approximately one percent) related to proposals for bylaw amendments providing for shareholder nominees to appear in the company's proxy materials. During the 2007-2008 proxy season, the staff received 432 no-action requests to exclude shareholder proposals pursuant to Rule 14a-8. Of these no-action requests, 6 (or approximately two percent) related to proposals for bylaw amendments providing for shareholder nominees to appear in the company's proxy materials. Because our proposed amendment to Rule 14a-8(i)(8) would narrow the scope of the exclusion and prohibit companies from excluding certain proposals that are excludable under the current Rule 14a-8(i)(8), we anticipate an increase in the number of shareholder proposals to amend, or request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations.

While the number of no-action requests the staff has received in the past is a useful starting point, other data also is helpful to gauge shareholder interest in nominating directors and predict the anticipated impact on the number of proposals submitted pursuant to Rule 14a-8 to amend, or request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations that otherwise would be excludable under current Rule 14a-8(i)(8). For example, based on publicly available information, from 2001 to 2005, there were an average of 14 contested elections per year.[314] In 2008, it is estimated that there were at least 32 contested elections.[315] We anticipate that as a result of the proposed amendment to Rule 14a-8(i)(8), shareholders will submit at least as many shareholder proposals to amend a company's governing documents to address the company's nomination procedures or disclosures related to director nominations as there are contested elections. We anticipate that if shareholders are willing to put forth the expense and effort to wage a contest to put forth their own nominees in 32 instances, there will be at least that many proposals submitted to companies pursuant to Rule 14a-8 because companies will no longer be permitted under the rule to exclude proposals that currently are excludable under Rule 14a-8(i)(8). We also anticipate that some shareholders that have submitted proposals in the past with regard to other board issues will submit proposals to address a company's nomination procedures or disclosures related to director nominations. According to information from RiskMetrics, approximately 118 Rule 14a-8 shareholder proposals regarding board issues were or will be submitted to shareholders for a vote in the 2008-2009 proxy season.[316] We estimate that approximately half of these shareholders would submit a proposal regarding nomination procedures or disclosures, resulting in 59 proposals.

In the case of reporting companies (other than registered investment companies), we anticipate that the amendments to Rule 14a-8 will result in an increase of 38 proposals annually from 2008, and a total of 97 proposals regarding nomination procedures or disclosures related to

314 See Lucian A. Bebchuk, The Myth of the Shareholder Franchise, 93 VA. L. REV. 675 (2007) ("Bebchuk 2007 Article") (citing data from proxy solicitation firm Georgeson Shareholder).

315 See RiskMetrics Group, 2008 Postseason Report Summary, Weathering the Storm: Investors Respond to the Global Credit Crisis, October 2008.

316 See footnote 303, above.

director nominations to companies per year.[317] We estimate the annual incremental burden for the shareholder to prepare the proposal to be 10 burden hours per proposal, for a total of 380 burden hours (38 proposals x 10 hours/proposal). This would correspond to 285 hours of shareholder time (38 proposals x 10 hours/proposal x .75) and $38,000 for the services of outside professionals (38 proposals x 10 hours/proposal x .25 x $400).

We estimate that 90% of companies that receive a shareholder proposal to amend, or request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations will seek to exclude the proposal from their proxy materials (so companies would seek to exclude 87 such proposals per proxy season). We estimate that the annual incremental burden for the company's submission of a notice of its intent to exclude the proposal and its reasons for doing so would average 65 hours per proposal, for a total of 5,655 burden hours (87 proposals x 65 hours/proposal) for reporting companies (other than registered investment companies). This would correspond to 4,241 hours of company time (87 proposals x 65 hours/proposal x .75) and $565,500 for the services of outside professionals (87 proposals x 65 hours/proposal x .25 x $400).

We also estimate that the annual incremental burden for the proponent's participation in the Rule 14a-8 no-action process would average 30 hours per proposal, for a total of 2,610

317 The increase is calculated by adding the number of proxy contests in 2008 (32) plus the number of no-action requests received in 2008 regarding proposals seeking to amend a company's bylaws to provide for shareholder director nominations (6). We have not included the estimated 59 proposals in this increase because we believe they will be submitted in lieu of other types of proposals (a shareholder is limited to submitting one shareholder proposal to each company). We recognize that a company that receives a shareholder proposal has no obligation to submit a no-action request to the staff under Rule 14a-8 unless it intends to exclude the proposal from its proxy materials. Based on historical data, companies generally seek no-action relief from the staff on approximately 60% of the proposals received. However, we anticipate that because the proposals that would be submitted pursuant to amended Rule 14a-8 could affect the composition of the company's board of directors, nearly all companies receiving such proposals would submit a written statement of its reasons for excluding the proposal to the staff. Thus, we estimate that 90% of the estimated 97 companies receiving proposals to amend, or request an amendment to, a company's governing documents to address nomination procedures or disclosures related to director nominations would submit a written statement of its reasons for excluding the proposal to the staff.

burden hours (87 proposals x 30 hours/proposal).[318] This would correspond to 1,958 hours of shareholder time (87 proposals x 30 hours/proposal x .75) and $261,000 for services of outside professionals (87 proposals x 30 hours/proposal x .25 x $400). These burdens would be added to the PRA burden of Schedules 14A and 14C.

In the case of registered investment companies, we anticipate that the amendments to Rule 14a-8 will result in an increase of 9 proposals annually, and a total of 18 proposals regarding nomination procedures or disclosures related to director nominations to companies per year.[319] We estimate the annual incremental burden for the shareholder proponent to prepare the proposal to be 10 hours per proposal, for a total of 90 burden hours (9 proposals x 10 hours/proposal). This would correspond to 68 hours of shareholder time (9 proposals x 10 hours/proposal x .75) and $9,000 for the services of outside professionals (9 proposals x 10 hours/proposal x .25 x $400).

Similar to reporting companies other than investment companies, we assume that 90% of registered investment companies that receive a shareholder proposal to amend, or request an amendment to, the company's governing documents regarding nomination procedures or disclosures related to shareholder nominations will seek to exclude the proposal from their proxy materials (so registered investment companies would seek to exclude 16 such proposals per

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318 As noted above, in footnote 311, we estimate that the average burden to a company associated with preparing and submitting a no-action request to the staff was approximately 65 burden hours. We believe that the average burden for a shareholder proponent to respond to a company's no-action request is likely to be less than a company's burden; therefore, we estimate 30 burden hours for a shareholder proponent to respond to a company's notice of intent to exclude to the Commission. In this regard, we also estimate that the average burden for a shareholder proponent to submit a shareholder proposal would be 10 hours.

319 The increase is calculated by adding the average number of registered investment company proxy contests in calendar years 2006, 2007, and 2008 (8) plus the average number of no-action letters issued by the staff regarding proposals seeking to amend a registered investment company's bylaws to provide for shareholder director nominations received in calendar years 2006, 2007, and 2008 rounded to the nearest whole number greater than zero (1). In addition, we estimate that investment companies currently receive as many proposals regarding nomination procedures or disclosures as there are contested elections and no-action letters issued by the staff, resulting in a total of 18 proposals regarding nomination procedures or disclosures related to director nominations to companies per year.

proxy season). Also similar to reporting companies other than investment companies, we assume that the annual incremental burden for the company's submission of a notice of its intent to exclude the proposal and its reasons for doing so would average 65 hours per proposal, for a total of 1,040 burden hours for registered investment companies (16 proposals x 65 hours/proposal). This would correspond to 780 hours of company time (16 proposals x 65 hours/proposal x .75) and $104,000 for the services of outside professionals (16 proposals x 65 hours/proposal x .25 x $400). We also estimate that the annual incremental burden for the proponent's participation in the Rule 14a-8 no-action process would average 30 hours per proposal, for a total of 480 burden hours (16 proposals x 30 hours/proposal). This would correspond to 360 hours of shareholder time (16 proposals x 30 hours/proposal x .75) and $48,000 for the services of outside professionals (16 proposals x 30 hours/proposal x .25 x $400). These burdens would be added to the PRA burden of Rule 20a-1.

3. Proposed Schedule 14N and Proposed Exchange Act Rules 14a-18 and 14a-19

Proposed Rule 14n-1 would establish a new filing requirement for the nominating shareholder or group, under which the nominating shareholder or group would be required to file notice of its intent to include a shareholder nominee or nominees for director pursuant to proposed Rule 14a-11, applicable state law provisions, or a company's governing documents, as well as disclosure about the nominating shareholder or group and nominee or nominees on proposed new Schedule 14N. New Schedule 14N was modeled after Schedule 13G, but with more extensive disclosure requirements than Schedule 13G. The Schedule 14N would require, among other items, disclosure about the amount and percentage of securities owned by the nominating shareholder or group, the length of ownership of such securities, and the nominating shareholder's or group's intent to continue to hold the securities through the date of the meeting.

In addition, the Schedule 14N would include disclosure required pursuant to proposed Rule 14a-18 or Rule 14a-19, as applicable. Proposed Rule 14a-18 would prescribe the disclosure required to be included in the nominating shareholder's notice to the company, on Schedule 14N, of its intent to require that the company include that shareholder's nominee in the company's proxy materials pursuant to proposed Rule 14a-11. Proposed Rule 14a-19 would prescribe the disclosure required to be included in the nominating shareholder's notice to the company, on Schedule 14N, of its intent to require the company to include a nominee pursuant to applicable state law provisions or a company's governing documents. With regard to the latter, we are seeking to assure that nominating shareholders or groups who submit a shareholder nomination for inclusion in company proxy materials pursuant to applicable state law provisions or the company's governing documents also provide disclosure similar to the disclosure required in a contested election to give shareholders the information needed to make an informed voting decision.

Both rules would require disclosures regarding the nature and extent of the relationships between the nominating shareholder and nominee and the company or any affiliate of the company. Pursuant to proposed Items 7(e)-(f) of Schedule 14A or, in the case of a registered investment company, Items 22(b)(18)-(19) of Schedule 14A, the company would be required to include the information set forth in Schedule 14N in its proxy materials. A nominating shareholder filing a Schedule 14N to provide disclosure required by proposed Rule 14a-19 when submitting a nominee for inclusion in company proxy materials pursuant to applicable state law provisions or the company's governing documents would not be required to provide the representations required for nominating shareholders using proposed Rule 14a-11.

We estimate that compliance with the proposed Schedule 14N requirements would result in a burden greater than Schedule 13G[320] but less than a Schedule 14A.[321] Therefore, we estimate that compliance with proposed Schedule 14N will result in 47 hours per response for nominees submitted pursuant to Rule 14a-11.[322] We also note that the burden associated with filing a Schedule 14N in connection with a nomination made pursuant to an applicable state law provision or the company's governing documents may be slightly less than a nomination made pursuant to Rule 14a-11 because certain disclosures, representations and certifications would not be required (including disclosure about intent to continue to own the company's securities, the representations that would be required to rely on Rule 14a-11, a supporting statement from the nominating shareholder or group, and the certification concerning lack of intent to change control or to gain more than a limited number of seats on the board that would be required for a nomination pursuant to Rule 14a-11). Therefore, we estimate that compliance with proposed Schedule 14N when a shareholder or group submits a nominee or nominees to a company pursuant to an applicable state law provision or the company's governing documents will result in 40 hours per response.

For purposes of the PRA, we estimate the total annual incremental paperwork burden for nominating shareholders or groups to prepare the disclosure that would be required under this portion of the proposed rules to be approximately 28,565 hours of shareholder time, and

320 We currently estimate the burden per response for preparing a Schedule 13G filing to be 12.4 hours.

321 We currently estimate the burden per response for preparing a Schedule 14A filing to be 101.50 hours and a Schedule 14C to be 102.62 hours.

322 We estimate that the burden of preparing the information in Schedule 14N for a nominating shareholder or group would be 1/3 of the disclosures typically required by a Schedule 14A filing, which would result in approximately 34 burden hours. For purposes of this analysis, we estimate that the 34 burden hours will be added to the 12.4 hours associated with filing a Schedule 13G, resulting in a total of approximately 47 burden hours. We estimate that 75% of the burden of preparation of Schedule 14N will be borne internally by the nominating shareholder or group, and that 25% will be carried by outside professionals. We believe the nominating shareholder or group would work with their nominee to prepare the disclosure and then have it reviewed by outside professionals.

$3,808,600 for the services of outside professionals.[323] This estimate includes the nominating shareholder's or group's preparation and filing of the notice and required disclosure and, as applicable, representations and certifications on Schedule 14N.

We do not expect that every shareholder that meets the eligibility threshold to submit a nominee for inclusion in a company's proxy materials pursuant to proposed Rule 14a-11, an applicable state law provision, or a company's governing documents will do so. As discussed above, we estimate that 208 reporting companies (other than registered investment companies) and 61 registered investment companies will receive notices of intent to submit nominees pursuant to proposed Rule 14a-11. We anticipate that some companies will receive nominees from more than one shareholder or group, though, as discussed above, for purposes of PRA estimates, we assume each company with an eligible shareholder would receive two nominees from only one shareholder or group.

We estimate that compliance with the requirements of Schedule 14N submitted pursuant to Rule 14a-11 will require 19,552 burden hours (208 notices x 47 hours/notice x 2 nominees/shareholder) in aggregate each year for nominating shareholders or groups of reporting companies (other than registered investment companies), which corresponds to 14,664 hours of shareholder time (208 notices x 47 hours/notice x 2 nominees/shareholder x .75) and costs of $1,955,200 (208 notices x 47 hours/notice x 2 nominees/shareholder .25 x $400) for the services of outside professionals. In the case of registered investment companies, we estimate that a nominating shareholder's or group's compliance with the requirements of Schedule 14N will require 5,734 burden hours (61 responses x 47 hours/response x 2 nominees) in aggregate each year, which corresponds to 4,301 hours of shareholder time (61 responses x 47 hours/response x

323 This figure represents the aggregate burden hours attributed to proposed Schedule 14N and is the sum of the burden associated with Schedules 14N submitted pursuant to Rule 14a-11, applicable state law provisions, and a company's governing documents.

2 nominees x .75) and costs of $573,400 for the services of outside professionals (61 responses x 47 hours/response x 2 nominees x .25 x $400). Therefore, we estimate a total of 25,286 burden hours for all reporting companies, including investment companies, broken down into 18,965 hours of shareholder time and $2,528,600 for services of outside professionals.

We assume that all nominating shareholders or groups will prepare a statement of support for the nominee or nominees, and we estimate the disclosure burden for the nominating shareholder or group to prepare a statement of support for its nominee or nominees to be approximately 10 burden hours per nominee. This results in an aggregate burden of 4,160 (208 statements x 10 hours/statement x 2 nominees/shareholder), which corresponds to 3,120 hours of shareholder time (208 statements x 10 hours/statement x 2 nominees/shareholder x .75) and $416,000 for services of outside professionals (208 statements x 10 hours/statement x 2 nominees/shareholder x .25 x $400) for shareholders of reporting companies (other than registered investment companies). For registered investment companies, this would result in an aggregate burden of 1,220 (61 statements x 10 hours/statement x 2 nominees/shareholder), which corresponds to 915 hours of shareholder time (61 statements x 10 hours/statement x 2 nominees/shareholder x .75) and $122,000 for services of outside professionals (61 statements x 10 hours/statement x 2 nominees/shareholder x .25 x $400). Therefore, we estimate a total of 5,380 burden hours for all reporting companies, including investment companies, broken down into 4,035 hours of shareholder time and $538,000 for services of outside professionals.

When a nominating shareholder or group submits a nominee or nominees to a company pursuant to an applicable state law provision or the company's governing documents, the nominating shareholder or group will be required to file a Schedule 14N to provide disclosure about the nominating shareholder or group and the nominee or nominees as provided in proposed

Rule 14a-19. As discussed, a company will be required to include certain disclosures about the nominating shareholder or group and the nominee or nominees in its proxy statement. As noted above, we estimate that the burden associated with filing a Schedule 14N in connection with a nomination made pursuant to an applicable state law provision or a company's governing documents is 40 hours. We also estimate that approximately 49 nominating shareholders or groups of reporting companies (other than registered investment companies) would submit a nomination pursuant to an applicable state law provision or a company's governing documents.[324] Thus, we estimate compliance with the requirements of Schedule 14N for nominating shareholders or groups submitting nominations pursuant to an applicable state law provision or the company's governing documents would result in 3,920 aggregate burden hours (49 notices x 40 hours/notice x 2 nominees/shareholder) each year for nominating shareholders or groups of reporting companies (other than registered investment companies), broken down into 2,940 hours of shareholder time (49 notices x 40 hours/notice x 2 nominees/shareholder x .75) and costs of $392,000 for the services of outside professionals (49 notices x 40 hours/notice x 2 nominees/shareholder x .25 x $400). In the case of registered investment companies, we estimate that approximately 9 nominating shareholders or groups would submit a nomination pursuant to an applicable state law provision or a company's governing documents.[325] We estimate that a nominating shareholder's or group's compliance with the requirements of Schedule 14N would result in 720 aggregate burden hours (9 notices x 40 hours/notice x 2

324 In this regard, we estimated that approximately 97 shareholder proponents would submit proposals regarding nomination procedures or disclosures related to shareholder nominations. For purposes of this analysis, we assume that approximately half (49) of those shareholders would be eligible to submit a nomination pursuant to applicable state law provisions or a company's governing documents.

325 In this regard, we estimated that approximately 18 shareholder proponents would submit proposals to registered investment companies regarding nomination procedures or disclosures related to shareholder nominations. We estimate that approximately half (9) of those shareholders would be eligible to submit a nomination pursuant to applicable state law provisions or a company's governing documents.

nominees/shareholder) each year, which corresponds to 540 hours of shareholder time (9 notices x 40 hours/notice x 2 nominees/shareholder x .75) and costs of $72,000 for the services of outside professionals (9 notices x 40 hours/notice x 2 nominees/shareholder x .25 x $400). Therefore, we estimate that the total burden hours would be 4,640 for all reporting companies, including investment companies, broken down into 3,480 hours of shareholder time and $464,000 for services of outside professionals.

We assume that all nominating shareholders or groups that submit a nominee or nominees pursuant to an applicable state law provision or a company's governing documents would prepare a statement of support for the nominee or nominees,[326] and we estimate the disclosure burden for the nominating shareholder or group to prepare a statement of support for its nominee or nominees to be approximately 10 burden hours per nominee. This results in an aggregate burden of 980 hours (49 statements x 10 hours/statement x 2 nominees/shareholder) for shareholders of reporting companies (other than registered investment companies), which corresponds to 735 hours of shareholder time (49 statements x 10 hours/statement x 2 nominees/shareholder x .75) and $98,000 for services of outside professionals (49 statements x 10 hours/statement x 2 nominees/shareholder x .25 x $400). For registered investment companies, this results in an aggregate burden of 180 hours (9 statements x 10 hours/statement x 2 nominees/shareholder), which would correspond to 135 hours of shareholder time (9 statements x 10 hours/statement x 2 nominees/shareholder x .75) and $18,000 for services of outside professionals (9 statements x 10 hours/statement x 2 nominees/shareholder x .25 x $400). This results in a total of 1,160 burden hours, broken down into 870 hours of shareholder time and $116,000 for the services of outside professionals.

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326 We are assuming for PRA purposes that any applicable state law provision or company's governing documents would allow for inclusion of such a statement by the nominating shareholder or group.

4. Proposed Amendments to Exchange Act Form 8-K

Under proposed Rule 14a-11, a nominating shareholder or group would have to provide a notice to the company, on Schedule 14N, of its intent to require that the company include the nominating shareholder's or group's nominee in the company's proxy materials by the date specified by the company's advance notice provision or, where no such provision is in place, no later than 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting.[327] If the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed more than 30 days from the prior year, then the nominating shareholder or group would be required to provide notice a reasonable time before the company mails its proxy materials, as specified by the company in a Form 8-K filed pursuant to proposed Item 5.07. We also are proposing to require a registered investment company that is a series company to file a Form 8-K disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of the company's shares that are entitled to vote for the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.

For purposes of the PRA, we estimate that approximately 4% of reporting companies (other than registered investment companies) would be required to file an Exchange Act Form 8-K because the company did not hold an annual meeting during the prior year, or the date of the meeting has changed by more than 30 days from the prior year.[328] Based on our estimate that

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327 The proposed amendment to Rule 14a-8(i)(8) is not expected to impact Form 8-K, so the burden estimates solely reflect the burden changes resulting from proposed Rule 14a-11.

328 Based on information obtained in 2003 from the Investor Responsibility Research Center, 3.7% of companies (other than registered investment companies) filed Form 8-Ks because they did not hold an annual meeting during the prior year or the date of the meeting has changed by more than 30 days from the prior year. See also footnote 195 in the 2003 Proposal.

there are approximately 11,000 reporting companies (other than registered investment companies), this corresponds to 440 companies that would be required to file a Form 8-K. In accordance with our current estimate of the burden of preparing a Form 8-K, we estimate 5 burden hours to prepare, review and file the Form 8-K, for a total burden of 2,200 hours (440 filings x 5 hours/filing). This total burden corresponds to 1,650 hours of company time (440 filings x 5 hours/filing x .75) and $220,000 for services of outside professionals (440 filings x 5 hours/filing x .25 x $400).

In the case of registered investment companies, we estimate that, similar to reporting companies other than registered investment companies, 4% of registered closed-end management investment companies subject to Rule 14a-11 that are traded on an exchange would be required to file an Exchange Act Form 8-K because the company did not hold an annual meeting during the prior year or the date of the meeting has changed by more than 30 days from the prior year.[329] We estimate that approximately 650 of the 1,225 registered investment companies responding to Investment Company Act Rule 20a-1 are closed-end funds that are traded on an exchange, resulting in 26 closed-end funds that would be required to file Form 8-K for these purposes (650 registered closed-end management investment companies x .04).[330] However, we estimate that few, if any, registered open-end management investment companies regularly hold annual meetings. Therefore, we estimate that 575 registered investment companies are not closed-end investment companies and would be required to file Form 8-K. This results in a total of 601 registered investment companies required to file Form 8-K (26 closed-end management

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329 We believe that the percentage for registered closed-end investment companies would be similar to other reporting companies because such investment companies are traded on an exchange and are required to hold annual meetings of shareholders.

330 We estimate that 1,225 registered investment companies hold annual meetings each year based on the number of responses to Rule 20a-1. Based on data provided by Lipper, the Commission estimates that approximately 650 registered closed-end management investment companies are traded on an exchange.

investment companies + 575 other registered investment companies) and 3,005 burden hours (601 filings x 5 hours/filing). This total burden corresponds to 2,254 hours of company time (601 filings x 5 hours/filing x .75) and $300,500 for services of outside professionals (601 filings x 5 hours/filing x .25 x $400).[331] Adding the totals for reporting companies (other than registered investment companies) and registered investment companies results in a total burden of 5,205, which corresponds to 3,904 hours of company time and $520,500 for services of outside professionals. This includes the requirement for a registered investment company that is a series company to file a Form 8-K disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of the company's shares that are entitled to vote for the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.

5. Form ID Filings[332]

Under proposed Rule 14a-11(c), a shareholder who submits a nominee or nominees for inclusion in the company's proxy statement must provide notice on Schedule 14N to the company of its intent to require that the company include the nominee or nominees in the company's proxy materials and file the Schedule 14N with the Commission. We anticipate that some shareholders that submit a nominee or nominees for inclusion in a company's proxy materials will not previously have filed an electronic submission with the Commission and will

331 Consistent with the current estimates for Form 8-K, we estimate that that 75% of the burden of preparation of Form 8-K is carried by the company and that 25% of the burden of preparation of Form 8-K is carried by outside professionals at an average cost of $400 per hour. The burden includes disclosure of the date by which a nominating shareholder or group must submit the notice required by proposed Rule 14a-11(c) as well as disclosure of net assets, outstanding shares, and voting.

332 The proposed amendment to Rule 14a-8(i)(8) is not expected to affect Form ID filings, so the burden estimates solely reflect the burden changes resulting from proposed Rule 14a-11.

file a Form ID. Form ID is the application form for access codes to permit filing on EDGAR. The proposed rules are not changing the form itself, but we anticipate that the number of Form ID filings may increase due to shareholders filing Schedule 14N when submitting a nominee or nominees to a company for inclusion in its proxy materials pursuant to proposed Rule 14a-11. We estimate that 90% of the shareholders who submit a nominee or nominees for inclusion in the company's proxy materials will not have filed previously an electronic submission with the Commission and would be required to file a Form ID.[333] As noted above, we estimate that approximately 208 reporting companies (other than registered investment companies) and 61 registered investment companies will receive shareholder nominations submitted pursuant to proposed Rule 14a-11. This corresponds to 242 additional Form ID filings. In addition, as noted above, we estimate that approximately 49 reporting companies (other than registered investment companies) and 9 registered investment companies will receive shareholder nominations submitted pursuant to an applicable state law provision or a company's governing documents. This corresponds to an additional 52 Form ID filings. As a result, the additional annual burden would be 44 hours (294 filings x .15 hours/filing).[334] For purposes of the PRA, we estimate that the additional burden cost resulting from the proposed amendments will be zero because we estimate that 100 percent of the burden will be borne internally by the nominating shareholder.

D. Revisions to PRA Reporting and Cost Burden Estimates

Table 1 below illustrates the incremental annual compliance burden of the collection of information in hours and in cost for proxy and information statements and current reports under

333 We estimate that 326 nominating shareholders or groups will submit nominations pursuant to Rule 14a-11, applicable state law provisions or a company's governing documents. As noted earlier, approximately 32 proxy contests were conducted in 2008. Of the 326 nominating shareholders or groups, we believe that 32 will have obtained EDGAR filer codes previously, therefore we estimate approximately 294 will need to file a Form ID. This results in an estimate of 90%.

334 We currently estimate the burden associated with Form ID is 0.15 hours per response.

the Exchange Act. The burden was calculated by multiplying the estimated number of responses by the estimated average number of hours each entity spends completing the form. We estimate that 75% of the burden of preparation of the proxy and information statement and current reports is carried by the company internally, while 25% of the burden of preparation is carried by outside professionals at an average cost of $400 per hour. We estimate that 75 percent of the burden of preparation of Schedule 14N and Schedule 14A (with regard to the legend required for additional soliciting materials) will be carried by the nominating shareholder or group internally and that 25 percent of the burden of preparation will be carried by outside professionals retained by the nominating shareholder or group. We estimate that 25 percent of the burden of preparation of Schedule 13G (for nominating shareholder groups that exceed 5%) will be carried by the nominating shareholder or group internally and that 75 percent of the burden of preparation will be carried by outside professionals retained by the nominating shareholder or group. The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried internally by the company and nominating shareholder or group is reflected in hours.

Table 1: Calculation of Incremental PRA Burden Estimates*

	Current Annual Responses (A)	Proposed Annual Responses (B)	Current Burden Hours (C)	Increase in Burden Hours (D)	Proposed Burden Hours (E) =C+D	Current Professional Costs (F)	Increase in Professional Costs (G)	Proposed Professional Costs =F+G
Sch 14A	7,300	7,300	555,683	14,692	570,375	$63,709,987	$1,958,760	$65,668,747
Sch 14C	680	680	52,337	1,632	53,969	$5,951,639	$217,640	$6,169,279
Sch 14N	0	269	0	28,565	28,565	0	$3,808,600	$3,808,600
Form 8-K	108,424	109,465	406,590	3,904	410,494	$54,212,000	$520,500	$54,732,500
Form ID	65,700	65,994	9,855	44	9,899	$0	0	0
Sch 13G	12,500	12,546	25,577	484	26,061	$42,694,200	$580,320	$43,274,520
Rule 20a-1	1,225	1,225	130,095	4,085	134,180	$18,375,000	$544,600	$18,919,600
Total				53,406			$7,630,420	

* The incremental burden estimate for Rule 20a-1 includes the disclosure that would be required on Schedule 14A and 14C, discussed above, with respect to funds.

E. Solicitation of Comment

We request comment on the accuracy of our estimates. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments to: (i) evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission's estimate of burden of the proposed collection of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) evaluate whether there are ways to minimize the burden of the collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

We request comment and supporting empirical data for purposes of the PRA on:

- how likely it would be for shareholders or groups to be able to meet the requirements under proposed Rule 14a-11;

- in how many instances qualifying shareholders or groups would use Rule 14a-11 to include disclosure concerning a nominee or nominees in a company's proxy materials;
- how many nominees qualifying shareholders or group might offer; and
- whether there would be an increase in the number of shareholder proposals submitted pursuant to Rule 14a-8 that companies receive as a result of the proposed amendments.

Any member of the public may direct to us any comments concerning the accuracy of these burden estimates and any suggestions for reducing these burdens. Persons submitting comments on the collection of information requirements should direct the comments to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should send a copy to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090, with reference to File No. S7-10-09. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-10-09, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, 100 F Street, NE, Washington, DC 20549-0213. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this release. Consequently, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

V. COST-BENEFIT ANALYSIS

A. Background

The Commission is proposing new rules that would, under certain circumstances, require companies to include in their proxy materials shareholder nominees for election as director, as well as other disclosure regarding those nominees and the nominating shareholder or group. In addition, the new rules would require companies to include in their proxy statements, under certain circumstances, shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11. The proposed rules are intended to remove certain impediments that the federal proxy process currently impose on shareholders' ability to exercise their state law right to nominate directors, and thereby reduce the costs to shareholders of exercising their rights. Below, we describe the additional disclosures shareholders would receive if the proposed rules are adopted and the direct and indirect economic effects of such new disclosures. Our discussion of the economic effects takes into account the incentives and actions of parties who would be able under the rulemaking to affect its scope and influence. These parties include shareholders, the board, and state legislatures.

Proposed Rule 14a-11 would require companies, where applicable, to include disclosures of shareholder nominations for director and disclosure about the nominating shareholder or group and the nominee or nominees in company proxy materials if, among other things, the nominating shareholder or group meets the requisite ownership threshold and has held the shares for at least one year prior to the date the shareholder provides notice on Schedule 14N of its intent to require the company to include a nominee or nominees in the company's proxy materials pursuant to Rule 14a-11. The nominating shareholder or group also would be required to represent that he or she intends to hold the shares through the date of the meeting. A nominating shareholder that includes a nominee or nominees in a company's proxy materials pursuant to Rule 14a-11 would be required to provide to the company, in its notice on Schedule 14N, disclosure similar to the disclosure required in a proxy contest.[335] Pursuant to proposed Item 7(e) of Schedule 14A (and, in the case of registered investment companies and business development companies, proposed Item 22(b)(18) of Schedule 14A), the company would be required to include the information in its proxy materials, where applicable. In addition, the proposed rules would enable shareholders to engage in limited solicitations to form nominating shareholder groups and engage in solicitations in support of their nominee or nominees without disseminating a proxy statement.[336]

The Commission also is proposing an amendment to Rule 14a-8 to narrow the exclusion in paragraph (i)(8), which addresses director elections. Under the proposed amendment, the company would not be permitted to rely on Rule 14a-8(i)(8) to omit from its proxy statement a shareholder proposal that would amend, or that requests an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, although any such proposals that conflict with proposed Rule 14a-11 or state law could still be excluded from the company's proxy materials. The current procedural requirements for submitting a proposal pursuant to Rule 14a-8 would remain the same.

No additional disclosures would be required from any shareholder that submits such a proposal; however, a nominating shareholder that includes a nominee or nominees in a company's proxy materials pursuant to an applicable state law provision or the company's governing documents would be required to provide to the company, in its notice on Schedule

335 See proposed Rule 14a-18.

336 See proposed Rule 14a-2(b)(7) – (8).

14N, disclosure similar to the disclosure required in a proxy contest.[337] Pursuant to proposed Item 7(f) of Schedule 14A (and, in the case of registered investment companies and business development companies, proposed Item 22(b)(19) of Schedule 14A), the company would be required to include the information in its proxy materials. We believe this information will provide shareholders with information that is useful to an informed voting decision.

The direct effect of proposed Rule 14a-11 and the related disclosure requirements would be to reduce shareholders' cost of nominating directors, which can otherwise be prohibitive since, to be successful, shareholders generally must conduct their own proxy contest. The amendments would do so without eliminating the traditional method of conducting a proxy contest. Therefore, were these amendments to become effective, the first-order economic effect would be that shareholders seeking to nominate directors may choose to move away from soliciting their own proxies for their nominees and instead require the company to include their nominee or nominees in the company proxy materials. The second-order economic effect would be that, due to the lowered cost of effectively nominating directors, where applicable, there may be an increase in shareholder nominees for director.

The amendment to Rule 14a-8(i)(8) would narrow the exclusion and no longer permit a company to exclude shareholder proposals that would amend, or request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations could result in additional shareholders being able to submit nominees for inclusion in a company's proxy materials, if approved by shareholders. Using Rule 14a-8 in this way could result in a two-year process to gain access to a company's proxy materials. The two-year process could result in different economic effects to those discussed above for proposed

337 See proposed Rule 14a-19 and Rule 14n-1.

Rule 14a-11, depending on the proponent's success (e.g., the inclusion of the proposal in the company's proxy materials and adoption of a binding bylaw proposal by appropriate shareholder vote), and the likelihood that the proponent would initiate the two-year process. The likelihood that the proponent would initiate the two-year process could be limited by the costs of the procedure arising from the additional time (including opportunity costs of holding securities where the shareholder may consider the company's board composition to be sub-optimal) and the risk of failure.[338]

The extent of the economic effect of proposed Rule 14a-11 and the related disclosure requirements may be affected by several factors. These factors include future possible actions by boards and states. They also include limits on the number of shareholder director nominees that must be disclosed in the company's proxy materials. Another relevant factor is how the requirement that a shareholder that intends to rely on proposed Rule 14a-11 may not be holding the securities it owns in the company "for the purpose of or with the effect of changing control" of the company would be applied in practice.

In the case of the proposed amendments to Rule 14a-8, future actions of boards may affect applicability of the rule. If Rule 14a-8(i)(8) is amended as proposed, a company would not be permitted to exclude a shareholder proposal that would amend, or that requests an amendment to, a company's governing documents to address shareholder nomination procedures or disclosures related to shareholder director nominations. It is reasonable to expect that at least some shareholders will submit this type of proposal – shareholder groups may be most likely to attempt to take this action when they perceive that the board does not currently represent their interests. Even if these proposals are no longer excludable pursuant to Rule 14a-8(i)(8),

338 In this regard, we note that we are proposing new rules that would require a shareholder submitting a nominee or nominees pursuant to an applicable state law provision or a company's governing documents to provide disclosure similar to what is required currently in a proxy contest.

companies may submit a no-action request to exclude these shareholder proposals from the proxy statement pursuant to other procedural or substantive bases for exclusion. In contrast, we believe that applicability of proposed Rule 14a-11 is not likely to be affected by future actions of companies, because it is our understanding that under existing state laws companies generally may not prohibit shareholders from nominating directors.[339]

Future actions of the states also could affect the applicability of the proposed amendments. Proposed Rule 14a-11, for instance, would not apply to companies incorporated in states that prohibit nominations of directors by shareholders or permit companies to prohibit such nominations and where the company's governing documents do so. Additionally, the proposed rule requires that the nominee's board candidacy and membership be consistent with state law. Under Rule 14a-8, shareholder proposals must be proper subjects for action by shareholders under state law. States may have incentives to affect the director nomination process, and these incentives may lead them to consider changes that could affect the availability of proposed Rule 14a-11 or Rule 14a-8. To the extent that states change their laws, for example, to prohibit the nomination of directors by shareholders, proposed Rule 14a-11 and Rule 14a-8 would apply less broadly.

The application of the term "changing control" affects the shareholders that may rely on the proposed amendments to require disclosure of their board nominees. The certification by the nominating shareholder or group on Schedule 14N that it does not hold the securities it owns in the company with the purpose or effect of changing control of the company will limit the shareholders that can use the procedure in proposed Rule 14a-11. Whether this requirement applies to a nominating shareholder or group will depend, however, on the facts and

339 We are not aware of any state laws that do so, but we seek comments on whether states currently have any prohibitions on shareholders' right to nominate directors, and whether, to the extent such a right is not explicitly allowed, shareholders are presumed to have nomination rights.

circumstances of each nominating shareholder or group. It is certainly not the Commission's intent that this requirement would restrict shareholders from using the new rule merely because it is nominating directors pursuant to the new rule. Nevertheless, other factors in addition to the nomination may support a finding of control.

The economic effects of the proposed rulemaking also are affected by the requirement that shareholders cannot nominate more than a maximum of one director or 25% of the existing board. In addition to this direct requirement, the cap on shareholder nominees may have additional, indirect implications for the economic effects of proposed Rule 14a-11. First, the number of shareholder nominees that can be included in the company's proxy materials overall is limited. If one shareholder or group nominates the maximum allowable number of candidates, any other shareholder's or group's nominees are not required to be disclosed in the same proxy statement. Second, if the maximum allowable number of existing shareholder nominees is currently in place on the board, additional shareholder nominees are not required to be disclosed in the proxy statement. Third, boards seeking to limit the effect of shareholder nominated directors under the proposed rule may, in some instances, choose to expand the board size to dilute, to an extent, those directors.[340]

Below we consider the benefits and costs of these economic effects of the proposed amendments.

B. Benefits

We anticipate that the proposals, where applicable, would result in (1) a reduction in the

340 As an example, a board of eight with two new shareholder-nominated directors, may expand to up to 11, diluting the influence of the shareholder-nominated directors without expanding the number of director slots for which they must place shareholder-nominated directors in the proxy statement because the proposed 25% limits in proposed Rule 14a-11 would include a provision allowing companies to round down the number of directors.

cost to shareholders of soliciting votes in support of a nominated candidate for election to the board of directors; (2) improved disclosure of shareholder nominated director candidates; (3) potential improved board performance; and (4) enhanced ability for shareholders and companies to adopt their preferred shareholder nomination procedures.

1. Reduction in Costs Related to Shareholder Nominations

Generally, a shareholder who attempts to nominate directors must conduct a proxy contest in which the shareholder is responsible for collecting information, preparing proxy materials with required disclosures concerning the director nomination, and mailing the proxy materials to each shareholder solicited. A shareholder conducting a proxy contest incurs large costs involved with preparing a proxy statement and soliciting on behalf of his or her nominee.[341] The costs can make it prohibitively expensive for shareholders to exercise their state law rights to nominate and elect directors. In addition, collective action concerns may discourage any one shareholder or group from assuming such costs for the benefit of other shareholders.[342]

Proposed new Rule 14a-11 would reduce both the direct and indirect costs of the proxy solicitation process. In particular, proposed new Rule 14a-11 would allow shareholders to avoid the direct costs of conducting a proxy contest and would mitigate collective action and free rider concerns that otherwise may deter many shareholders from engaging in a traditional proxy contest. In regard to the latter, the proposed rule changes would likely ameliorate the need for collective action among shareholders, because qualifying shareholders will have direct access to a company's proxy materials to more effectively nominate directors. To the extent that

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341 As noted in footnote 303, above, in 2008 there were at least 32 contested elections.

342 See, e.g., Lynn A. Stout, The Mythical Benefit of Shareholder Control, 93 VA. L. REV. 789, 789 (2007) ("In a public company with widely dispersed share ownership, it is difficult and expensive for shareholders to overcome obstacles to collective action and wage a proxy battle to oust an incumbent board."), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=978775.

shareholders substitute use of Rule 14a-11 for engaging in traditional election contests, the proposal could also help companies avoid potential disruptions and the diversion of resources resulting from traditional proxy contests that might take place in the absence of the proposed amendments. Because the level of this benefit is affected by the extent to which shareholders make such substitutions, it is also checked by the extent that use of proposed Rule 14a-11 is not a perfect substitute for traditional election contests. For example, the proposed rule restricts the number of shareholder director nominees that a company would be required to include in its proxy materials and the proposed rule would be available only to shareholders that do not hold the securities in the company with the purpose of, or with the effect of, changing control of the company. These elements of the proposed rule impose restrictions that are not present in a traditional proxy contest. Proxy contests also would still be available where shareholders have a control intent.

According to a study of proxy contests conducted during 2003, 2004, and 2005, the average cost to a soliciting shareholder of a proxy contest is $368,000.[343] The costs included those associated with proxy advisors and solicitors, processing fees, legal fees, public relations, advertising, and printing and mailing.[344] Approximately 95% of the cost was unrelated to printing and postage.[345] The cost of printing and postage averaged approximately $18,000.[346] Based on this information, we estimate that a shareholder using proposed Rule 14a-11 to submit a nominee or nominees for director to be included in a company's proxy statement will save at least $18,000 on average and may save more as a result of being able to use the company's proxy

343 See comment letter from Automatic Data Processing, Inc. (April 20, 2006) on File No. S7-10-05.

344 See id.

345 See id.

346 See id.

materials to solicit other shareholders. The nominating shareholder or group may or may not engage in public relations and advertising, or engage proxy solicitors, therefore, the extent of any cost savings may be greater.

The benefits of this reduction in costs also may be enhanced to the extent that companies' governing documents are modified to allow inclusion of additional shareholder nominees for director in company proxy materials. The instances of such changes in provisions in governing documents may increase as a result of the proposed amendment to Rule 14a-8(i)(8) to preclude companies from excluding proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11.

2. Improved Disclosure of Shareholder Nominated Director Candidates

The proposed new disclosure requirements in Rules 14a-11, 14a-18, and 14n-1 would require additional information to be provided on Schedule 14N, including certifications by shareholders who submit a nominee under proposed Rule 14a-11 about the nominee's independence, and disclosure of the information similar to that currently required in a proxy contest regarding the nominating shareholder and nominee. Proposed Rules 14a-19 and 14n-1 would require similar disclosures when a shareholder uses an applicable state law provision or company's governing documents to include shareholder nominees for director in the company's proxy materials. The information provided by such certifications and disclosures would help provide transparency to shareholders in voting on shareholder nominees for director and therefore may lead to better informed voting decisions. The information also will provide consistent and comparable information about shareholder nominated candidates across companies. With respect to Rule 14a-8(i)(8), companies have been permitted to exclude proposals to establish procedures to include shareholder nominees in company proxy materials. The Commission was concerned that allowing such proposals would result in contested elections without the disclosure that otherwise would be required in a traditional proxy contest.[347] The proposed disclosure requirements are designed to address that concern.

3. Potential Improved Board Performance and Company Performance

Both proposed Rule 14a-11 and the amendments to Rule 14a-8(i)(8) may result in improved company performance, arising from improvements in board performance. First, both proposals, by increasing the chances of a shareholder-nominated director to be elected to the board, may increase the potential for incumbent directors to face closer scrutiny from outsiders. Faced with this new prospect, incumbent directors may work more diligently to signal their value to the company through efforts to improve the performance of the board and, relatedly, the company.[348] Company performance may improve to the extent some directors are replaced by other directors whose actions are better aligned with the interests of shareholders.[349] Even where

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347 See Shareholder Proposal Proposing Release (proposing amendments to Rule 14a-8 to "make clear that director nominations made pursuant to [bylaw amendments concerning shareholder nominations of directors] would be subject to the disclosure requirements currently applicable to proxy contests" and noting that such disclosure is of "great importance" to an informed voting decision by shareholders).

348 The academic literature indicates the benefit to shareholders of having an independent, active and committed board of directors. See, e.g., Fitch Ratings, "Evaluating Corporate Governance" (December 12, 2007), available at: http://www.fitchratings.com/corporate/reports/report_frame.cfm?rpt_id=363502. Moreover, empirical evidence has indicated that the ability of significant shareholders to hold corporate managers accountable for activity that does not benefit investors may reduce agency costs and increase shareholder value. See, e.g., Brad M, Barber, "Monitoring the Monitor: Evaluating CalPERS' Activism" (November 2006), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=890321. See also Deutsche Bank, Global Equity Research, "Beyond the Numbers: Corporate Governance in Europe," (March 5, 2005).

349 See, e.g., Chris Cernich, et al., "Effectiveness of Hybrid Boards," IRRC Institute for Corporate Responsibility (May 2009) available at: http://www.irrcinstitute.org/pdf/IRRC_05_09_EffectiveHybridBoards.pdf (finding that in a study of 120 "hybrid" boards – boards formed when activist shareholders, through actual or threatened proxy contests, were able to elect dissident directors but not gain control of the entire board – such boards increased shareholder value at ongoing companies by 19.1% (16.6 percentage points more than peers) from the contest period through the board's one-year anniversary).

incumbents are not replaced, the requirements of the rule can lead to greater accountability on the part of incumbent directors. The level of board accountability will depend on the extent to which directors see a close link between their performance and the prospect of removal.[350]

Similarly, the inclusion in company proxy materials of shareholder nominees for director under proposed Rule 14a-11, or the possibility of shareholder nominees being included in company proxy materials pursuant to shareholder-initiated amendments to a company's governing documents permitted by the proposed amendments to Rule 14a-8, may enhance the quality of the shareholders' voice and result in a board whose interests are better aligned with shareholders' interests.[351]

Second, the possibility of shareholder nominated candidates being submitted for inclusion in a company's proxy materials, as well as the possibility of the shareholder nominee's election, may lead to enhanced board performance. If the proposed rules are adopted, the responsiveness of boards may increase in an effort to alleviate concerns expressed by shareholders on certain matters and thereby avoid shareholders submitting nominees pursuant to the new rules. The board may feel a need to be more attentive to the company's operations as a result of this enhanced accountability to shareholders. In addition, having a shareholder-

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350 The current proposal, by facilitating a reduction in the cost of nominating "outside" directors, would create a new threat of removal to incumbent directors, which can bring about increased accountability that would benefit investors. Economists have put forth theory and evidence on the link between incentives that are associated with accountability and performance. See, e.g., Benjamin E. Hermalin and Michael S. Weisbach, "Endogenously Chosen Board of Directors and Their Monitoring of the Board" 88 American Economic Review 96 (1998), available at: http://129.3.20.41/eps/mic/papers/9602/9602001.ps.gz. Milton Harris and Artur Raviv "Control of Corporate Decisions: Shareholders vs. Management" (May 29, 1998), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=965559.

351 Published research has reported that when chief executive officers are more involved in the nomination of independent directors, stock price reactions to independent director appointments are significantly lower, and companies appoint fewer independent directors. See Anil Shivdasani & David Yermack, "CEO Involvement in the Selection of New Board Members: An Empirical Analysis," 54 J. Finance 1829 (1999). This evidence is consistent with the idea that limiting total management control of the nomination process improves accountability.

nominated director elected to and serving on the board may increase the transparency in boards' decision-making process, which would make it easier for shareholders to monitor the board. This increased monitoring could enhance board performance and ultimately lead to improved corporate performance.[352]

Third, increasing shareholders' access to company proxy materials for the inclusion of shareholder nominees for director may result in a larger pool of qualified director nominees to choose from. To the extent that a company does not include shareholder nominees for director in its proxy materials, thereby reducing the pool of qualified nominees, an opportunity cost may be incurred by the company and thus the shareholders. Therefore, proposed Rule 14a-11 may reduce the opportunity costs to companies and shareholders.

4. Enhanced Ability for Shareholders and Companies to Adopt Procedures

The proposed amendment to Rule 14a-8(i)(8) also may facilitate shareholders and companies working together to tailor companies' governing documents to suit the specific interests of the company and its shareholders. The proposed amendment would allow shareholders to use Rule 14a-8 to submit proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, as long as the proposal does not conflict with Rule 14a-11. This may provide shareholders a more effective voice than simply being able to recommend candidates to the nominating committee or being able to nominate candidates in person at a shareholder meeting.

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[352] One benefit of corporate transparency is that it reduces information differences between the entities (e.g., the board of directors and the shareholders), and hence lowers the cost of trading the firm's securities and the firm's cost of capital. See, e.g., Diamond, Douglas W. and Robert E. Verrecchia, "Disclosure, Liquidity, and the Cost of Capital," Journal of Finance, September 1991, 46 (4), 1325–1359. For empirical evidence, see, e.g., Christian Leuz and Robert E. Verrecchia, "The Economic Consequences of Increased Disclosure," Journal of Accounting Research, 2000, 38 (supplement), 91–124.

The overall benefit of allowing shareholders to include director nominees in a company's proxy materials may depend on the extent to which shareholders choose to exercise their rights and on shareholders' perception of the merits of the nominees that are advanced by nominating shareholders.

C. Costs

We anticipate that the amendments, where applicable, may result in costs related to (1) potential adverse effects on company and board performance; (2) potential complexity of the proxy process; and (3) preparing the required disclosures, printing and mailing, and costs of additional solicitations.

1. Costs Related to Potential Adverse Effects on Company and Board Performance

The proposals would impose some direct costs on the companies that would be subject to the new rules. These costs would arise from potential changes to corporate behavior and potential lower board quality.

Most, if not all, companies have director nomination procedures. The proposed changes may lead some companies to incur costs associated with re-examining those procedures, especially if the company is subject to, or thinks it likely will be subject to, shareholder nominated director candidates. Companies accustomed to uncontested director elections may incur costs of adjusting their practices.[353] Further, the possibility of contested director elections may adversely influence corporate behavior. To the extent that incumbent board members may feel a greater need to respond to shareholders' various concerns, the board may incur costs in attempting to institute policies and procedures they believe will address shareholder concerns. It

353 See, e.g., comment letter on the 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from the U.S. Chamber of Commerce (October 2, 2007) ("Chamber 2007").

is possible that the time a board spends on shareholder relations could reduce the time that it would otherwise spend on strategic and long-term thinking and overseeing management, which may negatively affect shareholder value.[354] These costs are limited by the extent to which the additional communication results in better decision-making by the board, as well as shareholders' understanding that the board's time and other resources are in scarce supply and take these considerations into account in deciding to nominate directors.

In addition, the rule proposals could, in some cases, result in lower quality boards.[355] If a shareholder nominee is elected and disruptions or polarization in boardroom dynamics occur as a result, the disruptions may delay or impair the board's decision-making process.[356] In companies in which boards are already well-functioning, dissent can be counterproductive and could delay the board's decision-making process. Such a delay or impairment in the decision-making process could constitute an indirect economic cost to shareholder value.

Companies may expend more resources on efforts to defeat the election of shareholder

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354 See, e.g., Stout, footnote 342, above, at 792 ("Perhaps the most obvious [economic function of board governance] is promoting more efficient and informed business decisionmaking. It is difficult and expensive to arrange for thousands of dispersed shareholders to express their often-differing views on the best way to run the firm."); see generally Stephen M. Bainbridge, Director Primacy and Shareholder Disempowerment, 199 HARV. L. REV. 1, 25-27 (2006) (discussing how concern for accountability may undermine decision making discretion and authority). But see Lucian Arye Bebchuk, The Case for Increasing Shareholder Power, 118 HARV. L. REV. 833, 883 (2005) ("[M]ere recognition that back-seat driving might sometimes be counter-productive is hardly sufficient to mandate general deference to management. Such mandated deference would follow only if one assumes that shareholders are so irrational or undisciplined that they cannot be trusted to decide for themselves whether deference would best serve their interests."). See also, comment letter on the 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from ABA 2007.

355 See, e.g., comment letter on the 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from Chamber 2007; Stephen M. Bainbridge, "A Comment on the SEC Shareholder Access Proposal" (November 14, 2003) at 17, available at: http://ssrn.com/abstract=470121 ("The likely effects of electing a shareholder representative therefore will not be better governance. It will be an increase in affectional conflict . . . . It will be a reduction in the trust-based relationships that causes horizontal monitoring within the board to provide effective constraints on agency costs.").

356 See, e.g., comment letter on the 2007 Proposals (SEC File Nos. S7-16-07 and S7-17-07) from Society of Corporate Secretaries & Governance Professionals (October 5, 2007).

nominees for director. Commenters have drawn attention to the potential to turn every director election into an election contest.[357] This may be the case, for instance, if company directors determine to spend company resources to defeat shareholder nominees they believe are not in the best interests of the company (or for other reasons).[358] Such a reaction could discourage qualified board members from running. This potential would be limited by shareholders' understanding that board dynamics can be important, and that changing them may not always be beneficial. It also would be limited to the extent that company directors do not seek to substitute their judgment for the judgment of the shareholders when the question is who should comprise the board of directors.[359] We also have assumed that boards generally would be cautious in expending resources to defeat shareholder nominees insofar as incumbent board members generally are interested in the outcome of elections and in the corporation's policy in connection with opposing shareholder nominees. Nevertheless, to the extent that company directors make large expenditures to defeat shareholder nominees, those expenditures would represent a cost to

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357 See 2003 Summary of Comments and comment letters from ASCS and McKinnell, BRT.

358 See 2003 Summary of Comments; see also comment letters from ABA; Charlotte M. Bahin, ACB; The Allstate Corporation (December 23, 2003) ("Allstate"); Ashland; Richard H. Ayers (November 18, 2003) ("Ayers"); Callaway Golf Company (December 22, 2003) ("Callaway"); Caterpillar, Inc. (December 17, 2003) ("Caterpillar"); Cigna Corporation (January 2, 2004) ("Cigna"); ConocoPhillips (October 3, 2003) ("ConocoPhillips"); Cummins, Inc. (November 23, 2003) ("Cummins"); Debevoise & Plimpton (December 17, 2003); Exelon Corporation (December 22, 2003) ("Exelon"); FirstEnergy Corp. (December 10, 2003) ("FirstEnergy"); Ganske, Kelley & Profusek; General Mills (December 19, 2003); Roger L. Howe (November 26, 2003); Reed Hundt (December 16, 2003); International Paper (December 22, 2003); Letter Type D (representing 8 individuals or entities); Letter Type H (representing 7 individuals or entities); Letter Type N (representing 38 individuals or entities); Letter Type Q (representing 4 individuals or entities); McDATA Corporation (December 22, 2003) ("McDATA"); Pfizer, Inc. (December 11, 2003) ("Pfizer"); MDU Resources (December 22, 2003) ("MDU"); Malcolm S. Morris (November 6, 2003); National Association of Corporate Directors (March 26, 2004) ("NACD"); Office Depot, Inc. (December 22, 2003); Kerr-McGee Corporation (December 22, 2003); Progress Energy (December 22, 2003); Tribune Company (December 18, 2003); and Wachtell.

359 Cf. Blasius Indus. v. Atlas Corp., 564 A.2d 651, 663 (Del. Ch. 1988) (stating that "[although the] premise [that the board knows better than do the shareholders what is in the corporation's best interest] is no doubt true for any number of matters, it is irrelevant (except insofar as the shareholders wish to be guided by the board's recommendation) when the question is who should comprise the board of directors.").

shareholders. An additional cost could arise from the potential placement of directors who have insufficient experience or capabilities to serve effectively, as some commenters have suggested.[360] But to the extent that shareholders understand that experience and competence are important director qualifications, any associated costs may be limited.

Finally, the proposals could introduce a cost to shareholders to the extent that the nomination procedure is used by shareholders to promote an agenda that conflicts with other shareholders' interests. For example, it would be possible for an investor to try to maximize his private gains through board decisions at the expense of other shareholders.[361] This cost, however, is limited to the extent these nominees would be required to make certain disclosures designed to elicit their interests and relationships, and must ultimately be elected by the shareholders.[362]

2. Costs Related to Potential Complexity of Proxy Process

Under the proposed amendments, the process of determining which shareholder director nominee will be on the form of proxy and the limitations on the number of shareholder-nominated directors to appear in the company's proxy materials and eventually serve on the board may create a degree of complexity. If several shareholders or groups desire (and qualify) to nominate the maximum number of directors they are allowed to place in the company's proxy materials, only the first shareholder or group to submit a Schedule 14N will succeed. Additionally, under proposed Rule 14a-11, if the maximum allowable number of shareholder

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360 See, e.g., comment letter from Exelon Corporation (December 22, 2003) on the 2003 Proposal.

361 See, e.g, Stout, footnote 342 above, at 794 ("[B]y making it easier for large shareholders in public firms to threaten directors, a more effective shareholder franchise might increase the risk of intershareholder "rent-seeking" in public companies.").

362 See, e.g., Bebchuk, note 354 above, at 883 (arguing that proposals by special interest shareholders are generally unlikely to be adopted by the majority).

nominees is currently serving on the board, a company would not be required to include additional shareholder nominees in the company's proxy materials.

Under the proposed amendments to Rule 14a-8, shareholders would need to wait for two proxy seasons to utilize the particular procedures and disclosures adopted through a shareholder proposal under Rule 14a-8 – the first season to establish a shareholder director nomination procedure and the second season to nominate and elect directors.

These sources of complexity and any uncertainty that may arise in implementing the proposed amendments could result in costs to companies, to shareholders seeking to nominate directors, and to shareholder director nominees. For example, both companies and shareholders could incur costs to seek legal advice in connection with shareholder nominations submitted pursuant to Rule 14a-11, the inclusion of shareholder nominees in company proxy materials, and the process for submission of a notice of intent to exclude a nominee or nominees included in the rule.[363] A company that receives a shareholder nomination for director has no obligation to make a submission under Rule 14a-11 unless it intends to exclude the nominee from its proxy materials. Companies and shareholders also could incur costs to seek legal advice in connection with shareholder proposals submitted pursuant to Rule 14a-8 and the notice of intent to exclude process related to it. A company that receives a shareholder proposal has no obligation to make a submission under Rule 14a-8 unless it intends to exclude the proposal from its proxy materials. To the extent disputes on whether to include particular nominees or proposals are not resolved internally, companies and/or shareholders might seek recourse in courts, which would increase costs.

The proposed amendments to Rule 14a-8 would no longer permit companies to exclude

363 For example, the comment letter from ASCS on the 2003 Proposal estimated based on survey results that the cost of outside counsel in connection with opposing a shareholder nominee and supporting the company's nominees for directors would be 59.4 hours and $44,460.

from their proxy materials proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11. Expanding the types of proposals permitted under Rule 14a-8 may increase the number of shareholder proposals submitted to companies. This would likely result in increased costs to the company related to reviewing and processing such proposals to determine matters such as shareholder eligibility, and whether there is a basis for excluding the proposal under Rule 14a-8. In this regard, in a comment letter submitted in connection with the 2003 Proposal, a commenter submitted information from a survey conducted about the costs associated with including a shareholder proposal in the company's proxy materials, estimating that preparation and submission of a notice of intent to exclude the proposal to the SEC regarding a shareholder proposal would average 65 hours per proposal.[364] For purposes of PRA, we estimate that shareholders will submit approximately 97 proposals regarding nomination procedures or disclosures related to director nominations to companies per year. Assuming that 90% of companies prepare and submit a notice of intent to exclude these proposals, the resulting costs to companies would result in approximately 4,241 hours and $565,500 for the services of outside professionals. Alternatively, such costs could decrease to the extent that proposed Rule 14a-8 provides a clearer indication of which proposals are excludable.

3. Costs Related to Preparing Disclosure, Printing and Mailing and Costs of Additional Solicitations

The proposals may impose additional direct costs on companies and shareholders subject to the new rules, related to the preparation of required disclosure, printing and mailing costs and

[364] See 2003 Summary of Comments; see also letter from McKinnell, BRT (providing information from surveys conducted of BRT and ASCS members). See also footnote 311, above.

costs of additional solicitations that may be undertaken as a result of including one or more shareholder nominees for director in the company proxy materials.

For purposes of the PRA analysis, we estimate that the disclosure burden of the proposed amendments to reporting companies (other than registered investment companies) is 15,652 hours of personnel time and $2,087,000 for services of outside professionals. We also estimate for purposes of the PRA analysis that the disclosure burden to shareholders of the proposed amendments will be 31,865 hours of shareholder time and $4,758,420 for services of outside professionals. For registered investment companies, we estimate for purposes of the PRA analysis that the burden of the proposed amendments will be 5,888 hours of company time and $785,000 for the services of outside professionals.

Companies would incur additional printing and mailing costs to include shareholder nominees in the company's proxy materials pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents as a result of the proposed amendment to Rule 14a-8(i)(8).[365] These incremental printing and mailing costs could include the expense of adding the name and background information of shareholder nominees for director in their proxy materials as well as the increased weight of a company's proxy materials. The printing and mailing costs would increase as the number of shareholder nominees to be included in the company proxy materials increases. As noted above, this may result in a decrease in costs to shareholders that would have to conduct proxy contests in the absence of proposed Rule 14a-11, but may increase the costs for companies. The increased costs for companies may not be as

365 We note that these increased costs may be less for companies using notice and access. See Internet Availability of Proxy Materials, Release No. 34-55146 (January 22, 2007) ("Internet Proxy Availability Release").

much as would otherwise result if that shareholder engaged in a proxy contest.[366]

Companies also would incur printing and mailing costs with respect to the inclusion of a shareholder proposal related to changes to the company's governing documents regarding inclusion of shareholder nominees in company proxy materials. We have two sources of information estimating such costs. According to the information provided by one commenter, the average cost to a company to print and mail one shareholder proposal in its proxy materials is $15,324 and 34 hours.[367] The responses to a questionnaire that the Commission made available in 1997 relating to 1998 amendments to Rule 14a-8, however, suggest such costs to the companies responding averaged $50,000.[368] As noted above, we believe that the proposed amendment to Rule 14a-8(i)(8) could result in an additional 38 shareholder proposals submitted annually.[369] Based on this information, for purposes of our analysis, we assume printing and

366 One commenter on the 2003 Proposal estimated that a Rule 14a-11 contest would cost a company approximately one-third what a full proxy contest costs. See comment letter from Bainbridge. Based on this assumption, this commenter estimated, relying on data from a late 1980s survey, that the costs of such a contest to a public company would be $500,000. This commenter also cited data estimating companies' annual expenditures on Rule 14a-8 shareholder proposals to be $90 million. While this commenter noted that it is unlikely that there will be as many Rule 14a-11 election contests as Rule 14a-8 shareholder proposals, the commenter asserted that incumbent boards are likely to spend considerably more on opposing each Rule 14a-11 contest than on opposing a Rule 14a-8 shareholder proposal. This commenter estimated that $100 million may be an appropriate estimate for the lower boundary of the range within which Rule 14a-11's direct costs will fall. By contrast, another commenter estimated that under current rules the total cost of proxy contests for companies would exceed $15 million. See comment letter from McKinnell, BRT in connection with the 2003 Proposal (estimate was based on data provided in response to a 2003 survey of members of the Business Roundtable and the American Society of Corporate Secretaries).

367 See ASCS letter. We also note that these increased costs may be less for companies using notice and access. See Internet Proxy Availability Release.

368 In the adopting release for the amendments to Rule 14a-8 in 1998, we noted that responses to a questionnaire we made available in February 1997 suggested the average cost spent on printing costs (plus any directly related costs, such as additional postage and tabulation expenses) to include shareholder proposals in company proxy materials was approximately $50,000. The responses received may have accounted for the printing of more than one proposal.

369 We estimated that approximately 97 proposals would be submitted regarding nomination procedures or disclosures related to nomination procedures, however, our estimate assumed that 59 proposals that otherwise would have been submitted on other governance topics would instead relate to nomination procedures or disclosures related to nomination procedures. Assuming the 59 proposals would already be accounted for in companies' costs, we estimate that 38 additional proposals would be submitted to

mailing costs of one shareholder proposal in a company's proxy materials could be in the range of approximately $15,000 to $50,000. Assuming each of these proposals were included in company proxy materials, it could result in a total cost of approximately $570,000 to $1,900,000 for the affected companies.

The proposed rules also would present direct costs due to disclosure requirements. For example, companies that determine that they may exclude a shareholder nominee are required to provide a notice to the nominating shareholder or group regarding any eligibility or procedural deficiencies in the nomination and provide to the Commission notice of the basis for its determination.[370] Nominating shareholders or groups and the nominees also would be required to disclose information about themselves, which may be costly.[371] Most of this disclosure will be provided by the nominating shareholder or group in the notice to the company, which would be filed on new Schedule 14N. The Schedule 14N also would include information regarding the length of ownership, certifications, and other information.

We also anticipate the possibility of increased direct costs associated with additional solicitations by both companies and shareholders. Companies may increase solicitations to vote against shareholder proposals or to vote for their slate of directors. Shareholders may increase solicitations to vote for shareholder proposals, to withhold votes for a company's nominees for director, or to vote for the shareholder nominee or nominees. In addition, companies may face additional costs for solicitations if shareholders or groups submit nominees for inclusion in

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companies annually.

370 For purposes of the PRA analysis, we estimate these disclosure requirements would result in 2,633 burden hours of company time, and $351,000 for services of outside professionals.

371 For purposes of the PRA analysis, we estimate the Schedule 14N disclosure requirements for shareholders submitting nominees pursuant to Rule 14a-11 or a company's governing documents would result in a total of 28,565 hours of shareholder time and $3,808,600 for services of outside professionals.

company proxy materials pursuant to Rule 14a-11, an applicable state law, or a company's governing documents.

D. Small Business Issuers

Based on our staff's review of Rule 14a-8 shareholder proposals, it seems that smaller companies tend to receive relatively fewer shareholder proposals. Therefore, we assume that the proposed amendment to the rule would not substantially increase the number of shareholder proposals to smaller companies and likely would have little impact on small entities. With respect to proposed Rule 14a-11, there is some indication that proxy contests may occur disproportionately at smaller companies.[372] Accordingly, we assume that proposed Rule 14a-11 is likely to have a greater effect than the proposed amendments to Rule 14a-8 on smaller companies.[373]

E. Request for Comment

We have identified certain costs and benefits imposed by these proposals. In addition to the requests for comment throughout the release on the potential impact of the proposed rules, we specifically request comment on all aspects of this cost-benefit analysis, including identification of any additional costs and benefits. We encourage commenters to identify and supply relevant data concerning the costs and benefits of the proposed amendments. We also solicit comment on how the use of electronic proxy materials[374] may reduce the costs for companies that would be required to include shareholder nominees or shareholder proposals, as well as for shareholders that otherwise would be required to conduct a proxy contest.

372 See, e.g., Bebchuk 2007 Article.

373 For further discussion on the impact of the proposed amendments on smaller reporting companies, see discussion of Initial Regulatory Flexibility Act below.

374 See Internet Proxy Availability Release.

We also request comment on the following specific concerns:

- We solicit quantitative data to assist our assessment of the benefits and costs of enhanced shareholder access to company proxy materials. Will proposed Exchange Act Rule 14a-11 reduce shareholders' cost of nominating directors?
- We solicit quantitative data on how often shareholders meeting the proposed Rule 14a-11 thresholds would invoke the rule to propose nominees.
- We solicit quantitative data on the potential increases, if any, of shareholder proposals under Exchange Act Rule 14a-8(i)(8) as a result of these proposed rules.
- We solicit quantitative data on the incremental cost of mailing and printing company proxies that may be longer due to the inclusion of shareholder nominees. How does this compare with the cost of a stand-alone printing of the additional material, such as would be borne by a shareholder engaged in a proxy contest under the current rules?
- We solicit quantitative date on the time and cost spent by shareholders nominating directors through a proxy contest under the current rules.

VI. CONSIDERATION OF BURDEN ON COMPETITION AND PROMOTION OF EFFICIENCY, COMPETITION AND CAPITAL FORMATION

Section 23(a)(2) of the Exchange Act[375] requires us, when adopting rules under the Exchange Act, to consider the impact that any new rule would have on competition. In addition, Section 23(a)(2) prohibits us from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act. Section 3(f) of the Exchange Act[376] and Section 2(c) of the Investment Company Act[377] require us, when

375 15 U.S.C. 78w(a)(2).

376 15 U.S.C. 78c(f).

377 15 U.S.C. 80a-2(c).

engaging in rulemaking that requires us to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation.

The proposed rules are intended to remove impediments to the exercise of shareholders' rights to nominate and elect directors and provide shareholders with information about nominating shareholders and their nominees for director. The proposed rules, if adopted, would establish a process for inclusion of shareholder nominees for director in company proxy materials pursuant to Rule 14a-11 and disclosure regarding the nominating shareholder and nominees submitted pursuant to Rule 14a-11. The proposed rules also would provide an avenue for shareholders to submit proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations. In addition, the proposed rules would require disclosure of information regarding nominating shareholders or groups and any nominees submitted pursuant to an applicable state law provision or a company's governing documents, which would provide shareholders a better informed basis for deciding how to vote for nominees for election to the board of directors. Enabling shareholders to submit shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations should better reflect shareholders' preferences regarding shareholder director nomination procedures and disclosure. We expect the proposed rules to promote the efficiency of the exercise of shareholders' rights to nominate and elect directors.

We expect proposed Rule 14a-11 would increase efficiency because a shareholder will not have to engage in a formal proxy contest if the shareholder only wants to nominate a small number of directors and is not seeking control of a company's board. We also note that the proposal would increase efficiency because all or most nominees will be included on one proxy card with clear disclosure for shareholders to evaluate when deciding whether and how to grant authority to vote their shares by proxy, rather than having to evaluate more than one set of proxy materials sent by a company and an insurgent shareholder.

If a company is required to include shareholder nominees in its proxy materials, competition for board seats could increase, which might encourage or discourage qualified candidates from running. To the extent that this would discourage less-qualified candidates from running, or alternatively, would increase the quality of board members due to increased competition, investors may be more or less willing to invest in companies that receive shareholder nominees pursuant to the proposed rules. The proposed rules should improve and streamline information flow between investors and with the company, which we believe would give more direct effect to shareholder preferences regarding shareholder nominations for director.

Shareholders and the company's relationship with shareholders may benefit from the board devoting additional time to considering shareholder concerns; however, one possible adverse impact on efficiency, competition, and capital formation is that boards may devote less time to fulfilling their other responsibilities as a result. However, we believe that investors may be able to evaluate a company's board of directors more effectively and make more informed investment decisions as a result of the proposed rules. We also believe that these developments may have some positive impact on the efficiency of markets and capital formation because it may help to increase investor confidence during this time of uncertainty in our markets.

We request comment on whether the proposals, if adopted, would promote efficiency, competition and capital formation or have an impact or burden on competition. Commenters are requested to provide empirical data and other factual support for their view, if possible.

VII. INITIAL REGULATORY FLEXIBILITY ACT ANALYSIS

This Initial Regulatory Flexibility Act Analysis has been prepared in accordance with 5 U.S.C. 603. It relates to proposed revisions to the rules and forms under the Exchange Act and the Investment Company Act that would, under certain limited circumstances, require companies to include in their proxy materials shareholder nominees for election as director. It also relates to the proposed revisions to the rules and forms that would prohibit companies from excluding shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations. The proposals are intended to improve the ability of shareholders to receive consistent and comparable disclosure regarding, and participate meaningfully in, the nomination and election of directors.

A. Reasons for, and Objectives of, the Proposed Action

Today's proposals include features from the proposals on this topic in 2003 and 2007, and reflect much of what we learned through the public comment that the Commission has received concerning this topic over the past six years. The proposals are intended to remove impediments to shareholders' ability to participate meaningfully in the nomination and election of directors, to promote the exercise of shareholders' rights to nominate and elect directors, to open up communication between a company and its shareholders, and to provide shareholders with better information to make an informed voting decision by requiring disclosure about a nominating shareholder or group, as well as nominees for director submitted by a nominating shareholder or group. In particular, the proposed rules would create a process for long-term shareholders, or groups of long-term shareholders, with significant holdings to have their nominees for director included in company proxy materials. In addition, the proposed amendment to Rule 14a-8(i)(8) would narrow the exclusion and would not permit companies to exclude shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11, when certain conditions are met.

The rule proposals are intended to achieve the stated objectives without unduly burdening companies. We seek to limit the cost and burden on companies by limiting proposed Rule 14a-11 to nominations by shareholders who have maintained a significant continuous beneficial ownership in the company for at least one year at the time the notice of nomination is submitted. These limitations would lower the cost to companies while still improving disclosure in the company's proxy materials and thereby improve shareholders' ability to participate meaningfully in the nomination and election of directors. This increased participation may improve corporate governance by increasing director accountability and responsiveness and aligning the interests of the board and shareholders, thereby giving investors greater confidence that the board is serving the interests of shareholders. This may, in turn, enhance the value of shareholders' investments.

B. Legal Basis

We are proposing amendments to the forms and rules under the authority set forth in Sections 3(b), 13, 14, 15, 23(a) and 36 of the Securities Exchange Act of 1934, as amended, and Sections 10, 20(a) and 38 of the Investment Company Act of 1940, as amended.

C. Small Entities Subject to the Proposed Rules

The Regulatory Flexibility Act defines "small entity" to mean "small business," "small organization," or "small governmental jurisdiction."[378] The Commission's rules define "small business" and "small organization" for purposes of the Regulatory Flexibility Act for each of the types of entities regulated by the Commission.[379] A "small business" and "small organization," when used with reference to an issuer other than an investment company, generally means an issuer with total assets of $5 million as a company with total assets of $5 million or less on the last day of its most recent fiscal year. We estimate that there are approximately 1,229 issuers that may be considered small entities.[380]

For purposes of the Regulatory Flexibility Act, an investment company is a small entity if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.[381] We estimate that approximately 178 registered investment companies and 34 business development companies meet this definition. The proposed rules may affect each of the approximately 212 issuers that may be considered small entities, to the extent companies and shareholders take advantage of the proposed rules.

We request comment on the number of small entities that would be impacted by our proposals, including any empirical data.

378 5 U.S.C. 601(6).

379 Exchange Act Rule 0-10 [17 CFR 240.0-10].

380 The estimated number of reporting small entities is based on 2008 data, including the Commission's EDGAR database and Thomson Financial's Worldscope database.

381 Rule 0-10 under the Investment Company Act [17 CFR 270.0-10] contains the applicable definition.

D. Reporting, Recordkeeping and Other Compliance Requirements

The proposals would, under certain circumstances, require all companies subject to the federal proxy rules, including small entities, to permit certain shareholders to submit nominees for inclusion in the company's proxy materials. A company would be required to include shareholder nominees for director in its proxy materials unless state law or a company's governing documents prohibits shareholders from nominating directors. Nominating shareholders, including nominating shareholders that are small entities, would be required to provide disclosure in proposed Schedule 14N about the nominating shareholders and the nominee, and companies would be required to include the disclosure provided by the nominating shareholder or group in the company's proxy materials.

The proposals also would permit shareholders to submit proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11. A nominating shareholder or group, including a nominating shareholder or group that is a small entity, using an applicable state law provision or a provision in the company's governing documents to submit a nomination for director would be required to provide disclosure in proposed Schedule 14N about the nominating shareholder or group and the nominee. Companies also would be required to include disclosure about the nominating shareholder or group and the nominee in the company's proxy materials when a shareholder submits a nomination for director pursuant to an applicable state law provision or a company's governing documents.

Based on our staff's review of Rule 14a-8 shareholder proposals, it seems that smaller companies tend to receive relatively fewer shareholder proposals. Therefore, we assume that the proposed amendment to the rule would not substantially increase the number of shareholder proposals to smaller companies and likely would have little impact on small entities. With respect to proposed Rule 14a-11, there is some indication that proxy contests may occur disproportionately at smaller companies.[382] Accordingly, we assume that proposed Rule 14a-11 is likely to have a greater effect than the proposed amendments to Rule 14a-8 on smaller companies.

E. Duplicative, Overlapping or Conflicting Federal Rules

We believe that there are no rules that conflict with or duplicate the proposed rules.

F. Significant Alternatives

The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish the stated objective, while minimizing any significant adverse impact on small entities. In connection with the proposed amendments, we considered the following alternatives:

- the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities;
- the clarification, consolidation or simplification of the rule's compliance and reporting requirements for small entities;
- the use of performance rather than design standards; and
- an exemption for small entities from coverage under the proposals.

The Commission has considered a variety of reforms to achieve its regulatory objectives while minimizing the impact on small entities. As one possible approach, we considered requiring companies to include shareholder nominees for director in a company's proxy materials upon the occurrence of certain events so that the rule would apply only in situations

382 See, e.g., Bebchuk 2007 Article.

where there was a demonstrated failure in the proxy process related to director nominations and elections in 2003. We have not taken this approach in the current proposal because we believe that it is important to remove impediments to shareholders' exercise of their right to nominate directors at all companies subject to the proxy rules rather than only at those companies where specified events have occurred. Alternatively, we considered changes to Rule 14a-8(i)(8) that would enable shareholders to have their proposals for bylaw amendments regarding the procedures for nominating directors included in the company's proxy materials provided the shareholder submitting the proposal made certain disclosures and beneficially owned more than 5% of the company's shares in 2007. We did not take this approach because we seek to provide shareholders with a more immediate and direct means of effecting change in the boards of directors of the companies in which they invest. For these reasons, as well as the reasons discussed throughout the release, we believe that today's proposals may better achieve the Commission's objectives.

We have sought comment on whether the proposed tiered approach – under which shareholders or shareholder groups at larger companies would have to satisfy a lower ownership threshold than shareholders or shareholder groups at smaller companies in order to rely on Rule 14a-11 – is appropriate and workable. The effect of the tiered approach may make it less likely that shareholders at smaller companies will nominate directors under Rule 14a-11. We are not proposing different disclosure standards based on the size of the issuer. We believe the proposed uniform disclosure will be helpful to voting decisions on shareholder nominated directors at issuers of all sizes. However, we seek comment on whether the disclosure can be tiered based on the size of the company and still provide useful information to shareholders. We also have included requests for comment regarding the appropriate ownership threshold for non-accelerated filers. As noted, based on our staff's review of Rule 14a-8 shareholder proposals, it seems that smaller companies tend to receive relatively fewer shareholder proposals. Therefore, we assume that the proposed rule would not substantially increase the number of shareholder proposals to smaller companies and likely would have little impact on small entities. With respect to proposed Rule 14a-11, there is some indication that proxy contests may occur disproportionately at smaller companies.[383] Accordingly, we assume that proposed Rule 14a-11 is likely to have a greater effect than the proposed amendments to Rule 14a-8 on smaller companies.

We considered the use of performance standards rather than design standards in the proposed rules. The proposal contains both performance standards and design standards. We are proposing design standards to the extent that we believe compliance with particular requirements are necessary. However, to the extent possible, we are proposing rules that impose performance standards. For example, under Rule 14a-11, shareholder nominees can provide a 500 word statement of support concerning their nominee or nominees for director, but we do not specify the content. Similarly, shareholders can propose any nomination procedures or disclosures related to shareholder nominations under the proposed amendment to Rule 14a-8(i)(8), provided they do not conflict with Rule 14a-11. By allowing shareholders to submit proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, we seek to provide shareholders and companies with a measure of flexibility to tailor the means through which they can comply with the standards.

We request comment on whether separate requirements for small entities would be appropriate. The purpose of the proposed rules is to remove impediments to the exercise of

383 See id.

shareholders' rights to nominate and elect directors to company boards of directors and thereby enable shareholders to participate meaningfully in the nomination and election of directors at the companies in which they invest. Exempting small entities would not appear to be consistent with these goals. An exemption or separate requirements for small entities may not address the impediments to the exercise of shareholders' rights to nominate and elect directors to company boards of directors that may affect small entities as much as they would affect large companies. The establishment of any differing compliance or reporting requirements or timetables or any exemptions for smaller reporting companies may not be in keeping with the objective of the proposed rules.

G. Solicitation of Comment

We encourage comments with respect to any aspect of this Initial Regulatory Flexibility Analysis. In particular, we request comments regarding:

- How our rules could achieve their objective while lowering any burden on smaller entities;
- The number of small entities that may be affected by the proposals;
- The existence or nature of the potential impact of the proposals on small entities discussed in the analysis; and
- How to quantify the impact of the proposed rules.

We solicit comments as to whether the proposed changes could have an effect that we have not considered. Commenters are asked to describe the nature of any impact and provide empirical data supporting the extent of the impact. Such comments will be considered in the preparation of the Final Regulatory Flexibility Analysis, if the proposals are adopted, and will be placed in the same public file as comments on the proposed amendments themselves.

VIII. SMALL BUSINESS REGULATORY ENFORCEMENT FAIRNESS ACT

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996,[384] a rule is "major" if it has resulted, or is likely to result in:

- An annual effect on the economy of $100 million or more;
- A major increase in costs or prices for consumers or individual industries; or
- Significant adverse effects on competition, investment or innovation.

We request comment on whether our proposals would be a "major rule" for purposes of SBREFA. We solicit comment and empirical data on:

- The potential effect on the U.S. economy on an annual basis;
- Any potential increase in costs or prices for consumers or individual industries; and
- Any potential effect on competition, investment or innovation.

IX. STATUTORY BASIS AND TEXT OF PROPOSED AMENDMENTS

The amendments are proposed pursuant to Sections 3(b), 13, 14, 15, 23(a) and 36 of the Securities Exchange Act of 1934, as amended, and Sections 10, 20(a) and 38 of the Investment Company Act of 1940, as amended.

List of Subjects

17 CFR Parts 200

Freedom of information, Reporting and recordkeeping requirements, Securities.

17 CFR Parts 232, 240, and 249

Reporting and recordkeeping requirements, Securities.

17 CFR Part 274

Investment companies, Reporting and recordkeeping requirements, Securities.

In accordance with the foregoing, the Securities and Exchange Commission proposes to

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384 Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

amend Title 17, chapter II of the Code of Federal Regulations as follows:

PART 200 – ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS

Subpart D – Information and Requests

1. The authority citation for Part 200, Subpart D, continues to read, in part, as follows:

Authority: 5 U.S.C. 552, as amended, 15 U.S.C. 77f(d), 77s, 77ggg(a), 77sss, 78m(F)(3), 78w, 80a-37, 80a-44(a), 80a-44(b), 80b-10(a), and 80b-11.

* * * * *

2. Add §200.82a to read as follows:

§200.82a Public availability of materials filed pursuant to § 240.14a-11(f) and related materials.

Materials filed with the Commission pursuant to Rule 14a-11(f) under the Securities Exchange Act of 1934 (17 CFR 240.14a-11(f)), written communications related thereto received from any person, and each related no-action letter or other written communication issued by the staff of the Commission, shall be made available to any person upon request for inspection or copying.

PART 232 – REGULATION S-T – GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS

3. The authority citation for Part 232 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s(a), 77z-3, 77sss(a), 78c(b), 78l, 78m, 78n, 78o(d), 78w(a), 78ll, 80a-6(c), 80a-8, 80a-29, 80a-30, 80a-37, and 7201 et seq.; and 18 U.S.C. 1350.

* * * * *

4. Amend §232.13 by revising paragraph (a)(4) to read as follows:

(a) * * *

(4) Notwithstanding paragraph (a)(2) of this section, a Form 3, 4 or 5 (§§ 249.103, 249.104, and 249.105 of this chapter) or a Schedule 14N (§240.14n-101 of this chapter) submitted by direct transmission on or before 10 p.m. Eastern Standard Time or Eastern Daylight Saving Time, whichever is currently in effect, shall be deemed filed on the same business day.

* * * * *

PART 240 – GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

5. The authority citation for Part 240 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, and 7201, et seq.; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

6. Amend §240.13a-11 by revising paragraph (b) to read as follows:

§240.13a-11 Current reports on Form 8-K (§249.308 of this chapter).

* * * * *

(b) This section shall not apply to foreign governments, foreign private issuers required to make reports on Form 6-K (17 CFR 249.306) pursuant to §240.13a-16, issuers of American Depositary Receipts for securities of any foreign issuer, or investment companies required to file reports pursuant to §270.30b1-1 of this chapter under the Investment Company Act of 1940, except where such an investment company is required to file:

(1) Notice of a blackout period pursuant to §245.104 of this chapter;

(2) Disclosure pursuant to Instruction 2 to §240.14a-11(a) of the date by which a shareholder or shareholder group must submit the notice required pursuant to §240.14a-11(c); or

(3) Disclosure pursuant to Instruction 3 to §240.14a-11(b) of information concerning net assets, outstanding shares, and voting.

* * * * *

7. Amend §240.13d-1 by revising paragraphs (b)(1)(i) and (c)(1) and adding Instruction 1 to paragraph (b)(1) and Instruction 1 to paragraph (c)(1).

The revisions read as follows:

§240.13d-1 Filing of Schedules 13D and 13G.

* * * * *

(b)(1) * * *

(i) Such person has acquired such securities in the ordinary course of his business and not with the purpose nor with the effect of changing or influencing the control of the issuer, nor in connection with or as a participant in any transaction having such purpose or effect, including any transaction subject to §240.13d–3(b), other than activities solely in connection with a nomination under §240.14a-11; and

* * * * *

<u>Instruction 1 to paragraph (b)(1)</u>.

For purposes of paragraph (b)(1)(i) of this section, the exception for activities solely in connection with a nomination under §240.14a-11 will not be available after the election of a director nominated pursuant to §240.14a-11.

* * * * *

(c) * * *

(1) Has not acquired the securities with any purpose, or with the effect, of changing or influencing the control of the issuer, or in connection with or as a participant in any transaction having that purpose or effect, including any transaction subject to §240.13d-3(b), other than activities solely in connection with a nomination under §240.14a-11; * * *

Instruction 1 to paragraph (c)(1).

For purposes of paragraph (c)(1) of this section, the exception for activities solely in connection with a nomination under §240.14a-11 will not be available after the election of a director nominated pursuant to §240.14a-11.

* * * * *

8. Amend §240.14a-2 by:

a. Revising the first sentence of paragraph (b); and

b. Adding paragraphs (b)(7) and (b)(8).

The revision and additions read as follows:

§240.14a-2 Solicitations to which §240.14a-3 to §240.14a-15 apply.

* * * * *

(b) Sections 240.14a-3 to 240.14a-6 (other than paragraphs 14a-6(g) and 14a-6(p)), §240.14a-8, §240.14a-10, and §§240.14a-12 to 240.14a-15 do not apply to the following: * * *

* * * * *

(7) Any solicitation by or on behalf of any shareholder in connection with the formation of a nominating shareholder group pursuant to §240.14a-11, provided that:

(i) Each written communication includes no more than:

(A) A statement of each soliciting shareholder's intent to form a nominating shareholder group in order to nominate a director under §240.14a-11;

(B) Identification of, and a brief statement regarding, the potential nominee or nominees or, where no nominee or nominees have been identified, the characteristics of the nominee or nominees that the shareholder intends to nominate, if any;

(C) The percentage of securities that each soliciting shareholder beneficially owns or the aggregate percentage owned by any group to which the shareholder belongs; and

(D) The means by which shareholders may contact the soliciting party.

(ii) Any soliciting material published, sent or given to shareholders in accordance with this paragraph must be filed by the shareholder with the Commission, under the registrant's Exchange Act file number, or, in the case of a registrant that is an investment company registered under the Investment Company Act of 1940, under the registrant's Investment Company Act file number, no later than the date the material is first published, sent or given to shareholders. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered. The soliciting material must include a cover page in the form set forth in Schedule 14A (§240.14a-101) and the appropriate box on the cover page must be marked.

(8) Any written solicitation by or on behalf of a nominating shareholder or nominating shareholder group in support of a nominee placed on the registrant's form of proxy in accordance with §240.14a-11 or against the registrant's nominee or nominees, provided that:

(i) The soliciting party does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as proxy for a shareholder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization;

(ii) Each written communication includes:

(A) The identity of each nominating shareholder and a description of his or her direct or indirect interests, by security holdings or otherwise;

(B) A prominent legend in clear, plain language advising shareholders that a shareholder nominee is or may be included in the registrant's proxy statement and to read the registrant's proxy statement when it becomes available because it includes important information (or, if the registrant's proxy statement is publicly available, advising shareholders of that fact and encouraging shareholders to read the registrant's proxy statement because it includes important information). The legend also must explain to shareholders that they can find the registrant's proxy statement, and any other relevant documents, at no charge on the Commission's web site; and

(iii) Any soliciting material published, sent or given to shareholders in accordance with this paragraph must be filed by the nominating shareholder with the Commission, under the registrant's Exchange Act file number, or, in the case of a registrant that is an investment company registered under the Investment Company Act of 1940, under the registrant's Investment Company Act file number, no later than the date the material is first published, sent or given to shareholders. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered. The soliciting material must include a cover page in the form set forth in Schedule 14A (§240.14a-101) and the appropriate box on the cover page must be marked.

9. Amend §240.14a-4 by:

a. Revising the first sentence of paragraph (b)(2) introductory text; and

b. Adding a sentence to the end of the undesignated paragraph following paragraph (b)(2)(iv).

The revision and addition read as follows:

§240.14a-4 Requirements as to proxy.

* * * * *

(b) * * *

(2) A form of proxy that provides for the election of directors shall set forth the names of persons nominated for election as directors, including any person whose nomination by a shareholder or shareholder group satisfies the requirements of §240.14a-11, an applicable state law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials. * * *

* * * * *

(iv) * * *

* * * Means to grant authority to vote for any nominees as a group or to withhold authority for any nominees as a group may not be provided if the form of proxy includes one or more shareholder nominees in accordance with §240.14a-11, an applicable state law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials.

* * * * *

10. Amend §240.14a-6 by:

a. Redesignating paragraphs (a)(4), (a)(5) and (a)(6) as paragraphs (a)(5), (a)(6) and (a)(7) respectively;

b. Adding new paragraph (a)(4);

c. Adding a sentence at the end of Note 3; and

d. Adding paragraph (p).

The revisions and additions read as follows:

§240.14a-6 Filing requirements.

(a) * * *

(4) A shareholder nominee for director included pursuant to §240.14a-11, an applicable state law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials.

* * * * *

Note 3. * * * The inclusion of a shareholder nominee in the registrant's proxy materials pursuant to §240.14a-11, an applicable state law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials does not constitute a "solicitation in opposition," even if the registrant opposes the shareholder nominee and solicits against the shareholder nominee and in favor of a registrant nominee.

* * * * *

(p) Solicitations subject to §240.14a-11. Any soliciting material that is published, sent or given to shareholders in connection with §240.14a-2(b)(7) or (b)(8) must be filed with the Commission as specified in that section.

11. Amend §240.14a-8 by revising paragraph (i)(8) as follows:

§240.14a-8 Shareholder proposals.

* * * * *

(i) * * *

(8) Director elections: If the proposal:

(i) Would disqualify a nominee who is standing for election;

(ii) Would remove a director from office before his or her term expired;

(iii) Questions the competence, business judgment, or character of one or more nominees or directors;

(iv) Nominates a specific individual for election to the board of directors, other than pursuant to §240.14a-11, an applicable state law provision, or the company's governing documents; or

(v) Otherwise could affect the outcome of the upcoming election of directors.

* * * * *

12. Amend §240.14a-9 by adding a paragraph (c) and removing the authority citation following its section to read as follows:

§240.14a-9 False or misleading statements.

* * * * *

(c) No nominee, nominating shareholder or nominating shareholder group, or any member thereof, shall cause to be included in a registrant's proxy materials, either pursuant to the federal proxy rules, an applicable state law provision, or a registrant's governing documents as they relate to including shareholder nominees for director in registrant proxy materials, any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.

* * * * *

13. Add §240.14a-11 to read as follows:

§240.14a-11 Shareholder nominations.

(a) Applicability. In connection with an annual meeting of shareholders (or a special meeting in lieu of the annual meeting) at which directors are elected, a registrant (other than a registrant subject to the proxy rules solely because it has a class of debt registered under Exchange Act §12) will be required to include in its proxy statement and form of proxy the name of a person or persons nominated by a shareholder or group of shareholders for election to the board of directors and include in its proxy statement the disclosure about such nominee or nominees and the nominating shareholder or members of a nominating shareholder group that is specified in §240.14a-18(e)-(l), provided that:

(1) Applicable state law or the registrant's governing documents do not prohibit the registrant's shareholders from nominating a candidate or candidates for election as a director;

(2) The nominee's candidacy or, if elected, board membership would not violate controlling state law, the registrant's governing documents, federal law, or rules of a national securities exchange or national securities association applicable to the registrant (other than rules of a national securities exchange or national securities association regarding director independence);

(3) The nominating shareholder or members of the nominating shareholder group have satisfied the eligibility requirements in paragraph (b) of this section;

(4) All information required to be included in the notice to the registrant required pursuant to paragraph (c) of this section is so included;

(5) No representation or certification required to be included in the notice to the registrant required pursuant to paragraph (c) of this section is false or misleading in any material

respect; and

(6) The provisions of paragraph (d) of this section limiting the number of nominees required to be included would not necessitate exclusion of the nominee.

Instruction 1 to paragraph (a).

A nominating shareholder will not be deemed an "affiliate" of the registrant under the Securities Act of 1933 (15 U.S.C 77a et. seq.) or the Securities Exchange Act of 1934 (15 U.S.C. 78a et. seq.) solely as a result of nominating a candidate for director or soliciting for the election of such a director nominee or against a registrant's nominee pursuant to this section. Where a shareholder nominee is elected, and the nominating shareholder or nominating shareholder group does not have an agreement or relationship with that director, otherwise than relating to the director's nomination pursuant to §240.14a-11, solicitation for the election of the shareholder director nominee or against a registrant's nominee, or the election of the shareholder director nominee, the nominating shareholder or nominating shareholder group will not be deemed an affiliate solely by virtue of having nominated that director.

Instruction 2 to paragraph (a).

If the registrant did not hold an annual meeting the previous year, or if the date of the current year's annual meeting has been changed by more than 30 calendar days from the date of the previous year's annual meeting, the registrant must disclose pursuant to Item 5.07 of Form 8-K (§249.308 of this chapter) the date by which a shareholder or shareholder group must submit the notice required pursuant to paragraph (c) of this section, which date shall be a reasonable time prior to the date the registrant mails its proxy materials for the meeting.

(b) Nominating shareholder eligibility. A shareholder or group of shareholders nominating a person or persons must satisfy the following requirements:

(1) The shareholder individually, or the shareholder group in the aggregate, must beneficially own, as of the date the shareholder or group of shareholders provides notice to the registrant on Schedule 14N of their intent to include a nominee or nominees in the registrant's proxy materials pursuant to §240.14a-11:

(i) For large accelerated filers as defined in §240.12b-2, and investment companies registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.) with net assets of $700 million or more, at least 1% of the registrant's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or a special meeting in lieu of the annual meeting);

(ii) For accelerated filers as defined in §240.12b-2, and investment companies registered under the Investment Company Act of 1940 with net assets of $75 million or more but less than $700 million, at least 3% of the registrant's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or a special meeting in lieu of the annual meeting); and

(iii) For non-accelerated filers as defined in §240.12b-2, and investment companies registered under the Investment Company Act of 1940 with net assets of less than $75 million, at least 5% of the registrant's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or a special meeting in lieu of the annual meeting); and

(2) The shareholder or each member of the shareholder group must have held the securities that are used for purposes of determining the applicable ownership threshold required by paragraph (b)(1) of this section continuously for at least one year as of the date it provides notice to the registrant on Schedule 14N and intend to continue to hold those securities through the date of the subject election of directors.

Instruction 1 to paragraph (b).

In the case of a registrant other than an investment company registered under the Investment Company Act of 1940, for purposes of (b)(1) of this section, in determining the securities that are entitled to be voted on the election of directors, the nominating shareholder or nominating shareholder group may rely on information set forth in the registrant's most recent quarterly or annual report, and any current report subsequent thereto, filed with the Commission pursuant to this Act, unless the nominating shareholder or nominating shareholder group knows or has reason to know that the information contained therein is inaccurate.

In the case of a registrant that is an investment company registered under the Investment Company Act of 1940, for purposes of paragraph (b)(1) of this section, in determining the securities that are entitled to be voted on the election of directors, the nominating shareholder or nominating shareholder group may rely on information set forth in the following documents, unless the nominating shareholder or nominating shareholder group knows or has reason to know that the information contained therein is inaccurate:

a. in the case of a registrant that is a series company as defined in Rule 18f-2(a) under the Investment Company Act of 1940 (§270.18f-2(a) of this chapter), the Form 8-K described in Instruction 3 to paragraph (b); or

b. in the case of other investment companies, the registrant's most recent annual or semi-annual report filed with the Commission on Form N-CSR (17 CFR 249.331; 17 CFR 274.128).

Instruction 2 to paragraph (b).

For purposes of paragraph (b)(1) of this section, the amount of net assets of an investment company registered under the Investment Company Act of 1940 shall be the amount of net assets of the company as of the end of the company's second fiscal quarter in the fiscal year immediately preceding the fiscal year of the meeting, as disclosed in the registrant's Form N-CSR filed with the Commission, except that, for a series company (as defined in §270.18f-2(a) of this chapter), the amount of net assets shall be the amount disclosed in the Form 8-K described in Instruction 3 to paragraph (b).

Instruction 3 to paragraph (b).

If the registrant is an investment company that is a series company (as defined in §270.18f-2(a) of this chapter), the registrant must disclose pursuant to Item 5.07 of Form 8-K (§249.308 of this chapter):

a. The registrant's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting; and

b. The total number of shares of the registrant outstanding and entitled to be voted (or if the votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) at an annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.

(c) Shareholder notice. To have a nominee included in the registrant's proxy statement and form of proxy, the nominating shareholder must provide notice to the registrant on Schedule 14N as specified by §240.14n-1 of its intent to require that the registrant include that shareholder's nominee on the registrant's form of proxy and include the disclosures required pursuant to §240.14a-18. This notice must be filed with the Commission on the date provided to the registrant.

(d) Number of shareholder nominees.

(1) The registrant will not be required to include in its proxy statement and form of

proxy more than one shareholder nominee or the number of nominees that represents 25 percent of the registrant's board of directors, whichever is greater;

(2) Where the registrant has one or more directors currently serving on its board of directors who were elected as a shareholder nominee pursuant to this section, and the term of that director or directors extends past the date of the meeting of shareholders for which it is soliciting proxies, the registrant will not be required to include in the proxy statement or form of proxy more shareholder nominees than could result in the total number of directors who were elected as shareholder nominees pursuant to §240.14a-11 and serving on the board being more than one shareholder nominee or 25 percent of the registrant's board of directors, whichever is greater; and

(3) In the event that more than one shareholder or group of shareholders is otherwise permitted to nominate a person or persons to a registrant's board of directors pursuant to §240.14a-11, the registrant shall include in the proxy statement and form of proxy the nominee or nominees of the first nominating shareholder or nominating shareholder group from which the registrant receives timely notice as specified in paragraph (c) of this section, up to and including the total number required to be included by the registrant pursuant to this paragraph. Where the first nominating shareholder or nominating shareholder group to deliver timely notice as specified in paragraph (c) of this section does not nominate the maximum number of directors required to be included by the registrant, the nominee or nominees of the next nominating shareholder or nominating shareholder group from which the registrant receives timely notice as specified in paragraph (c) of this section would be included in the registrant's proxy materials, up to and including the total number required to be included by the registrant.

Instruction 1 to paragraph (d).

Depending on board size, 25% of the board may not result in a whole number. In those instances, the maximum number of shareholder nominees for director that a registrant will be required to include in its proxy materials will be the closest whole number below 25%.

Instruction 2 to paragraph (d).

If a nominee, a nominating shareholder, or any member of a nominating shareholder group has any agreement with the registrant or any affiliate of the registrant regarding the nomination of a candidate for election as a member of the registrant's board of directors, any such nominee or any nominee of such nominating shareholder or nominating shareholder group shall not be included in calculating the number of nominees required under this section.

(e) False or misleading statements. The registrant is not responsible for any information in the notice from the nominating shareholder or nominating shareholder group submitted as required by paragraph (c) of this section or otherwise provided by the nominating shareholder or nominating shareholder group, except where the registrant knows or has reason to know that the information is false or misleading.

(f) Determinations regarding eligibility.

(1) Upon the registrant's receipt of a notice described in paragraph (c) of this section, the registrant shall determine whether any of the events permitting exclusion of a shareholder nominee has occurred;

(2) If the registrant determines that it will include a shareholder nominee, it must notify in writing the nominating shareholder or nominating shareholder group no later than 30 calendar days before it files its definitive proxy statement and form of proxy with the Commission. The registrant is responsible for providing this notice in a manner that evidences its timely receipt by the nominating shareholder or each member of the nominating shareholder group;

(3) If the registrant determines that it may exclude a shareholder nominee, the registrant must notify in writing the nominating shareholder or nominating shareholder group of this determination. This notice must be postmarked or transmitted electronically no later than 14 calendar days after the registrant receives the notice required by paragraph (c) of this section. The registrant is responsible for providing this notice in a manner that evidences its timely receipt by the nominating shareholder or each member of the nominating shareholder group;

(4) The registrant's notice to the nominating shareholder or nominating shareholder group under paragraph (f)(3) of this section that it has determined that it may exclude a shareholder nominee must include an explanation of the registrant's basis for determining that it may exclude the nominee;

(5) The nominating shareholder or nominating shareholder group shall have 14 calendar days after receipt of the registrant's notice under paragraph (f)(3) of this section to respond to the registrant's notice and correct any eligibility or procedural deficiencies identified in that notice, as required by paragraph (f)(4) of this section. The nominating shareholder's or nominating shareholder group's response must be postmarked, or transmitted electronically, within the timeframe identified in the preceding sentence. The nominating shareholder or nominating shareholder group is responsible for providing the response in a manner that evidences its timely receipt;

(6) Neither the composition of the nominating shareholder group nor the shareholder nominee may be changed as a means to correct a deficiency identified in the registrant's notice to the nominating shareholder or nominating shareholder group under paragraph (f)(3) of this section – those matters must remain as they were described in the notice to the registrant submitted pursuant to paragraph (c) of this section; however, where a nominating shareholder or

nominating shareholder group inadvertently submits a number of nominees that exceeds the maximum number required to be included by the registrant, the nominating shareholder or nominating shareholder group may specify which nominee or nominees are not to be included in the registrant's proxy materials;

(7) If the registrant determines that it may exclude a shareholder nominee, after providing the requisite notice of and time for the nominating shareholder or nominating shareholder group to remedy any eligibility or procedural deficiencies in the nomination, the registrant must provide notice of the basis for its determination to the Commission no later than 80 calendar days before it files its definitive proxy statement and form of proxy with the Commission. The Commission may permit the registrant to make its submission later than 80 days before the registrant files its definitive proxy statement and form of proxy if the registrant demonstrates good cause for missing the deadline;

(8) The registrant's notice to the Commission shall include:

(i) Identification of the nominating shareholder or each member of the nominating shareholder group, as applicable;

(ii) The name of the nominee;

(iii) An explanation of the registrant's basis for determining that the registrant may exclude the nominee; and

(iv) A supporting opinion of counsel when the registrant's basis for excluding a nominee relies on a matter of state law;

(9) Unless otherwise indicated in this section, the burden is on the registrant to demonstrate that it may exclude a nominee;

(10) The registrant must file its notice with the Commission and simultaneously provide

a copy to the nominating shareholder or each member of the nominating shareholder group;

(11) The nominating shareholder or nominating shareholder group may submit a response to the registrant's notice to the Commission. This response must be postmarked or transmitted electronically to the Commission no later than 14 calendar days after the nominating shareholder's or nominating shareholder group's receipt of the registrant's notice to the Commission. The nominating shareholder or nominating shareholder group must provide a copy of its response to the Commission simultaneously to the registrant;

(12) The Commission staff may provide an informal statement of its views to the registrant and the nominating shareholder or nominating shareholder group;

(13) The registrant shall provide the nominating shareholder or nominating shareholder group with notice, no later than 30 calendar days before it files its definitive proxy statement and form of proxy with the Commission, of whether it will include or exclude the shareholder nominee; and

(14) The exclusion of a shareholder nominee by a registrant where that exclusion is not permissible under §240.14a-11(a) shall be a violation of this section.

14. Amend §240.14a-12 by removing the heading "Instructions to §240.14a-12"; by removing the numbers 1. and 2. of instructions 1 and 2 to §240.14a-12 and adding in their places the phrases "Instruction 1. to §240.14a-12." and "Instruction 2. to §240.14a-12.", respectively; and adding Instruction 3 to read as follows:

§240.14a-12 Solicitation before furnishing a proxy statement.

* * * * *

Instruction 3. to §240.14a-12. Solicitations by a nominating shareholder or nominating shareholder group that are made in connection with a §240.14a-11 nomination will not be deemed a solicitation in opposition subject to §240.14a-12(c).

15. Add §240.14a-18 to read as follows:

§240.14a-18 Disclosure regarding nominating shareholders and nominees submitted for inclusion in a registrant's proxy materials pursuant to §240.14a-11.

To have a nominee included in a registrant's proxy materials pursuant to §240.14a-11, the nominating shareholder or nominating shareholder group must provide notice to the registrant of its intent to do so on a Schedule 14N and file that notice with the Commission on the date first sent to the registrant. This notice on Schedule 14N shall be sent to the registrant by the date specified by the registrant's advance notice bylaw provision or, where no such provision is in place, no later than 120 calendar days before the date that the registrant mailed its proxy materials for the prior year's annual meeting, except that, if the registrant did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, then the nominating shareholder or nominating shareholder group must provide and file its notice a reasonable time before the registrant mails its proxy materials, as specified by the registrant in a Form 8-K (§249.308 of this chapter) filed pursuant to Item 5.07 of Form 8-K. This notice must include:

(a) A representation that, to the knowledge of the nominating shareholder or nominating shareholder group, the nominee's candidacy or, if elected, board membership would not violate controlling state law, federal law or rules of a national securities exchange or national securities association applicable to the registrant (other than rules of a national securities exchange or national securities association regarding director independence);

(b) A representation that the nominating shareholder or nominating shareholder group satisfies the conditions in §240.14a-11(b);

(c). In the case of a registrant other than an investment company, a representation that the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the registrant, if any, or, in the case of a registrant that is an investment company, a representation that the nominee is not an "interested person" of the registrant as defined in section 2(a)(19) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(19));

Instruction to paragraph (c).

For this purpose, the nominee would be required to meet the definition of "independence" that generally is applicable to directors of the registrant and not any particular definition of independence applicable to members of the audit committee of the registrant's board of directors. To the extent a national securities exchange or national securities association rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board (for example, requiring that the board of directors or any group or committee of the board of directors make a determination regarding the existence of factors material to a determination of a nominee's independence), the nominee would not be required to represent that the nominee meets the subjective determination of independence as part of the shareholder nomination process.

(d) A representation that neither the nominee nor the nominating shareholder nor, where there is a nominating shareholder group, any member of the nominating shareholder group, has an agreement with the registrant regarding the nomination of the nominee;

Instruction to paragraph (d).

For purposes of paragraph (d), negotiations between the nominee, the nominating shareholder or nominating shareholder group and the nominating committee or board of the registrant to have the nominee included on the registrant's proxy card as a management nominee, where those negotiations are unsuccessful, or negotiations that are limited to whether the registrant is required to include the shareholder nominee on the registrant's proxy card in accordance with §240.14a-11, will not represent a direct or indirect agreement with the registrant.

(e) A statement from the nominee that the nominee consents to be named in the registrant's proxy statement and form of proxy and, if elected, to serve on the registrant's board of directors;

(f) A statement that the nominating shareholder or nominating shareholder group intends to continue to own the requisite shares through the date of the meeting of shareholders. Additionally, the nominating shareholder or nominating shareholder group must provide a statement regarding the nominating shareholder's or nominating shareholder group's intent with respect to continued ownership after the election.

(g) Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A (§240.14a-101), as applicable;

(h) Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A, as applicable;

(i) Disclosure about whether the nominating shareholder or each member of a nominating shareholder group has been involved in any legal proceeding during the past five years, as specified in Item 401(f) of Regulation S-K (§229.10 of this chapter). Disclosure pursuant to this section need not be provided if provided in response to Items 4(b) and 5(b) of Schedule 14A;

Instruction 1 to paragraphs (h) and (i).

Where the nominating shareholder is a general or limited partnership, syndicate or other group, the information called for in paragraphs (h) and (i) of this section must be given with respect to:

a. each partner of the general partnership;

b. each partner who is, or functions as, a general partner of the limited partnership;

c. each member of the syndicate or group; and

d. each person controlling the partner or member.

Instruction 2 to paragraphs (h) and (i).

If the nominating shareholder is a corporation or if a person referred to in a., b., c. or d. of Instruction 1 to paragraphs (h) and (i) is a corporation, the information called for in paragraphs (h) and (i) of this section must be given with respect to:

a. each executive officer and director of the corporation;

b. each person controlling the corporation; and

c. each executive officer and director of any corporation or other person ultimately in control of the corporation.

(j) The following information regarding the nature and extent of the relationships between the nominating shareholder or nominating shareholder group and nominee and the registrant or any affiliate of the registrant:

(1) Any direct or indirect material interest in any contract or agreement between the nominating shareholder or nominating shareholder group or the nominee and the registrant or any affiliate of the registrant (including any employment agreement, collective bargaining agreement, or consulting agreement);

(2) Any material pending or threatened litigation in which the nominating shareholder or nominating shareholder group or nominee is a party or a material participant, involving the registrant, any of its officers or directors, or any affiliate of the registrant; and

(3) Any other material relationship between the nominating shareholder or nominating shareholder group or the nominee and the registrant or any affiliate of the registrant not otherwise disclosed;

Note to paragraph (j)(3).

Any other material relationship of the nominating shareholder or nominating shareholder group with the registrant or any affiliate of the registrant may include, but is not limited to, whether the nominating shareholder or nominating shareholder group currently has, or has had in the past, an employment relationship with the registrant or any affiliate of the registrant (including consulting arrangements).

(k) The website address on which the nominating shareholder or nominating shareholder group may publish soliciting materials, if any; and

(l) Any statement in support of the shareholder nominee or nominees, which may not exceed 500 words, if the nominating shareholder or nominating shareholder group elects to have such statement included in the registrant's proxy materials.

16. Add §240.14a-19 to read as follows:

§240.14a-19 Disclosure regarding nominating shareholders and nominees submitted for inclusion in a registrant's proxy materials pursuant to applicable state law or a registrant's governing documents.

To have a nominee included in a registrant's proxy materials pursuant to a procedure set forth under applicable state law or the registrant's governing documents addressing the inclusion of shareholder director nominees in the registrant's proxy materials, the nominating shareholder or nominating shareholder group must provide notice to the registrant of its intent to do so on a Schedule 14N and file that notice with the Commission on the date first sent to the registrant. This notice shall be sent to the registrant by the date specified by the registrant's advance notice provision or, where no such provision is in place, no later than 120 calendar days before the date that the registrant mailed its proxy materials for the prior year's annual meeting, except that, if the registrant did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, then the nominating shareholder or nominating shareholder group must provide notice a reasonable time before the registrant mails its proxy materials, as specified by the registrant in a Form 8-K (§249.308 of this chapter) filed pursuant to Item 5.07 of Form 8-K. This notice must include:

(a) A statement from the nominee that the nominee consents to be named in the registrant's proxy statement and form of proxy and, if elected, to serve on the registrant's board of directors;

(b) Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A (§240.14a-101), as applicable;

(c) Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A (§240.14a-101), as applicable;

(d) Disclosure about whether the nominating shareholder or member of a nominating shareholder group has been involved in any legal proceeding during the past five years, as specified in Item 401(f) of Regulation S-K (§229.10 of this chapter). Disclosure pursuant to this section need not be provided if provided in response to Items 4(b) and 5(b) of Schedule 14A

(§240.14a-101);

Instruction 1 to paragraphs (c) and (d).

Where the nominating shareholder is a general or limited partnership, syndicate or other group, the information called for in paragraphs (c) and (d) of this section must be given with respect to:

a. each partner of the general partnership;

b. each partner who is, or functions as, a general partner of the limited partnership;

c. each member of the syndicate or group; and

d. each person controlling the partner or member.

Instruction 2 to paragraphs (c) and (d).

If the nominating shareholder is a corporation or if a person referred to in a., b., c. or d. of Instruction 1 to paragraphs (c) and (d) is a corporation, the information called for in paragraphs (c) and (d) of this section must be given with respect to:

a. each executive officer and director of the corporation;

b. each person controlling the corporation; and

c. each executive officer and director of any corporation or other person ultimately in control of the corporation.

(e) The following information regarding the nature and extent of the relationships between the nominating shareholder or nominating shareholder group and nominee and the registrant or any affiliate of the registrant:

(1) Any direct or indirect material interest in any contract or agreement between the nominating shareholder or nominating shareholder group or the nominee and the registrant or any affiliate of the registrant (including any employment agreement, collective bargaining

agreement, or consulting agreement);

(2) Any material pending or threatened litigation in which the nominating shareholder or nominating shareholder group or nominee is a party or a material participant, involving the registrant, any of its officers or directors, or any affiliate of the registrant; and

(3) Any other material relationship between the nominating shareholder or nominating shareholder group or the nominee and the registrant or any affiliate of the registrant not otherwise disclosed; and

Instruction to paragraph (e)(3).

Any other material relationship of the nominating shareholder or nominating shareholder group with the registrant or any affiliate of the registrant may include, but is not limited to, whether the nominating shareholder or nominating shareholder group currently has, or has had in the past, an employment relationship with the registrant or any affiliate of the registrant (including consulting arrangements).

(f) The website address on which the nominating shareholder or nominating shareholder group may publish soliciting materials, if any.

Note to §240.14a-19. The registrant is not responsible for any information in the notice from the nominating shareholder or nominating shareholder group or otherwise provided by the nominating shareholder or nominating shareholder group, except where the registrant knows or has reason to know that the information is false or misleading.

17. Amend §240.14a-101 by:

a. Adding on the cover page one box before the box "Soliciting Material under §240.14a-12";

b. Revising Item 7 as follows:

i. Redesignating paragraph (e) as paragraph (g); and

ii. Adding new paragraph (e) and paragraph (f); and

c. Adding paragraphs (18) and (19) to Item 22(b).

.The additions and revisions read as follows:

§240.14a-101 – Schedule 14A. Information required in proxy statement.

SCHEDULE 14A INFORMATION

* * * * *

[ ] Soliciting Material under §240.14a-11

* * * * *

Item 7. * * *

* * * * *

(e) If a shareholder nominee or nominees are submitted to the registrant and the registrant is not permitted to exclude the nominee or nominees pursuant to the provisions of §240.14a-11, the registrant must include the disclosure required from the nominating shareholder or nominating shareholder group under §240.14a-18(e)-(l) with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to Item 7(e).

The information disclosed pursuant to paragraph (e) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933, the Securities Exchange Act of 1934, or the Investment Company Act of 1940, except to the extent that the registrant specifically incorporates that information by reference.

(f) If a shareholder nominee or nominees are submitted to the registrant for inclusion in the registrant's proxy materials pursuant to a procedure set forth under applicable state law or the registrant's governing documents providing for the inclusion of shareholder director nominees in the registrant's proxy materials, the registrant must include the disclosure required from the nominating shareholder or nominating shareholder group under §240.14a-19(a)-(f) with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to Item 7(f).

The information disclosed pursuant to paragraph (f) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933, the Securities Exchange Act of 1934, or the Investment Company Act of 1940, except to the extent that the registrant specifically incorporates that information by reference.

* * * * *

Item 22. Information required in investment company proxy statement.

* * * * *

(b) * * *

(18) If a shareholder nominee or nominees are submitted to the Fund and the Fund is not permitted to exclude the nominee or nominees pursuant to the provisions of §240.14a-11, the Fund must include the disclosure required from the nominating shareholder or nominating shareholder group under §240.14a-18(e)-(l) with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to paragraph (b)(18).

The information disclosed pursuant to paragraph (b)(18) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933, the Securities Exchange Act of 1934, or the Investment Company Act of 1940, except to the extent that the Fund specifically incorporates that information by reference.

(19) If a shareholder nominee or nominees are submitted to the Fund for inclusion in the Fund's proxy materials pursuant to a procedure set forth under applicable state law or the Fund's governing documents providing for the inclusion of shareholder director nominees in the Fund's proxy materials, the Fund must include the disclosure required from the nominating shareholder or nominating shareholder group under §240.14a-19(a)-(f) with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

<u>Instruction to paragraph (b)(19)</u>.

The information disclosed pursuant to paragraph (b)(19) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933, the Securities Exchange Act of 1934, or the Investment Company Act of 1940, except to the extent that the Fund specifically incorporates that information by reference.

* * * * *

18. Amend Part 240 by adding an undesignated center heading and §§240.14n-1 through 240.14n-3 and §240.14n-101 to read as follows:

REGULATION 14N: FILINGS REQUIRED BY CERTAIN NOMINATING SHAREHOLDERS

§ 240.14n-1 Filing of Schedule 14N.

(a) A shareholder or group of shareholders that submits a nominee or nominees in accordance with §240.14a-11 or a procedure set forth under applicable state law or a registrant's governing documents providing for the inclusion of shareholder director nominees in the registrant's proxy materials shall file with the Commission a statement containing the information required by Schedule 14N (§240.14n-101) and simultaneously provide the notice on Schedule 14N to the registrant.

(b)(1) Whenever two or more persons are required to file a statement containing the information required by Schedule 14N (§240.14n-101), only one statement need be filed. The statement must identify all such persons, contain the required information with regard to each such person, indicate that the statement is filed on behalf of all such persons, and include, as an exhibit, their agreement in writing that the statement is filed on behalf of each of them. Each person on whose behalf the statement is filed is responsible for the timely filing of that statement and any amendments thereto, and for the completeness and accuracy of the information concerning such person contained therein; such person is not responsible for the completeness or accuracy of the information concerning the other persons making the filing, unless such person knows or has reason to know that the information is inaccurate.

(2) If the group's members elect to make their own filings, each filing should identify all members of the group but the information provided concerning the other persons making the filing need only reflect information which the filing person knows or has reason to know.

§ 240.14n-2 Filing of amendments to Schedule 14N.

(a) If any material change occurs in the facts set forth in the Schedule 14N (§240.14n–101) required by §240.14n–1(a), the person or persons who were required to file the statement shall promptly file or cause to be filed with the Commission an amendment disclosing that change.

(b) An amendment shall be filed within 10 calendar days of the final results of the election being announced by the registrant stating the nominating shareholder's or the nominating shareholder group's intention with regard to continued ownership of their shares.

§ 240.14n-3 Dissemination.

One copy of Schedule 14N (§240.14n-101) filed pursuant to §§240.14n–1 and 240.14n–

2 shall be sent to the issuer of the security at its principal executive office by registered or certified mail. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered.

§ 240.14n-101 Schedule 14N – Information to be included in statements filed pursuant to §240.14n-1 and amendments thereto filed pursuant to §240.14n-2.

Securities and Exchange Commission, Washington, D.C. 20549

Schedule 14N

Under the Securities Exchange Act of 1934

(Amendment No._)*

____

(Name of Issuer)

____

(Title of Class of Securities)

____

(CUSIP Number)

____

[ ] Notice of Submission of a Nominee or Nominees in Accordance with §240.14a-11

[ ] Notice of Submission of a Nominee or Nominees in Accordance with Procedures Set Forth Under Applicable State Law or the Registrant's Governing Documents

*The remainder of this cover page shall be filled out for a reporting person's initial filing on this form, and for any subsequent amendment containing information which would alter the disclosures provided in a prior cover page.

The information required in the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act but shall be subject to all other provisions of the Act.

(1) Names of reporting persons

(2) Amount of securities beneficially owned and entitled to be voted on the election of directors held by each reporting person: ___________________

(3) Percent of securities entitled to be voted on the election of directors represented by amount in Row (2): _________________

Instructions for Cover Page:

(1) Names of Reporting Persons – Furnish the full legal name of each person for whom the report is filed – i.e., each person required to sign the schedule itself – including each member of a group. Do not include the name of a person required to be identified in the report but who is not a reporting person.

(2) and (3) Amount Held by Each Reporting Person – Rows (2) and (3) are to be completed in accordance with the provisions of Item 3 of Schedule 14N. All percentages are to be rounded off to the nearest tenth (one place after decimal point).

Notes: Attach as many copies of the second part of the cover page as are needed, one reporting person per page.

Filing persons may, in order to avoid unnecessary duplication, answer items on Schedule 14N by appropriate cross references to an item or items on the cover page(s). This approach may only be used where the cover page item or items provide all the disclosure required by the schedule item. Moreover, such a use of a cover page item will result in the item becoming a part of the schedule and accordingly being considered as "filed" for purposes of section 18 of the Act or otherwise subject to the liabilities of that section of the Act.

SPECIAL INSTRUCTIONS FOR COMPLYING WITH SCHEDULE 14N

Under Sections 14 and 23 of the Securities Exchange Act of 1934 and the rules and regulations thereunder, the Commission is authorized to solicit the information required to be supplied by this schedule. The information will be used for the primary purpose of determining and disclosing the holdings and interests of a nominating shareholder or nominating shareholder group. This statement will be made a matter of public record. Therefore, any information given will be available for inspection by any member of the public.

Because of the public nature of the information, the Commission can use it for a variety of purposes, including referral to other governmental authorities or securities self-regulatory organizations for investigatory purposes or in connection with litigation involving the Federal securities laws or other civil, criminal or regulatory statutes or provisions. Failure to disclose the information requested by this schedule may result in civil or criminal action against the persons involved for violation of the Federal securities laws and rules promulgated thereunder.

<u>Instructions</u>

The item numbers and captions of the items shall be included but the text of the items is to be omitted. The answers to the items shall be prepared so as to indicate clearly the coverage of the items without referring to the text of the items. Answer every item. If an item is inapplicable or the answer is in the negative, so state.

Item 1(a). **Name of registrant**

Item 1(b). **Address of registrant's principal executive offices**

Item 2(a). **Name of person filing**

Item 2(b). **Address or principal business office or, if none, residence**

Item 2(c). **Title of class of securities**

Item 2(d). **CUSIP No.**

Item 3. **Ownership**

Provide the following information regarding the aggregate number and percentage of the securities of the registrant identified in Item 1.

(a) Amount of securities beneficially owned and entitled to be voted on the election of directors at the meeting: _____.

(b) Percent of securities entitled to be voted on the election of directors at the meeting: _____.

Item 4. **Notice of Dissolution of Group**

Notice of dissolution of a nominating shareholder group or the termination of a shareholder nomination shall state the date of the dissolution or termination.

Item 5. **Statement of Ownership From a Nominating Shareholder or Each Member of a Nominating Shareholder Group Submitting this Notice Pursuant to §240.14a-11**

(a) If the nominating shareholder, or each member of the nominating shareholder group, is the registered holder of the shares, please so state. Otherwise, attach to Schedule 14N a written statement from the "record" holder of the nominating shareholder's shares (usually a broker or bank) verifying that, at the time of submitting the shareholder notice to the registrant on Schedule 14N, the nominating shareholder continuously held the securities being used to satisfy the applicable ownership threshold for a period of at least one year. In the alternative, if the nominating shareholder has filed a Schedule 13D, Schedule 13G, Form 3, Form 4, and/or Form 5, or amendments to those documents, so state and attach a copy or incorporate that filing by reference.

(b) Provide a written statement that the nominating shareholder, or each member of the nominating shareholder group, intends to continue to own the requisite shares through the date of the meeting of shareholders. Additionally, at the time this Schedule is filed, the nominating shareholder or each member of the nominating shareholder group must provide a written statement regarding the nominating shareholder's or nominating shareholder group member's intent with respect to continued ownership after the election.

Item 6. Representations and Disclosure Required by §240.14a-18

If a nominating shareholder or nominating shareholder group is submitting this notice in connection with the inclusion of a shareholder nominee or nominees for director in the company's proxy materials pursuant to §240.14a-11, provide the information required by §240.14a-18.

Item 7. Disclosure Required by §240.14a-19

If a nominating shareholder or nominating shareholder group is submitting this notice in connection with the inclusion of a shareholder nominee or nominees for director in the company's proxy materials pursuant to a procedure set forth under applicable state law or the registrant's governing documents, provide the information required by §240.14a-19.

Item 8. Certification for Nominating Shareholder Notices Submitted under §240.14a-11

The following certification shall be provided by the filing person, or in the case of a group, each filing person whose securities are being aggregated for purposes of meeting the ownership threshold set out in §240.14a-11(b):

By signing below I certify that, to the best of my knowledge and belief, the securities referred to above are not held for the purpose of or with the effect of changing control of the issuer of the securities or to gain more than a limited number of seats on the board.

Signature

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

Dated: ___________

Signature: __________________

Name/Title: ____________________

The original statement shall be signed by each person on whose behalf the statement is filed or his authorized representative. If the statement is signed on behalf of a person by his authorized representative other than an executive officer or general partner of the filing person, evidence of the representative's authority to sign on behalf of such person shall be filed with the statement, provided, however, that a power of attorney for this purpose which is already on file with the Commission may be incorporated by reference. The name and any title of each person who signs the statement shall be typed or printed beneath his signature.

Attention: Intentional misstatements or omissions of fact constitute Federal criminal violations (see 18 U.S.C. 1001).

19. Amend §240.15d-11 by revising paragraph (b) to read as follows:

§240.15d-11 Current reports on Form 8-K (§249.308 of this chapter).

* * * * *

(b) This section shall not apply to foreign governments, foreign private issuers required to make reports on Form 6-K (17 CFR 249.306) pursuant to §240.15d-16, issuers of American Depositary Receipts for securities of any foreign issuer, or investment companies required to file reports pursuant to §270.30b1-1 of this chapter under the Investment Company Act of 1940, except where such an investment company is required to file:

(1) Notice of a blackout period pursuant to §245.104 of this chapter;

(2) Disclosure pursuant to Instruction 2 to §240.14a-11(a) of the date by which a nominating shareholder or nominating shareholder group must submit the notice required pursuant to §240.14a-11(c); or

(3) Disclosure pursuant to Instruction 3 to §240.14a-11(b) of information concerning net assets, outstanding shares, and voting.

* * * * *

PART 249 – FORMS, SECURITIES EXCHANGE ACT OF 1934

20. The authority citation for Part 249 continues to read in part as follows:

Authority: 15 U.S.C. 78a et seq., 7201 et seq.; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

21. Amend Form 8-K (referenced in §249.308) by:

a. Adding a sentence at the end of General Instruction B.1;

b. Removing the heading "Section 5.06" and adding in its place "Item 5.06"; and

c. Adding Item 5.07.

The additions read as follows:

Note: The text of Form 8-K does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 8-K

* * * * *

GENERAL INSTRUCTIONS

* * * * *

B. Events to be Reported and Time for Filing Reports

1. * * * A report pursuant to Item 5.07 is to be filed within four business days after the registrant determines the anticipated meeting date.

* * * * *

Item 5.07 Shareholder Nominations Pursuant to Exchange Act Rule 14a-11

(a) If the registrant did not hold an annual meeting the previous year, or if the date of this year's annual meeting has been changed by more than 30 calendar days from the date of the previous year's meeting, then the registrant is required to disclose the date by which a nominating shareholder or nominating shareholder group must submit the notice required pursuant to §240.14a-11(c), which date shall be a reasonable time before the registrant mails its' proxy materials for the meeting.

(b) If the registrant is a series company as defined in Rule 18f-2(a) under the Investment Company Act of 1940 (17 CFR §270.18f-2), then the registrant is required to disclose in connection with the election of directors at an annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders):

(1) The registrant's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting; and

(2) The total number of shares of the registrant outstanding and entitled to be voted (or if the votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) at such meeting of shareholders as of the end of the most recent calendar quarter.

* * * * *

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Date: June 10, 2009

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 10, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13511

In the Matter of Xentel Interactive, Inc., XXSYS Technologies, Inc., Yuma Gold Mines Ltd. (n/k/a Yuma Copper Corp.), Zion Development Corp., and Zomex Distribution, Inc., Respondents.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Xentel Interactive, Inc., XXSYS Technologies, Inc., Yuma Gold Mines Ltd. (n/k/a Yuma Copper Corp.), Zion Development Corp., and Zomex Distribution, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Xentel Interactive, Inc. (CIK No. 1034989) is an Alberta corporation located in Calgary, Alberta, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Xentel Interactive is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-FR/A amended registration statement on August 28, 1997, which reported a net loss of $7,406,710 (Canadian) for the year ended December 31, 1996.

2. XXSYS Technologies, Inc. (CIK No. 885976) is a California corporation located in San Diego, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). XXSYS Technologies is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 1998, which reported a net loss of $649,961 for the prior three months.

3. Yuma Gold Mines Ltd. (n/k/a Yuma Copper Corp.) (CIK No. 1005833) is a British Columbia corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Yuma Gold Mines is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-FR registration statement on January 11, 1996, which reported a net loss of $1,156,332 (Canadian) for the prior year ended May 31, 1995.

4. Zion Development Corp. (CIK No. 1172325) is a Nevada corporation located in St. George, Utah with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Zion Development is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-SB/A on March 29, 2004, which reported a net loss of $40,272 for the nine months ended September 30, 2003.

5. Zomex Distribution, Inc. (CIK No. 1070639) is a Nevada corporation located in Peachland, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Zomex Distribution is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 2005, which reported a net loss of $78,944 from the company's August 12, 1998 inception.

B. DELINQUENT PERIODIC FILINGS

6. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

7. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires domestic issuers to file quarterly reports. Rule 13a-16 requires certain foreign private issuers to furnish quarterly and other material reports to the Commission under cover of Form 6-K if they make or are required to make the information public under the laws of the jurisdiction of their domicile or in which they are incorporated or organized; if they file or are required to file information with a stock exchange on which their securities are traded and the information was made public by the exchange; or if they distribute or are required to distribute information to their security holders.

8. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 or 13a-16 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

Attachment

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Appendix 1

Chart of Delinquent Filings
In the Matter of Xentel Interactive, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Xentel Interactive, Inc.					
	20-F	12/31/97	06/30/98	Not filed	132
	20-F	12/31/98	06/30/99	Not filed	120
	20-F	12/31/99	06/30/00	Not filed	108
	20-F	12/31/00	07/02/01	Not filed	95
	20-F	12/31/01	07/01/02	Not filed	83
	20-F	12/31/02	06/30/03	Not filed	72
	20-F	12/31/03	06/30/04	Not filed	60
	20-F	12/31/04	06/30/05	Not filed	48
	20-F	12/31/05	06/30/06	Not filed	36
	20-F	12/31/06	07/02/07	Not filed	23
	20-F	12/31/07	06/30/08	Not filed	12
Total Filings Delinquent	**10**				
XXSYS Technologies, Inc.					
	10-QSB	03/31/99	05/17/99	Not filed	121
	10-QSB	06/30/99	08/16/99	Not filed	118
	10-KSB	09/30/99	12/29/99	Not filed	114
	10-QSB	12/31/99	02/14/00	Not filed	112
	10-QSB	03/31/00	05/15/00	Not filed	109
	10-QSB	06/30/00	08/14/00	Not filed	106
	10-KSB	09/30/00	12/29/00	Not filed	102
	10-QSB	12/31/00	02/14/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94
	10-KSB	09/30/01	12/31/01	Not filed	90
	10-QSB	12/31/01	02/14/02	Not filed	88

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
XXSYS Technologies, Inc.					
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-KSB	09/30/02	12/30/02	Not filed	78
	10-QSB	12/31/02	02/14/03	Not filed	76
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-KSB	09/30/03	12/29/03	Not filed	66
	10-QSB	12/31/03	02/17/04	Not filed	64
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-KSB	09/30/04	12/29/04	Not filed	54
	10-QSB	12/31/04	02/14/05	Not filed	52
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-KSB	09/30/05	12/29/05	Not filed	42
	10-QSB	12/31/05	02/14/06	Not filed	40
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-KSB	09/30/06	12/29/06	Not filed	30
	10-QSB	12/31/06	02/14/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-KSB	09/30/07	12/31/07	Not filed	18
	10-QSB	12/31/07	02/14/08	Not filed	16
	10-QSB	03/31/08	05/15/08	Not filed	13
	10-QSB	06/30/08	08/14/08	Not filed	10
	10-KSB	09/30/08	11/14/08	Not filed	7
	10-QSB	12/31/08	02/16/09	Not filed	4
	10-QSB	03/31/09	05/15/09	Not filed	1

Total Filings Delinquent **41**

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Yuma Gold Mines, Ltd. (n/k/a Yuma Copper Corp.)					
	20-F	05/31/96	12/02/96	Not filed	150
	20-F	05/31/97	12/01/97	Not filed	138
	20-F	05/31/98	11/30/98	Not filed	127
	20-F	05/31/99	11/30/99	Not filed	115
	20-F	05/31/00	11/30/00	Not filed	103
	20-F	05/31/01	11/30/01	Not filed	91
	20-F	05/31/02	12/02/02	Not filed	78
	20-F	05/31/03	12/01/03	Not filed	66
	20-F	05/31/04	11/30/04	Not filed	55
	20-F	05/31/05	11/30/05	Not filed	43
	20-F	05/31/06	11/30/06	Not filed	31
	20-F	05/31/07	11/30/07	Not filed	19
	20-F	05/31/08	12/01/08	Not filed	6
Total Filings Delinquent	**13**				
Zion Development Corp.					
	10-QSB	09/30/03	02/12/04	Not filed	64
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Zion Development Corp.					
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	10-Q1	03/31/08	05/15/08	Not filed	13
	10-Q1	06/30/08	08/14/08	Not filed	10
	10-Q1	09/30/08	11/14/08	Not filed	7
	10-K1	12/31/08	03/31/09	Not filed	3
	10-Q1	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**23**				
Zomex Distribution, Inc.					
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	10-Q1	03/31/08	05/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Zomex Distribution, Inc.					
	10-Q[1]	06/30/08	08/14/08	Not filed	10
	10-Q[1]	09/30/08	11/14/08	Not filed	7
	10-K[1]	12/31/08	03/31/09	Not filed	3
	10-Q[1]	03/31/09	05/15/09	Not filed	1

Total Filings Delinquent **14**

[1]Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, are in the process of being removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal is taking effect over a transition period that will conclude on March 15, 2009, so by that date, all reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB will be required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) will have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60098 / June 11, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2989 / June 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13515

In the Matter of **ELIZABETH MONRAD, CPA,** **Respondent.**	**ORDER OF FORTHWITH SUSPENSION PURSUANT TO RULE 102(e)(2) OF THE COMMISSION'S RULES OF PRACTICE**

I.

The Securities and Exchange Commission deems it appropriate to issue an order of forthwith suspension of Elizabeth Monrad ("Monrad") pursuant to Rule 102(e)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.102(e)(2)].[1]

II.

The Commission finds that:

1. Monrad was licensed as a certified public accountant in Massachusetts from 1983 to June 30, 1993, when her licensed expired. She was the chief financial officer of General Re Corporation ("Gen Re") from June 2000 until July 2003 when she left Gen Re to become the chief financial officer of another company. From May 2002 through July 2003, Monrad also was a member of the executive committee of Gen Re's board of directors. From 1997, Monrad was the chief financial officer of Gen Re's North American Operations.

[1] Rule 102(e)(2) provides in pertinent part: "Any ... person who has been convicted of a felony or a misdemeanor involving moral turpitude shall be forthwith suspended from appearing or practicing before the Commission."

2. On April 14, 2009, a judgment of conviction was entered against Monrad in *United States v. Elizabeth Monrad, et al*, No. 06 CR 137 (CFI), in the United States District Court for the District of Connecticut, finding her guilty of sixteen felony counts, including 1 count of conspiracy to violate the Federal securities laws and to commit mail fraud, 7 counts of securities fraud, 5 counts of making false statements to the Commission, and 3 counts of mail fraud. The criminal indictment against Monrad resulted from her participation in a scheme to help American International Group, Inc. ("AIG") structure two sham reinsurance transactions. These sham transactions were a fraudulent device by which AIG added a total of $500 million in phony loss reserves to its balance sheet, $250 million in the fourth quarter of 2000 and another $250 million in the first quarter of 2001.

3. The court sentenced Monrad to 18 months imprisonment followed by 24 months of supervised release and ordered her to pay a fine of $250,000.

III.

In view of the foregoing, the Commission finds that Monrad has been convicted of a felony within the meaning of Rule 102(e)(2) of the Commission's Rules of Practice.

Accordingly, it is ORDERED, that Elizabeth Monrad is forthwith suspended from appearing or practicing before the Commission pursuant to Rule 102(e)(2) of the Commission's Rules of Practice.

By the Commission.

Elizabeth M. Murphy
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. 60095 / June 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13514

In the Matter of RICKY D. VAN VLEET, 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 Ricky D. Van Vleet ("Van Vleet" 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.

III.

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

1. From February 2003 through November 2004, Van Vleet, though not registered with the Commission, acted as a broker with respect to the offer and sale of securities, including promissory notes. Van Vleet, 64 years old, is a resident of Fort Collins, Colorado.

2. On November 4, 2008, Van Vleet pled guilty to one count of securities fraud, a class three felony, in violation of Colo. Rev. Stat. § 11-51-501(1)(b) before the Colorado District Court, Larimer County, in People v. Van Vleet, Case No. 08CR389. On February 24, 2009, a judgment in the criminal case was entered against Van Vleet. He was sentenced to a prison term of ten years followed by five years of mandatory parole and ordered to make restitution in the amount of $2,995,500.

3. The count of the criminal indictment to which Van Vleet pled guilty alleged, inter alia, that between February 2003 and November 2004, Van Vleet defrauded investors by means of materially false and misleading statements and omissions in connection with the offer or sale of securities in Colorado.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act, that Respondent Van Vleet 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.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13516

In the Matter of **Toltec Real Estate Corp.,** **Tong Ah Global Ventures Corp.,** **TotalAxcess.com, Inc.,** **Touch Tone America, Inc.,** **Tour CFG, Inc.,** **Tradeqwest, Inc.,** **Triteal Corp., and** **Trojan Transition Corp.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Toltec Real Estate Corp., Tong Ah Global Ventures Corp., TotalAxcess.com, Inc., Touch Tone America, Inc., Tour CFG, Inc., Tradeqwest, Inc., Triteal Corp., and Trojan Transition Corp.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Toltec Real Estate Corp. (CIK No. 92522) is a void Delaware corporation located in Eloy, Arizona with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Toltec is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K for the period ended May 31, 1998. On June 19, 1998, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Arizona, a reorganization plan was confirmed on February 8, 1999, and the case was terminated on November 7, 2006.

2. Tong Ah Global Ventures Corp. (CIK No. 1103582) is a void Delaware corporation located in Vista, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tong Ah is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 2001.

3. TotalAxcess.com, Inc. (CIK No. 828956) is a void Delaware corporation located in Oakland, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). TotalAxcess.com is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB/A for the period ended March 31, 2001, which reported a net loss of over $3.1 million for the prior nine months. On January 22, 2004, TotalAxcess.com filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Northern District of California, and the case was terminated on May 5, 2005. As of June 8, 2009, the company's stock (symbol "TXCS") was traded on the over-the-counter markets.

4. Touch Tone America, Inc. (CIK No. 945364) is a suspended California corporation located in Las Vegas, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Touch Tone is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended November 30, 1997, which reported a net loss of over $1.8 million for the prior six months.

5. Tour CFG, Inc. (CIK No. 730626) is a void Delaware corporation located in Tampa, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tour CFG is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 1997, which reported a net loss of $3.75 million for the prior nine months. On March 3, 1998, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Middle District of Florida, and the case was terminated on September 24, 1998. As of June 8, 2009, the company's stock (symbol "TOUR") was traded on the over-the-counter markets.

6. Tradeqwest, Inc. (CIK No. 1101508) is a void Delaware corporation located in Inglewood, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tradeqwest is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 2001, which reported a net loss of $7,700 for the prior three months.

7. Triteal Corp. (CIK No. 1000925) is a void Delaware corporation located in San Diego, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Triteal is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the

period ended September 30, 1997, which reported a net loss of over $8 million for the prior six months. On April 2, 1999, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Southern District of California, and the case was terminated on December 29, 2004.

8. Trojan Transition Corp. (CIK No. 1112867) is a suspended California corporation located in Irvine, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Trojan is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 2001, which reported a net loss of $2,358 since inception on February 17, 2000.

B. DELINQUENT PERIODIC FILINGS

9. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

10. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

11. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

Attachment

By: J. Lynn Taylor
Assistant Secretary

Chart of Delinquent Filings
Toltec Real Estate Corp., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Toltec Real Estate Corp.					
	10-Q	08/31/98	10/15/98	Not filed	128
	10-Q	11/30/98	01/14/99	Not filed	125
	10-Q	02/28/99	04/14/99	Not filed	122
	10-K	05/31/99	08/30/99	Not filed	118
	10-Q	08/31/99	10/15/99	Not filed	116
	10-Q	11/30/99	01/14/00	Not filed	113
	10-Q	02/29/00	04/14/00	Not filed	110
	10-K	05/31/00	08/29/00	Not filed	106
	10-Q	08/31/00	10/16/00	Not filed	104
	10-Q	11/30/00	01/16/01	Not filed	101
	10-Q	02/28/01	04/16/01	Not filed	98
	10-K	05/31/01	08/29/01	Not filed	94
	10-Q	08/31/01	10/15/01	Not filed	92
	10-Q	11/30/01	01/14/02	Not filed	89
	10-Q	02/28/02	04/15/02	Not filed	86
	10-K	05/31/02	08/29/02	Not filed	82
	10-Q	08/31/02	10/15/02	Not filed	80
	10-Q	11/30/02	01/14/03	Not filed	77
	10-Q	02/28/03	04/14/03	Not filed	74
	10-K	05/31/03	08/29/03	Not filed	70
	10-Q	08/31/03	10/15/03	Not filed	68
	10-Q	11/30/03	01/14/04	Not filed	65
	10-Q	02/28/04	04/13/04	Not filed	62
	10-K	05/31/04	08/30/04	Not filed	58
	10-Q	08/31/04	10/15/04	Not filed	56
	10-Q	11/30/04	01/14/05	Not filed	53
	10-Q	2/28/05	04/14/05	Not filed	50
	10-K	5/31/05	08/29/05	Not filed	46
	10-Q	08/31/05	10/17/05	Not filed	44
	10-Q	11/30/05	01/17/06	Not filed	41
	10-Q	2/28/06	04/14/06	Not filed	38
	10-K	5/31/06	08/29/06	Not filed	34
	10-Q	08/31/06	10/16/06	Not filed	32
	10-Q	11/30/06	01/16/07	Not filed	29
	10-Q	2/28/07	04/16/07	Not filed	26
	10-K	5/31/07	08/29/07	Not filed	22

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
***Toltec Real Estate Corp.* (Continued)**	*10-Q*	08/31/07	10/15/07	Not filed	20
	10-Q	11/30/07	01/14/08	Not filed	17
	10-Q	2/28/08	04/14/08	Not filed	14
	10-K	5/31/08	08/29/08	Not filed	10
	10-Q	08/31/08	10/15/08	Not filed	8
	10-Q	11/30/08	01/14/09	Not filed	5
	10-Q	2/28/09	04/14/09	Not filed	2
Total Filings Delinquent	**43**				
Tong Ah Global Ventures Corp.					
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	10-Q [1]	03/31/08	05/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
***Tong Ah Global Ventures Corp.* (Continued)**	*10-Q* [1]	06/30/08	08/14/08	Not filed	10
	10-Q [1]	09/30/08	11/14/08	Not filed	7
	10-K [1]	12/31/08	03/31/09	Not filed	3
	10-Q [1]	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**31**				
TotalAxcess.com, Inc.					
	10-KSB	06/30/01	9/28/01	Not filed	93
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-QSB	12/31/01	2/14/02	Not filed	88
	10-QSB	03/31/02	5/15/02	Not filed	85
	10-KSB	06/30/02	9/30/02	Not filed	81
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-QSB	12/31/02	2/14/03	Not filed	76
	10-QSB	03/31/03	5/15/03	Not filed	73
	10-KSB	06/30/03	9/29/03	Not filed	69
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-QSB	12/31/03	2/17/04	Not filed	64
	10-QSB	03/31/04	5/17/04	Not filed	61
	10-KSB	06/30/04	9/28/04	Not filed	57
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-QSB	12/31/04	2/14/05	Not filed	52
	10-QSB	03/31/05	5/16/05	Not filed	49
	10-KSB	06/30/05	9/28/05	Not filed	45
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-QSB	12/31/05	2/14/06	Not filed	40
	10-QSB	03/31/06	5/15/06	Not filed	37
	10-KSB	06/30/06	9/28/06	Not filed	33
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-QSB	12/31/06	2/14/07	Not filed	28
	10-QSB	03/31/07	5/15/07	Not filed	25
	10-KSB	06/30/07	9/28/07	Not filed	21
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	2/14/08	Not filed	16
	10-QSB	03/31/08	5/15/08	Not filed	13
	10-KSB	06/30/08	9/29/08	Not filed	9
	10-Q [1]	09/30/08	11/14/08	Not filed	7

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
TotalAxcess.com, Inc. (Continued)	*10-Q* [1]	12/31/08	2/17/09	Not filed	4
	10-Q [1]	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**32**				
Touch Tone America, Inc.					
	10-QSB	02/28/98	04/14/98	Not filed	134
	10-KSB	05/31/98	08/31/98	Not filed	130
	10-QSB	08/31/98	10/15/98	Not filed	128
	10-QSB	11/30/98	01/14/99	Not filed	125
	10-QSB	02/28/99	04/14/99	Not filed	122
	10-KSB	05/31/99	08/30/99	Not filed	118
	10-QSB	08/31/99	10/15/99	Not filed	116
	10-QSB	11/30/99	01/14/00	Not filed	113
	10-QSB	02/29/00	04/14/00	Not filed	110
	10-KSB	05/31/00	08/29/00	Not filed	106
	10-QSB	08/31/00	10/16/00	Not filed	104
	10-QSB	11/30/00	01/16/01	Not filed	101
	10-QSB	02/28/01	04/16/01	Not filed	98
	10-KSB	05/31/01	08/29/01	Not filed	94
	10-QSB	08/31/01	10/15/01	Not filed	92
	10-QSB	11/30/01	01/14/02	Not filed	89
	10-QSB	02/28/02	04/15/02	Not filed	86
	10-KSB	05/31/02	08/29/02	Not filed	82
	10-QSB	08/31/02	10/15/02	Not filed	80
	10-QSB	11/30/02	01/14/03	Not filed	77
	10-QSB	02/28/03	04/14/03	Not filed	74
	10-KSB	05/31/03	08/29/03	Not filed	70
	10-QSB	08/31/03	10/15/03	Not filed	68
	10-QSB	11/30/03	01/14/04	Not filed	65
	10-QSB	02/28/04	04/13/04	Not filed	62
	10-KSB	05/31/04	08/30/04	Not filed	58
	10-QSB	08/31/04	10/15/04	Not filed	56
	10-QSB	11/30/04	01/14/05	Not filed	53
	10-QSB	2/28/05	04/14/05	Not filed	50
	10-KSB	5/31/05	08/29/05	Not filed	46
	10-QSB	08/31/05	10/17/05	Not filed	44
	10-QSB	11/30/05	01/17/06	Not filed	41
	10-QSB	2/28/06	04/14/06	Not filed	38

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Touch Tone America, Inc. (Continued)	*10-KSB*	5/31/06	08/29/06	Not filed	34
	10-QSB	08/31/06	10/16/06	Not filed	32
	10-QSB	11/30/06	01/16/07	Not filed	29
	10-QSB	2/28/07	04/16/07	Not filed	26
	10-KSB	5/31/07	08/29/07	Not filed	22
	10-QSB	08/31/07	10/15/07	Not filed	20
	10-QSB	11/30/07	01/14/08	Not filed	17
	10-QSB	2/28/08	04/14/08	Not filed	14
	10-KSB	5/31/08	08/29/08	Not filed	10
	10-Q [1]	08/31/08	10/15/08	Not filed	8
	10-Q [1]	11/30/08	01/14/09	Not filed	5
	10-Q [1]	2/28/09	04/14/09	Not filed	2
Total Filings Delinquent	45				
Tour CFG, Inc.					
	10-KSB	09/30/97	12/29/97	Not filed	138
	10-QSB	12/31/97	02/17/98	Not filed	136
	10-QSB	03/31/98	05/15/98	Not filed	133
	10-QSB	06/30/98	08/14/98	Not filed	130
	10-KSB	09/30/98	12/29/98	Not filed	126
	10-QSB	12/31/98	02/16/99	Not filed	124
	10-QSB	03/31/99	05/17/99	Not filed	121
	10-QSB	06/30/99	08/16/99	Not filed	118
	10-KSB	09/30/99	12/29/99	Not filed	114
	10-QSB	12/31/99	02/14/00	Not filed	112
	10-QSB	03/31/00	05/15/00	Not filed	109
	10-QSB	06/30/00	08/14/00	Not filed	106
	10-KSB	09/30/00	12/29/00	Not filed	102
	10-QSB	12/31/00	02/14/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94
	10-KSB	09/30/01	12/31/01	Not filed	90
	10-QSB	12/31/01	02/14/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-KSB	09/30/02	12/30/02	Not filed	78
	10-QSB	12/31/02	02/14/03	Not filed	76

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tour CFG, Inc. (Continued)	*10-QSB*	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-KSB	09/30/03	12/29/03	Not filed	66
	10-QSB	12/31/03	02/17/04	Not filed	64
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-KSB	09/30/04	12/29/04	Not filed	54
	10-QSB	12/31/04	02/14/05	Not filed	52
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-KSB	09/30/05	12/29/05	Not filed	42
	10-QSB	12/31/05	02/14/06	Not filed	40
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-KSB	09/30/06	12/29/06	Not filed	30
	10-QSB	12/31/06	02/14/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-KSB	09/30/07	12/29/07	Not filed	18
	10-QSB	12/31/07	02/14/08	Not filed	16
	10-QSB	03/31/08	05/15/08	Not filed	13
	10-QSB	06/30/08	08/14/08	Not filed	10
	10-KSB	09/30/08	12/29/08	Not filed	6
	10-Q [1]	12/31/08	02/17/09	Not filed	4
	10-Q [1]	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**47**				
Tradeqwest, Inc.					
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tradeqwest, Inc. (Continued)					
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	10-Q[1]	03/31/08	05/15/08	Not filed	13
	10-Q[1]	06/30/08	08/14/08	Not filed	10
	10-Q[1]	09/30/08	11/14/08	Not filed	7
	10-K[1]	12/31/08	03/31/09	Not filed	3
	10-Q[1]	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**31**				
Triteal Corp.					
	10-Q	12/31/97	02/17/98	Not filed	136
	10-K	03/31/98	06/29/98	Not filed	132
	10-Q	06/30/98	08/14/98	Not filed	130
	10-Q	09/30/98	11/16/98	Not filed	127
	10-Q	12/31/98	02/16/99	Not filed	124
	10-K	03/31/99	06/29/99	Not filed	120
	10-Q	06/30/99	08/16/99	Not filed	118
	10-Q	09/30/99	11/15/99	Not filed	115
	10-Q	12/31/99	02/14/00	Not filed	112
	10-K	03/31/00	06/29/00	Not filed	108
	10-Q	06/30/00	08/14/00	Not filed	106
	10-Q	09/30/00	11/14/00	Not filed	103
	10-Q	12/31/00	02/14/01	Not filed	100

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Triteal Corp. (Continued)	*10-K*	03/31/01	06/29/01	Not filed	96
	10-Q	06/30/01	08/14/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-Q	12/31/01	02/14/02	Not filed	88
	10-K	03/31/02	07/01/02	Not filed	83
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-Q	12/31/02	02/14/03	Not filed	76
	10-K	03/31/03	06/30/03	Not filed	72
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-Q	12/31/03	02/17/04	Not filed	64
	10-K	03/31/04	06/29/04	Not filed	60
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-Q	12/31/04	02/14/05	Not filed	52
	10-K	03/31/05	06/29/05	Not filed	48
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-Q	12/31/05	02/14/06	Not filed	40
	10-K	03/31/06	06/29/06	Not filed	36
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-Q	12/31/06	02/14/07	Not filed	28
	10-K	03/31/07	06/29/07	Not filed	24
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-Q	12/31/07	02/14/08	Not filed	16
	10-K	03/31/08	06/30/08	Not filed	12
	10-Q	06/30/08	08/14/08	Not filed	10
	10-Q	09/30/08	11/14/08	Not filed	7
	10-Q	12/31/08	02/17/09	Not filed	4
Total Filings Delinquent	**45**				
Trojan Transition Corp.					
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Trojan Transition Corp.					
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	10-Q [1]	03/31/08	05/15/08	Not filed	13
	10-Q [1]	06/30/08	08/14/08	Not filed	10
	10-Q [1]	09/30/08	11/14/08	Not filed	7
	10-K [1]	12/31/08	03/31/09	Not filed	3
	10-Q [1]	03/31/09	05/15/09	Not filed	1

Total Filings Delinquent **30**

1 Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, have been removed from the federal securities laws. *See* Release No. 34-56994 (December 19, 2007). The removal took effect over a transition period that concluded on March 15, 2009. All reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB are now required to use Forms 10-Q and 10-K instead. forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60107; File No. PCAOB-2008-04)

June 12, 2009

Public Company Accounting Oversight Board; Notice of Filing of Proposed Rules on Annual and Special Reporting by Registered Public Accounting Firms

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on June 10, 2008, the Public Company Accounting Oversight Board (the "Board" or "PCAOB") filed with the Securities and Exchange Commission (the "Commission" or "SEC") the proposed rules described in Items I and II below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rules from interested persons.

I. Board's Statement of the Terms of Substance of the Proposed Rule

On June 10, 2008, the Board adopted rules consisting of eight new rules (PCAOB Rules 2200-2207) concerning annual and special reporting by registered public accounting firms, instructions to two forms to be used for such reporting (Form 2 and Form 3), and related amendments to existing Board Rules. The proposed rules text is set out below.

SECTION 2. REGISTRATION AND REPORTING

Part 2 – Reporting

2200. Annual Report

Each registered public accounting firm must file with the Board an annual report on Form 2 by following the instructions to that form. Unless directed otherwise by the

Board, the registered public accounting firm must file such annual report and exhibits thereto electronically with the Board through the Board's Web-based system.

2201. Time for Filing of Annual Report

Each registered public accounting firm must file the annual report on Form 2 no later than June 30 of each year, provided, however, that a registered public accounting firm that has its application for registration approved by the Board in the period between and including April 1 and June 30 of any year shall not be required to file an annual report in that year.

> Note: Pursuant to Rule 1002, in any year in which the filing deadline falls on a Saturday, Sunday, or federal legal holiday, the deadline for filing the annual report shall be the next day that is not a Saturday, Sunday, or federal legal holiday.

2202. Annual Fee

Each registered public accounting firm must pay an annual fee to the Board on or before July 31 of any year in which the firm is required to file an annual report on Form 2. The Board will, from time to time, announce the current annual fee. No portion of the annual fee is refundable.

2203. Special Reports

(a) A registered public accounting firm must file a special report on Form 3 to report information to the Board as follows –

(1) Upon the occurrence, on or after [effective date of this rule], of any event specified in Form 3, a registered public accounting firm must report the event in a special report filed no later than thirty days after the occurrence of the event;

(2) No later than thirty days after receiving notice of Board approval of its application for registration, a registered public accounting firm that becomes registered after [effective date of this rule] must file a special report to report any event specified in Form 3 that occurred after the date used by the firm for purposes of General Instruction 9 to Form 1 and before the date that the Board approved the firm's registration; and

(3) No later than [date thirty days after the effective date of this rule], a registered public accounting firm that is registered as of [effective date of this rule], must file a special report to report, to the extent applicable to the firm, certain information described in General Instruction 4 to Form 3 and current as of [effective date of this rule].

(b) A registered public accounting firm required to file a special report shall do so by filing with the Board a special report on Form 3 in accordance with the instructions to that form. Unless directed otherwise by the Board, a registered public accounting firm must file such special report and exhibits thereto electronically with the Board through the Board's Web-based system.

2204. Signatures

Each signatory to a report on Form 2 or Form 3 shall manually sign a signature page or other document authenticating, acknowledging or otherwise adopting his or her signature that appears in typed form within the electronic submission. Such document shall be executed before or at the time the electronic submission is made and shall be retained by the filer for a period of seven years. Upon request, an electronic filer shall provide to the Board or its staff a copy of all documents retained pursuant to this Rule.

2205. Amendments

Amendments to a filed report on Form 2 or Form 3 shall be made by filing an amended report on Form 2 or Form 3 in accordance with the instructions to those forms concerning amendments. Amendments shall not be filed to update information in a report that was correct at the time the report was filed, but only to correct information that was incorrect at the time the report was filed or to provide information that was omitted from the report and was required to be provided at the time the report was filed.

2206. Date of Filing

(a) An annual report shall be deemed to be filed on the date on which the registered public accounting firm submits a Form 2 in accordance with Rule 2200 that includes the signed certification required in Part X of Form 2.

(b) A special report on Form 3 shall be deemed to be filed on the date that the registered public accounting firm submits a Form 3 in accordance with Rule 2203 that includes the signed certification required in Part VIII of Form 3.

2207. Assertions of Conflicts with Non-U.S. Laws

If, in a report on Form 2 or Form 3, a foreign registered public accounting firm omits any information or affirmation required by the instructions to the relevant form on the ground that it cannot provide such information or affirmation on the form filed with the Board without violating non-U.S. law, the foreign registered public accounting firm shall –

(a) In accordance with the instructions to the form –

(1) Indicate that it has omitted required information or affirmations on the ground that it cannot provide such information or affirmations on the form filed with the Board without violating non-U.S. law;

(2) Identify all Items on the form with respect to which it has withheld any required information or affirmation on that ground; and

(3) Represent that, with respect to all such omitted information or affirmations, the foreign registered public accounting firm has satisfied the requirements of paragraph (b) of this Rule and has in its possession the materials required by paragraph (c) of this Rule;

(b) Before filing the form with the Board, make reasonable, good faith efforts, where not prohibited by law, to seek any consents or waivers that would be sufficient to allow it to provide the required information or affirmation on the form filed with the Board without violating non-U.S. law;

(c) Have in its possession, before the date on which the foreign registered public accounting firm files the form with the Board and for a period of seven years thereafter –

(1) An electronic version of the form that includes all information required by the instructions to the form (including certification and signature) and a manually signed signature page or other document that would satisfy the requirement of Rule 2204 if that version of the form were filed with the Board;

(2) A copy of the provisions of non-U.S. law that the foreign registered public accounting firm asserts prohibit it from providing the required information or affirmations on the form filed with the Board, and an English translation of any such provisions that are not in English;

(3) A legal opinion, in English, addressed to the foreign registered public accounting firm and that the foreign registered public accounting firm has reason to believe is current with respect to the relevant point of law, that the firm cannot provide the omitted information or affirmation on the form filed with the Board without violating non-U.S. law;

(4) A written representation, in English, that the Firm has made reasonable efforts, and a written description of those efforts, to obtain consents or waivers that would be sufficient to allow it to provide the required information or affirmation on the form filed with the Board, manually signed by the same person whose signature appears in the certification portion of the form, and indicating that the signer has reviewed the description and that the description is, based on the signer's knowledge, accurate and does not contain any untrue statements of material fact or omit to state a material fact necessary to make the statements made not misleading, and dated –

(i) for Form 2, after the end of the reporting period and no later than the date of the Form 2 filing; and

(ii) for Form 3, after the date of the reportable event and no later than the date of the Form 3 filing;

(d) Not later than the fourteenth day after any request by the Board or by the Director of the Division of Registration and Inspections for any of the documents described in subparagraphs (2) – (4) of paragraph (c) of this Rule, file an amended report on Form 2 or Form 3 including, as an exhibit to the amended report, the requested documents; and

(e) Not later than the fourteenth day after any request by the Board for any of the information included in the document described in subparagraph (1) of paragraph (c) of this Rule, file an amended report on Form 2 or Form 3 including the requested information.

Note: Rule 2207(c)(1) does not require that the version of the form maintained by the firm include any affirmation required by Part IX of Form 2. If the firm withholds any such affirmation, however, the asserted legal conflict must be addressed in accordance with subparagraphs (2) – (4) of Rule 2207(c).

Note: Rule 2207(c)(1) does not require a firm to include on the form maintained by the firm any information (1) that the firm does not possess, and (2) as to which the firm asserts that the firm would violate non-U.S. law by requiring another person to provide the information to the firm. The asserted legal conflict that prevents the firm from requiring another person to provide the information to the firm, however, must be addressed in accordance with subparagraphs (2) - (4) of Rule 2207(c).

Note: The "reasonable efforts" element of Rule 2207(c)(4) does not require a firm to renew efforts to seek consents or waivers from parties who have previously declined to provide consents or waivers with respect to disclosure of similar types of information and does not require a firm to seek consents or waivers from parties other than firm personnel and firm clients.

FORMS

FORM 2 – ANNUAL REPORT FORM

GENERAL INSTRUCTIONS

1. Submission of this Report. A registered public accounting firm must use this Form to file with the Board the annual report required by Section 102(d) of the Act and Rule 2200 and to file any amendments to an annual report. Unless otherwise directed by the Board, the Firm must file this Form, and all exhibits to this Form, electronically with the Board through the Board's Web-based system.

2. Defined Terms. The definitions in the Board's rules apply to this Form. Italicized terms in the instructions to this Form are defined in the Board's rules. In addition, as used in the instructions to this Form, the term "the Firm" means the registered public accounting firm that is filing this Form with the Board.

3. When Report is Considered Filed. Annual reports on this Form are required to be filed each year on or before June 30, subject to the qualification in Rule 2201 concerning any firm that has its application for registration approved by the Board in the period between and including April 1 and June 30. An annual report is considered filed when the Firm has submitted to the Board a Form 2 in accordance with Rule 2200 that includes the signed certification required in Part X of Form 2.

4. Period Covered by this Report. Annual reports on this Form shall cover a 12-month period from April 1 to March 31, subject to the qualification in Part VIII of Form 2 relating to the first annual report filed by a firm that becomes registered after [effective date of Rule 2201]. In the instructions to this Form, this is the period referred to as the "reporting period."

5. Amendments to this Report. Amendments shall not be filed to update information in a filed Form 2 that was correct at the time the Form was filed, but only to correct information that was incorrect at the time the Form was filed or to provide information that was omitted from the Form and was required to be provided at the time the Form was filed. When filing a Form 2 to amend an earlier filed Form 2, the Firm must supply not only the corrected or supplemental information, but must include in the amended Form 2 all information, affirmations, and certifications that were required to be included in the original Form 2. The Firm may access the originally filed Form 2 through the Board's Web-based system and make the appropriate amendments without needing to re-enter all other information.

Note: The Board will designate an amendment to an annual report as a report on "Form 2/A."

6. Rules Governing this Report. In addition to these instructions, the rules contained in Part 2 of Section 2 of the Board's rules govern this Form. Please read these rules and the instructions carefully before completing this Form.

7. Requests for Confidential Treatment. The Firm may, by marking the Form in accordance with the instructions provided, request confidential treatment of any information submitted in Part VI, Part VII, or Exhibit 99.3 of this Form that has not otherwise been publicly disclosed and that either contains information reasonably identified by the Firm as proprietary information or that is protected from public disclosure by applicable laws related to confidentiality of proprietary, personal, or other information. See Rule 2300. Foreign registered public accounting firms may also request confidential treatment for Item 3.2 and Exhibit 3.2, though U.S. firms may not do so. If the Firm requests confidential treatment, it must identify the information in Part VI, Part VII, or Exhibit 99.3 (or, for a foreign registered public accounting firm, Item 3.2 and Exhibit 3.2) that it desires to keep confidential, and include, as Exhibit 99.1 to this Form, an exhibit that complies with the requirements of Rule 2300(c)(2). The Board will determine whether to grant confidential treatment requests on a case-by-case basis. If the Firm fails to include Exhibit 99.1, or includes an Exhibit 99.1 that fails to comply with Rule 2300(c)(2), the request for confidential treatment may be denied solely on the basis of that failure.

8. Assertions of Conflicts with Non-U.S. Law. If the Firm is a foreign registered public accounting firm, the Firm may, unless otherwise directed by the Board pursuant to Rule 2207(e), decline to provide certain information and affirmations required by this Form if the Firm could not provide such information or affirmations without violating non-U.S. law and the Firm proceeds in accordance with Rule 2207. The Firm may withhold responsive information and affirmations on that basis from any Part of the Form other than Parts I, II, and X and Items 3.1.a, 3.1.b, 3.1.d, and 4.1. If the firm withholds responsive information or affirmations, the Firm must indicate, in accordance with the instructions in the relevant Part of the Form, the particular Items with respect to which the Firm has withheld responsive information or a required affirmation. The Firm may not use the Form to make any general assertion that a particular requirement may conflict with non-U.S. law, but only to indicate that, on the basis of an asserted conflict, the Firm has in fact withheld from this Form required information or a required affirmation.

9. Language. Information submitted as part of this Form, including any exhibit to this Form, must be in the English language.

PART I – IDENTITY OF THE FIRM AND CONTACT PERSONS

In Part I, the Firm should provide information that is current as of the date of the certification in Part X.

Item 1.1 Name of the Firm

a. State the legal name of the Firm.

b. If different than its legal name, state the name or names under which the Firm issues audit reports, or issued any audit report during the reporting period.

c. If the Firm's legal name at the beginning of the reporting period was different than the name provided under Item 1.1.a, state that legal name and any other legal name the Firm had during the reporting period. Include the legal name of any registered public accounting firm that merged into, or was acquired by, the Firm during the reporting period.

Item 1.2 Contact Information of the Firm

a. State the physical address (and, if different, mailing address) of the Firm's headquarters office.

b. State the telephone number and facsimile number of the Firm's headquarters office. If available, state the Website address of the Firm.

Item 1.3 Primary Contact with the <u>Board</u>

State the name, business title, physical business address (and, if different, business mailing address), business telephone number, business facsimile number, and business e-mail address of a partner or authorized officer of the Firm who will serve as the Firm's primary contact with the <u>Board</u>, including for purposes of the annual report filed on this Form and any special reports filed on Form 3.

PART II – GENERAL INFORMATION CONCERNING THIS REPORT

Item 2.1 Reporting Period

State the reporting period covered by this report.

Note: The reporting period, which the Firm should enter in Item 2.1, is the period beginning on April 1 of the year before the year in which the annual report is required to be filed and ending March 31 of the year in which the annual report is required to be filed. That is the period referred to where this Form refers to the "reporting period." Note, however, the special instruction at the beginning of Part VIII concerning the first annual report filed by certain firms.

Item 2.2 Amendments

If this is an amendment to a report previously filed with the Board –

a. Indicate, by checking the box corresponding to this item, that this is an amendment.

b. Identify the specific Item numbers of this Form (other than this Item 2.2) as to which the Firm's response has changed from that provided in the most recent Form 2 or amended Form 2 filed by the Firm with respect to the reporting period.

PART III – GENERAL INFORMATION CONCERNING THE FIRM

Item 3.1 The Firm's Practice Related to the Registration Requirement

a. Indicate whether the Firm issued any audit report with respect to an issuer during the reporting period.

b. In the event of an affirmative response to Item 3.1.a, indicate whether the issuers with respect to which the Firm issued audit reports during the reporting period were limited to employee benefit plans that file reports with the Commission on Form 11-K.

c. In the event of a negative response to Item 3.1.a, indicate whether the Firm played a substantial role in the preparation or furnishing of an audit report with respect to an issuer during the reporting period.

d. In the event of a negative response to both Items 3.1.a and 3.1.c, indicate whether, during the reporting period, the Firm issued any document with respect to financial statements of a non-issuer broker-dealer in which the Firm either set forth an opinion on the financial statements or asserted that no such opinion can be expressed.

Item 3.2 Fees Billed to Issuer Audit Clients

a. Of the total fees billed by the Firm to all clients for services that were rendered in the reporting period, state the percentage (which may be rounded, but no less specifically than to the nearest five percent) attributable to fees billed to issuer audit clients for–

1. Audit services;
2. Other accounting services;
3. Tax services; and

4. Non-audit services.

b. Indicate, by checking the appropriate box, which of the following two methods the Firm used to calculate the percentages reported in Item 3.2.a –

1. The Firm used as a denominator the total fees billed to all clients for services rendered during the reporting period and used as numerators (for each of the four categories) total fees billed to issuer audit clients for the relevant services rendered during the reporting period.

2. The Firm used as a denominator the total fees billed to all clients in the Firm's fiscal year that ended during the reporting period and used as numerators (for each of the four categories) total issuer audit client fees as determined by reference to the fee amounts disclosed to the Commission by those clients for each client's fiscal year that ended during the reporting period (including, for clients who have not made the required Commission filings, the fee amounts required to be disclosed).

c. If the Firm has used a reasonable method to estimate the components of the calculations described in Item 3.2.b, rather than using the specific data, check this box and attach Exhibit 3.2 briefly describing the reasons for doing so and the methodology used in making those estimates.

Note: In responding to Item 3.2, careful attention should be paid to the definitions of the italicized terms, which are found in Board Rules 1001(i)(iii) (issuer), 1001(a)(v) (audit), 1001(a)(vii) (audit services), 1001(o)(i) (other accounting services), 1001(t)(i) (tax services), and 1001(n)(ii) (non-audit services). The definitions of the four categories of services correspond to the Commission's descriptions of the services for which an issuer must disclose fees paid to its auditor. Compare the descriptions of services in Item 9(e) of Commission Schedule 14A (17 C.F.R. § 240.14a-101) under the headings "Audit Fees," "Audit-Related Fees," "Tax Fees," and "All Other Fees" with, respectively, the Board's definitions of Audit Services, Other Accounting Services, Tax Services, and Non-Audit Services.

PART IV – AUDIT CLIENTS AND AUDIT REPORTS

Item 4.1 Audit Reports Issued by the Firm

a. Provide the following information concerning each issuer for which the Firm issued any audit report(s) during the reporting period –

1. The issuer's name;
2. The issuer's CIK number, if any; and
3. The date(s) of the audit report(s).

b. If the Firm identified any issuers in response to Item 4.1.a., indicate, by checking the box corresponding to the appropriate range set out below, the total number of Firm personnel who exercised the authority to sign the Firm's name to an audit report during the reporting period. If the Firm checks the box indicating that the number is in the range of 1-9, provide the exact number.

1-9

10-25

26-50

51-100

101-200

More than 200

Note: In responding to Item 4.1, careful attention should be paid to the definition of audit report, which is found in Rule 1001(a)(vi) of the Board's Rules, and which does not encompass reports prepared for entities that are not issuers, as that term is defined in Rule 1001(i)(iii). Careful attention should also be paid to the definition of issuer. The Firm should not, for example, overlook the fact that investment companies may be issuers, or that employee benefit plans that file reports on Commission Form 11-K are issuers.

Note: In responding to Item 4.1, do not list any issuer more than once. For each issuer, provide in Item 4.1.a.3 the audit report dates (as described in AU 530, Dating of the Independent Auditor's Report) of all such audit reports for that issuer, including each date of any dual-dated audit report.

Note: In responding to Item 4.1.a.3, it is not necessary to provide the date of any consent to an issuer's use of an audit report previously issued for that issuer, except that, if such consents constitute the only instances of the Firm issuing audit reports for a particular issuer during the reporting period, the Firm should include that issuer in Item 4.1 and include the dates of such consents in Item 4.1.a.3.

Item 4.2 Audit Reports With Respect to Which the Firm Played a Substantial Role during the Reporting Period

a. If no issuers are identified in response to Item 4.1.a, but the Firm played a substantial role in the preparation or furnishing of an audit report that was issued during the reporting period, provide the following information concerning each issuer with respect to which the Firm did so –

1. The issuer's name;

2. The issuer's CIK number, if any;

3. The name of the registered public accounting firm that issued the audit report(s);

4. The end date(s) of the fiscal period(s) covered by the financial statements that were the subject of the audit report(s); and

5. A description of the substantial role played by the Firm with respect to the audit report(s).

Note: If the Firm identifies any issuer in response to Item 4.1, the Firm need not respond to Item 4.2.

Note: In responding to Item 4.2, do not list any issuer more than once.

PART V – OFFICES AND AFFILIATIONS

In Part V, the Firm should provide information that is current as of the last day of the reporting period.

Item 5.1 Firm's Offices

List the physical address and, if different, the mailing address, of each of the Firm's offices.

Item 5.2 Audit-related Memberships, Affiliations, or Similar Arrangements

a. State whether the Firm has any:

1. Membership or affiliation in or with any network, arrangement, alliance, partnership or association that licenses or authorizes audit procedures or manuals or related materials, or the use of a name in connection with the provision of audit services or accounting services;

2. Membership or affiliation in or with any network, arrangement, alliance, partnership or association that markets or sells audit services or through which joint audits are conducted; or

3. Arrangement, whether by contract or otherwise, with another entity through or from which the Firm employs or leases personnel to perform audit services.

b. If the Firm provides an affirmative response to Item 5.2.a, identify, by name and address, the entity with which the Firm has each such relationship, and provide a brief description of each such relationship.

Note: Item 5.2.b does not require information concerning every other entity that is part of the network, arrangement, alliance, partnership or association, but only information concerning the network, arrangement, alliance, partnership or association itself, or the principal entity through which it operates.

PART VI – PERSONNEL

In Part VI, the Firm should provide information that is current as of the last day of the reporting period.

Item 6.1 Number of Firm Personnel

Provide the following numerical totals –

a. Total number of the Firm's accountants;

b. Total number of the Firm's certified public accountants (include in this number all accountants employed by the Firm with comparable licenses from non-U.S. jurisdictions); and

c. Total number of the Firm's personnel.

PART VII – CERTAIN RELATIONSHIPS

Item 7.1 Individuals with Certain Disciplinary or Other Histories

a. Other than a relationship required to be reported in Item 4.1 of Form 3, and only if the Firm has not previously identified the individual and the sanction or Commission order on Form 1, Form 2, or Form 3, state whether, as of the end of the reporting period, the Firm has any employee, partner, shareholder, principal, member, or owner who was the subject of a Board disciplinary sanction or a Commission order under Rule 102(e) of the Commission's Rules of Practice, entered within the five years preceding the end of the reporting period and without that sanction or order having been vacated on review or appeal, and who provided at least ten hours of audit services for any issuer during the reporting period.

b. If the Firm provides an affirmative response to Item 7.1.a, provide –

1. The name of each such individual;

2. A description of the nature of the relationship;

3. The date that the Firm entered into the relationship; and

4. The date of the relevant order and an indication whether it was a Board order or a Commission order.

Item 7.2 Entities with Certain Disciplinary or Other Histories

a. Other than a relationship required to be reported in Item 4.2 of Form 3, and only if the Firm has not previously reported the information on Form 1, Form 2, or Form 3, state whether, as of the end of the reporting period, the Firm was owned or partly owned by an entity that was the subject of (a) a Board disciplinary sanction entered within the five years preceding the end of the reporting period, which has not been vacated on review or appeal, suspending or revoking that entity's registration or disapproving that entity's application for registration, or (b) a Commission order under Rule 102(e) of the Commission's Rules of Practice entered within the five years preceding the end of the reporting period, which has not been vacated on appeal, suspending or denying the privilege of appearing or practicing before the Commission.

b. If the Firm provides an affirmative response to Item 7.2.a, provide –

1. The name of each such entity;

2. A description of the nature of the relationship;

3. The date that the Firm entered into the relationship; and

4. The date of the relevant order and an indication whether it was a Board order or a Commission order.

Item 7.3 Certain Arrangements to Receive Consulting or Other Professional Services

a. Other than a relationship required to be reported in Item 4.3 of Form 3, state whether the Firm received, or entered into a contractual or other arrangement to receive, from any individual or entity meeting the criteria described in Items 7.1.a. or 7.2.a, consulting or other professional services related to the Firm's audit practice or related to services the Firm provides to issuer audit clients.

b. If the Firm provides an affirmative response to Item 7.3.a, provide –

1. The name of each such individual or entity;
2. A description of the nature of the relationship;
3. The date that the Firm entered into the relationship;
4. A description of the services provided or to be provided to the Firm by the individual or entity; and
5. The date of the relevant order and an indication whether it was a Board order or a Commission order.

PART VIII – ACQUISITION OF ANOTHER PUBLIC ACCOUNTING FIRM OR SUBSTANTIAL PORTIONS OF ANOTHER PUBLIC ACCOUNTING FIRM'S PERSONNEL

If the Firm became registered on or after [effective date of Rule 2201], the first annual report that the Firm files must provide this information for the period running from the date used by the Firm for purposes of General Instruction 9 of

Form 1 (regardless of whether that date was before or after the beginning of the reporting period) through March 31 of the year in which the annual report is required to be filed.

Item 8.1 Acquisition of Another Public Accounting Firm or Substantial Portions of Another Public Accounting Firm's Personnel

a. State whether the Firm acquired another public accounting firm.

b. If the Firm provides an affirmative response to Item 8.1.a, provide the name(s) of the public accounting firm(s) that the Firm acquired.

c. State whether the Firm, without acquiring another public accounting firm, took on as employees, partners, shareholders, principals, members, or owners 75% or more of the persons who, as of the beginning of the reporting period, were the partners, shareholders, principals, members, or owners of another public accounting firm.

d. If the Firm provides an affirmative response to Item 8.1.c, provide the name of the other public accounting firm and the number of the other public accounting firm's former partners, shareholders, principals, members, owners, and accountants that joined the Firm.

PART IX – AFFIRMATION OF CONSENT

Item 9.1 Affirmation of Understanding of, and Compliance with, Consent Requirements

Whether or not the Firm, in applying for registration with the Board, provided the signed statement required by Item 8.1 of Form 1, affirm that –

a. The Firm has consented to cooperate in and comply with any request for testimony or the production of documents made by the Board in furtherance of its authority and responsibilities under the Sarbanes-Oxley Act of 2002;

b. The Firm has secured from each of its associated persons, and agrees to enforce as a condition of each such person's continued employment by or other association with the Firm, a consent indicating that the associated person consents to cooperate in and comply with any request for testimony or the production of documents made by the Board in furtherance of its authority under the Sarbanes-Oxley Act of 2002, and that the associated person understands and agrees that such consent is a condition of his or her continued employment by or other association with the Firm; and

c. The Firm understands and agrees that cooperation and compliance, as described in Item 9.1.a, and the securing and enforcing of consents from its associated persons as described in Item 9.1.b, is a condition to the continuing effectiveness of the registration of the Firm with the Board.

Note 1: The affirmation in Item 9.1.b shall not be understood to include an affirmation that the Firm has secured such consents from any associated person that is a registered public accounting firm.

Note 2: The affirmation in Item 9.1.b shall not be understood to include an affirmation that the Firm has secured such consents from any associated person that is a foreign public accounting firm in circumstances where that associated person asserts that non-U.S. law prohibits it from providing the consent, so long as the Firm possesses in its files documents relating to the associated person's assertion about non-U.S. law that would be sufficient to satisfy the requirements of subparagraphs (2) through (4) of Rule 2207(c) if that associated person were a registered public accounting firm filing a Form 2 and withholding this affirmation. This exception to the affirmation in Item 9.1.b does not relieve the Firm of its obligation to enforce cooperation and compliance with Board demands by any such associated person as a condition of continued association with the Firm.

Note 3: If the Firm is a foreign registered public accounting firm, the affirmations in Item 9.1 that relate to associated persons shall be understood to encompass every accountant who is a proprietor, partner, principal, shareholder, officer, or audit manager of the Firm and who provided at least ten hours of audit services for any issuer during the reporting period.

PART X – CERTIFICATION OF THE FIRM

Item 10.1 Signature of Partner or Authorized Officer

This Form must be signed on behalf of the Firm by an authorized partner or officer of the Firm including, in accordance with Rule 2204, both a signature that appears in typed form within the electronic submission and a corresponding manual signature retained by the Firm. The signer must certify that –

a. the signer is authorized to sign this Form on behalf of the Firm;

b. the signer has reviewed this Form;

c. based on the signer's knowledge, the Firm has filed a special report on Form 3 with respect to each event that occurred before the end of the reporting period and for which a special report on Form 3 is required under the Board's rules;

d. based on the signer's knowledge, this Form does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading; and

e. either –

1. based on the signer's knowledge, the Firm has not failed to include in this Form any information or affirmation that is required by the instructions to this Form, or

2. based on the signer's knowledge –

(A) the Firm is a foreign registered public accounting firm and has not failed to include in this Form any information or affirmation that is required by the instructions to this Form except for information or affirmations that the Firm asserts it cannot provide to the Board on this Form 2 without violating non-U.S. law;

(B) with respect to any such withheld information or affirmation, the Firm has satisfied the requirements of PCAOB Rule 2207(b) and has in its possession the materials required by PCAOB Rule 2207(c); and

(C) the Firm has indicated, in accordance with the instructions to this Form, each Item of this Form with respect to which the Firm has withheld any required information or affirmation.

The signature must be accompanied by the signer's title, the capacity in which the signer signed the Form, the date of signature, and the signer's business mailing address, business telephone number, business facsimile number, and business e-mail address.

PART XI – EXHIBITS

To the extent applicable under the foregoing instructions or the Board's rules, each annual report must be accompanied by the following exhibits:

Exhibit 3.2 Description of Methodology Used to Estimate Components of Calculation in Item 3.2 and Reasons for Using Estimates

Exhibit 99.1 Request for Confidential Treatment

Exhibit 99.3 Materials Required by Rule 2207(c)(2)–(4) – Submit Only as an Exhibit to an Amended Form 2 in Response to a Request Made Pursuant to Rule 2207(d)

FORM 3 – SPECIAL REPORT FORM

GENERAL INSTRUCTIONS

1. Submission of this Report. Effective [effective date of Rule 2203], a registered public accounting firm must use this Form to file special reports with the Board pursuant to Section 102(d) of the Act and Rule 2203 and to file any amendments

to a special report. Unless otherwise directed by the Board, the Firm must file this Form, and all exhibits to this Form, electronically with the Board through the Board's Web-based system.

2. Defined Terms. The definitions in the Board's rules apply to this Form. Italicized terms in the instructions to this Form are defined in the Board's rules. In addition, as used in the instructions to this Form, the term "the Firm" means the registered public accounting firm that is filing this Form with the Board.

3. When this Report is Required and When It is Considered Filed. Upon the occurrence of any event specified in Part II of this Form, the Firm must report the event on this Form by following the instructions to this Form. With respect to events that occur on or after [effective date of Rule 2203] and while the Firm is registered, the Firm must file the Form no later than thirty days after the occurrence of the event reported. Certain additional requirements apply, but they vary depending on whether a firm was registered as of [effective date of Rule 2203]. A firm that becomes registered after [effective date of Rule 2203], must, within thirty days of receiving notice of Board approval of its registration application, file this Form to report any reportable events that occurred in a specified period before approval of the firm's application for registration. See Rule 2203(a)(2). A firm that was registered as of [effective date of Rule 2203], must, by [date 30 days after effective date of Rule 2203], file this Form to report certain additional information that is current as of [effective date of Rule 2203].

See Rule 2203(a)(3) and General Instruction No. 4 below. A special report shall be deemed to be filed on the date that the Firm submits a Form 3 in accordance with Rule 2203 that includes the signed certification required in Part VIII of Form 3.

4. Required Filing to Bring Current Certain Information for Firms Registered as of [effective date of Rule 2203]. If the Firm is registered as of [effective date of Rule 2203], the Firm must file a special report on this Form no later than [date 30 days after effective date of Rule 2203], to report the information specified below, to the extent that it has not been reported on the Firm's Form 1 filing. The Firm must make this Form 3 filing to report the following information even if the Firm has previously informally disclosed the information to the Board or its staff–

a. Information responsive to Items 2.4 through 2.9 and Item 4.1 if (1) the proceeding is pending as of [effective date of Rule 2203], and (2) the defendants or respondents as of that date include either the Firm or a person who is a partner, shareholder, principal, owner, member, or audit manager of the Firm as of that date;

b. Information responsive to Items 2.10 and 4.2 if (1) the conclusion of a proceeding as to any party specified there occurred after the date used by the firm for purposes of General Instruction 9 to Form 1 and before [effective date of Rule 2203], and (2) the proceeding resulted in any conviction of, judgment against, imposition of any liability or sanction on, or Commission Rule 102(e) order against the Firm or any person who is a partner, shareholder, principal, owner, member, or audit manager of the Firm as of [effective date of Rule 2203];

c. Information responsive to Items 2.11 and 4.3 if the Firm is the subject of a petition or proceeding described there as of [effective date of Rule 2203];

d. Information responsive to Items 2.12 through 2.14 and Part V if (1) the relationship commenced after the date used by the firm for purposes of General Instruction 9 to Form 1, (2) the specified disciplinary sanction or Commission Rule 102(e) order continued to be in effect as of [effective date of Rule 2203], and (3) the specified relationship continues to exist as of [effective date of Rule 2203];

e. Information responsive to Items 2.15 and 6.1 if (1) the loss of authorization relates to a jurisdiction or authority identified in Item 1.7 of the Firm's Form 1 and, (2) as of [effective date of Rule 2203], the Firm continues to lack the specified authorization in that jurisdiction;

f. Information responsive to Items 2.16 and 6.2 if the license or certification is in effect as of [effective date of Rule 2203]; and

g. Information responsive to Items 2.17 and 2.18 and Part VII that is current as of [effective date of Rule 2203] to the extent that it differs from the corresponding information provided on the Firm's Form 1.

5. Completing the Form. A firm filing this Form must always complete Parts I, II, and VIII of this Form. Parts III through VII should be completed to the extent applicable, as described more fully in the instructions to Part II of the Form.

6. Amendments to this Report. Amendments shall not be filed to update information in a filed Form 3 that was correct at the time the Form was filed, but only to correct information that was incorrect at the time the Form was filed or to provide information that was omitted from the Form and was required to be provided at the time the Form was filed. When filing a Form 3 to amend an earlier filed Form 3, the Firm must supply not only the corrected or supplemental information, but must include in the amended Form 3 all information, affirmations, and certifications that were required to be included in the original Form 3. The Firm may access the originally filed Form 3 through the Board's Web-based system and make the appropriate amendments without needing to re-enter all other information.

Note: The Board will designate an amendment to a special report as a report on "Form 3/A."

7. <u>Rules</u> Governing this Report. In addition to these instructions, the <u>rules</u> contained in Part 2 of Section 2 of the <u>Board's rules</u> govern this Form. Please read these <u>rules</u> and the instructions carefully before completing this Form.

8. Requests for Confidential Treatment. The Firm may, by marking the Form in accordance with the instructions provided, request confidential treatment of any information submitted in Item 3.1.c, Part IV, Part V, Item 6.1.d, Item 7.1.d, or Exhibit 99.3 of this Form that has not otherwise been publicly disclosed and that either contains information reasonably identified by the Firm as proprietary information or that is protected from public disclosure by applicable laws related to confidentiality of proprietary, personal, or other information. See Rule 2300. If the Firm requests confidential treatment, it must identify the information in Item 3.1.c, Part IV, Part V, Item 6.1.d, Item 7.1.d, or Exhibit 99.3 that it desires to keep confidential, and include, as Exhibit 99.1 to this Form, an exhibit that complies with the requirements of Rule 2300(c)(2). The <u>Board</u> will determine whether to grant confidential treatment requests on a case-by-case basis. If the Firm fails to include Exhibit 99.1, or includes an Exhibit 99.1 that fails to comply with Rule 2300(c)(2), the request for confidential treatment may be denied solely on the basis of that failure.

9. Assertions of Conflicts with Non-U.S. Law. If the Firm is a <u>foreign registered public accounting firm</u>, the Firm may, unless otherwise directed by the <u>Board</u> pursuant to Rule 2207(e), decline to provide certain information required by this

Form if the Firm could not provide such information without violating non-U.S. law and the Firm proceeds in accordance with Rule 2207. The Firm may withhold responsive information on that basis from any Part of the Form other than Parts I, II, and VIII, and Items 7.1.a, 7.1.b, 7.1.c, and 7.2. If the firm withholds responsive information, the Firm must indicate, in accordance with the instructions in the relevant Part of the Form, the particular Items with respect to which the Firm has withheld responsive information. The Firm may not use the Form to make any general assertion that a particular requirement may conflict with non-U.S. law, but only to indicate that, on the basis of an asserted conflict, the Firm has in fact withheld from this Form required information.

10. Language. Information submitted as part of this Form, including any exhibit to this Form, must be in the English language.

PART I – IDENTITY OF THE FIRM

Item 1.1 Name of Firm

a. State the legal name of the Firm.

Note: If the Firm is filing this Form 3 to report that the Firm's legal name has changed, the name entered in Item 1.1.a should be the Firm's legal name before the name change that is being reported. The Firm's new name should be included in the response to Item 1.1.c.

b. If different than its legal name, state the name or names under which the Firm issues audit reports.

c. If the Firm is filing this Form 3 to report that the Firm's legal name has changed, state the new legal name of the Firm.

PART II – REASON FOR FILING THIS REPORT

Indicate, by checking the relevant box(es) from among Items 2.1 through 2.18 below, the event(s) being reported on this Form. More than one event may be reported in the same Form 3 filing. For each event indicated below, proceed to the Parts and Items of this Form indicated parenthetically for the specific event being reported and provide the information therein described. Provide responses only to those Parts and Items of the Form specifically indicated for the event or events that the Firm identifies in this Part II as an event being reported on this Form. (For example, if the Form is being filed solely to report that the Firm has changed its name, check the box for Item 2.17 in this Part of the Form, and complete only Item 7.1 and Part VIII of the Form.) If the Firm is filing this Form to amend a previous filing, the Firm also should complete Item 2.19.

Note: In Items 2.4 through 2.11 and Item 2.15, the reportable event is described in terms of whether the Firm "has become aware" of certain facts. For these purposes, the Firm is deemed to have become aware of the relevant facts on the date that any partner, shareholder, principal, owner, or member of the Firm first becomes aware of the facts.

Audit Reports

Item 2.1 The Firm has withdrawn an audit report on financial statements, or withdrawn its consent to the use of its name in a report, document, or written communication containing an issuer's financial statements, and the issuer has failed to comply with a Commission requirement to make a report concerning the matter pursuant to Item 4.02 of Commission Form 8-K. (Complete Item 3.1 and Part VIII.)

Item 2.2 The Firm has issued audit reports with respect to more than 100 issuers in a calendar year immediately following a calendar year in which the Firm did not issue audit reports with respect to more than 100 issuers. (Complete Part VIII.)

Item 2.3 The Firm has issued audit reports with respect to 100 or fewer issuers in a completed calendar year immediately following a calendar year in which the Firm issued audit reports with respect to more than 100 issuers. (Complete Part VIII.)

Certain Legal Proceedings

Item 2.4 The Firm has become aware that the Firm has become a defendant in a criminal proceeding prosecuted by a governmental criminal law enforcement authority. (Complete Item 4.1 and Part VIII.)

Item 2.5 The Firm has become aware that, in a matter arising out of his or her conduct in the course of providing audit services or other accounting services to an issuer, a partner, shareholder, principal, owner, member, or audit manager of the Firm has become a defendant in a criminal proceeding prosecuted by a governmental criminal law enforcement authority. (Complete Item 4.1 and Part VIII.)

Item 2.6 The Firm has become aware that a partner, shareholder, principal, owner, member, or audit manager of the Firm who provided at least ten hours of audit services for any issuer during the Firm's current fiscal year or its most recently completed fiscal year has become a defendant in a criminal proceeding prosecuted by a governmental criminal law enforcement authority and is charged with fraud, embezzlement, forgery, extortion, bribery, obstruction of justice, perjury, or false statements; or charged with any crime arising out of alleged conduct relating to accounting, auditing, securities, banking, commodities, taxation, consumer protection, or insurance. (Complete Item 4.1 and Part VIII.)

Item 2.7 The Firm has become aware that, in a matter arising out of the Firm's conduct in the course of providing professional services for a client, the Firm has become a defendant or respondent in a civil or alternative dispute resolution proceeding initiated by a governmental entity or in an administrative or disciplinary proceeding other than a Board disciplinary proceeding. (Complete Item 4.1 and Part VIII.)

Item 2.8 The Firm has become aware that, in a matter arising out of his or her conduct in the course of providing audit services or other accounting services to an issuer, a partner, shareholder, principal, owner, member, or audit manager of the Firm has become a defendant or respondent in a civil or alternative dispute resolution proceeding initiated by a governmental entity or in an administrative or disciplinary proceeding other than a Board disciplinary proceeding. (Complete Item 4.1 and Part VIII.)

Item 2.9 The Firm has become aware that, in a matter arising out of his or her conduct in the course of providing professional services for a client, a partner, shareholder, principal, owner, member, or audit manager of the Firm who provided at least ten hours of audit services for any issuer during the Firm's current fiscal year or its most recently completed fiscal year has become a defendant or respondent in a civil or alternative dispute resolution proceeding initiated by a governmental entity or in an administrative or disciplinary proceeding other than a Board disciplinary proceeding. (Complete Item 4.1 and Part VIII.)

Item 2.10 The Firm has become aware that a proceeding meeting the criteria described in Items 2.4, 2.5, 2.6, 2.7, 2.8, or 2.9 above has been concluded as to the Firm or a partner, shareholder, principal, owner, member, or audit manager of the Firm (whether by dismissal, acceptance of pleas, through consents or settlement agreements, the entry of a final judgment, or otherwise). (Complete Item 4.2 and Part VIII.)

Item 2.11 The Firm has become aware that the Firm, or the parent or a subsidiary of the Firm, has become the subject of a petition filed in a bankruptcy court, or has otherwise become the subject of a proceeding in which a court or governmental agency (or, in a non-U.S. jurisdiction, a person or entity performing a comparable function) has assumed jurisdiction over substantially all of the assets or business of the Firm or its parent or a subsidiary. (Complete Item 4.3 and Part VIII.)

Certain Relationships

Item 2.12 The Firm has taken on as an employee, partner, shareholder, principal, or member, or has otherwise become owned or partly owned by, a person who is currently the subject of (a) a Board disciplinary sanction suspending or barring the person from being an associated person of a registered public accounting firm or (b) a Commission order under Rule 102(e) of the Commission's Rules of Practice suspending or denying the privilege of appearing or practicing before the Commission. (Complete Item 5.1 and Part VIII.)

Item 2.13 The Firm has become owned or partly owned by an entity that is currently the subject of (a) a Board disciplinary sanction suspending or revoking that entity's registration or disapproving that entity's application for registration, or (b) a Commission order under Rule 102(e) of the Commission's Rules of Practice suspending or denying the privilege of appearing or practicing before the Commission. (Complete Item 5.2 and Part VIII.)

Item 2.14 The Firm has entered into a contractual or other arrangement to receive consulting or other professional services from a person or entity meeting any of the criteria described in Items 2.12 or 2.13 above. (Complete Item 5.3 and Part VIII.)

Licenses and Certifications

Item 2.15 The Firm has become aware that its authorization to engage in the business of auditing or accounting in a particular jurisdiction has ceased to be effective or has become subject to conditions or contingencies other than conditions or contingencies imposed on all firms engaged in the business of auditing or accounting in the jurisdiction. (Complete Item 6.1 and Part VIII.)

Item 2.16 The Firm has obtained a license or certification authorizing the Firm to engage in the business of auditing or accounting and which has not been identified on any Form 1 or Form 3 previously filed by the Firm, or there has been a change in a license or certification number identified on a Form 1 or Form 3 previously filed by the Firm. (Complete Item 6.2 and Part VIII.)

Changes in the Firm or the Firm's <u>Board</u> Contact Person

Item 2.17 The Firm has changed its legal name while otherwise remaining the same legal entity that it was before the name change. (Complete Item 7.1 and Part VIII.)

Item 2.18 There has been a change in the business mailing address, business telephone number, business facsimile number, or business e-mail of the person most recently designated by the Firm (on Form 2, Form 3, or Form 4) as the Firm's primary contact with the <u>Board</u>, or the Firm is designating a new person to serve as the primary contact. (Complete Item 7.2 and Part VIII.)

Amendment

Item 2.19 Amendments

If this is an amendment to a report previously filed with the Board –

a. Indicate, by checking the box corresponding to this item, that this is an amendment.

b. Identify the specific Item numbers of this Form (other than this Item 2.19) as to which the Firm's response has changed from that provided in the most recent Form 3 or amended Form 3 filed by the Firm with respect to the events reported on this Form.

PART III – WITHDRAWN AUDIT REPORTS

Item 3.1 Withdrawn audit reports and consents

If the Firm has withdrawn an audit report on financial statements, or withdrawn its consent to the use of its name in a report, document, or written communication containing an issuer's financial statements, and the issuer has failed to comply with a Commission requirement to make a report concerning the matter pursuant to Item 4.02 of Commission Form 8-K, provide –

a. The issuer's name and CIK number, if any;

b. The date(s) of the audit report(s) that the Firm has withdrawn, or to which the Firm's withdrawal of consent relates; and

c. A description of the reason(s) the Firm has withdrawn the audit report(s) or the consent.

> Note: The 30-day period in which the Firm must report the event does not begin to run unless and until the issuer fails to report on Form 8-K within the time required by the Commission's rules. The Firm must then report the event on Form 3 within 30 days of the expiration of the required Form 8-K filing deadline, unless, within that 30-day period, the issuer reports on a late-filed Form 8-K.

PART IV – CERTAIN PROCEEDINGS

Item 4.1 Criminal, Governmental, Administrative, or Disciplinary Proceedings

If the Firm has indicated in this Form 3 that any of the events described in Items 2.4, 2.5, 2.6, 2.7, 2.8 or 2.9 has occurred, provide the following information with respect to each such event –

a. The name, filing date, and case or docket number of the proceeding, and the nature of the proceeding, i.e., whether it is a criminal proceeding, a civil or alternative dispute resolution proceeding, or an administrative or disciplinary proceeding.

b. The name of the court, tribunal, or body in or before which the proceeding was filed.

c. An indication whether the Firm itself is a defendant or respondent in the proceeding and, if so, the statutes, rules, or legal duties that the firm is alleged to have violated, and a brief description of the firm's alleged conduct in violation of those statutes, rules, or legal duties.

d. The names of every defendant or respondent who is a partner, shareholder, principal, owner, member, or audit manager of the Firm, or who was such either at the time the Firm received notice of the proceeding or at the time of the alleged conduct on which any claim or charge is based, and who provided at least ten hours of audit services for any issuer during the Firm's current fiscal year or its most recent fiscal year; and, as to each such defendant or respondent, the statutes, rules, or legal duties that he or she is alleged to have violated, and a brief description of his or her alleged conduct in violation of those statutes, rules, or legal duties.

e. The name of any client that was the recipient of the professional services to which any claim or charge in the proceeding relates.

Note: For the purpose of this Part, administrative or disciplinary proceedings include those of the Commission; any other federal, state, or non-U.S. agency, board, or administrative or licensing authority; and any professional association or body.

Investigations that have not resulted in the commencement of a proceeding need not be included.

Item 4.2 Concluded Criminal, Governmental, Administrative, or Disciplinary Proceedings

If any proceeding meeting the criteria described in Items 2.4, 2.5, 2.6, 2.7, 2.8 or 2.9, including any proceeding reported in Item 4.1, has been concluded as to the Firm or a partner, shareholder, principal, owner, member, or audit manager of the Firm (whether by dismissal, acceptance of pleas, through consents or settlement agreements, the entry of a final judgment, or otherwise), provide –

a. The name, filing date, and case or docket number of the proceeding, and the nature of the proceeding, i.e., whether it is a criminal proceeding, a civil or alternative dispute resolution proceeding, or an administrative or disciplinary proceeding;

b. The name of the court, tribunal, or body in or before which the proceeding was filed; and

c. A brief description of the terms of the conclusion of the proceeding as to the Firm or partner, shareholder, principal, owner, member, or audit manager.

Item 4.3 Bankruptcy or Receivership

If the Firm, or the parent or a subsidiary thereof, has become the subject of a petition filed in a bankruptcy court, or has otherwise become the subject of a proceeding in which a court or governmental agency (or, in a non-U.S. jurisdiction, a person or entity performing a comparable function) has assumed jurisdiction over substantially all of the assets or business of the Firm or its parent or a subsidiary, provide –

a. the name of the proceeding;

b. the name of the court or governmental body;

c. the date of the filing or of the assumption of jurisdiction; and

d. the identity of the receiver, fiscal agent or similar officer, if applicable, and the date of his or her appointment.

PART V – CERTAIN RELATIONSHIPS

Item 5.1 New Relationship with Person Subject to Bar or Suspension

If the Firm has taken on as an employee, partner, shareholder, principal, or member, or has otherwise become owned or partly owned by, a person who is currently the subject of (a) a Board disciplinary sanction suspending or barring the person from being an associated person of a registered public accounting firm or (b) a Commission order under Rule 102(e) of the Commission's Rules of Practice suspending or denying the privilege of appearing or practicing before the Commission, provide –

a. the name of the person;

b. the nature of the person's relationship with the Firm; and

c. the date on which the person's relationship with the Firm began.

Item 5.2 New Ownership Interest by Firm Subject to Bar or Suspension

If the Firm has become owned or partly owned by an entity that is currently the subject of (a) a Board disciplinary sanction suspending or revoking that entity's registration or disapproving that entity's application for registration, or (b) a Commission order under Rule 102(e) of the Commission's Rules of Practice suspending or denying the privilege of appearing or practicing before the Commission, provide –

a. the name of the entity that has obtained an ownership interest in the Firm;

b. the nature and extent of the ownership interest; and

c. the date on which the ownership interest was obtained.

Item 5.3 Certain Arrangements to Receive Consulting or Other Professional Services

If the Firm has entered into a contractual or other arrangement to receive consulting or other professional services from a person or entity meeting any of the criteria described in Items 2.12 or 2.13 above, provide –

a. the name of the person or entity;

b. the date that the Firm entered into the contract or other arrangement; and

c. a description of the services to be provided to the Firm by the person or entity.

PART VI – LICENSES AND CERTIFICATIONS

Item 6.1 Loss of, or Limitations Imposed on, Authorization to Engage in the Business of Auditing or Accounting

If the Firm's authorization to engage in the business of auditing or accounting in a particular jurisdiction has ceased to be effective or has become subject to conditions or contingencies other than conditions or contingencies imposed on all firms engaged in the business of auditing or accounting in the jurisdiction, provide –

a. the name of the state, agency, board or other authority that had issued the license or certification related to such authorization;

b. the number of the license or certification;

c. the date that the authorization ceased to be effective or became subject to conditions or contingencies, and

d. a brief description of the reason(s) for such action, including a description of the conditions or contingencies, if any.

Item 6.2 New License or Certification

If the Firm has obtained any license or certification authorizing the Firm to engage in the business of auditing or accounting, and which has not been identified on any Form 1 or Form 3 previously filed by the Firm, or there has been a change in any license or certification number identified on a Form 1 or Form 3 previously filed by the Firm, provide –

a. the name of the issuing state, agency, board or other authority;

b. the number of the license or certification;

c. the date the license or certification took effect; and

d. if the license or certification replaces another license or certification issued by the same authority, the number of the replaced license or certification.

Note: If the Firm is filing a Form 4 to report a change in its form of organization, change in jurisdiction, or a business combination, the Firm should report on Form 4, rather than Form 3, any related license change that takes effect before the submission of the Form 4.

PART VII – CHANGES IN THE FIRM OR THE FIRM'S BOARD CONTACT PERSON

Item 7.1 Change in Name of Firm

If the Firm is reporting a change in its legal name –

a. State the new legal name of the Firm;

b. State the legal name of the Firm immediately preceding the new legal name;

c. State the effective date of the name change;

d. Provide a brief description of the reason(s) for the change; and

e. Affirm, by checking the box corresponding to this Item, that, other than the name change, the Firm is the same legal entity that it was before the name change.

Note: If, other than the name change, the Firm is not the same legal entity that it was before the name change, whether because of a change in the Firm's legal form of organization or because of other transactions, the registration status of the predecessor firm does not automatically attach to the Firm, and the Firm cannot report the event as a name change. If the Firm cannot make the affirmation required by Item 7.1.e, the Firm cannot execute the certification in Part VIII as to Item 7.1, and this Form cannot be deemed filed under Rule 2206.

In that event, the Firm should consider whether, pursuant to the provisions of Rule 2108, the Firm can make the representations required in a Form 4 filing to enable the predecessor firm's registration to attach to the Firm. If the Firm cannot or does not file with the Board a Form 4 making all necessary representations, the predecessor firm's registration does not attach to the Firm. In those circumstances, the Firm may not lawfully prepare or issue an audit report without first filing an application for registration on Form 1 and having that application approved by the Board.

Note: If the Firm is filing a Form 4 to report a change in its form of organization, change in jurisdiction, or a business combination, the Firm should report any related name change on Form 4 and not on Form 3.

Item 7.2 Change in Contact Information

If there has been a change in the business mailing address, business telephone number, business facsimile number, or business e-mail address of the person most recently designated by the Firm (on Form 2, Form 3, or Form 4) as the Firm's primary contact with the Board, or if the Firm is designating a new person to serve as the primary contact, provide the name and current business mailing address, business telephone number, business facsimile number, and business e-mail of the partner or authorized officer of the Firm who will serve as the Firm's primary contact with the Board.

PART VIII – CERTIFICATION OF THE FIRM

Item 8.1 Signature of Partner or Authorized Officer

This Form must be signed on behalf of the Firm by an authorized partner or officer of the Firm including, in accordance with Rule 2204, both a signature that appears in typed form within the electronic submission and a corresponding manual signature retained by the Firm. The signer must certify that –

a. the signer is authorized to sign this Form on behalf of the Firm;

b. the signer has reviewed this Form;

c. based on the signer's knowledge, this Form does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading; and

d. either –

1. based on the signer's knowledge, the Firm has not failed to include in this Form any information or affirmation that is required by the instructions to this Form, with respect to the event or events being reported on this Form, or

2. based on the signer's knowledge –

   (A) the Firm is a foreign registered public accounting firm and has not failed to include in this Form any information or affirmation that is required by the instructions to this Form, with respect to the event or events being reported on this Form, except for information or affirmations that the Firm asserts it cannot provide to the Board on this Form 3 without violating non-U.S. law;

   (B) with respect to any such withheld information or affirmation, the Firm has made the efforts required by PCAOB Rule 2207(b) and has in its possession the materials required by PCAOB Rule 2207(c); and

(C) the Firm has indicated, in accordance with the instructions to this Form, each Item of this Form with respect to which the Firm has withheld any required information.

The signature must be accompanied by the signer's title, the capacity in which the signer signed the Form, the date of signature, and the signer's business mailing address, business telephone number, business facsimile number, and business e-mail address.

PART IX – EXHIBITS

To the extent applicable under the foregoing instructions, each special report must be accompanied by the following exhibits:

Exhibit 99.1 Request for Confidential Treatment

Exhibit 99.3 Materials Required by Rule 2207(c)(2)-(4) – <u>Submit Only as an Exhibit to an Amended Form 3 in Response to a Request Made Pursuant to Rule 2207(d)</u>

In addition to the above rules and form instructions, the Board has adopted related amendments to PCAOB Rules 1001, 2107, 2300, 4000, and 4003. The amendments are shown below, with new language italicized, deleted language in brackets, and unchanged language indicated by a series of three asterisks.

SECTION 1. GENERAL PROVISIONS

Rule 1001. Definitions of Terms Employed in Rules

When used in the Rules, unless the context otherwise requires:

* * *

(a)(vii) Audit Services

The term "audit services" means [–

(1) subject to paragraph (a)(vii)(2) of this Rule, professional services rendered for the audit of an issuer's annual financial statements, and (if applicable) for the reviews of an issuer's financial statements included in the issuer's quarterly reports.

(2) effective after December 15, 2003,] professional services rendered for the audit of an issuer's annual financial statements, and (if applicable) for the reviews of an issuer's financial statements

included in the issuer's quarterly reports or services that are normally provided by the accountant in connection with statutory and regulatory filings or engagements for those fiscal years.

* * *

(n)(ii) Non-Audit Services

The term "non-audit services" means [–

(1) subject to paragraph (n)(ii)(2) of this Rule, services related to financial information systems design and implementation as defined in Rule 2-01(c)(4)(ii) of Regulation S-X, 17 C.F.R. 2-01(c)(4)(ii), and all other services, other than audit services or other accounting services.

(2) effective after December 15, 2003,] all [other] services other than audit services, other accounting services, and tax services.

* * *

(o)(i) Other Accounting Services

The term "other accounting services" means [–

(1) subject to paragraph (o)(i)(2) of this Rule, services that are normally provided by the public accounting firm that audits the issuer's financial statements in connection with statutory and regulatory filings or engagements and assurance and related services that are reasonably related to the performance of the audit or review of the issuer's financial statements, other than audit services.

(2) effective after December 15, 2003,] assurance and related services that are reasonably related to the performance of the audit or review of the issuer's financial statements, other than audit services.

* * *

SECTION 2. REGISTRATION AND REPORTING

Part 1 – Registration of Public Accounting Firms

* * *

Rule 2107. Withdrawal from Registration

* * *

(c) Effect of Filing

[(1)] Beginning on the date of Board receipt of a completed Form 1-WD, [the firm that filed the Form 1-WD shall not engage in the preparation or issuance of, or play a substantial role in the preparation or furnishing of, an audit report, other than to issue a consent to the use of an audit report for a prior period, unless it first withdraws its Form 1-WD.

(2) Beginning on the fifth day following the Board's receipt of a completed Form 1-WD,] and continuing for as long as the Form 1-WD is pending –

[(i) the firm may satisfy the annual reporting requirement by submitting a report stating that a completed Form 1-WD has been filed and is pending;]

(1) the firm shall not engage in the preparation or issuance of, or play a substantial role in the preparation or furnishing of, an audit report, other than to issue a consent to the use of an audit report for a prior period;

(2[i]) the firm's obligation to file annual reports on Form 2, and special reports on Form 3 shall be suspended;

[(ii) any annual fee assessed shall be zero;]

(3[iii]) the Board shall have the discretion to forego any regular inspection that would otherwise commence pursuant to Rule 4003(a) or Rule 4003(b); and

(4[iv]) the firm's registration status shall be designated as "registered – withdrawal request pending," and the firm shall not publicly represent its registration status without specifying it as "registered – withdrawal request pending."

* * *

(f) Withdrawal of Form 1-WD

A registered public accounting firm that has submitted a Form 1-WD may withdraw the form at any time by filing with the Board a written notice of intent to withdraw the Form 1-WD along with any annual fee [and], annual report, and special report that the firm would have been required to submit during the period that the Form 1-WD was pending if not for the provisions of paragraph (c)(2).

Part 3 – Public Availability of Applications and Reports

Rule 2300. Public Availability of Information Submitted to the Board; Confidential Treatment Requests.

(a) Except as provided in paragraph (b) below –

(1) an application for registration will be publicly available as soon as practicable after the Board approves or disapproves such application; and

(2) all other forms filed pursuant to Part 1 or Part 2 of this Section of the Rules of the Board, and any amendments thereto, will be publicly available as soon as practicable after filing, except to the extent otherwise specified in the Board's rules or the instructions to the form.

(b) Confidential Treatment Requests.

(1) A public accounting firm may request confidential treatment of any information submitted to the Board in connection with its application for registration on Form 1, and may request confidential treatment of information on other forms filed pursuant to Part 1 or Part 2 of this Section of the Rules of the Board to the extent specified in the instructions to the form, provided that the information as to which confidential treatment is requested –

([1]i) has not otherwise been publicly disclosed, and

([2]ii) either (A[i]) contains information reasonably identified by the public accounting firm as proprietary information, or (B[ii]) is protected from public disclosure by applicable laws related to the confidentiality of proprietary, personal, or other information.

(2) Failure to provide an exhibit that complies with the requirements of paragraph (c)(2) of this Rule constitutes sufficient grounds for denial of any request for confidential treatment.

(c) Application Procedures.

To request confidential treatment of information for which such requests are permitted by paragraph (b)(1) of this Rule[submitted to the Board in connection with an application for registration], the [applicant] requestor must –

(1) identify, in accordance with the instructions [on Form 1] to the form, the information that it desires to keep confidential; and

(2) include as an exhibit to [Form 1 a detailed explanation as to why, based on the facts and circumstances of the particular case, the information meets the requirements of paragraph (b) of this Rule.]the form a representation that, to the requestor's knowledge, the information for which confidential treatment is requested has not otherwise been publicly disclosed and –

(i) a detailed explanation of the grounds on which the information is considered proprietary; or

(ii) a detailed explanation of the basis for asserting that the information is protected by law from public disclosure and a copy of the specific provision of law that the requestor claims protects the information from public disclosure.

* * *

(f) Unless the [applicant] requestor requests otherwise, the exhibit containing an explanation supporting a confidential treatment request will be afforded confidential treatment without the need for a request for confidential treatment.

(g) Information as to which the Board grants confidential treatment under this [r]Rule will not be made available to the public by the Board. The granting of confidential treatment will not, however, limit the ability of the Board (1) to provide the information as to which confidential treatment was granted to the Commission, or (2) to comply with any subpoena validly issued by a court or other body of competent jurisdiction. In the event the Board receives such a subpoena, the Board will notify the [applicant] public accounting firm of such subpoena, to the extent permitted by law, to allow the [applicant] public accounting firm the opportunity to object to such subpoena.

* * *

SECTION 4. INSPECTIONS

Rule 4000. General

(a) Every registered public accounting firm shall be subject to all such regular and special inspections as the Board may from time-to-time conduct in order to assess the degree of compliance of each registered public accounting firm and associated persons of that firm with the Act, the Board's rules, the rules of the Commission, and professional standards, in connection with its performance of audits, issuance of audit reports, and related matters involving issuers.

(b) In furtherance of the Board's inspection process, the Board may at any time request that a registered public accounting firm provide to the Board additional information or documents relating to information provided by the firm in any report filed pursuant to Section 2 of these Rules, or relating to information that has otherwise come to the Board's attention. Any request for information or documents made pursuant to this Rule, and any information or documents provided in response to such a request, shall be considered to be in connection with the next regular or special inspection of the registered public accounting firm.

(c) Inspection steps and procedures shall be performed by the staff of the Division of Registration and Inspections, and by such other persons as the Board may authorize to participate in particular inspections or categories of inspections.

* * *

Rule 4003. Frequency of Inspections

* * *

(c) With respect to a registered public accounting firm that has filed a completed Form 1-WD under Rule 2107, the Board shall have the discretion to forego any regular inspection that would otherwise commence during the period beginning on the [fifth day following the filing of the] <u>date of Board receipt of a</u> completed Form 1-WD and continuing until the firm's registration is deemed withdrawn or the firm withdraws the Form 1-WD.

* * *

II. <u>Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule</u>

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed rule. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. <u>Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rules</u>

(a) Purpose

Section 102(d) of the Act provides that each registered public accounting firm shall provide an annual report to the Board, and may be required to report more frequently, as necessary to update information in its application for registration and to provide such additional information as the Board or the Commission may specify. The purpose of the proposed new rules and forms is to establish the foundation of a reporting and disclosure system for registered public accounting firms pursuant to Section 102(d) of the Act, and to specify the details of certain reporting obligations and provide forms for such reporting. To the extent that the Board identifies additional reporting requirements that are necessary or appropriate in the public interest or for the protection of investors, the Board may propose and adopt them in the future.

The proposed reporting requirements serve three fundamental purposes. First, firms will report information to keep the Board's records current about such basic matters as the firm's name, location, contact information, and licenses. Second, firms will report information reflecting the extent and nature of the firm's audit practice related to issuers in order to facilitate analysis and planning related to the Board's inspection responsibilities and to inform other Board functions, as well as for the value the information may have to the public. Third, firms will report circumstances or events that could merit follow-up through the Board's inspection process or its enforcement process, and that also may otherwise warrant being brought to the public's attention (such as a firm's withdrawal of an audit report in circumstances where the information is not otherwise publicly available).

The reporting framework includes two types of reporting obligations. First, it requires each registered firm to provide basic information once a year about the firm and the firm's issuer-related practice over the most recent 12-month period. The firm must do so by filing an annual report on Form 2. Second, upon the occurrence of specified events, a firm must report certain information by filing a special report on Form 3.

Proposed Rule 2201 sets June 30 as the deadline for the annual filing of Form 2. The reporting period covered by the report would be April 1 to March 31, leaving each firm with three months to prepare and file a Form 2 reflecting information from that 12-month period. Any firm that was registered as of March 31 of a particular year would be required to file Form 2 by June 30 of that year, but any firm that became registered in the period between and including April 1 and June 30 would not be required to file a Form 2 until June 30 of the following year.

Under the proposed rules, the occurrence of specified events triggers an obligation to file a special report on Form 3. The proposed rules provide that special reports must be filed within 30 days of the triggering event.

The Board expects annual and special reports to be complete and accurate, and inaccuracies or omissions could form the basis for disciplinary sanctions for failing to comply with the reporting requirements reflected in Rules 2200 and 2203 and the instructions to Forms 2 and 3. Proposed Rule 2205 provides for the filing of amendments to previously filed annual or special reports if the originally filed report included information that was incorrect at the time of the filing, or if the originally filed form omitted any information or affirmation that was, at the time of such filing, required to be included in that report.

Annual and special reports will be made public on the Board's Web site promptly upon being filed by a firm, subject to exceptions for information for which a firm requests confidential treatment. The Board intends that as much reported information as possible be publicly available as soon as possible after filing. The proposed forms identify certain categories of information for which a firm may request confidential treatment. The proposed rules include new requirements concerning the support that a firm must supply for a confidential treatment request.[1] The proposed amendments require that a firm support a request with both a representation that the information has not otherwise been publicly disclosed and either (1) a detailed explanation of the grounds on which the information is considered proprietary, or (2) a detailed explanation of the basis for asserting that the information is protected by law from public disclosure and a copy of the specific provision of law. The proposed amendments also provide that the firm's failure to supply the required support constitutes sufficient grounds for denial of the request.

Under proposed Rule 2207, a non-U.S. firm may withhold required information from Form 2 or Form 3 if the firm cannot provide the information without violating non-U.S. law. If the firm withholds information on that ground, it must have certain supporting materials, including (1) a copy of the relevant provisions of non-U.S. law, (2) a legal opinion concluding that the firm would violate non-U.S. law by submitting the information to the Board, and (3) a written explanation of the firm's efforts to seek consents or waivers that would be sufficient to overcome the conflict with respect to the information. The firm must certify on the form that it has the supporting materials in its possession. The rule reserves to the Board, and to the Director of the Division of Registration and Inspections, the discretion to require that a firm submit any of those supporting materials in a particular case. The rule also reserves to the Board the

[1] The proposed amendments to Rule 2300(b)-(c), concerning the required support, would also apply prospectively to confidential treatment requests on applications for registration on Form 1.

discretion to require that the firm provide any of the withheld information in a particular case.

The proposed rules include an amendment to the Board's inspection rules that makes clear that the Board may require a firm to provide additional information. Specifically, existing Rule 4000 provides that registered firms shall be subject to such regular and special inspections as the Board chooses to conduct. The proposed amendment adds a paragraph providing that the Board, in the exercise of its inspection authority, may at any time request that a registered firm provide additional information or documents relating to information provided on Form 2 or Form 3, or relating to information that has otherwise come to the Board's attention. The amendment provides that the request and response are considered to be in connection with the firm's next regular or special inspection. Accordingly, the cooperation requirements of Rule 4006 apply, and the request and response are subject to the confidentiality restrictions of Section 105(b)(5) of the Act.

Existing Rule 2107 governs the process by which a firm may seek to withdraw from registration with the Board. Under Rule 2107, a firm cannot withdraw at will, but must request the Board's permission to withdraw, and the Board may withhold that permission under certain conditions. The proposed rules include an amendment to Rule 2107 to change the way it addresses the reporting obligations of a firm that has filed Form 1-WD seeking leave to withdraw. Existing Rule 2107(c)(2)(i) provides that, beginning on the fifth day after the Board receives a completed Form 1-WD, the firm can satisfy any annual reporting requirement by submitting a report stating that a completed Form 1-WD has been filed and is pending. Under the proposed amendment, the firm's reporting obligation, including both annual and special reporting, would simply be suspended while Form 1-WD was pending. If a firm withdraws its Form 1-WD and continues as a registered firm, however, Rule 2107 would require the filing of any annual or special reports, and the payment of any annual fee, that otherwise would have been required while the Form 1-WD was pending. The Board is also eliminating from Rule 2107 the five-day delay between receipt of a completed Form 1-WD and the effect of that filing on a firm's reporting obligation. Suspension of that obligation would occur immediately upon the Board's receipt of the completed Form 1-WD.[2]

The Board also proposed to delete from definitions in PCAOB Rule 1001 certain provisions that ceased to apply after December 15, 2003. Specifically, the Board proposes to amend Rules 1001(a)(vii) (definition of "audit services"), 1001(o)(i) (definition of "other accounting services"), and 1001(n)(ii) (definition of "tax services") by deleting the paragraph denominated "(1)" from each rule.

The proposed rules would take effect 60 days after Securities and Exchange Commission approval.

(b) Statutory Basis

The statutory basis for the proposed rule is Title I of the Act.

B. Board's Statement on Burden on Competition

The Board does not believe that the proposed rules will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

[2] In connection with that change to Rule 2107, the amendment also eliminates the five-day delay before certain other consequences take effect. Among other things, the Board is amending Rule 2107(c)(2)(iii) so that the Board would, immediately upon receipt of the completed Form 1-WD, have the discretion to forego any regular inspection of the firm that otherwise would commence. This change necessitates a conforming change to Rule 4003(c), and the Board is making that conforming change as well.

The proposed rules impose no burden beyond burdens clearly imposed and contemplated by the Act.

C. Board's Statement on Comments on the Proposed Rules Received from Members, Participants or Others

The Board released the proposed rules and form instructions for public comment in Release No. 2006-004 (May 23, 2006). A copy of Release No. 2006-004 and the comment letters received in response to the PCAOB's request for comment are available on the PCAOB's Web site at www.pcaobus.org. The Board received twelve written comment letters. The Board has clarified and modified certain aspects of the proposed rules and form instructions in response to the comments it received, as discussed below.

Commenters voiced concern about burdens associated with the proposed requirement to report the percentage of total fees billed to all clients that is attributable to fees billed in each of four categories of services provided to issuer audit clients. Commenters indicated that firms, particularly large firms, may not be able to comply with the proposed requirement without making costly changes to their internal systems. The Board has weighed these concerns carefully, bearing in mind that the purposes for which the information is sought do not depend upon a high level of precision in the data. The Board is adopting a modified version of the proposed requirement, incorporating some elements of alternatives suggested by commenters.

Form 2 will allow a firm to select from two methods of calculating the percentages to report. Firms that are reasonably able to report the requested percentages based on data precisely coinciding with the annual reporting period (i.e., the data specified by the proposed requirement) may do so. As an alternative, a firm may, for each category of services, report the percentage derived by (1) using as a denominator the total fees billed to all clients in the firm's fiscal year that ended during the annual reporting period and (2) using as a numerator the total issuer audit client fees as determined by reference to the fee amounts disclosed to the Commission by those clients for each client's fiscal year that ended during the reporting period (or, for clients who have not made the required Commission filings, the fee amounts required to be disclosed). Under either approach, a firm may use any reasonable method to estimate the components and may round the reported percentages to the nearest five percent. Firms that use estimated data in their calculations should briefly describe their methodology in an exhibit to Form 2.

Some commenters also expressed concern about what they saw as a disconnect between the four categories of services used in the proposed form and the four categories of fees that the Commission requires issuers to report in proxy filings. The Board reiterates that its definitions of these four categories of services correspond to the Commission's descriptions of services for which an issuer must disclose the fees paid to its auditor.[3/] The Board is not adopting commenters' suggestions to make the Board's labels conform to the Commission's labels (i.e., to say "audit-related services" instead of "other accounting services" and to say "all other services" instead of "non-audit services") because the labels that the Board uses come from Section 102(b)(2)(B) of the Act and have been used in all applications for registration on Form 1. Commenters also noticed a disconnect between Item 3.2's focus on fees billed and the reference to "revenues" in Item

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[3/] Compare the descriptions of services in Item 9(e) of Commission Schedule 14A (17 CFR 240.14a-101) under the headings "Audit Fees," "Audit-Related Fees," "Tax Fees," and "All Other Fees" with, respectively, the Board's definitions of "Audit Services" (Rule 1001(a)(vii)), "Other Accounting Services" (Rule 1001(o)(i)), "Tax Services" (Rule 1001(t)(i)), and "Non-Audit Services" (Rule 1001(n)(ii)). The note to Item 3.2 on Form 2 has been expanded to highlight this point.

3.2's caption. The Board has changed the caption to refer to fees billed instead of revenues.

Item 4.1 of Form 2 requires information relating to a firm's issuance of audit reports during the reporting period. As it was proposed, Item 4.1 would have required, among other things, the total number of firm personnel who exercised authority to sign the firm's name to an audit report during the reporting period. Commenters suggested various alternatives to requiring that precise number. Bearing in mind that, here too, the purposes for which the information is sought – principally inspection scoping and planning – do not depend upon precise information, the Board has adopted a slightly modified version of an approach suggested by a commenter. As adopted, Item 4.1.b requires a firm to indicate from among the following ranges how many individuals exercised the authority to sign the firm's name to an audit report in the reporting period: 1-9, 10-25, 26-50, 51-100, 101-200, or more than 200. If the firm indicates that the range is 1-9, the firm must also provide the exact number.

One commenter sought clarification on whether the audit report date being requested referred to the date of the auditor's report, the report release date pursuant to PCAOB Auditing Standard No. 3, Audit Documentation, or the date that the issuer filed the report with the Commission. A note to Item 4.1 now clarifies that the date called for by Item 4.1.a.3 is the date of the audit report, as described in AU 530, Dating of the Independent Auditor's Report. A note has also been added to clarify that it is not necessary to provide the date of any consent to an issuer's use of an audit report previously issued for that issuer, except that, if such consents constitute the only instances of the firm issuing audit reports for a particular issuer during the reporting period, the firm should include that issuer in Item 4.1 and include the dates of such consents in Item 4.1.a.3.

If, during the reporting period, a firm plays a substantial role in the preparation or furnishing of an audit report that was issued in the reporting period, but the firm did not issue audit reports required to be reported under Item 4.1, the firm must report certain information under Item 4.2. As proposed, Item 4.2.a.4 would have required the firm to report the date of each such audit report. One commenter expressed concern that a firm might not have access to the date of an audit report issued by another firm. The Board has revised Item 4.2.a.4 to require, instead, the end date of the fiscal period covered by the financial statements that were the subject of the audit report.

Item 5.2.a.3, as proposed, would have required the firm to state whether it has any "affiliation, whether by contract or otherwise, with another entity through or from which the firm commonly employs or leases personnel to perform audit services, or with which the firm otherwise engages in an alternative practice structure." Commenters asked for clarification of "commonly" and also suggested that the term "affiliation" could cause confusion since the item does not appear intended to be limited to relationships commonly viewed as "affiliate" relationships. The final version of Item 5.2.a.3 avoids the use of "affiliation" and "commonly" and requires the firm to state whether it has any "arrangement, whether by contract or otherwise, with another entity through or from which the firm employs or leases personnel to perform audit services." One commenter also asked the Board to clarify that Item 5.2.a.3 does not encompass a firm's hiring of, or contracting for, support personnel. Item 5.2.a.3, by its terms, encompasses only arrangements through which the firm employs or leases "personnel to perform audit services."

Regarding Part VI, commenters expressed concern about Item 6.1.d's requirement to provide information about the number of firm personnel, segregated by functional level, who provided audit services during the reporting period. Commenters stated that some firms cannot readily track with precision the number of such individuals. Commenters constructively suggested various alternative ways to collect a rough surrogate for that number. The Board has concluded, however, not to adopt any version of Item 6.1.d at this time.

Item 6.1.b requires the firm to report the total number, as of the end of the reporting period, of the firm's certified public accountants, and requires the firm to include in that number any firm accountants with "comparable licenses" from non-U.S. jurisdictions. One commenter asked for clarification of the "comparable license" concept. The "comparable license" concept is not new, but is employed in the Form 1 application for registration. Even so, the commenter suggested clarifying that the requirement refers to accountants that are (1) licensed by the jurisdiction in which they render services and (2) by virtue of such license, are certified to perform the functions of a public accountant. The Board confirms this as the appropriate understanding of the requirement.

In Part VII of Form 2, the firm must report information if it stands in certain relationships to individuals who, or entities that, were the subject of a Board order imposing a disciplinary sanction or a Commission Rule 102(e) order entered within the five years preceding the end of the reporting period.

As proposed, the Part VII items would have required a firm to report new relationships commenced during the reporting period, and the proposal would have required every firm's first Form 2 filing to report this information not only for the reporting period but for the entire period back to the cut-off date that the firm used for information it supplied in its Form 1 application. For hundreds of firms' first Form 2 filings, that period would be more than five years.

In response to comments about that burden, the Board has restructured the Part VII items relating to firm personnel or owners to capture only relationships that (1) exist as of the end of the reporting period, (2) are with individuals or entities whose relevant disciplinary sanction or Rule 102(e) order was entered within the five years preceding the end of the reporting period, and (3) have not previously been reported by the firm on Forms 1, 2, or 3. The Board has also restructured the Part VII item relating to receipt of consulting or professional services to capture only relationships that involve services received, or contracted for, in the reporting period. With these changes, a firm's first Form 2 will still effectively serve to fill any gap, but the burden will only extend to currently relevant information. Subsequent Form 2 filings need not report the same information again just because the relationship continues to exist at the end of the reporting period.

In response to commenters' concerns and suggestions, the Board has also limited the scope of relevant firm personnel to those who provided at least ten hours of audit services for any issuer during the reporting period. It is important to note, however, how this change intersects with the structural change described above. Just because an individual does not meet the ten-hour threshold during the reporting period in which the relationship begins does not mean that the firm need never report the relationship. If there is a later reporting period in which that person meets the ten-hour threshold, and that reporting period end is still within five years of the entry of the disciplinary sanction or Commission order, the firm must report that relationship in its annual report for that period. The relationship need only be reported one time, however, and need not be reported again for future reporting periods in which the criteria are met.

Also in response to comments, the Board has added a scope limitation to Part VII's approach concerning the firm's receipt of consulting or other professional services. The Board has narrowed the reporting trigger to encompass only arrangements for services related to the firm's audit practice or related to services the firm provides to issuer audit clients. The reporting obligation is triggered for any reporting period that ends less than five years after entry of the disciplinary sanction or Commission order and in which the firm has received or arranged to receive such services.

Finally, the Board is eliminating one category of reportable relationships that was included in the proposal. The Board proposed that firms report information if they entered into a relationship with any individual who, while not having been sanctioned personally, was a principal of a firm at the time of conduct for which the firm was later subjected to specified sanctions. After carefully considering comments, however, the Board is persuaded that any occasional value this information might have is outweighed by the fact that treating this information as a risk indicator about either the firm or the individual has the potential to diminish the professional opportunities of (1) individuals who had no connection to the misconduct at all, and (2) individuals who had a connection to alleged misconduct, but who never had an opportunity to defend against charges because a regulator was satisfied to conclude the matter through a settlement with the firm. In addition, the Board is sensitive to the unusual burden that would be placed on firms not only to ascertain this information at the time they commence the relationship, but also to continually monitor for it, since the relevant sanction might not be entered until years after the conduct.

In Part VIII of Form 2, the firm must report information if it has acquired another public accounting firm or taken on 75 percent or more of another accounting firm's principals. Commenters suggested the need for some clarification, and the Board has made changes to clarify two points. First, where the proposal referred only to acquisition of an "accounting firm" – which commenters correctly noted is not a term defined in the Act or the Board's rules – the final form now refers to a "public accounting firm," which is defined in both the Act and the rules. Second, with respect to taking on 75 percent or more of another firm's principals, the final form includes language clarifying that the reference is to 75 percent of the persons who were principals of the other firm "as of the beginning of the reporting period."

Form 2 requires an annual affirmation related to the Act's requirements that the firm consent to cooperate with the Board and enforce cooperation by the firm's associated persons. Tracking the consent language included in Form 1, Form 2 requires the firm (1) to affirm its consent to cooperate with Board requests for testimony or documents, (2) to affirm that it has secured from each of its associated persons the required consents to cooperate with the Board, and (3) to affirm the firm's understanding and agreement that its cooperation and compliance, and the securing and enforcing of consents from its associated persons, is a condition of its continued registration with the Board.

One commenter seemed to misunderstand the proposal and suggested that the Board make clear that this requirement is an update of the Form 1 consent and is required only for new employees since a firm's initial registration. The Form 2 affirmation does not impose a new substantive requirement but merely requires the firm to affirm that it remains aware of its continuing obligation to cooperate and that it has in fact been keeping up with its ongoing obligation to secure the requisite consents from all of its associated persons.

The reporting framework includes accommodations for firms faced with potential non-U.S. legal obstacles to their ability to comply with Form 2 requirements. One such accommodation is reflected in a note to the Form 2 affirmation section. The note explains that the affirmation shall not be understood to include an affirmation that the firm has secured consents from associated persons that are unregistered foreign firms that assert that non-U.S. law prohibits them from providing the consent, as long as certain requirements concerning that assertion are satisfied. Two commenters expressed concern about the note's provision that the registered firm (filing the Form 2) must have in its possession documents relating to the unregistered firm's asserted conflict that would be sufficient to satisfy the requirements of Rule 2207(c)(2)-(4). The commenters expressed concern about whether that language effectively requires the registered firm (filing the Form 2) to assess the substance of the unregistered non-U.S. firm's conflict assertion. The note requires no such assessment by the registered firm, but only requires the firm to ascertain that the documents appear, on their face, to be the documents described in Rule 2207(c)(2)-(4).

Rule 2201 sets June 30 as the deadline for the annual filing of Form 2. The reporting period covered by the report would be April 1 to March 31. Commenters suggested alternatives, such as tying a firm's reporting deadline to that firm's fiscal year, to avoid what those commenters saw as unnecessary burdens on firms. In the Board's view, a single filing deadline for all firms is more appropriate than varying deadlines tied to individual firms' fiscal years. The Board has considered the comments about burden and has made changes that will address those concerns – such as allowing a firm to use its and its clients' fiscal year data in reporting the fee billing information – without introducing varying reporting periods and deadlines for different firms. With those changes, the required Form 2 reporting does not involve any complexity or burden that makes it unreasonable to require all firms to supply the information according to the same schedule.

Under the rules, the occurrence of specified events triggers an obligation to file a special report on Form 3. The list of reporting triggers reflects the Board's decision, after consideration of comments, to drop some items from the list that was proposed and to refine the focus of other items. The changes and clarifications relate to a client's unauthorized use of the firm's name, reportable criminal and other proceedings, reportable new relationships, and changes in authorization to engage in the business of auditing.

The Board has excluded from the final requirements one special reporting trigger that was proposed: an issuer's unauthorized use of the firm's name, such as by making a filing with the Commission that includes an audit report that the issuer falsely represents as having been issued by the firm. In proposing that item, the Board noted that it might protect investors and serve the public interest by drawing attention to a potential problem relatively quickly. The commenters who addressed the point expressed a view that this reporting requirement would be fundamentally about issuer conduct and, therefore, is more appropriately left to the Commission in the context of its disclosure framework and its framework for addressing Section 10A(b) reports from auditors. After consideration of those comments, the Board has decided not to adopt such a requirement at this time.

The proposed rules included a requirement that a firm file a special report when it withdraws an audit report, but also provided an exception to that requirement if the issuer audit client had already disclosed the relevant information in a Form 8-K filing with the Commission. The views expressed by commenters on this point were similar to the views described above with respect to an issuer's unauthorized use of a firm's name.

The Board is adopting this item as proposed. The point of this item is not to have the firm draw the Board's attention to potential problems with an issuer's financial statements. A withdrawn audit report is a risk indicator concerning the auditor's conduct preceding the withdrawal, not merely a risk indicator concerning the issuer's financial statements. The Board has a regulatory interest in being aware of that information and possibly following up on that information for reasons directly related to its oversight of auditors.

Nor is the point of the item to have the firm draw the Board's attention to a failure by the issuer to file a required Form 8-K. The Board's interest is in the fact of the withdrawn audit report. In the usual case, the Board can obtain that information from issuer Form 8-K filings without requiring duplicative filing by the firm, but the Board cannot do so if the issuer does not file the Form 8-K. For that reason, the Form 3 requirement is limited to circumstances in which the information is not otherwise available to the Board through a Form 8-K filing.

One commenter noted that if an issuer is no longer a client, the firm may not be in a position to monitor whether that former client has made the Form 8-K filing. Item 4.02(c) of Form 8-K, however, requires the issuer to provide the firm with a copy of the disclosures it is making in response to Item 4.02 no later than the day the issuer files the Form 8-K, and also requires the issuer to request that the firm furnish to the issuer a letter addressed to the Commission stating whether the firm agrees with the statements made by the issuer in response to Item 4.02. The firm should, therefore, generally be in a position to know whether the issuer has made the filing.

As proposed, Form 3 would have required a firm to file a special report if a partner, shareholder, principal, owner, member, or audit manager of the firm became a defendant in criminal proceedings involving certain categories of offenses. After consideration of comments, the Board has narrowed this requirement in two respects. First, the Board has reformulated these Form 3 reporting triggers to distinguish between proceedings that arise out of conduct in providing audit services or other accounting services for issuers and proceedings that do not arise out of such conduct. As to the latter category, the reporting obligation will be triggered only if the relevant individual provided at least ten hours of audit services for any issuer during the firm's current or most recently completed fiscal year. Second, the Board has eliminated from the categories of relevant offenses two relatively broadly described categories: crimes arising out of alleged conduct relating to "dishonesty," and crimes arising out of alleged conduct that, if proven, "would bear materially on the individual's fitness to provide audit services to issuers."

One commenter expressed uncertainty about whether a firm would need to report the event if the firm suspended or terminated the individual or prohibited the individual from providing audit services for issuers. The reporting obligation includes no such qualification. The firm's reporting obligation is triggered when it becomes aware of the proceeding, and that obligation is not cut off if the firm terminates its relationship with the individual.

Some commenters sought clarification about the inclusion of "managers" and "members" within the scope of relevant individuals. One commenter asked whether "members" was meant to include employees generally. "Members" is not meant to include all employees but, rather, is intended as it is often used in firms' structures and parlance to distinguish those with certain ownership or governance rights from others. Some commenters noted that "managers" typically are not owners or partners and so questioned whether the Board intended to include them within the scope of this requirement. The Board is aware of the distinction and does intend the requirement to encompass manager-level personnel. The Board has, however, referred in the final rules to "audit manager" rather than merely "manager," to avoid any possible confusion about other sorts of managers, as the term is more generally used.

Some commenters expressed concern about the information that Form 3 would require the firm to provide about the proceedings that triggered the reporting requirement. Commenters suggested that providing descriptions of the proceedings could be burdensome, that the descriptions would be inherently subjective, and that the descriptions should not be in the public arena while the proceeding is ongoing. The Board has not made any changes related to this point. Form 3 requires the firm to list the statutes, rules, or legal duties that are alleged to have been violated, which involves no subjective or qualitative analysis, and requires a brief description of the alleged conduct, which can be drawn from the relevant complaint or charging document without creating any implication that the firm concedes anything about the allegations. If grounds exist, under Rule 2300, for keeping the reported information confidential, the firm may request confidential treatment.

Form 3 requires a firm to file a special report if it enters into certain specified relationships with individuals or entities that are currently subject to any of the following: (1) a Board disciplinary sanction suspending or barring an individual from being an associated person of a registered public accounting firm, (2) a Board order disapproving an entity's application for registration, or (3) a Commission order under Rule 102(e) of the Commission's Rules of Practice suspending or denying the privilege of appearing or practicing before the Commission. Commenters suggested that the scope of relevant individuals should be limited to those who provide audit services. Although the Board has made such a change to the similar Form 2 requirement, such a change is not appropriate for this Form 3 requirement, which is generally intended to gather information about new relationships with persons or entities that are effectively restricted from providing audit services. In this context, the qualification suggested by commenters would have the effect of either negating the requirement entirely or transforming it into a requirement for a firm to report that a person or entity is violating such a restriction in connection with audits performed by the firm. For similar reasons, the Board has rejected suggestions to narrow the scope of consulting and professional services received by the firm that trigger this reporting requirement.

Commenters also expressed concern about the burden associated with identifying the existence of the sanction or 102(e) order. Firms should understand, however, that to a significant extent that burden effectively exists regardless of whether the firm has a reporting obligation. Not only does the firm have an obvious need to know, for its own purposes, of any such limitations on the person's ability to provide services, but Board Rule 5301(b) provides that "no registered public accounting firm that knows, or in the exercise of reasonable care should have known, of the suspension or bar of a person may permit such person to become or remain associated with it, without the consent of the Board, pursuant to Rule 5302, or the Commission."[4/]

Form 3 requires a firm to file a special report regarding certain changes in its authorization to engage in the business of auditing or accounting in a particular jurisdiction. After considering comments, the Board has made wording changes to clarify three points: (1) the requirement is intended only to cover circumstances that involve a loss of the firm's authorization to engage in the business of auditing or accounting; (2) the proposed phrase, "made subject to condition or contingencies," was not intended to encompass conditions or contingencies that are broadly applicable to all firms licensed in the jurisdiction; and (3) the requirement to report new licenses or certifications, or changes in existing licenses or certifications, is limited to licenses and certifications that authorize the firm to engage in the business of auditing or accounting.

[4/] Rule 5301(b)'s prohibition on allowing such a person to "become or remain associated with" the firm is not a prohibition against any and all employment or other relationships, but only a prohibition against allowing the person to be an "associated" person as that term is defined in Section 2(a)(9) of the Act and Board Rule 1001(p)(i).

The proposed rules would have required that special reports on Form 3 be filed no later than 14 days after the triggering event. Several commenters expressed concern that 14 days was not sufficient time in which to review and assess an event and report the required information, and that this was particularly true for non-U.S. firms that may need to assess possible legal obstacles to reporting and prepare the materials necessary to comply with Rule 2207. Commenters' alternative suggestions included 30 days, 45 days, 60 days, and 90 days. The Board is persuaded that a longer period than 14 days is appropriate and is adopting a requirement to file special reports within 30 days of the triggering event.

Commenters also raised questions about when, for certain reportable events, the "trigger" actually occurs. In particular, several triggering events are described in Form 3 in terms of when the firm has "become aware" that something has occurred. Commenters asked for clarification of what it means, in this context, to say that the firm has become aware of a matter. The Board has added a note to the beginning of Part II of Form 3 to specify that the firm is deemed to have become aware of the relevant facts on the date that any partner, shareholder, principal, owner, or member of the firm first becomes aware of the facts. The Board believes it is reasonable to expect a firm to have controls designed to ensure that any such person who becomes aware of relevant facts understands the firm's reporting obligation and brings the matter to the attention of persons responsible for compliance with the obligation.

As proposed, Rule 2205 would have required a firm to amend its filing within a fixed time after becoming aware of an error or omission. Commenters raised concerns about the practical difficulties posed in this context by reliance on the concept of a firm becoming "aware" of an error or omission. The Board recognizes those difficulties. Rather than prescribe requirements for firms to have systems and procedures to surface such errors or omissions and then report them within a prescribed time, the Board's revised approach relies on the firm understanding its self-interest. The Board expects annual and special reports to be complete and accurate, and inaccuracies or omissions could form the basis for disciplinary sanctions for failing to comply with the reporting requirements reflected in Rules 2200 and 2203 and the instructions to Forms 2 and 3. Firms should be sufficiently motivated to have procedures to detect any need for amendments, and to amend filings as soon as possible, in order to mitigate the possibility of disciplinary sanctions for the inaccurate original filing.

The amendment to Rule 4000 adds a paragraph providing that the Board, in the exercise of its inspection authority, may at any time request that a registered firm provide additional information or documents relating to information provided on Form 2 or Form 3, or relating to information that has otherwise come to the Board's attention. The amendment provides that the request and response are considered to be in connection with the firm's next regular or special inspection. In response to concerns raised by some commenters, the Board confirms that the information-gathering activity described in the amendment is an exercise of the Board's inspection authority. It does not provide a basis for the Board to compel a firm to provide information beyond the scope of information encompassed by the inspection authority, or for purposes other than assessing compliance by the firm or its associated persons with the "Act, the rules of the Board, the rules of the

Commission, or professional standards, in connection with its performance of audits, issuance of audit reports, and related matters involving issuers."[5]

Annual and special reports will be made public on the Board's Web site promptly upon being filed by a firm, subject to exceptions for information for which a firm requests confidential treatment. The amendments to Rule 2300 require that a firm support a request with both a representation that the information has not otherwise been publicly disclosed and either (1) a detailed explanation of the grounds on which the information is considered proprietary, or (2) a detailed explanation of the basis for asserting that the information is protected by law from public disclosure and a copy of the specific provision of law. The amendments also provide that the firm's failure to supply the required support constitutes sufficient grounds for denial of the request.

In response to questions raised by commenters, the Board emphasizes that this approach to confidential treatment requests does nothing to change a firm's right to seek review of an initial denial of confidential treatment. Initial decisions will continue to be made by the Director of Registration and Inspections, pursuant to delegated authority, under Rule 2300(h). A firm may, under Rule 5468, seek Board review of any denial.

One commenter noted that confidentiality protection might arise from sources other than statutes and regulation, including common law, judicial orders, and contractual terms, and that the Board should more broadly define the scope of documentation that may be presented in support of a confidential treatment request. Rule 2300(b), however, does not limit the scope of documentation that a firm may present to support its argument that the rule's criteria for confidentiality are satisfied. The Board also agrees that

[5] Section 104(a) of the Act.

"applicable law related to the confidentiality of proprietary, personal, or other information" that may protect information from public disclosure is not limited to statutes and regulations. At the same time, however, a contractual agreement between two parties does not constitute "applicable law" and is unlikely to satisfy the rule's criteria.

Under proposed Rule 2207, a non-U.S. firm may initially withhold required information from Form 2 or Form 3 if it could not provide the information without violating non-U.S. law. If non-U.S. firm withholds information on that ground, it must have certain supporting materials, including (1) a copy of the relevant provisions of non-U.S. law, (2) a legal opinion concluding that the firm would violate non-U.S. law by submitting the information to the Board, and (3) a written explanation of the firm's efforts to seek consents or waivers that would be sufficient to overcome the conflict with respect to the information.

To address a concern raised by commenters, the Board has revised Rule 2207(c)(4), and added a related note at the end of the rule, to make clear that the rule does not require a firm to repeat previously futile efforts to obtain consents and waivers. Specifically, Rule 2207(c)(4) requires the firm to prepare and maintain a written representation that it has made "reasonable efforts" to obtain relevant consents and waivers. The note at the end of the rule makes clear that the "reasonable efforts" element of the rule does not require either (1) that the firm renew efforts with parties that have previously declined to provide consents or waivers with respect to similar types of information, or (2) that the firm seek consents or waivers from parties other than firm personnel and firm clients.

In its initial proposal, the Board stated that it intended for the reporting requirements to take effect 21 days after Commission approval, with "catch-up" Form 3 filings due 14 days later. The Board has considered comments expressing concern that this is too ambitious a schedule, and the Board is now taking a different approach. The Board intends that the rules, rule amendments, and Forms 2 and 3 that it is adopting today will take effect on the date that is 60 days after Commission approval. This will build in more than ample lead time for firms to become aware of Commission approval of the rules and to prepare any reports that will be due after the rules take effect.

III. Date of Effectiveness of the Proposed Rules and Timing for Commission Action

Within 60 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Board consents, the Commission will:

(a) by order approve such proposed rules; or

(b) institute proceedings to determine whether the proposed rules should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rules are consistent with the requirements of Title I of the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/pcaob.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number PCAOB 2008-04 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number PCAOB 2008-04. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web sit (http://www.sec.gov/rules/pcaob/shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule that are filed with the Commission, and all written communications relating to the proposed rule between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filing will also be available for inspection and copying at the principal office of the PCAOB. 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. All submissions should refer to File No. PCAOB-2008-04 and should be submitted on or before [insert 30 days from publication in the Federal Register].

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60108; File No. PCAOB-2008-05)

June 12, 2009

Public Company Accounting Oversight Board; Notice of Filing of Proposed Rules on Succeeding to the Registration Status of a Predecessor Firm

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on August 4, 2008, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission" or "SEC") the proposed rules described in Items I and II below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rules from interested persons.

I. Board's Statement of the Terms of Substance of the Proposed Rules

On July 29, 2008, the Board adopted rules and a form related to succeeding to the registration status of a predecessor firm. New PCAOB Rules 2108-2109 and the instructions to a new form, Form 4, are set out below.

SECTION 2. REGISTRATION AND REPORTING

Part 1 – Registration of Public Accounting Firms

* * *

2108. Succeeding to the Registration Status of a Predecessor

(a) In the event that a registered public accounting firm changes its form of organization or changes the jurisdiction under the law of which it is organized, in circumstances that do not involve an acquisition or combination as described in paragraph (b) of this Rule, the entity in its new form shall succeed to the registration status of the predecessor if the new entity is a public accounting firm and files a Form 4 in accordance with Rule 2109.

(b) In the event that a registered public accounting firm is acquired by an entity that is not a registered public accounting firm, or combines with any other entity or entities to form a new legal entity –

(1) if the acquiring entity or the new entity is a public accounting firm that files a Form 4 in accordance with Rule 2109, and the answer provided to each subpart of Item 3.2.e of that Form 4 is "no," that entity shall succeed to the registration status of the registered firm;

(2) if the acquiring entity or the new entity is a public accounting firm that files a Form 4 in accordance with Rule 2109, and the answer provided to any subpart of Item 3.2.e of that Form 4 is other than "no," that entity shall not succeed to the registration status of the registered firm; provided, however, that if that entity represents on Form 4 that it has filed, or that it intends to file within 45 days of the effective date of the acquisition or combination, an application for registration on Form 1, then –

(i) subject to the qualifications in subparagraphs (ii), (iii), and (iv), that entity shall temporarily succeed to the registration status of the registered firm for a transitional period, but that registration will cease to be effective on the earlier of the date that the entity's application on Form 1 is approved or the date that is 91 days after the effective date of the acquisition or combination as reported on Form 4;

(ii) subject to the qualifications in subparagraphs (iii) and (iv), if the acquisition or combination took effect before the effective date of this rule, that entity shall temporarily succeed to the registration status of the registered firm for a transitional period, but that registration will cease to be effective on the earlier of the date that the entity's application on Form 1 is approved or the date that is 91 days after the effective date of this rule;

(iii) if the Board requests additional information from the entity pursuant to Rule 2106(c) with less than 60 days remaining in the original transitional period, the entity's temporary succession to registration status shall continue to the date that is 60 days after the date of the Board's request; and

(iv) if, after the original transition period has been extended pursuant to subparagraph (iii), the Board makes any further requests for additional information from the entity pursuant to Rule 2106(c), the Board may in its discretion extend the temporary succession to registration status for such finite period as the Board shall specify.

(c) Subject to paragraph (d) of this rule, a public accounting firm that results from events described in paragraphs (a) or (b) of this rule shall not, in the absence of compliance with the provisions of Rule 2109, succeed to the registration status of a predecessor registered public accounting firm.

(d) Notwithstanding paragraph (c) of this rule, if a public accounting firm's failure to comply with the provisions of Rule 2109 is solely a failure concerning the timeliness of the submission, the firm may request leave to file Form 4 out of time by indicating and supporting that request in accordance with the instructions to the form. The Board will evaluate any such request in light of the relevant facts and circumstances and the public interest and may, in its discretion, grant or deny the request. If the Board grants leave to file the form out of time, the Form 4 shall be deemed filed and the provisions of paragraphs (a) and (b) shall apply as if the Form 4 had been timely filed. A Form 4 that has been submitted out of time may be withdrawn by the firm at any time before the Board has approved or disapproved the request for leave to file out of time.

2109. Procedure for Succeeding to the Registration Status of a Predecessor

(a) A public accounting firm seeking to succeed to the registration status of a predecessor registered public accounting firm pursuant to the provisions of Rule 2108 must do so by filing a Form 4 –

(1) no later than the 14th day after the change or business combination takes effect, if the change or business combination takes effect on or after [insert effective date of this rule]; or

(2) no later than [insert date 14 days after effective date of this rule], if the change or business combination took effect before [insert effective date of this rule].

(b) A public accounting firm filing a Form 4 must do so by filing the Form 4 in accordance with the instructions to that form. Unless directed otherwise by the Board, a public accounting firm filing a Form 4 must file the Form 4 and exhibits thereto electronically with the Board through the Board's Web-based system.

(c) A Form 4 shall be deemed to be filed on the date that the public accounting firm submits a Form 4 in accordance with Rule 2109(b) that includes the signed certification required in Part V of Form 4, provided, however, that any report so submitted after the applicable deadline as prescribed in paragraph (a) of this rule, shall not be deemed filed unless and until the Board, pursuant to Rule 2108(d), grants leave to file the Form 4 out of time.

(d) The provisions of Rule 2204 concerning signatures, shall apply to each signature required by Form 4 as if it were a signature to a report on Form 3. Rule 2205 concerning amendments, and Rule 2207 concerning assertions of conflicts with non-U.S. laws, shall apply to any submission on Form 4 as if the submission were a report on Form

FORM 4 – SUCCEEDING TO REGISTRATION STATUS OF PREDECESSOR

GENERAL INSTRUCTIONS

1. Purpose of this Form. Effective [insert effective date of Rule 2109], this Form must be used to submit information, representations, and affirmations to the Board, pursuant to Rule 2109, by a public accounting firm that seeks to succeed to the registration status of a predecessor firm in circumstances described in Rule 2108.

2. Defined Terms. The definitions in the Board's rules apply to this Form. Italicized terms in the instructions to this Form are defined in the Board's rules. In addition, as used in the instructions to this Form, the term "the Firm" means the public accounting firm that is submitting this Form to the Board, and the term "the predecessor firm" means the registered public accounting firm identified in Item 1.1.a of the Form.

3. Submission of this Form. Unless otherwise directed by the Board, the Firm must submit this Form, and all exhibits to this Form, to the Board electronically by

completing the Web-based version of this Form available on the Board's Website. The Firm must use the predecessor firm's user ID and password to access the system and submit the Form. In the event of a transaction involving the combination of multiple registered public accounting firms, the Firm must access the system using only the user ID and password of the firm specifically identified in Item 1.1.a, and not those of any other registered public accounting firm.

4. When this Form Should be Submitted and When It is Considered Filed. To succeed to the registration status of the predecessor firm pursuant to the provisions of Rule 2108(a) or (b), the Firm must provide the information and representations required by this Form, in accordance with the instructions to this Form, and must file the Form no later than the 14th day after the effective date of the change in form of organization, change in jurisdiction of organization, or business combination. Different timing requirements apply with respect to events that occurred before [insert effective date of Rule 2109]. See Rule 2109(a)(2). Form 4 is considered filed when the Firm has submitted to the Board, through the Board's Web-based reporting system, a Form 4 that includes the signed certification required in Part V of Form 4, provided, however, that any Form 4 so submitted after the applicable filing deadline shall not be deemed filed unless and until the Board, pursuant to Rule 2108(d), grants leave to file the Form 4 out of time.

5. Seeking Leave To File this Form Out of Time. To request leave to file Form 4 out of time, pursuant to the provisions of Rule 2108(d), the Firm must file the request on Form 4 and must attach as Exhibit 99.5 a detailed statement describing

why, despite the passage of time since the event described on the Form 4, the Board should permit the Firm to succeed to the registration status of the predecessor firm. Any Form 4 that has been submitted out of time, and as to which a Board decision on whether to allow the form to be filed is pending, may be withdrawn by accessing the pending submission in the Board's Web-based system and selecting the "Withdraw" option.

6. Completing the Form. The Firm must complete Parts I, II, IV and V of this Form. Part III should be completed to the extent applicable, as described more fully in the instructions to Part II of the Form.

7. Amendments to this Form. Amendments shall not be submitted to update information into a Form 4 that was correct at the time the Form was submitted, but only to correct information that was incorrect at the time the Form was submitted or to provide information that was omitted from the Form and was required to be provided at the time the Form was submitted. When submitting a Form 4 to amend an earlier submitted Form 4, the Firm must supply not only the corrected or supplemental information, but must include in the amended Form 4 all information, affirmations, and certifications that were required to be included in the original Form 4. The Firm may access the originally filed Form 4 through the Board's Web-based system and make the appropriate amendments without needing to re-enter all other information. (Note that, pursuant to Rule 2109(d), the provisions of Rule 2205 concerning amendments apply to any submission on this Form as if the submission were a report on Form 3.)

Note: The Board will designate an amendment to a report on Form 4 as a report on "Form 4/A."

Note: Any change to a Form 4 that was originally submitted out of time, and as to which a Board decision on whether to allow the form to be filed is pending, shall not be treated as an amendment. To make a change to any such pending Form 4 submission, the Firm must access the pending submission in the Board's Web-based system, select the "Withdraw and Replace" option, and submit a new completed Form 4 in place of the previously pending submission. The certification required in Part V of the new submission must be executed specifically for the replacement version of the Form and dated accordingly.

8. Rules Governing this Form. In addition to these instructions, the rules contained in Part 2 of Section 2 of the Board's rules govern this Form. Please read these rules and the instructions carefully before completing this Form.

9. Requests for Confidential Treatment. The Firm may, by marking the Form in accordance with the instructions provided, request confidential treatment of any information submitted in Exhibit 99.3 or Exhibit 99.5 of this Form that has not otherwise been publicly disclosed and that either contains information reasonably identified by the Firm as proprietary information or that is protected from public disclosure by applicable laws related to confidentiality of proprietary, personal, or other information. See Rule 2300. If the Firm requests confidential treatment, it must identify the information in Exhibit 99.3 or Exhibit 99.5 that it desires to keep confidential, and include, as Exhibit 99.1 to this Form, an exhibit that complies

with the requirements of Rule 2300(c)(2). The Board will determine whether to grant confidential treatment requests on a case-by-case basis. If the Firm fails to include Exhibit 99.1, or includes an Exhibit 99.1 that fails to comply with Rule 2300(c)(2), the request for confidential treatment may be denied solely on the basis of that failure.

10. Assertions of Conflicts with Non-U.S. Law. If the Firm is a foreign registered public accounting firm, the Firm may, unless otherwise directed by the Board pursuant to Rule 2207(e), decline to provide the affirmation required by Item 4.1 of this Form and any answer required by Item 3.2.e of this Form if doing so would constitute a violation of non-U.S. law by the Firm and the Firm proceeds in accordance with Rule 2207. (Note that, pursuant to Rule 2109(d), the provisions of Rule 2207 apply to any submission on this Form as if the submission were a report on Form 3.) If the firm withholds the affirmation or answer, the Firm must indicate, in accordance with the instructions in the relevant Part of the Form, that it has done so.

11. Language. Information submitted as part of this Form, including any exhibit to this Form, must be in the English language.

PART I – IDENTITY OF THE FIRM AND CONTACT PERSONS

Item 1.1 Names of Firm and Predecessor Registered Public Accounting Firm

a. State the legal name of the registered public accounting firm to whose registration status the Firm seeks to succeed.

Note: The name provided in Item 1.1.a should be the legal name of the registered public accounting firm as last reported to the Board on Form 1 or Form

3. This is the firm referred to in this Form as "the predecessor firm." In accessing and submitting this Form through the Board's Web-based system, the Firm must use the predecessor firm's user ID and password.

b. State the legal name of the Firm filing this Form.

Note: The name provided in Item 1.1.b will be the name under which the Firm is registered with the Board if this Form is filed in accordance with Rule 2109.

c. If different than the name provided in Item 1.1.b, state the name or names under which the Firm issues or intends to issue audit reports.

Item 1.2 Contact Information of the Firm

a. State the physical address (and, if different, mailing address) of the Firm's headquarters office.

b. State the telephone number and facsimile number of the Firm 's headquarters office. If available, state the Website address of the Firm.

Item 1.3 Primary Contact and Signatory

State the name, business title, physical business address (and, if different, business mailing address), business telephone number, business facsimile number, and business e-mail address of a partner or authorized officer of the Firm who will serve as the Firm's primary contact with the Board, including for purposes of this Form 4, any annual reports filed on Form 2, and any special reports filed on Form 3.

PART II – GENERAL INFORMATION CONCERNING THE FILING OF THIS FORM

Item 2.1 Reason for Filing this Form

Indicate, by checking the box for either Item a or Item b below, the reason the Firm is filing this Form. Then proceed to the Parts and Items of this Form indicated parenthetically for the relevant item and provide the information described there. Provide responses only to those Parts and Items of the Form specifically indicated for the event or events that the Firm identifies in this Part II as the reason for filing this Form. (For example, if the Form is being submitted because the Firm has changed its form of organization, check the box for Item 2.1.a, and complete only Item 3.1 and Parts IV and V of the Form. Complete Item 2.2 or Item 2.3 if applicable.)

a. There has been a change in the Firm's form of organization, or the Firm has changed the jurisdiction under the law of which it is organized. (Complete Item 3.1, Part IV, and Part V; complete Item 2.2 or Item 2.3 if applicable.)

b. There has been an acquisition of a registered public accounting firm by an entity that was not a registered public accounting firm at the time of the acquisition, or a registered public accounting firm has combined with another entity or other entities to form a new legal entity. (Complete Item 3.2, Part IV, and Part V; complete Item 2.2 or Item 2.3 if applicable.)

Item 2.2 Request for Leave To File this Form Out of Time

If this Form is not submitted in accordance with Rule 2109(b) on or before the filing deadline set by Rule 2109(a), the Firm may request leave to file this Form 4 out of time by checking the box for this Item, completing this Form 4 as is otherwise required, and providing, as Exhibit 99.5 to this Form, a description of the reason(s) the Form was not timely filed and a statement of the grounds on which the Firm asserts that the Board should grant leave to file the Form out of time.

Note: Requests for leave to file Form 4 out of time are not automatically granted.

See Rule 2108(d).

Item 2.3 Amendments

If this is an amendment to a Form 4 previously filed with the Board –

a. Indicate, by checking the box corresponding to this item, that this is an amendment; and

b. Identify the specific Item numbers of this Form (other than this Item 2.3) as to which the Firm's response has changed from that provided in the most recent Form 4 or amended Form 4 filed by the Firm with respect to the event reported on this Form.

PART III – CHANGES IN THE FIRM

Item 3.1 Changes in Form of Organization or in Relevant Jurisdiction

If this Form 4 is being submitted in connection with a change in the Firm's form of organization or a change in the jurisdiction under the law of which the Firm is organized–

a. State the Firm's current (i.e., after the change in legal form or jurisdiction) legal form of organization;

b. Identify the jurisdiction under the law of which the Firm is organized currently (i.e., after the change in legal form or jurisdiction);

c. State the date that the change took effect;

d. Affirm that, after the change reported or described in this Item 3.1, the Firm is a public accounting firm under substantially the same ownership as the predecessor firm;

Note: Neither the Act nor Board rules include any provision by which a registered public accounting firm may, in effect, transfer its Board registration to another entity. Rule 2108(a), in conjunction with this Form, allows the succession of registration status in circumstances in which a registered public accounting firm changes its legal form of organization while remaining under substantially the same ownership. For purposes of this Item, the Firm is considered to be under substantially the same ownership as the predecessor firm if a majority of the persons who held an equity ownership interest in the predecessor also constitute a majority of the persons who hold an equity ownership interest in the Firm.

e. If, in connection with the change described in this Item 3.1, the Firm has obtained, or will practice under, a license or certification number, authorizing it to engage in the business of auditing or accounting, that is different from any such license or certification number previously reported to the Board by the predecessor firm, provide as to each such license –

1. the name of the issuing state, agency, board, or other authority;
2. the number of the license or certification; and
3. the date the license or certification took effect;

f. If, in connection with the change described in this Item 3.1, any license or certification that authorized the predecessor firm to engage in the business of auditing or accounting has ceased to be effective or has become subject to any conditions or contingencies other than conditions or contingencies imposed on all firms engaged in the business of auditing or accounting in the jurisdiction, provide, as to each such license –

1. the name of the issuing state, agency, board, or other authority;
2. the number of the license or certification; and

3. the date that the authorization ceased to be effective or became subject to conditions or contingencies.

Item 3.2 Acquisitions of, or Combinations Involving, A Registered Public Accounting Firm

a. If this Form 4 is being submitted in connection with a transaction concerning which a person who holds an equity ownership interest in the Firm, or is employed by the Firm, can certify the points set out in Item 3.2.b. and Exhibit 99.4, –

1. Provide the name of each entity, other than the predecessor firm, that was involved in the transaction and that was a registered public accounting firm immediately before the transaction, and as to each such entity –

    (i) affirm that the entity has filed with the Board a request for leave to withdraw from registration on Form 1-WD; and

    (ii) state the date that the entity filed Form 1-WD;

2. Provide the name of each entity, including any acquiror, that was involved in the transaction and that was not a registered public accounting firm immediately before the transaction;

3. Provide the date that the transaction took effect; and

4. Provide a brief description of the nature of the transaction.

b. Provide as Exhibit 99.4 to this Form, a statement in the form set out below, signed by a person who, immediately before the transaction, was an officer of, or held an equity ownership interest in, the predecessor firm and who now either holds an equity ownership interest in, or is employed by, the Firm. The statement must be submitted on behalf of the Firm. Exhibit 99.4 must include a signature that appears in typed form in the electronic submission and a corresponding manual signature retained by the Firm in accordance with Rule 2109(d). The signature must be accompanied by the signer's current title, the signer's title immediately before the event described in Item 3.2.a, the date of signature, and the signer's business mailing address, business telephone number, business facsimile number, and business e-mail address. Other than the insertion of the relevant names, Exhibit 99.4 must be in the exact following words –

On behalf of [name of the Firm], I certify that (1) I was an officer of, or held an equity ownership interest in, [name of predecessor firm] immediately before the transaction described in Item 3.2.a of the Form 4 to which this exhibit is attached; (2) immediately before that transaction [name of predecessor firm] was a registered public accounting firm; (3) as part of that transaction, a majority of the persons who held equity ownership interests in [name of predecessor firm] obtained equity ownership interests in, or became employed by, [name of the Firm]; (4) [name of predecessor firm] intended that [name of the Firm] succeed to the Board registration status of [name of predecessor firm] to the extent permitted by the Board's rules; and (5) [name of predecessor firm] is no longer a public accounting firm.

c. If, in connection with the transaction described in Item 3.2.a, the Firm has obtained, or will practice under, a license or certification number, authorizing it to engage in the business of auditing or accounting, that is different from any such license or certification number previously reported to the Board by the predecessor firm, provide, as to each such license –

1. the name of the issuing state, agency, board or other authority;
2. the number of the license or certification; and

3. the date the license or certification took effect.

d. If, in connection with the transaction described in Item 3.2.a, any license or certification that authorized the predecessor firm to engage in the business of auditing or accounting has ceased to be effective or has become subject to any conditions or contingencies other than conditions or contingencies imposed on all firms engaged in the business of auditing or accounting in the jurisdiction, provide, as to each such license –

1. the name of the issuing state, agency, board, or other authority;

2. the number of the license or certification; and

3. the date that the authorization ceased to be effective or became subject to conditions or contingencies.

e. Provide a "yes" or "no" answer to each of the following questions –

1. Is there identified in Item 3.2.a.2 any entity that, if it were filing an application for registration on Form 1 on the date of the certification in Part V of this Form, would have to provide an affirmative response to Item 5.1.a of Form 1 in order to file a complete and truthful Form 1?

   Note: In considering whether an affirmative response would be required to Item 5.1.a of Form 1, the Firm should take into account the guidance provided by question number 33 in Frequently Asked Questions Regarding Registration with the Board, PCAOB Release No. 2003-011A (Nov. 13, 2003).

2. Is there identified in Item 3.2.a.2 any entity that (i) issued an audit report with respect to an issuer on or after October 22, 2003 (or, if the entity is a non-U.S. entity, July 19, 2004), while not registered with the Board, and (ii) has never had an application for registration on Form 1 approved by the Board?

3. Is the Firm operating without holding any license or certification issued by a <u>state</u>, agency, board, or other authority authorizing the Firm to engage in the business of auditing or accounting?

Note: If the Firm answers "yes" to any question in Item 3.2.e or asserts as to any of those questions that non-U.S. law prohibits it from providing an answer, the Firm cannot succeed outright to the registration of the predecessor. If this Form 4 is submitted in accordance with Rule 2109, however, the Firm will temporarily succeed to the registration of the predecessor for a transitional period as described in Rule 2108(b)(2) as long as the Firm makes the representation required in Item 3.2.f below. If the Firm answers "yes" to any question in Item 3.2.e or asserts as to any of those questions that non U.S. law prohibits it from providing an answer but fails to make the representation required in Item 3.2.f, this Form 4 will not be accepted for filing and the Firm will not succeed to the predecessor's registration even on a temporary basis. <u>See</u> Rule 2108(b)(2).

f. If the Firm answered "yes" to any question in Item 3.2.e or asserts as to any of those questions that non-U.S. law prohibits it from providing an answer, affirm, by checking the box corresponding to the appropriate item, that one of the following statements is true –

1. The Firm has filed an application for registration on Form 1 on or after the date provided in Item 3.2.a.3.

2. The Firm intends to file an application for Registration on Form 1 no later than 45 days after the date provided in Item 3.2.a.3.

PART IV – CONTINUING OBLIGATIONS

Item 4.1 Continuing Consent to Cooperate

Affirm that –

a. The Firm consents to cooperate in and comply with any request for testimony or the production of documents made by the Board in furtherance of its authority and responsibilities under the Sarbanes-Oxley Act of 2002;

b. The Firm has secured from each of its associated persons, and agrees to enforce as a condition of each such person's continued employment by or other association with the Firm, a consent indicating that the associated person consents to cooperate in and comply with any request for testimony or the production of documents made by the Board in furtherance of its authority under the Sarbanes-Oxley Act of 2002, and that the associated person understands and agrees that such consent is a condition of his or her continued employment by or other association with the Firm; and

c. The Firm understands and agrees that cooperation and compliance, as described in Item 4.1.a., and the securing and enforcing of consents from its associated persons as described in Item 4.1.b., is a condition to the continuing effectiveness of the registration of the Firm with the Board.

> Note: The affirmation in Item 4.1.b. shall not be understood to include an affirmation that the Firm has secured such consents from any associated person that is a registered public accounting firm.

> Note: The affirmation in Item 4.1.b. shall not be understood to include an affirmation that the Firm has secured such consents from any associated person that is a foreign public accounting firm in circumstances where that associated

person asserts that non-U.S. law prohibits it from providing the consent, so long as the Firm possesses in its files documents relating to the associated person's assertion about non-U.S. law that would be sufficient to satisfy the requirements of subparagraphs (2) through (4) of Rule 2207(c) if that associated person were a registered public accounting firm filing a Form 2 and withholding this affirmation. This exception to the affirmation in Item 4.1.b. does not relieve the Firm of its obligation to enforce cooperation and compliance with Board demands by any such associated person as a condition of continued association with the Firm.

Note: If the Firm is a foreign registered public accounting firm, the affirmations in Item 4.1 that relate to associated persons shall be understood to encompass every accountant who is a proprietor, partner, principal, shareholder, officer, or manager of the Firm and who provided at least ten hours of audit services for any issuer during the reporting period.

Item 4.2 Continuing Responsibility to the Board for Previous Conduct

Affirm that, for purposes of the Board's authority with respect to registered public accounting firms, including but not limited to the authority to require reporting of information and the authority to impose disciplinary sanctions, the Firm either has retained or assumes responsibility for the conduct of any predecessor registered public accounting firm before the change or business combination reported on this Form took effect.

Note: As used in Item 4.2 the term "predecessor registered public accounting firm," means (1) in circumstances not involving a transaction described in Item

3.2, the predecessor firm and (2) in circumstances involving a transaction described in Item 3.2, each registered public accounting firm that was involved in the business combination.

Note: The continuing responsibility in Item 4.2 includes, among other things, responsibility for reporting information on Form 2 and events on Form 3. Thus, for example, if a registered public accounting firm experienced a Form 3 reportable event before the event that is the subject of this Form, the Firm, as successor, has the obligation to report that event on Form 3, and bears responsibility for any failure by any predecessor to have filed a timely Form 3 to report the matter.

Note: The Board's rules do not require that any entity retain or assume responsibility as set forth above. In the absence of an affirmation that it retains or assumes responsibility for such conduct at least for purposes of the Board's authority, however, an entity cannot succeed to the Board registration status of any predecessor entity. See Rule 2108.

PART V – CERTIFICATION OF THE FIRM Item 5.1 Signature of Partner or Authorized Officer

This Form must be signed on behalf of the Firm by an authorized partner or officer of the Firm including, in accordance with Rule 2109(d), both a signature that appears in typed form within the electronic submission and a corresponding manual signature retained by the Firm. The signer must certify that –

a. the signer is authorized to sign this Form on behalf of the Firm;

b. the signer has reviewed this Form;

c. based on the signer's knowledge, this Form does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading; and

d. either –

1. based on the signer's knowledge, the Firm has not failed to include in this Form any information or affirmation that is required by the instructions to this Form, with respect to the event or events being described on this Form, or

2. based on the signer's knowledge –

(A) the Firm is a foreign public accounting firm and has not failed to include in this Form any information or affirmation that is required by the instructions to this Form other than an affirmation required by Item 4.1 and/or an answer to Item 3.2.e.; and

(B) the Firm asserts that it is prohibited by non-U.S. law from providing any such withheld affirmation or response to the Board on this Form and, with respect to each such withheld affirmation or response, the Firm has made the efforts described in PCAOB Rule 2207(b) and has in its files the materials described in PCAOB Rule 2207(c).

The signature must be accompanied by the signer's title, the capacity in which the signer signed the Form, the date of signature, and the signer's business mailing address, business telephone number, business facsimile number, and business e-mail address.

PART VI – EXHIBITS

To the extent applicable under the foregoing instructions, each report must be accompanied by the following exhibits:

Exhibit 99.1 Request for Confidential Treatment

Exhibit 99.3 Materials Required by Rule 2207(c)(2)–(4) – Submit Only as an Exhibit to an Amended Form 4 in Response to a Request Made Pursuant to Rule 2207(d)

Exhibit 99.4 Acknowledgment Concerning Registration Status in Certain Transactions

Exhibit 99.5 Statement in Support of Request for Leave To File Form 4 Out of Time.

II. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed rule. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Board's Statement of the Purpose Of, and Statutory Basis for, the Proposed Rules

(a) Purpose

Under Section 102(a) of the Sarbanes-Oxley Act of 2002 and PCAOB Rule 2100, a public accounting firm must be registered with the PCAOB in order to prepare or issue audit reports for public companies or to play a substantial role in the preparation or furnishing of such audit reports. To become registered, a public accounting firm files an application for registration on PCAOB Form 1, which the Board may approve or disapprove. The proposed rules identify the circumstances in which a firm may succeed to the registration status of a predecessor registered firm, without filing a new Form 1, and provide a mechanism for the firm to do so.

The rules afford the opportunity for continuity of registration in two general categories of circumstances: (1) changes related to a firm's legal form of organization or the jurisdiction in which it is organized, and (2) transactions in which a registered firm is acquired by an unregistered entity or combines with other entities to form a new legal entity. The events to which the rules apply are events for which a firm plans, not unanticipated events to which a firm reacts. The rules are designed to facilitate a firm's ability to factor into its planning, and to predict with certainty, whether and how continuity of registration can be maintained.

The rules provide for a form the firm must file (Form 4), set a deadline for filing the form, and require certain information and representations in the form. If the firm files the form within the required timeframe, provides the required representations, and certifies that all required information is included, then continuity of registration is automatic, without the need for separate Board action. The rules and form also build in safeguards to ensure that the Form 1 process is not circumvented in circumstances where that process is more appropriate than Form 4 succession.

To obtain continuing effectiveness of an existing registration, the firm must acknowledge the continuity of, and commit to honor, certain obligations that accompany the registration status. Those obligations fall into two categories: continuing consent to cooperate with the Board and continuing responsibility to the Board for the conduct of predecessor registered firms.

With respect to circumstances in which a registered firm is acquired by an unregistered entity, or when a registered firm combines with other entities to form a new legal entity, the proposed Form 4 requires, among other things, information that determines whether succession to the predecessor's registration is permanent or temporary. Based on this information, succession may be outright and permanent or may only be temporary for a transition period intended to allow to the firm to seek registration through the Form 1 process.

For succession to registration to take effect automatically upon filing under the rules, Form 4 must be filed within 14 days after the effective date of the change in legal form or other event. The rules make some allowance for late filing. A firm that fails to file Form 4 within the 14-day period may submit a late Form 4 and request that the Board grant leave to file the form out of time. In a late submission, the firm should include as an exhibit to the form a statement in support of its request for leave to file out of time. If the Board grants the request and allows the form to be filed, the firm will succeed to the predecessor's registration.

The proposed rules would take effect 60 days after Securities and Exchange Commission approval.

(b) Statutory Basis

The statutory basis for the proposed rule is Title I of the Act.

B. <u>Board's Statement on Burden on Competition</u>

The Board does not believe that the proposed rules will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

The proposed rules provide a registration succession mechanism that firms may elect to use but are not required to use.

C. Board's Statement on Comments on the Proposed Rules Received from Members, Participants or Others

The Board released the proposed rules and form instructions for public comment in Release No. 2006-005 (May 23, 2006). A copy of Release No. 2006-005 and the comment letters received in response to the PCAOB's request for comment are available on the PCAOB's Web site at www.pcaobus.org. The Board received five written comment letters. The Board has clarified and modified certain aspects of the proposed rules and form instructions in response to the comments it received, as discussed below.

Commenters addressed the Form 4 item that requires a Form 4 filer to affirm that it retains or assumes responsibility for the conduct of predecessor registered firms for purposes of the Board's authority. Commenters expressed concern that the affirmation might erode otherwise valid legal defenses in contexts such as criminal or private civil proceedings, and suggested that the Board should make clear that no such result is intended. The Board reiterates what it said in proposing the requirement for comment: The affirmation of continuing responsibility for a predecessor's conduct is not intended to create any new liability, nor is it intended to affect the legal consequences of the transaction with respect to any person or entity other than the Board. As between the firm and the Board, however, the Board views the affirmation as indispensable if a firm wishes to make use of the Form 4 process. In an effort to reduce the possibility of misunderstanding about the intended scope, the Board has made slight changes to the wording of Item 4.2 – such as changing the heading to specify that the item is about continuing responsibility "to the Board," and removing the broad adjective "legal" in describing the nature of the responsibility being retained or assumed – but the Board is adopting the substance of the requirement essentially as proposed.

One commenter expressed the view that a successor firm should not be precluded from assuming a predecessor firm's registration status just because less than a majority of its predecessor's owners remained with the successor firm. In the Board's view, that suggestion is unworkable for a process intended to provide for automatic succession upon the satisfaction of bright line criteria. Without supplemental information and the intervention of judgment, the Board could not provide for succession in those circumstances without running a risk that more than one "successor" entity might lay claim to the same predecessor's registration.

One commenter suggested that the Board should define "acquisition" in this context, and raised questions concerning whether, to be an "acquisition" for which Form 4 succession is available, the transaction must involve acquisition of the predecessor firm's assets or a substantial portion thereof. For Form 4 succession to be available, the Board does not require that the transaction include anything other than what is described in the Exhibit 99.4 certification: a majority of the equity owners in a predecessor registered firm have become equity owners or employees of an unregistered firm, and the predecessor registered firm ceases to be a public accounting firm. For clarity on this point, the wording of Item 3.2.a. has been revised to refer to an acquisition of "any portion of" a registered public accounting firm, though Form 4 succession following any such acquisition is available only if all of the Exhibit 99.4 criteria are satisfied.

The Exhibit 99.4 certification also includes a statement that the predecessor registered firm intended for the successor firm to succeed to its registration status. One commenter questioned the appropriateness of allowing a single individual to certify that the predecessor intended such succession, and expressed concern about the Board acting on such a certification by someone who may only have had a marginal role in the predecessor registered firm. As proposed and adopted, however, the required certification would be included in a filing that cannot be made except by the successor firm, which cannot make the filing unless a majority of the predecessor's owners are part of that successor firm. In those circumstances, it is not necessary to more specifically limit which of the predecessor's former owners or officers must execute the required certification.

In the context of a combination of firms, Form 4 succession is available only if the predecessor registered firm ceases to exist as a public accounting firm. One commenter questioned this requirement and suggested that a firm should be able to spin off its issuer audit business, including its registration status, to another firm and still remain a public accounting firm. The Board is not precluding the possibility that a firm can spin off its issuer audit business and still remain a public accounting firm; rather, the Board is identifying this criterion – whether the predecessor continues to exist as a public accounting firm – as relevant to whether registration status can move to the new firm through the Form 4 process or whether that firm can obtain registration status only through the Form 1 process.

If the predecessor registered firm continues to exist as the same legal entity that registered with the Board and continues to be engaged in the practice of public accounting, then the transaction suggested by the commenter would involve an existing public accounting firm – an entity which can legally be registered – conveying its registration to another public accounting firm, a transaction that the Board views as fundamentally inappropriate. Accordingly, in that circumstance, the firm to which the predecessor's issuer audit practice moved could not use the Form 4 process but would need to apply for registration on Form 1 – which it could do even before the relevant transaction takes effect.

In contrast, if the legal entity that originally registered ceases to exist as a public accounting firm, then it cannot legally be a registered public accounting firm. For that entity's registration status to move with elements of that entity into another entity, through the Form 4 process, does not raise the same concerns about transferability of registration from one existing public accounting firm to another.

One commenter questioned the requirement to file a Form if a firm involved in the transaction would need to answer "yes" on the Form 1 disciplinary history question if filing a Form 1. The commenter suggested that this requirement could be punitive, especially for large registered firms that combine with smaller firms. Item 3.2.e. of Form 4, however, does not pose any significant risk of that sort. If a large registered firm acquires a smaller unregistered firm, the large registered firm would merely be required to report that in its annual report on Form 2, without resort to the Form 4 process. Alternatively, if a large registered firm were involved in a transaction that did lead to a Form 4 filing, the disciplinary histories of that firm and its associated persons would be irrelevant to Item 3.2.e. because the large firm was already registered at the time of the transaction. Item 3.2.e. relates only to disciplinary history information of entities (and their associated persons) that were not already registered at the time of the transaction.

Commenters suggested that the proposed 90-day limit on the temporary transition period (for firms that may not succeed permanently to the predecessor's registration) was too short and too inflexible. They noted that the Board has 45 days to act on an application, and also noted that the Board could ask for additional information, thereby restarting the 45-day clock and potentially pushing a registration decision out beyond the 90-day period. One commenter suggested revising the proposal so that the temporary registration status would continue until the Board makes a final decision on the Form 1. Another suggested revising the proposal to give the Board flexibility to extend the temporary registration status in situations where the Board does not take final action on the Form 1 within the 90 days.

The Board does not believe it would be appropriate to adopt a rule providing for a temporary registration period that continues until the Board acts on the Form 1, since firms could then keep the temporary registration status in place by not filing Form 1 or by delaying a response to a Board request for additional information on the application. The Board, however, sees the value in a measure of flexibility on this point. Accordingly, in Rule 2108(b)(2), the Board has retained the proposed 90 days as the initial transition period but has also added certain qualifications. If the Board formally requests additional information from the firm with less than 60 days remaining in the initial 90-day period, the temporary registration will continue to the date that is 60 days after the date of the Board's request. The effect will be that a firm has 15 days to respond to the Board's request if the firm wants to stay on track to keep its temporary registration until Board action on the Form 1. If the Board makes follow-up requests for information, the Board has the discretion to extend the temporary registration to a later date. Depending on the circumstances, however, the Board might, in making a follow-up request, conclude that further extension of the temporary registration is unwarranted, and could communicate that to the firm in the second request.

One commenter suggested that the Board should adopt procedures by which a firm that anticipates that a successor will need to file a new Form 1 could review the relevant facts with the Board's staff before the transaction to determine whether the staff sees significant obstacles to approving the successor's application. In the Board's view, however, to the extent it is appropriate for the staff to review information relevant to a prospective Form 1 filing, the staff may already do so without the need for special procedures.

One commenter addressed the requirement that, in the context of more than two firms combining, any registered firm other than the firm whose registration is intended to continue, must, before Form 4 is filed, file a request to withdraw from registration. The commenter expressed concern that there may be a registration gap for the predecessor firm that files the Form 1-WD prior to the transaction if the withdrawal is granted prior to the close of the transaction. The representation concerning the filing of a 1-WD, however, does not apply to the "predecessor firm," but only to other registered firms, if any, that are merging into the filing entity as part of the transaction. In connection with any Form 4 filing, the firm designated as the "predecessor firm" should not seek leave to withdraw from registration. In addition, in transactions involving additional registered firms, the Form 1-WD filings need not occur far in advance of the Form 4 filing. The Form 4 requirements can be satisfied even if the relevant Form 1-WD filings occur immediately before the Form 4 filing.

One commenter noted that changes in licenses and certifications may occur after the filing of a Form 4 and suggested that the Board should expressly state that such changes may be described in an amendment to Form 4. Because a firm succeeds to registration automatically upon the Form 4 being filed, however, the firm immediately becomes subject to the same annual and special reporting requirements as any other registered firm. Accordingly, a license change that occurs after the filing of the Form 4 should be reported on Form 3 in accordance with Rule 2203.

For succession to registration to take effect automatically upon filing under the rules, Form 4 must be filed within 14 days after the effective date of the change in legal form or other event. Commenters expressed a view that 14 days is too short a period, and suggested that it was insufficient time for non-U.S. firms to evaluate the impact of non-U.S. law in a particular case or to obtain consents, waivers, and legal opinions relating to potential legal conflicts. More generally, one commenter noted that 14 days does not allow sufficient time after the event for a firm to assess its reporting obligations and complete the form. Two commenters suggested expanding the 14-day period to a 45-day period.

The Board has considered these comments but has decided to adopt the 14-day deadline. Given the purpose of the filing – avoiding breaks in registration status – the Board believes that the rule should require filing of the form in as short a period as reasonably possible, so that any questions about the entity's registration status are kept to as narrow a period as possible. In addition, the events giving rise to a Form 4 are events for which firms plan, and such planning can encompass prompt filing of the relatively short and simple Form 4.

Even so, the rules make some allowance for late filing. A firm that fails to file Form 4 within the 14-day period may submit a late Form 4 and request that the Board grant leave to file the form out of time. In a late submission, the firm should include as an exhibit to the form a statement in support of its request for leave to file out of time. If the Board grants the request and allows the form to be filed, the firm will succeed to the predecessor's registration (either outright or for the transitional period described above).

One commenter sought clarification of a firm's registration status during a period in which a Form 4 is pending with a request for leave to file out of time, suggesting that it is unclear whether the firm can issue audit reports while the request is pending. As discussed in the proposing release, a firm submitting a late Form 4 should make no assumption about whether the Board will allow it to be filed. Accordingly, during the period that the request is pending with the Board, a firm should not assume that it is a registered public accounting firm and, therefore, should not assume that it may issue audit reports. The rule's provision for late submissions is not principally intended as an accommodation to firms, but is intended to afford the Board the opportunity to allow Form 4 succession, despite a late filing, when doing so would be consistent with the public interest. Eventual favorable Board action on the request would effectively confer registered status on the firm back to the date of the transaction that is the subject of the Form 4 filing (just as with a timely filed Form 4), but unfavorable Board action would mean that the entity filing the Form 4 was never registered.

One commenter suggested that non-U.S. firms might also sometimes face legal obstacles to answering the Item 3.2.e. yes-no questions that determine whether succession is permanent or temporary. The Board has determined to allow non-U.S. firms to withhold those answers on legal conflict grounds. The consequence of doing so, however, will be the same as if the firm had supplied a "no" answer: the succession afforded by the Form 4 process will only be for a transitional period to allow the firm an opportunity to seek registration through the Form 1 process.

Form 4 limits the categories of information for which a firm can request confidential treatment. Confidential treatment requests that have no genuine basis in law needlessly distract Board resources and delay the availability of information to the public. In the case of Form 4, the basic, nonpersonal, and nonproprietary nature of the required information leads the Board to foreclose confidential treatment requests for almost all of the items in the form.

The Board encouraged commenters to comment on whether the proposal overlooked actual or realistically foreseeable legal requirements to maintain the confidentiality of information. Commenters who addressed the point did so only in vague terms without providing any specific basis for concluding that the proposal overlooked any potentially applicable protection. One commenter stated generally that certain information required by Form 4 may need to be kept confidential under non-U.S. law or by the terms of an agreement between predecessor and successor entities. The commenter did not identify what information in Form 4 might fall into that category and did not provide an example of the type of non-U.S. law that might protect its confidentiality. Moreover, in the absence of relevant law, an agreement between private parties to keep information confidential does not in itself satisfy the confidential treatment criteria described in Rule 2300(b)(1). The commenter also expressed slightly more focused concern about the protection of "information regarding the acquisition," but did not specify what information, among the very basic acquisition-related information required by Form 4, could be considered confidential or proprietary.

Another commenter raised potential confidentiality concerns about Item 3.2.e.1. As adopted, that Item asks whether the acquisition or combination involves any previously unregistered entity that, if it were filing an application for registration on Form 1, would have to provide an affirmative response to Item 5.1.a, which asks about the existence of certain specified disciplinary histories. The commenter suggested that indicating whether a firm would have to answer "yes" to that question might lead others to draw unfavorable conclusions that could expose the firm to an increased risk of liability claims. Whether that is true, though, is a separate question from whether that "yes" answer is information that is protected from disclosure by applicable law. The commenter did not suggest how that would be the case. Moreover, as a practical matter, any reader of the Form 4 would recognize that a firm's request for confidential treatment of its answer to Item 3.2.e.1. would mean that its answer was "yes."

In weighing these comments, the Board views as relevant the fact that Form 4 is not a required filing. While the Board does not view its optional nature as justification for dispensing with the possibility of confidential treatment, the Board does not believe that the comments on this point warrant any change from what was proposed.

III. Date of Effectiveness of the Proposed Rules and Timing for Commission Action

Within 60 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Board consents, the Commission will:

(a) by order approve such proposed rules; or

(b) institute proceedings to determine whether the proposed rules should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rules are consistent with the requirements of Title I of the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/pcaob.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number PCAOB 2008-05 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number PCAOB 2008-05. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web sit (http://www.sec.gov/rules/pcaob/shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule that are filed with the Commission, and all written communications relating to the proposed rule between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filing will also be available for inspection and copying at the principal office of the PCAOB. 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. All submissions should refer to File No. PCAOB-2008-05 and should be submitted on or before [insert 30 days from publication in the Federal Register].

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 12, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13517

In the Matter of **I Join Systems, Inc.,** **I-Tel Networks, Inc.,** **I-Transaction Net, Inc.,** **iGenisys, Inc.,** **IITC Holdings, Ltd.,** **Iksorb Enterprises, Inc., and** **The Imagemakers Photography, Inc.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents I Join Systems, Inc., I-Tel Networks, Inc., I-Transaction Net, Inc., iGenisys, Inc., IITC Holdings, Ltd., Iksorb Enterprises, Inc., and The Imagemakers Photography, Inc.

II.

After an investigation, the Division of Enforcement alleges that

A. RESPONDENTS

1. I Join Systems, Inc. (CIK No. 1073780) is a void Delaware corporation located in Boise, Idaho with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). I Join Systems is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-KSB for the period ended December 31, 2001, which reported a net loss of $5.9 million for that year.

2. I-Tel Networks, Inc. (CIK No. 1124862) is a revoked Nevada corporation located in Phoenix, Arizona with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). I-Tel Networks is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a

Form 10-QSB for the period ended September 30, 2001, which reported a net loss of over $1.4 million for the prior nine months.

3. I-Transaction Net, Inc. (CIK No. 1106005) is a New Jersey corporation located in Mississagua, Ontario, Canada with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). I-Transaction is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 2001, which reported a net loss of $285,381 for the prior nine months.

4. iGenisys, Inc. (CIK No. 1098065) is a delinquent Colorado corporation located in Denver, Colorado with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). iGenisys is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 2001, which reported a net loss of over $1.24 million for the year ended March 31, 2001.

5. IITC Holdings, Ltd. (CIK No. 857871) is an Alberta, Canada corporation located in Calgary, Alberta, Canada with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). IITC is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F for the fiscal year ended September 30, 1996.

6. Iksorb Enterprises, Inc. (CIK No. 1133811) is a permanently revoked Nevada corporation located in Salt Lake City, Utah with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). Iksorb is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-SB registration statement on August 7, 2001, which reported a net loss of over $14,116 from inception on January 28, 1976 to December 31, 2000.

7. The Imagemakers Photography, Inc. (CIK No. 1129216) is a permanently revoked Nevada corporation located in Henderson, Nevada with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). Imagemakers is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 2001, which reported a net loss of $33,763 for the six months ended June 30, 2001.

B. DELINQUENT PERIODIC FILINGS

8. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

9. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires domestic issuers to file quarterly reports. Rule 13a-16 requires foreign private issuers to furnish quarterly and other reports to the Commission under cover of Form 6-K if they make or are required to make the information public under the laws of the jurisdiction of their domicile or in which they are incorporated or organized; if they file or are required to file information with a stock exchange on which their securities are traded and the information was made public by the exchange; or if they distribute or are required to distribute information to their security holders.

10. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 or 13a-16 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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 it 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

Attachment

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

Appendix 1

Chart of Delinquent Filings
In the Matter of I Join Systems, Inc. et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
I Join Systems, Inc.					
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	04/01/09	Not filed	2
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	29				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
I-Tel Networks, Inc.					
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	04/01/09	Not filed	2
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	30				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
I-Transaction Net, Inc.					
	10-KSB	06/30/01	09/28/01	Not filed	93
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-QSB	12/31/01	2/14/02	Not filed	88
	10-QSB	03/31/02	5/15/02	Not filed	85
	10-KSB	06/30/02	9/30/02	Not filed	81
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-QSB	12/31/02	2/14/03	Not filed	76
	10-QSB	03/31/03	5/15/03	Not filed	73
	10-KSB	06/30/03	9/29/03	Not filed	69
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-QSB	12/31/03	2/17/04	Not filed	64
	10-QSB	03/31/04	5/17/04	Not filed	61
	10-KSB	06/30/04	9/28/04	Not filed	57
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-QSB	12/31/04	2/14/05	Not filed	52
	10-QSB	03/31/05	5/16/05	Not filed	49
	10-KSB	06/30/05	9/28/05	Not filed	45
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-QSB	12/31/05	2/14/06	Not filed	40
	10-QSB	03/31/06	5/15/06	Not filed	37
	10-KSB	06/30/06	9/28/06	Not filed	33
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-QSB	12/31/06	2/14/07	Not filed	28
	10-QSB	03/31/07	5/15/07	Not filed	25
	10-KSB	06/30/07	9/28/07	Not filed	21
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	2/14/08	Not filed	16
	10-QSB	03/31/08	5/15/08	Not filed	13
	10-KSB	06/30/08	9/29/08	Not filed	9
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-Q**	12/31/08	2/17/09	Not filed	4
	*10-Q**	03/31/09	5/15/09	Not filed	1
Total Filings Delinquent	32				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
iGenisys, Inc.					
	10-KSB	03/31/02	07/01/02	Not filed	83
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-QSB	12/31/02	02/14/03	Not filed	76
	10-KSB	03/31/03	06/30/03	Not filed	72
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-QSB	12/31/03	02/17/04	Not filed	64
	10-KSB	03/31/04	06/29/04	Not filed	60
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-QSB	12/31/04	02/14/05	Not filed	52
	10-KSB	03/31/05	06/29/05	Not filed	48
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-QSB	12/31/05	02/14/06	Not filed	40
	10-KSB	03/31/06	06/29/06	Not filed	36
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-QSB	12/31/06	02/14/07	Not filed	28
	10-KSB	03/31/07	06/29/07	Not filed	24
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	02/14/08	Not filed	16
	10-KSB	03/31/08	06/30/08	Not filed	12
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-Q**	12/31/08	02/17/09	Not filed	4

Total Filings Delinquent 28

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
IITC Holdings, Ltd.					
	20-F	09/30/97	03/31/98	Not filed	135
	20-F	09/30/98	03/31/99	Not filed	123
	20-F	09/30/99	03/31/00	Not filed	111
	20-F	09/30/00	04/02/01	Not filed	98
	20-F	09/30/01	04/01/02	Not filed	86
	20-F	09/30/02	03/31/03	Not filed	75
	20-F	09/30/03	03/31/04	Not filed	63
	20-F	09/30/04	03/31/05	Not filed	51
	20-F	09/30/05	03/31/06	Not filed	39
	20-F	09/30/06	04/02/07	Not filed	26
	20-F	09/30/07	03/31/08	Not filed	15
	20-F	09/30/08	03/31/09	Not filed	3
Total Filings Delinquent	12				
Iksorb Enterprises, Inc.					
	10-QSB	03/31/01	11/20/01	Not filed	91
	10-QSB	06/30/01	11/20/01	Not filed	91
	10-QSB	09/30/01	11/20/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Iksorb Enterprises, Inc.					
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	04/01/09	Not filed	2
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	19				
The Imagemakers Photography, Inc.					
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
The Imagemakers Photography, Inc.					
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	04/01/09	Not filed	2
	*10-Q**	03/31/09	05/15/09	Not filed	1

Total Filings Delinquent 15

*Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, are in the process of being removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal is taking effect over a transition period that will conclude on March 15, 2009, so by that date, all reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB will be required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) will have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 15, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13518

In the Matter of **Falcon Entertainment Corp.,** **Fanatics Only, Inc.,** **Fidelity Leasing Income Fund,** **Finger Lakes Financial Corp.,** **First Cincinnati, Inc., and** **First Mutual, Inc.** **(n/k/a First Community, Inc.),** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Falcon Entertainment Corp., Fanatics Only, Inc., Fidelity Leasing Income Fund, Finger Lakes Financial Corp., First Cincinnati, Inc., and First Mutual, Inc. (n/k/a First Community, Inc.).

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Falcon Entertainment Corp. (CIK No. 1089046) is a void Delaware corporation located in New York, New York with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Falcon is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended November 30, 2002, which reported a net loss of over $2.9 million for the prior six months. As of June 11, 2009, the company's stock (symbol "INDE") was traded on the over-the-counter markets.

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2. Fanatics Only, Inc. (CIK No. 720815) is a dissolved Colorado corporation located in Lakewood, Colorado with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Fanatics is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-KSB for the period ended December 31, 1996, which reported a net loss of over $7.7 million for the prior twelve months. As of June 11, 2009, the company's stock (symbol "FONL") was traded on the over-the-counter markets.

3. Fidelity Leasing Income Fund (CIK No. 740867) is a Pennsylvania corporation located in Radnor, Pennsylvania with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Fidelity is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K for the period ended December 31, 1993.

4. Finger Lakes Financial Corp. (CIK No. 1062423) is a federally chartered bank company located in Geneva, New York with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Finger Lakes is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 30, 2000.

5. First Cincinnati, Inc. (CIK No. 1034898) is a cancelled Ohio corporation located in Cincinnati, Ohio with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). First Cincinnati is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 30, 2000, which reported a net loss of over $25 million for the prior nine months. As of June 11, 2009, the company's common stock (symbol "FCNN") was traded on the over-the-counter markets.

6. First Mutual, Inc. (n/k/a First Community, Inc.) (CIK No. 692880) is a Delaware corporation located in Needham, Massachusetts with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). First Mutual is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for fiscal year March 31, 1999, which reported an accumulated deficit of $4.45 million.

B. DELINQUENT PERIODIC FILINGS

7. As discussed in more detail above, all of the respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

8. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration

is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

9. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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 it 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Attachment

Appendix 1

Chart of Delinquent Filings
In the Matter of Falcon Entertainment Corp., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Falcon Entertainment Corp.					
	10-QSB	02/28/01	04/16/01	Not filed	98
	10-KSB	05/31/01	08/29/01	Not filed	94
	10-QSB	08/31/01	10/15/01	Not filed	92
	10-QSB	11/30/01	01/14/02	Not filed	89
	10-QSB	02/28/02	04/15/02	Not filed	86
	10-KSB	05/31/02	08/29/02	Not filed	82
	10-QSB	08/31/02	10/15/02	Not filed	80
	10-QSB	11/30/02	01/14/03	Not filed	77
	10-QSB	02/28/03	04/14/03	Not filed	74
	10-KSB	05/31/03	08/29/03	Not filed	70
	10-QSB	08/31/03	10/15/03	Not filed	68
	10-QSB	11/30/03	01/14/04	Not filed	65
	10-QSB	02/29/04	04/14/04	Not filed	62
	10-KSB	05/31/04	08/30/04	Not filed	58
	10-QSB	08/31/04	10/15/04	Not filed	56
	10-QSB	11/30/04	01/14/05	Not filed	53
	10-QSB	02/28/05	04/14/05	Not filed	50
	10-KSB	05/31/05	08/29/05	Not filed	46
	10-QSB	08/31/05	10/17/05	Not filed	44
	10-QSB	11/30/05	01/17/06	Not filed	41
	10-QSB	02/28/06	04/14/06	Not filed	38
	10-KSB	05/31/06	08/29/06	Not filed	34
	10-QSB	08/31/06	10/16/06	Not filed	32
	10-QSB	11/30/06	01/16/07	Not filed	29
	10-QSB	02/28/07	04/16/07	Not filed	26
	10-KSB	05/31/07	08/29/07	Not filed	22
	10-QSB	08/31/07	10/15/07	Not filed	20
	10-QSB	11/30/07	01/14/08	Not filed	17

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Falcon Entertainment Corp.	*10-QSB*	02/29/08	04/15/08	Not filed	14
(continued)	*10-KSB*	05/31/08	08/29/08	Not filed	10
	*10-Q**	08/31/08	10/15/08	Not filed	8
	*10-Q**	11/30/08	01/14/09	Not filed	5
	*10-Q**	02/28/09	04/14/09	Not filed	2
Total Filings Delinquent	33				
Fanatics Only, Inc.					
	10-QSB	03/31/97	05/15/97	Not filed	145
	10-QSB	06/30/97	08/14/97	Not filed	142
	10-QSB	09/30/97	11/14/97	Not filed	139
	10-KSB	12/31/97	03/31/98	Not filed	135
	10-QSB	03/31/98	05/15/98	Not filed	133
	10-QSB	06/30/98	08/14/98	Not filed	130
	10-QSB	09/30/98	11/16/98	Not filed	127
	10-KSB	12/31/98	03/31/99	Not filed	123
	10-QSB	03/31/99	05/17/99	Not filed	121
	10-QSB	06/30/99	08/16/99	Not filed	118
	10-QSB	09/30/99	11/15/99	Not filed	115
	10-KSB	12/31/99	03/30/00	Not filed	111
	10-QSB	03/31/00	05/15/00	Not filed	109
	10-QSB	06/30/00	08/14/00	Not filed	106
	10-QSB	09/30/00	11/14/00	Not filed	103
	10-KSB	12/31/00	04/02/01	Not filed	98
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Fanatics Only, Inc.	*10-KSB*	12/31/04	03/31/05	Not filed	51
(continued)	*10-QSB*	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	49				
Fidelity Leasing Income Fund					
	10-Q	03/31/94	05/16/94	Not filed	181
	10-Q	06/30/94	08/15/94	Not filed	178
	10-Q	09/30/94	11/14/94	Not filed	175
	10-K	12/31/94	03/31/95	Not filed	171
	10-Q	03/31/95	05/15/95	Not filed	169
	10-Q	06/30/95	08/14/95	Not filed	166
	10-Q	09/30/95	11/14/95	Not filed	163
	10-K	12/31/95	04/01/96	Not filed	158
	10-Q	03/31/96	05/15/96	Not filed	157
	10-Q	06/30/96	08/14/96	Not filed	154
	10-Q	09/30/96	11/14/96	Not filed	151
	10-K	12/31/96	03/31/97	Not filed	147
	10-Q	03/31/97	05/15/97	Not filed	145
	10-Q	06/30/97	08/14/97	Not filed	142
	10-Q	09/30/97	11/14/97	Not filed	139
	10-K	12/31/97	03/31/98	Not filed	135
	10-Q	03/31/98	05/15/98	Not filed	133
	10-Q	06/30/98	08/14/98	Not filed	130

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Fidelity Leasing Income Fund	*10-Q*	09/30/98	11/16/98	Not filed	127
(continued)	*10-K*	12/31/98	03/31/99	Not filed	123
	10-Q	03/31/99	05/17/99	Not filed	121
	10-Q	06/30/99	08/16/99	Not filed	118
	10-Q	09/30/99	11/15/99	Not filed	115
	10-K	12/31/99	03/30/00	Not filed	111
	10-Q	03/31/00	05/15/00	Not filed	109
	10-Q	06/30/00	08/14/00	Not filed	106
	10-Q	09/30/00	11/14/00	Not filed	103
	10-K	12/31/00	04/02/01	Not filed	98
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/31/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-K	12/31/02	03/31/03	Not filed	75
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-K	12/31/03	03/30/04	Not filed	63
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-K	12/31/04	03/31/05	Not filed	51
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-K	12/31/05	03/31/06	Not filed	39
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-K	12/31/07	03/31/08	Not filed	15
	10-Q	03/31/08	05/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Fidelity Leasing Income Fund	*10-Q*	06/30/08	08/14/08	Not filed	10
(continued)	*10-Q*	09/30/08	11/14/08	Not filed	7
	10-K	12/31/08	03/31/09	Not filed	3
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	61				
Finger Lakes Financial Corp.					
	10-K	12/31/00	04/02/01	Not filed	98
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/31/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-K	12/31/02	03/31/03	Not filed	75
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-K	12/31/03	03/30/04	Not filed	63
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-K	12/31/04	03/31/05	Not filed	51
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-K	12/31/05	03/31/06	Not filed	39
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Finger Lakes Financial Corp.	*10-K*	12/31/07	03/31/08	Not filed	15
(continued)	*10-Q*	03/31/08	05/15/08	Not filed	13
	10-Q	06/30/08	08/14/08	Not filed	10
	10-Q	09/30/08	11/14/08	Not filed	7
	10-K	12/31/08	03/31/09	Not filed	3
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	34				
First Cincinnati, Inc.					
	10-K	12/31/00	04/02/01	Not filed	98
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/31/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-K	12/31/02	03/31/03	Not filed	75
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-K	12/31/03	03/30/04	Not filed	63
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-K	12/31/04	03/31/05	Not filed	51
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-K	12/31/05	03/31/06	Not filed	39
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-K	12/31/07	03/31/08	Not filed	15
	10-Q	03/31/08	05/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
First Cincinnati, Inc.	*10-Q*	06/30/08	08/14/08	Not filed	10
(continued)	*10-Q*	09/30/08	11/14/08	Not filed	7
	10-K	12/31/08	03/31/09	Not filed	3
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	34				
First Mutual, Inc.					
	10-Q	06/30/99	08/16/99	Not filed	118
	10-K	09/30/99	12/29/99	Not filed	114
	10-Q	12/31/99	02/14/00	Not filed	112
	10-Q	03/31/00	05/15/00	Not filed	109
	10-Q	06/30/00	08/14/00	Not filed	106
	10-K	09/30/00	12/29/00	Not filed	102
	10-Q	12/31/00	02/14/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-K	09/30/01	12/31/01	Not filed	90
	10-Q	12/31/01	02/14/02	Not filed	88
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-K	09/30/02	12/30/02	Not filed	78
	10-Q	12/31/02	02/14/03	Not filed	76
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-K	09/30/03	12/29/03	Not filed	66
	10-Q	12/31/03	02/17/04	Not filed	64
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-K	09/30/04	12/29/04	Not filed	54
	10-Q	12/31/04	02/14/05	Not filed	52
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-K	09/30/05	12/29/05	Not filed	42
	10-Q	12/31/05	02/14/06	Not filed	40
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-K	09/30/06	12/29/06	Not filed	30
	10-Q	12/31/06	02/14/07	Not filed	28
	10-Q	03/31/07	05/15/07	Not filed	25

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
First Mutual, Inc.	*10-Q*	06/30/07	08/14/07	Not filed	22
(continued)	*10-K*	09/30/07	12/29/07	Not filed	18
	10-Q	12/31/07	02/14/08	Not filed	16
	10-Q	03/31/08	05/15/08	Not filed	13
	10-Q	06/30/08	08/14/08	Not filed	10
	10-K	09/30/08	12/29/08	Not filed	6
	10-Q	12/31/08	02/17/09	Not filed	4
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	39				

*Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, are in the process of being removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal is taking effect over a transition period that will conclude on March 15, 2009, so by that date, all reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB will be required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) will have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

June 15, 2009

IN THE MATTER OF HUNT GOLD CORPORATION f/k/a PRIME TIME GROUP, INC. File No. 500-1	ORDER OF SUSPENSION OF TRADING

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Hunt Gold Corporation, f/k/a Prime Time Group, Inc. ("Hunt Gold") because questions have been raised about the accuracy and adequacy of publicly disseminated information concerning, among other things, Hunt Gold's gold mining exploration business.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of Hunt Gold.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in Hunt Gold securities is suspended for the period from 9:30 a.m. EDT on June 15, 2009, through 11:59 p.m. EDT on June 26, 2009.

By the Commission.

Elizabeth M. Murphy
Secretary

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

Chairman Schapiro and Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60114 / June 15, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-11839

In the Matter of **CIBC MELLON TRUST COMPANY,** **Respondent.**	**ORDER AMENDING ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTIONS 15(b) AND 17A(c) OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS**

I.

On March 2, 2005, the Securities and Exchange Commission ("Commission") instituted public administrative proceedings pursuant to Sections 15(b) and 17A(c) of the Securities Exchange Act of 1934 ("Exchange Act") against CIBC Mellon Trust Company ("CIBC Mellon Trust" or the "Respondent").

II.

In anticipation of those proceedings, Respondent consented to the entry of an Order Instituting Administrative Proceedings Pursuant to Sections 15(b) and 17A(c) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions ("the 2005 Order").[1] The 2005 Order censured CIBC Mellon and directed it to comply with various undertakings.

Among the undertakings required by the 2005 Order, CIBC Mellon undertook, prior to issuing or transferring any restricted securities for an issuer with securities registered pursuant to Section 12 of the Exchange Act, to obtain an attorney opinion letter authorizing such issuance or transfer. 2005 Order at Section IV. B., paragraph 7.

III.

Respondent has submitted an Amended Offer of Settlement (the "Offer") proposing to modify its obligation to obtain an attorney opinion letter prior to issuing or transferring restricted securities as described in the 2005 Order at Section IV. B., paragraph 7, which the Commission has determined to accept. Solely for purposes of these proceedings and any other proceedings brought

[1] *See* Securities Exch. Act Rel. No. 51297, Mar. 2, 2005, Admin. Proc. File No. 3-11839.

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, CIBC Mellon consents to the entry of this Order Amending Order Instituting Administrative Proceedings Pursuant to Sections 15(b) and 17A(c) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions, as set forth below.

IV.

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 that:

A. Section IV. B., paragraph 7 of the 2005 Order is amended as follows to order:

(7) beginning 30 days from the date of the entry of this Order for a period of five years (ending on March 2, 2010), CIBC Mellon Trust shall, before it issues or transfers any restricted securities for an issuer with securities registered pursuant to Section 12 of the Exchange Act, whether or not CIBC Mellon Trust is the registered transfer agent for such issuer: (i) obtain an attorney opinion letter authorizing such issuance or transfer to any person known by CIBC Mellon Trust to be in the United States; (ii) obtain an attorney opinion letter authorizing the removal of any restrictive legends in connection with the transfer of all securities registered pursuant to Section 12 of the Exchange Act for a period of one year after the date the certificate bearing the restrictive legend was issued; (iii) place appropriate legends on all certificates of restricted stock sent by it to any person in the United States identifying such stock as restricted; (iv) enter and maintain appropriate stop orders relating to such restricted securities; and

B. With the exception of Section IV. A. set forth above, all other findings, remedial sanctions and undertakings in the 2005 Order remain in full effect.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 16, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13519

In the Matter of **Warehouse Club, Inc.,** **Wavemat, Inc.,** **Wilson Lee Engineering Co., Inc.** **(n/k/a Lee Wilson Engineering Co., Inc.),** **Winthrop Resources Corp., and** **WorldCall Corp.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Warehouse Club, Inc., Wavemat, Inc., Wilson Lee Engineering Co., Inc. (n/k/a Lee Wilson Engineering Co., Inc.), Winthrop Resources Corp., and WorldCall Corp.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Warehouse Club, Inc. (CIK No. 716180) is a forfeited Delaware corporation located in Skokie, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Warehouse Club is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended July 2, 1994, which reported a net loss of $161,678 for the prior thirteen weeks. On February 3, 1995, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Northern District of Illinois, a reorganization plan was confirmed on July 1, 1996, and the case was terminated on June 5, 2001.

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2. Wavemat, Inc. (CIK No. 803957) is a Delaware corporation located in Plymouth, Michigan with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Wavemat is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 1998, which reported a net loss of $312,626 for the prior nine months.

3. Wilson Lee Engineering Co., Inc. (n/k/a Lee Wilson Engineering Co., Inc.) (CIK No. 58429) is a "dead" Ohio corporation located in Rocky River, Ohio with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Wilson Lee is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 1994, which reported a net loss of over $41,300 for the prior nine months.

4. Winthrop Resources Corp. (CIK No. 886948) is a Minnesota corporation located in Minnetonka, Minnesota with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Winthrop Resources is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended March 31, 1997.

5. WorldCall Corp. (CIK No. 712803) is a Delaware corporation located in East Lansing, Michigan with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). WorldCall is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended November 30, 1998, which reported a net loss of $338,946 for the prior three months.

B. DELINQUENT PERIODIC FILINGS

6. As discussed in more detail above, all of the respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

7. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

8. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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 it 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Attachment

Appendix 1

Chart of Delinquent Filings
In the Matter of Warehouse Club, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Warehouse Club, Inc.					
	10-K	10/01/94	12/30/94	Not filed	167
	10-Q	12/31/94	02/14/95	Not filed	166
	10-Q	04/01/95	05/16/95	Not filed	163
	10-Q	07/01/95	08/15/95	Not filed	160
	10-K	09/30/95	12/29/95	Not filed	157
	10-Q	12/30/95	02/13/96	Not filed	153
	10-Q	03/30/96	05/14/96	Not filed	150
	10-Q	06/29/96	08/13/96	Not filed	147
	10-K	09/28/96	12/27/96	Not filed	144
	10-Q	12/28/96	02/11/97	Not filed	141
	10-Q	03/29/97	05/13/97	Not filed	139
	10-Q	06/28/97	08/12/97	Not filed	136
	10-K	09/27/97	12/26/97	Not filed	133
	10-Q	12/27/97	02/10/98	Not filed	130
	10-Q	03/28/98	05/12/98	Not filed	127
	10-Q	06/27/98	08/11/98	Not filed	124
	10-K	10/03/98	01/04/99	Not filed	121
	10-Q	01/02/99	02/16/99	Not filed	118
	10-Q	04/03/99	05/18/99	Not filed	115
	10-Q	07/03/99	08/17/99	Not filed	112
	10-K	10/02/99	01/03/00	Not filed	109
	10-Q	01/01/00	02/15/00	Not filed	112
	10-Q	04/01/00	05/16/00	Not filed	109
	10-Q	07/01/00	08/15/00	Not filed	106
	10-K	09/30/00	12/29/00	Not filed	102
	10-Q	12/30/00	02/13/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-K	09/29/01	12/28/01	Not filed	90
	10-Q	12/29/01	02/12/02	Not filed	88
	10-Q	03/30/02	05/14/02	Not filed	85
	10-Q	06/29/02	08/13/02	Not filed	82
	10-K	09/28/02	12/27/02	Not filed	78
	10-Q	12/28/02	02/11/03	Not filed	76
	10-Q	03/29/03	05/13/03	Not filed	73

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Warehouse Club, Inc.	*10-Q*	06/28/03	08/12/03	Not filed	70
(continued)	*10-K*	09/27/03	12/26/03	Not filed	66
	10-Q	12/27/03	02/10/04	Not filed	64
	10-Q	03/27/04	05/11/04	Not filed	61
	10-Q	06/26/04	08/10/04	Not filed	58
	10-K	10/02/04	12/31/04	Not filed	54
	10-Q	01/01/05	02/15/05	Not filed	52
	10-Q	04/02/05	05/18/05	Not filed	49
	10-Q	07/02/05	08/16/05	Not filed	46
	10-K	10/01/05	12/30/05	Not filed	42
	10-Q	12/31/05	02/14/06	Not filed	40
	10-Q	04/01/06	05/16/06	Not filed	37
	10-Q	07/01/06	08/15/06	Not filed	34
	10-K	09/30/06	12/29/06	Not filed	30
	10-Q	12/30/06	02/13/07	Not filed	28
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-K	09/29/07	12/28/07	Not filed	18
	10-Q	12/29/07	02/12/08	Not filed	16
	10-Q	03/29/08	05/13/08	Not filed	13
	10-Q	06/28/08	08/12/08	Not filed	10
	10-K	09/27/08	12/26/08	Not filed	6
	10-Q	12/27/08	02/10/09	Not filed	4
	10-Q	03/28/09	05/12/09	Not filed	1
Total Filings Delinquent	**59**				
Wavemat, Inc.					
	10-KSB	12/31/98	03/31/99	Not filed	123
	10-QSB	03/31/99	05/17/99	Not filed	121
	10-QSB	06/30/99	08/16/99	Not filed	118
	10-QSB	09/30/99	11/15/99	Not filed	115
	10-KSB	12/31/99	03/30/00	Not filed	111
	10-QSB	03/31/00	05/15/00	Not filed	109
	10-QSB	06/30/00	08/14/00	Not filed	106
	10-QSB	09/30/00	11/14/00	Not filed	103
	10-KSB	12/31/00	04/02/01	Not filed	98
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94
	10-QSB	09/30/01	11/14/01	Not filed	91

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Wavemat, Inc.	*10-KSB*	12/31/01	04/01/02	Not filed	86
(continued)	*10-QSB*	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**41**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Wilson Lee Engineering Co., Inc. (n/k/a Lee Wilson Engineering Co., Inc.)					
	10-K	09/30/94	12/29/94	Not filed	174
	10-Q	12/31/94	02/14/95	Not filed	172
	10-Q	03/31/95	05/15/95	Not filed	169
	10-Q	06/30/95	08/14/95	Not filed	166
	10-K	09/30/95	12/29/95	Not filed	162
	10-Q	12/31/95	02/14/96	Not filed	160
	10-Q	03/31/96	05/15/96	Not filed	157
	10-Q	06/30/96	08/14/96	Not filed	154
	10-K	09/30/96	12/30/96	Not filed	150
	10-Q	12/31/96	02/14/97	Not filed	148
	10-Q	03/31/97	05/15/97	Not filed	145
	10-Q	06/30/97	08/14/97	Not filed	142
	10-K	09/30/97	12/29/97	Not filed	138
	10-Q	12/31/97	02/17/98	Not filed	136
	10-Q	03/31/98	05/15/98	Not filed	133
	10-Q	06/30/98	08/14/98	Not filed	130
	10-K	09/30/98	12/29/98	Not filed	126
	10-Q	12/31/98	02/16/99	Not filed	124
	10-Q	03/31/99	05/17/99	Not filed	121
	10-Q	06/30/99	08/16/99	Not filed	118
	10-K	09/30/99	12/29/99	Not filed	114
	10-Q	12/31/99	02/14/00	Not filed	112
	10-Q	03/31/00	05/15/00	Not filed	109
	10-Q	06/30/00	08/14/00	Not filed	106
	10-K	09/30/00	12/29/00	Not filed	102
	10-Q	12/31/00	02/14/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-K	09/30/01	12/31/01	Not filed	90
	10-Q	12/31/01	02/14/02	Not filed	88
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-K	09/30/02	12/30/02	Not filed	78
	10-Q	12/31/02	02/14/03	Not filed	76
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-K	09/30/03	12/29/03	Not filed	66

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Wilson Lee Engineering Co., Inc. (n/k/a Lee Wilson Engineering Co., Inc.) *(continued)*	*10-Q*	12/31/03	02/17/04	Not filed	64
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-K	09/30/04	12/29/04	Not filed	54
	10-Q	12/31/04	02/14/05	Not filed	52
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-K	09/30/05	12/29/05	Not filed	42
	10-Q	12/31/05	02/14/06	Not filed	40
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-K	09/30/06	12/29/06	Not filed	30
	10-Q	12/31/06	02/14/07	Not filed	28
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-K	09/30/07	12/29/07	Not filed	18
	10-Q	12/31/07	02/14/08	Not filed	16
	10-Q	03/31/08	05/15/08	Not filed	13
	10-Q	06/30/08	08/14/08	Not filed	10
	10-K	09/30/08	12/29/08	Not filed	6
	10-Q	12/31/08	02/17/09	Not filed	4
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**59**				
Winthrop Resources Corp.					
	10-Q	06/30/97	08/14/97	Not filed	142
	10-Q	09/30/97	11/14/97	Not filed	139
	10-K	12/31/97	03/31/98	Not filed	135
	10-Q	03/31/98	05/15/98	Not filed	133
	10-Q	06/30/98	08/14/98	Not filed	130
	10-Q	09/30/98	11/16/98	Not filed	127
	10-K	12/31/98	03/31/99	Not filed	123
	10-Q	03/31/99	05/17/99	Not filed	121
	10-Q	06/30/99	08/16/99	Not filed	118
	10-Q	09/30/99	11/15/99	Not filed	115
	10-K	12/31/99	03/30/00	Not filed	111
	10-Q	03/31/00	05/15/00	Not filed	109

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Winthrop Resources Corp.	*10-Q*	06/30/00	08/14/00	Not filed	106
(continued)	*10-Q*	09/30/00	11/14/00	Not filed	103
	10-K	12/31/00	04/02/01	Not filed	98
	10-Q	03/31/01	05/15/01	Not filed	97
	10-Q	06/30/01	08/14/01	Not filed	94
	10-Q	09/30/01	11/14/01	Not filed	91
	10-K	12/31/01	04/01/02	Not filed	86
	10-Q	03/31/02	05/15/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	82
	10-Q	09/30/02	11/14/02	Not filed	79
	10-K	12/31/02	03/31/03	Not filed	75
	10-Q	03/31/03	05/15/03	Not filed	73
	10-Q	06/30/03	08/14/03	Not filed	70
	10-Q	09/30/03	11/14/03	Not filed	67
	10-K	12/31/03	03/30/04	Not filed	63
	10-Q	03/31/04	05/17/04	Not filed	61
	10-Q	06/30/04	08/16/04	Not filed	58
	10-Q	09/30/04	11/15/04	Not filed	55
	10-K	12/31/04	03/31/05	Not filed	51
	10-Q	03/31/05	05/16/05	Not filed	49
	10-Q	06/30/05	08/15/05	Not filed	46
	10-Q	09/30/05	11/14/05	Not filed	43
	10-K	12/31/05	03/31/06	Not filed	39
	10-Q	03/31/06	05/15/06	Not filed	37
	10-Q	06/30/06	08/14/06	Not filed	34
	10-Q	09/30/06	11/14/06	Not filed	31
	10-K	12/31/06	04/02/07	Not filed	26
	10-Q	03/31/07	05/15/07	Not filed	25
	10-Q	06/30/07	08/14/07	Not filed	22
	10-Q	09/30/07	11/14/07	Not filed	19
	10-K	12/31/07	03/31/08	Not filed	15
	10-Q	03/31/08	05/15/08	Not filed	13
	10-Q	06/30/08	08/14/08	Not filed	10
	10-Q	09/30/08	11/14/08	Not filed	7
	10-K	12/31/08	03/31/09	Not filed	3
	10-Q	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**47**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Worldcall Corp.					
	10-KSB	02/28/99	06/01/99	Not filed	120
	10-QSB	05/31/99	07/15/99	Not filed	119
	10-QSB	08/31/99	10/15/99	Not filed	116
	10-QSB	11/30/99	01/14/00	Not filed	113
	10-KSB	02/29/00	05/30/00	Not filed	109
	10-QSB	05/31/00	07/17/00	Not filed	107
	10-QSB	08/31/00	10/16/00	Not filed	104
	10-QSB	11/30/00	01/16/01	Not filed	101
	10-KSB	02/28/01	05/29/01	Not filed	97
	10-QSB	05/31/01	07/16/01	Not filed	95
	10-QSB	08/31/01	10/15/01	Not filed	92
	10-QSB	11/30/01	01/14/02	Not filed	89
	10-KSB	02/28/02	05/29/02	Not filed	85
	10-QSB	05/31/02	07/15/02	Not filed	83
	10-QSB	08/31/02	10/15/02	Not filed	80
	10-QSB	11/30/02	01/14/03	Not filed	77
	10-KSB	02/28/03	05/29/03	Not filed	73
	10-QSB	05/31/03	07/15/03	Not filed	71
	10-QSB	08/31/03	10/15/03	Not filed	68
	10-QSB	11/30/03	01/14/04	Not filed	65
	10-KSB	02/29/04	06/01/04	Not filed	60
	10-QSB	05/31/04	07/15/04	Not filed	59
	10-QSB	08/31/04	10/15/04	Not filed	56
	10-QSB	11/30/04	01/14/05	Not filed	53
	10-KSB	02/28/05	05/31/05	Not filed	49
	10-QSB	05/31/05	07/15/05	Not filed	47
	10-QSB	08/31/05	10/17/05	Not filed	44
	10-QSB	11/30/05	01/17/06	Not filed	41
	10-KSB	02/28/06	05/30/06	Not filed	37
	10-QSB	05/31/06	07/17/06	Not filed	35
	10-QSB	08/31/06	10/16/06	Not filed	32
	10-QSB	11/30/06	01/16/07	Not filed	29
	10-KSB	02/28/07	05/29/07	Not filed	25
	10-QSB	05/31/07	07/16/07	Not filed	23
	10-QSB	08/31/07	10/15/07	Not filed	20
	10-QSB	11/30/07	01/14/08	Not filed	17
	10-KSB	02/29/08	05/29/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Worldcall Corp.	*10-Q**	05/31/08	07/15/08	Not filed	11
(continued)	*10-Q**	08/31/08	10/15/08	Not filed	8
	*10-Q**	11/30/08	01/14/09	Not filed	5
	*10-K**	02/28/09	05/29/09	Not filed	1
Total Filings Delinquent	**41**				

* Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, have been removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal took effect over a transition period that concluded on March 15, 2009. All reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB are now required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60118 / June 16, 2009

INVESTMENT ADVISERS ACT OF 1940
Release No. 2892 / June 16, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13520

In the Matter of BERNARD L. MADOFF, 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 Bernard L. Madoff ("Madoff" or "Respondent").

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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 and Section 203(f) of the 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. Madoff, 70, a resident of New York, NY and a former chairman of the board of directors of the NASDAQ stock market, is the sole owner of Bernard L. Madoff Investment Securities LLC ("BMIS"). BMIS, founded in 1960, is a broker-dealer and investment adviser registered with the Commission that purportedly engages in three different operations: investment adviser services, market-making services, and proprietary trading. Madoff oversees and controls the investment adviser services at BMIS as well as the overall finances of BMIS.

2. On February 9, 2009, a Partial Judgment on Consent Imposing Permanent Injunction and Continuing Other Relief was entered by consent against Madoff, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Exchange Act 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. Bernard L. Madoff and Bernard L. Madoff Investment Securities LLC, Civil Action Number 08-10791 (LLS), in the United States District Court for the Southern District of New York.

3. The Commission's complaint alleged the following facts: Madoff and BMIS conducted a $50 billion fraudulent scheme through the firm's investment advisory business. In or around early December 2008, Madoff had told senior employees at BMIS that there had been approximately $7 billion in advisory client redemption requests and he was struggling to obtain the liquidity necessary to meet those obligations. When the employees pressed Madoff for more information, Madoff said that his advisory business was a fraud, "just one big lie [and] basically, a giant Ponzi scheme" that had been paying returns to certain investors out of principal received from other investors. Madoff said that he intended to surrender to authorities after he paid out remaining money to selected employees, friends and family members.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Madoff'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 Madoff be, and hereby is barred from association with any broker, dealer, or investment adviser.

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.

Elizabeth M. Murphy
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. 60119 / June 16, 2009

INVESTMENT ADVISERS ACT OF 1940
Release No. 2893 / June 16, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13521

In the Matter of

Mitchel S. Guttenberg,

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 Mitchel S. Guttenberg ("Guttenberg" 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.3 and 5 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 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. Guttenberg, 44 years old, is a resident of Fort Dix, New Jersey.

2. From August 1999 through March 2007, Guttenberg was a registered representative associated with UBS Securities LLC ("UBS"), a broker-dealer and investment adviser registered with the Commission.

3. On June 2, 2009, a final judgment was entered by consent against Guttenberg, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder, in the civil action entitled Securities and Exchange Commission v. Guttenberg, et al., Civil Action No. 07 CV 1774, in the United States District Court for the Southern District of New York.

4. The Commission's complaint alleged that from 2001 through 2006, Guttenberg misappropriated from UBS material, nonpublic information concerning upcoming analyst recommendations, and tipped this confidential information to David Tavdy and Erik Franklin, in exchange for sharing their illicit profits from trading on that information.

5. On February 27, 2008, Guttenberg pled guilty to two counts of conspiracy to commit securities fraud, in violation of Title 15, United States Code, Sections 78j(b) & 78ff, and Title 17, Code of Federal Regulations, Sections 240.10b-5 and 240.10b5-2, and four counts of securities fraud, in violation of Title 17, Code of Federal Regulations, Sections 240.10b-5, before the United States District Court for the Southern District of New York, in United States v. Mitchel Guttenberg and David Tavdy, Crim. Indictment No. 1:07-CR-141.

6. The counts of the criminal indictment to which Guttenberg pled guilty alleged, inter alia, that Guttenberg misappropriated material, nonpublic information from UBS and unlawfully passed that information to David Tavdy and another coconspirator, and that David Tavdy and this other coconspirator illegally traded using that information and then shared the illegal profits with Guttenberg.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Guttenberg'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 Guttenberg be, and hereby is barred from association with any broker, dealer, or investment adviser.

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.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 17, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13523

In the Matter of	:	
Keystone Ventures, Inc.	:	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934
Respondent.	:	

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

Keystone Ventures, Inc. (CIK No. 0001119378), is a Nevada corporation with its principal office located in El Cajon, CA. Keystone's common stock is identified with the symbol "KYSV" and is registered under Section 12(g) of the Exchange Act [15 U.S.C. § 78l(g)].

B. NON-COMPLIANT PERIODIC FILINGS

1. Keystone Ventures filed a Form 10SB registration statement on August 2, 2000, but has not filed a periodic report with the Commission since December 28, 2001.

2. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers with classes of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the

registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports (Forms 10-K or 10-KSB), and Rule 13a-13 requires issuers to file quarterly reports (Forms 10-Q or 10-QSB).

3. As a result of the foregoing, the Respondent has failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest to institute public administrative proceedings to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondent identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY 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 it 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 the Respondent personally or by certified mail.

IT IS FURTHER HEREBY ORDERED that the Administrative Law Judge shall issue an initial decision not later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

June 18, 2009

IN THE MATTER OF PETRO AMERICA CORP. File No. 500-1	: : : : :	ORDER OF SUSPENSION OF TRADING

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Petro America Corp. ("Petro America") (trading symbol: PTRZ) because of questions regarding the accuracy and adequacy of assertions by Petro America concerning, among other things: the company's business operations and assets, including regarding its purported oil trading and storage business and holdings, its purported millions of dollars in assets, and its securities issued and outstanding.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in securities related to the above company.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed company is suspended for the period from 9:30 a.m. EDT, June 18, 2009 through 11:59 p.m. EDT, on July 1, 2009.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Chairman Schapiro and Commissioner Casey not participating

SECURITIES AND EXCHANGE COMMISSION

Securities Exchange Act of 1934
Release No. 60136 / June 18, 2009

ORDER EXEMPTING CIBC MELLON TRUST COMPANY FROM BROKER-DEALER REGISTRATION

I. Introduction

Pursuant to Section 15(a)(2) of the Securities Exchange Act of 1934 ("Exchange Act"), the Securities and Exchange Commission ("Commission") is granting CIBC Mellon Trust Company ("CIBC Mellon Trust") a conditional exemption from the broker-dealer registration requirement of Section 15(a)(1) of the Exchange Act to the extent CIBC Mellon Trust acts, subsequent to the entry of this order, as a broker as defined in Section 3(a)(4) of the Exchange Act in connection with its administration of dividend reinvestment and stock purchase plans (collectively, "DRSPPs"), employee stock purchase plans, employee stock option plans, and odd-lot programs with U.S. resident investors. For purposes of this order, DRSPPs, employee stock purchase plans, employee stock option plans, and odd-lot programs shall be referred to collectively as "Stock Plans." Pursuant to Section 36 of the Exchange Act, the Commission also is granting CIBC Mellon Trust a conditional exemption from the reporting and other requirements specifically imposed by the Exchange Act, and the rules and regulations thereunder, on a broker or dealer that is not registered with the Commission to the extent CIBC Mellon Trust acts, subsequent to the entry of this order, as a broker under Section 3(a)(4) of the Exchange Act in connection with its administration of Stock Plans with U.S. resident investors.

II. Background

CIBC Mellon Trust has agreed to consent to the entry of an order, without admitting or denying the findings, in which the Commission finds that it violated Sections 15(a)(1) and 17A(c)(1) of the Exchange Act. With respect to Section 15(a)(1), the Commission finds that, from 1998 to the present, CIBC Mellon Trust acted as a broker and dealer as defined in Sections 3(a)(4) and 3(a)(5) of the Exchange Act in connection with its administration of Stock Plans by engaging in the business of effecting securities transactions in these Stock Plans with U.S. resident investors.[1] With respect to Section 17A(c)(1), the Commission finds that, from 1998 to 2004, CIBC Mellon Trust acted as a transfer agent, as defined by Section 3(a)(25) of the Exchange Act, for 113 companies that have securities registered under Section 12 of the Exchange Act. At the time of this activity, CIBC Mellon Trust was not registered as a broker-dealer or as a transfer agent as required by Sections 15(a)(1) and 17A(c)(1) of the Exchange Act,

[1] For purposes of this order, a U.S. resident investor is any participant in a Stock Plan who permanently resides in the United States. CIBC Mellon Trust shall treat all Stock Plan participants with U.S. mailing addresses as U.S. resident investors unless CIBC Mellon has been informed that a participant with a U.S. address is not a permanent U.S. resident.

respectively. Effective February 6, 2004, CIBC Mellon Trust registered with the Commission as a transfer agent.

In addition, CIBC Mellon Trust agreed to consent to the entry of a permanent injunction in a civil action in the United States District Court for the District of Columbia, permanently enjoining CIBC Mellon Trust from, among other things, future violations of Sections 15(a) and 17A(c) of the Exchange Act.

III. Discussion

Section 15(a)(1) of the Exchange Act generally requires any broker or dealer that makes use of the mails or any instrumentality of interstate commerce to effect transactions in, or to induce the purchase or sale of, any security to register with the Commission. Section 3(a)(4) of the Exchange Act generally defines a broker as any person engaged in the business of effecting transactions in securities for the account of others, and Section 3(a)(5) of the Exchange Act generally defines a dealer as any person engaged in the business of buying and selling securities for its own account, whether through a broker or otherwise. In its complaint, the Commission alleged that, over the time period at issue, CIBC Mellon Trust violated Section 15(a)(1) by, in connection with its administration of Stock Plans, engaging in the business of effecting securities transactions for U.S. resident investors without being a registered broker-dealer.[2] Absent an exception or exemption, CIBC Mellon Trust would be required to register as a broker-dealer with the Commission to continue this activity.[3]

Section 15(a)(2) of the Exchange Act authorizes the Commission to exempt, either conditionally or unconditionally, from the broker-dealer registration requirements of Section 15(a)(l) of the Exchange Act any broker or dealer or class of broker or dealer, by rule or order, as it considers consistent with the public interest and the protection of investors. Similarly, but more broadly, Section 36 of the Exchange Act authorizes the Commission to exempt, either conditionally or unconditionally, any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of the Exchange Act or any rule or regulation thereunder, by rule, regulation, or order, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

Banks registered as transfer agents are conditionally excepted from broker-dealer registration under Section 3(a)(4)(B)(iv) of the Exchange Act for their activities in administering

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[2] CIBC Mellon Trust has consented to the entry of an injunction enjoining it from violating Section 15(a) of the Exchange Act based upon the allegations in the Commission's complaint. As the Commission recognized in addressing the Direct Registration System, some activities in connection with dividend reinvestment and stock purchase plans may require broker-dealer registration under Section 15(a) of the Exchange Act. See Exchange Act Release No. 35038 (Dec. 1, 1994), 59 FR 63652 (Dec. 8, 1994).

[3] Absent an exception or exemption, CIBC Mellon Trust also would be in violation of the injunction pertaining to Section 15(a) of the Exchange Act by engaging in these activities without being registered as a broker-dealer pursuant to Section 15(b) of the Exchange Act.

Stock Plans. CIBC Mellon Trust, however, is not a bank as defined in Section 3(a)(6) of the Exchange Act. Absent an exemption, CIBC Mellon Trust would be required to register with the Commission as a broker-dealer to continue to administer Stock Plans with U.S. resident investors.

The Commission has determined to grant CIBC Mellon Trust a limited conditional exemption from broker-dealer registration. The Commission finds that a limited exemption from broker-dealer registration, subject to the conditions set forth below, is consistent with the public interest and the protection of investors. CIBC Mellon Trust's Stock Plan administration activities require CIBC Mellon Trust to engage in limited broker-dealer activities, as well as transfer agent activities. CIBC Mellon Trust represents that in each case it is retained directly by the issuer or its affiliate to provide Stock Plan services to that issuer's employees or shareholders. CIBC Mellon Trust will only administer DRSPPs and odd-lot programs with U.S. resident investors for issuers for which it acts as transfer agent.[4] The Commission believes that granting a limited conditional exemption is warranted because (1) CIBC Mellon Trust is registered with the Commission as a transfer agent; (2) CIBC Mellon Trust's broker services will be provided only directly on behalf of the issuer's Stock Plan;[5] (3) the conditions of the exemption impose appropriate protections designed to safeguard investors' funds and securities; and (4) CIBC Mellon Trust's broker-dealer activities performed in connection with administering Stock Plans with U.S. resident investors will be limited, which will limit the risk that U.S. investors will be subject to abusive sales practices.[6] Moreover, the exemption will allow investors that have established relationships with issuers through Stock Plans administered by CIBC Mellon Trust to continue those relationships without interruption. Under these circumstances, the Commission believes that it is not necessary to require CIBC Mellon Trust to register both as a transfer agent and a broker-dealer.

The Commission therefore finds that it is consistent with the public interest and the protection of investors to exempt, subject to the conditions set forth below, CIBC Mellon Trust from the broker-dealer registration requirement of Section 15(a)(1) of the Exchange Act to the extent that CIBC Mellon Trust acts as a broker in connection with administering Stock Plans

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[4] The allegations in the Commission's complaint were limited to CIBC Mellon Trust's administration of Stock Plans with one or more U.S. resident investors. CIBC Mellon Trust's administration of Stock Plans with no U.S. resident investors was not the subject of Commission action. Neither this order nor the conditions set forth herein apply to Stock Plans with no U.S. resident investors.

[5] CIBC Mellon Trust represents that in each case it will be in direct privity of contract with the issuer or its affiliate.

[6] CIBC Mellon Trust will be prohibited from engaging in certain activities that it engaged in prior to the issuance of this order, such as netting customer orders to buy and sell issuer plan securities.

with U.S. resident investors for issuers.[7] This order is granted subject to the following conditions:

1. CIBC Mellon Trust will maintain its registration as a transfer agent under Section 17A of the Exchange Act as long as it continues to administer Stock Plans with U.S. resident investors.

2. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will not solicit transactions or provide investment advice to U.S. resident investors with respect to the purchase or sale of securities in connection with the Stock Plan, other than by delivering written or electronic Stock Plan materials to U.S. resident employees of the issuer, U.S. resident shareholders of the issuer, or U.S. resident members of affinity groups of the issuer so long as such materials are comparable in scope or nature to those permitted by the Commission as of the date of enactment of the Gramm-Leach-Bliley Act.[8]

3. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will not net customers' buy and sell orders. To the extent that CIBC Mellon Trust's administration of Stock Plans with U.S.

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[7] The Commission notes, however, that this order only addresses broker-dealer registration issues with regard to CIBC Mellon Trust as a Stock Plan administrator, and that nothing in this order affects prior positions with respect to plans or programs. See, e.g., Exchange Act Release No. 38067 (Dec. 20, 1996), 62 FR 520, 532 at n. 98 (Jan. 3, 1997)(adopting Regulation M governing the activities of underwriters, issuers, selling security holders and others in connection with offerings of securities). The Commission also recognizes that the administrative costs of such plans may be borne by either the issuers or the plan participants themselves. See, e.g., The Securities Transfer Association, Inc., SEC No-Action Letter (Dec. 1, 1994) (acknowledging that issuers may offer DRSPPs in which plan participants pay administrative fees).

[8] See Section 3(a)(4)(B)(iv) of the Exchange Act. For example, each brochure for Stock Plans with U.S. resident investors sponsored and administered by CIBC Mellon Trust will include a prominent statement on the cover that: "The Program is sponsored and administered by CIBC Mellon Trust, not by [the appointing issuer]." Each brochure will indicate that the securities held in program accounts are not subject to protection under the Securities Investor Protection Act of 1970. Each brochure will be plain and factual in tone and approach, and will be descriptive of all material Stock Plan features, contractual terms, and fee and processing arrangements, but not of the issuer's securities. The brochure will not encourage individuals to engage in any particular transactions, whether purchases or sales, and no advice or recommendations will be included in the brochure (or otherwise be given during the administration of Stock Plans).

Administration of Stock Plans involving shares required to be registered pursuant to the Securities Act of 1933 continues to be subject to the provisions set forth in the exemption issued to The Securities Transfer Association, Inc. See Exchange Act Release No. 35041 (Dec. 1, 1994).

resident investors results in a trade in the United States, CIBC Mellon Trust will direct such trade to a U.S.-registered broker or dealer for execution.

4. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will maintain with a bank (or banks) at all times a bank account (or accounts) for the exclusive benefit of customers that shall be separate from any other CIBC Mellon Trust bank account. Solely for purposes of this condition, a bank shall have the same meaning as in Exchange Act Rule 15c3-3(a)(7).[9] The account (or accounts) shall be designated as a "Special Bank Account for the Exclusive Benefit of Customers." All customers' funds in CIBC Mellon Trust's custody and possession that are related to Stock Plans with U.S. resident investors will be maintained in such account (or accounts) until paid to the customer or the issuer, or used to settle a transaction with or through a broker or dealer.

5. In connection with administering Stock Plans with U.S. resident investors that make periodic purchases, if the specified time intervals for such periodic purchases are quarterly or more frequent, CIBC Mellon Trust will send each U.S. resident investor, at least quarterly, a written account statement containing at a minimum the information in items (a) through (h), below. In connection with administering all other Stock Plans with U.S. resident investors, CIBC Mellon Trust will send each U.S. resident investor, not later than four trading days after the date of the last transaction effected in the aggregated batch, a written transaction notification containing, at a minimum, the following information:

   (a) The name of CIBC Mellon Trust;

   (b) The name of the customer;

   (c) The capacity in which CIBC Mellon Trust is acting;

   (d) The date of each transaction for the account of the customer;

   (e) The identity, price, and number of shares or units purchased or sold for the customer in each such transaction; and, in a periodic statement, the total number of shares or units of such securities held by the customer at the end of the account period;

   (f) The aggregate amount of fees that the customer has paid or will pay in connection with the transaction;

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[9] 17 CFR 240.15c3-3(a)(7). Under this rule, with respect to a broker or dealer that maintains its principal place of business in the Dominion of Canada, the term "bank" also means a Canadian bank subject to supervision by an authority of the Dominion of Canada.

(g) The source and amount of remuneration CIBC Mellon Trust has or will receive from a party other than the customer, unless the written statement or notification discloses whether CIBC Mellon Trust has received or will receive remuneration from a party other than the customer, and that CIBC Mellon Trust will furnish within a reasonable time the source and amount of this remuneration upon written request of the U.S. resident customer. This election is not available however, if, with respect to a purchase, CIBC Mellon Trust was participating in a distribution of that security or, with respect to a sale, CIBC Mellon Trust was participating in a tender offer for that security;[10] and

(h) The name of the registered broker-dealer utilized; or where there is no registered broker-dealer, the name of the person from whom the security was purchased or to whom the security was sold, or a statement that CIBC Mellon Trust will furnish this information within a reasonable time upon written request of the U.S. resident customer.

6. In connection with administering Stock Plans with U.S. resident investors, personnel at any call center operated by or on behalf of CIBC Mellon Trust will be limited to responding to inquiries received from a U.S. resident customer about a Stock Plan, but may not: (a) identify to a U.S. resident investor a particular security except as requested by the investor and then only as necessary to be responsive to the specific inquiry; (b) respond to inquiries from U.S. resident investors concerning the advisability of investing in the particular security or participating in the Stock Plan rather than using the services of a registered broker-dealer; or (c) take verbal orders to buy or sell securities for U.S. resident investors. Call center personnel may provide U.S. resident customers general information about Stock Plan services as described in the Stock Plan brochure and the status of the customer's account, as well as accommodate telephone requests for brochures, account statements, certificated shares and replacement dividend checks. CIBC Mellon Trust will be responsible for ensuring that call center personnel are strictly instructed not to provide recommendations or advice to U.S. resident customers and that they will be monitored and supervised closely in this respect.[11]

7. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will effect purchases and sales at least once a day

[10] CIBC Mellon Trust would not be required to disclose any payments it receives from issuers for acting in a transfer agent capacity.

[11] This condition would not affect, for example, CIBC Mellon Trust's ability to operate a call center outside of the U.S. that takes orders from non-U.S. residents.

unless orders received produce such a low share volume as to dictate less frequent transaction intervals. In all cases, purchases and sales will occur at least once a week (assuming an order is received during the week), except in the case of Odd-Lot Plans, where purchases and sales will occur when sufficient shares have been tendered to constitute a standard unit of trading on the marketplace.

8. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will not receive payment for order flow, as defined in Exchange Act Rule 10b-10.[12]

9. In connection with administering Stock Plans with U.S. resident investors, CIBC Mellon Trust will make and keep current all material books and records relating to customers' funds, securities, and orders to purchase or sell securities, including the following:

   (a) Records reflecting customer ownership in the Stock Plan;

   (b) Any statement, checkbook, or cancelled check regarding any bank account established pursuant to condition 4 above; and records reflecting funds submitted by Stock Plan customers, funds held on behalf of customers pursuant to condition 4 above, and reconciliation of the funds submitted and the funds held;

   (c) An original of any communication received by CIBC Mellon Trust from a Stock Plan customer or a copy of any materials sent to Stock Plan customers by CIBC Mellon Trust;

   (d) A record of any order by a Stock Plan customer to purchase or sell securities;

   (e) A copy of any transaction notification or statement sent pursuant to condition 5 above;

   (f) A copy of any supervisory procedures relating to condition 6 above;

   (g) A copy of any transaction notification received pursuant to condition 7 above; and

   (h) A copy of any agreement relating to Stock Plans entered into with an affiliated or unaffiliated third party, including agreements with banks, broker-dealers, and entities providing services related to processing and call centers.

[12] 17 CFR 240.10b-10.

10. Any record maintained pursuant to condition 9 will be retained for a period of not less than six years, the first year in a readily accessible place for purposes of examination and inspection by the Commission.

In sum, in finding that this exemption is appropriate in the public interest, we stress that (1) CIBC Mellon Trust will provide Stock Plan services to issuers' employees or shareholders only when it is retained directly by the issuer or its affiliate; (2) CIBC Mellon Trust will only administer DRSPPs and odd-lot programs with U.S. resident investors for issuers for which it acts as transfer agent; and (3) its activities as a registered transfer agent are subject to Commission regulation and inspection.[13] This exemption is subject to modification or revocation at any time the Commission determines that such modification or revocation is consistent with the public interest or the protection of investors.

IT IS THEREFORE ORDERED, pursuant to Section 15(a)(2) of the Exchange Act, that a conditional exemption for CIBC Mellon Trust from the registration requirements of Section 15(a)(l) of the Exchange Act to the extent CIBC Mellon Trust is acting as a broker under Section 3(a)(4) of the Exchange Act be, and hereby is, granted. This exemption is limited to administering Stock Plans with U.S. resident investors and subject to the conditions listed above.

IT IS FURTHER ORDERED, pursuant to Section 36 of the Exchange Act, that CIBC Mellon Trust shall be exempt, in connection with engaging in Stock Plan administration activities consistent with the conditions set forth above, from the reporting and other requirements specifically imposed by the Exchange Act, and the rules and regulations thereunder, on a broker or dealer that is not registered with the Commission to the extent CIBC Mellon Trust is acting as a broker under Section 3(a)(4) of the Exchange Act.[14]

IT IS FURTHER ORDERED, that the exemptions granted herein to CIBC Mellon Trust pursuant to Section 15(a)(2) and Section 36 of the Exchange Act shall become effective upon the date the United States District Court for the District of Columbia enters a final order permanently enjoining CIBC Mellon Trust from, among other things, future violations of Sections 15(a) and 17A(c) of the Exchange Act.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

[13] In contrast, the Stock Plan activities that are the subject of the Commission's enforcement order were conducted more broadly and outside any Commission oversight.

[14] CIBC Mellon Trust remains subject to all other applicable provisions of the federal securities laws, including, without limitation, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. 17 CFR 240.10b-5.

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60152)

Order Granting Application for Extension of a Temporary Conditional Exemption Pursuant to Section 36(a) of the Exchange Act by the International Securities Exchange, LLC Relating to the Ownership Interest of International Securities Exchange Holdings, Inc. in an Electronic Communications Network

June 19, 2009

I. Introduction

On December 22, 2008, the Securities and Exchange Commission ("Commission") approved a proposal filed by the International Securities Exchange, LLC ("ISE" or "Exchange") in connection with corporate transactions (the "Transactions") in which, among other things, the parent company of ISE, International Securities Exchange Holdings, Inc. ("ISE Holdings"), purchased a 31.54% ownership interest in Direct Edge Holdings LLC ("Direct Edge"), the owner and operator of Direct Edge ECN ("DECN"), a registered broker-dealer and electronic communications network ("ECN").[1] Following the closing of the Transactions (the "Closing"), Direct Edge's wholly-owned subsidiary, Maple Merger Sub LLC ("Merger Sub") began to operate a marketplace for the trading of U.S. cash equity securities by Equity Electronic Access Members of ISE (the "Facility"), under ISE's rules and as a "facility," as defined in Section 3(a)(2) of the Securities Exchange Act of 1934 ("Exchange Act"),[2] of ISE.[3]

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1 See Securities Exchange Act Release No. 59135 (December 22, 2008), 73 FR 79954 (December 30, 2008) (order approving File No. SR-ISE-2008-85).

2 15 U.S. C. 78c(a)(2).

3 Under Section 3(a)(2) of the Act, the term "facility," when used with respect to an exchange, includes "its premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any service thereof for the purpose of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service."

DECN, which operates as an ECN and submits its limit orders to the Facility for display and execution, is an affiliate of ISE through ISE Holdings' equity interest in DE Holdings. DECN also is a facility, as defined in Section 3(a)(2) of the Exchange Act, of ISE because it is an affiliate of ISE used for the purpose of effecting and reporting securities transactions. Because DECN is a facility of ISE, ISE, absent exemptive relief, would be obligated under Section 19(b) of the Exchange Act to file with the Commission proposed rules governing the operation of DECN's systems and subscriber fees.

On December 22, 2008, the Commission exercised its authority under Section 36 of the Exchange Act to grant ISE a temporary exemption, subject to certain conditions, from the requirements under Section 19(b) of the Exchange Act with respect to DECN's proposed rules.[4]

On June 15, 2009, ISE filed with the Commission, pursuant to Rule 0-12[5] under the Exchange Act, an application under Section 36(a)(1) of the Exchange Act[6] to extend the relief granted in the Exemption Order for an additional 180 days, subject to certain conditions.[7] This order grants ISE's request for a temporary extension of the relief provided in the Exemption Order, subject to the satisfaction of certain conditions, which are outlined below.

II. Application for an Extension of the Temporary Conditional Exemption from the Section 19(b) Rule Filing Requirements

On June 15, 2009, ISE requested that the Commission exercise its authority under Section 36 of the Exchange Act to temporarily extend, subject to certain conditions, the temporary conditional exemption granted in the Exemption Order from the rule filing procedures

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4 See Securities Exchange Act Release No. 59133 (December 22, 2008), 73 FR 79940 (December 30, 2008) ("Exemption Order").

5 17 CFR 240.0-12.

6 15 U.S.C. 78mm(a)(1).

7 See letter from Michael J. Simon, General Counsel and Secretary, ISE, to Elizabeth M. Murphy, Secretary, Commission, dated June 15, 2009 ("Exemption Request").

of Section 19(b) of the Exchange Act in connection with ISE Holdings' equity ownership interest in DE Holdings and the continued operation of DECN as a facility of ISE.[8]

The Exemption Request notes that on May 7, 2009, EDGA Exchange, Inc., and EDGX Exchange, Inc. (together, the "Exchange Subsidiaries"), two wholly-owned subsidiaries of DE Holdings, filed with the Commission Form 1 applications (the "Form 1 Applications") to register as national securities exchanges under Section 6 of the Exchange Act.[9] According to the Exemption Request, DECN intends to file a "Cessation of Operations Report" with the Commission and to cease operations as an ECN shortly following any Commission approval of the Form 1 Applications and the Exchange Subsidiaries commencing operations as national securities exchanges.[10]

Because DECN will cease operations as an ECN if the Commission approves the Form 1 Applications, ISE expects that DECN will continue to operate as a facility of ISE for a relatively brief period.[11] In addition, ISE believes that it would be unduly burdensome and inefficient to require DECN's operating rules to be separately subject to the Section 19(b) rule filing process because DECN is only operating temporarily as a facility of ISE while the Commission considers the Form 1 Applications.[12] ISE notes, further, that the Commission is reviewing the rules governing the operation of the Exchange Subsidiaries as part of its review of the Form 1 Applications.[13]

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8 See Section 3(a)(2) of the Exchange Act, 15 U.S.C. 78c3(a)(2) (definition of "facility").

9 See Exemption Request at 2.

10 Id.

11 Id.

12 Id.

13 Id.

ISE has asked the Commission to exercise its authority under Section 36 of the Exchange Act to grant ISE a 180-day extension of the Exemption Order's relief, subject to certain conditions, from the Section 19(b) rule filing requirements that otherwise would apply to DECN as a facility of ISE.[14] The extended temporary conditional exemption would commence immediately and would permit the continued operation of DECN while the Commission considers the Form 1 Applications that, if approved, would allow the Exchange Subsidiaries to operate in place of DECN.[15] ISE believes that the extended temporary conditional exemption will help to ensure an orderly transition from DECN to the proposed Exchange Subsidiaries.[16]

ISE states, in addition, that the extended exemption will not diminish the Commission's ability to monitor ISE and DECN.[17] In this regard, ISE notes that to the extent that ISE makes changes to its systems, including the Facility, during the extended temporary exemption period, or thereafter, it remains subject to Section 19(b) and thus obligated to file proposed rule changes with the Commission.[18] Further, in the Exemption Request, ISE commits to satisfying certain conditions, as outlined below, which are identical to the conditions in the Exemption Order.[19] For example, as a condition to the extended temporary exemption, ISE will be required to submit proposed rule changes with respect to any material changes to DECN's functions during the

14 Id.

15 According to ISE, it would be impracticable for DECN to display its limit orders other than on the Facility. See Exemption Request at 3.

16 See Exemption Request at 2.

17 Id.

18 See Exemption Request at 2-3.

19 The ISE also represents that it has complied with the conditions in the Exemption Order and that it will continue to comply with these conditions during any extension of the relief granted in the Exemption Order. See Exemption Request at 3.

exemption period.[20] ISE notes, however, that neither ISE nor DECN anticipates any material changes to DECN's functionality during the extended temporary exemption period.[21]

III. Order Granting Extension of Temporary Conditional Section 36 Exemption

In 1996, Congress gave the Commission greater flexibility to regulate trading systems, such as DECN, by granting the Commission broad authority to exempt any person from any of the provisions of the Exchange Act and to impose appropriate conditions on their operation.[22] Specifically, NSMIA added Section 36(a)(1) to the Exchange Act, which provides that "the Commission, by rule, regulation, or order, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of [the Exchange Act] or of any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors."[23] In enacting Section 36, Congress indicated that it expected that "the Commission will use this authority to promote efficiency, competition and capital formation."[24] It particularly intended to give the Commission sufficient flexibility to respond to changing market and competitive conditions:

> The Committee recognizes that the rapidly changing marketplace dictates that effective regulation requires a certain amount of flexibility. Accordingly, the bill grants the SEC general exemptive authority under both the Securities Act and the Securities Exchange Act. This exemptive authority will allow the Commission the flexibility to explore and adopt new approaches to registration and disclosure. It will also enable the Commission to address issues relating to the securities markets more generally. For example, the SEC could deal with the regulatory

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20 See Exemption Request at note 5.

21 See Exemption Request at note 4.

22 15 U.S.C. 78mm(a). Section 36 of the Exchange Act was enacted as part of the National Securities Markets Improvements Act 1996, Pub. L. No. 104-290 ("NSMIA").

23 15 U.S.C. 78mm(a)(1).

24 H.R. Rep. No. 104-622, 104th Cong., 2d Sess. 38 (1996).

> concerns raised by the recent proliferation of electronic trading systems, which do not fit neatly into the existing regulatory framework.[25]

As noted above, in December 2008 the Commission exercised its Section 36 exemptive authority to grant ISE a temporary exemption, subject to certain conditions, from the 19(b) rule filing requirements in connection with the Transaction.[26] In 2004, the Commission granted similar exemptive relief in connection with the acquisition by The Nasdaq Stock Market, Inc. ("Nasdaq") of Brut, LLC, the operator of the Brut ECN.[27]

Section 19(b)(1) of the Exchange Act requires a self-regulatory organization ("self-regulatory organization" or "SRO"), including ISE, to file with the Commission its proposed rule changes accompanied by a concise general statement of the basis and purpose of the proposed rule change. Once a proposed rule change has been filed with the Commission, the Commission is required to publish notice of it and provide an opportunity for public comment. The proposed rule change may not take effect unless approved by the Commission by order, unless the rule change is within the class of rule changes that are effective upon filing pursuant to Section 19(b)(3)(A) of the Act.[28]

Section 19(b)(1) of the Exchange Act defines the term "proposed rule change" to mean "any proposed rule or rule change in, addition to, or deletion from the rules of [a] self-regulatory organization." Pursuant to Section 3(a)(27) and 3(a)(28) of the Exchange Act, the term "rules of a self-regulatory organization" means (1) the constitution, articles of incorporation, bylaws and rules, or instruments corresponding to the foregoing, of an SRO, and (2) such stated policies,

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25 S. Rep. No. 104-293, 104th Cong., 2d Sess. 15 (1996).

26 See Exemption Order, supra note 4.

27 See Securities Exchange Act Release No. 50311 (September 3, 2004), 69 FR 54818 (September 10, 2004).

28 15 U.S.C. 78s(b)(3)(A).

practices and interpretations of an SRO (other than the Municipal Securities Rulemaking Board) as the Commission, by rule, may determine to be necessary or appropriate in the public interest or for the protection of investors to be deemed to be rules. Rule 19b-4(b) under the Exchange Act,[29] defines the term "stated policy, practice, or interpretation" to mean generally "any material aspect of the operation of the facilities of the self-regulatory organization or any statement made available to the membership, participants, or specified persons thereof that establishes or changes any standard, limit, or guideline with respect to rights and obligations of specified persons or the meaning, administration, or enforcement of an existing rule."

The term "facility" is defined in Section 3(a)(2) of the Exchange Act, with respect to an exchange, to include "its premises, tangible or intangible property whether on the premises or not, any right to use such premises or property or any service thereof for the purpose of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service."

In its Exemption Request, ISE acknowledges that since the Closing, Merger Sub has operated the Facility as a facility of ISE.[30] Absent an exemption, Section 19(b) of the Exchange Act and Rule 19b-4 thereunder would require ISE to file proposed rules with the Commission to allow ISE to operate DECN as a facility of ISE.

In its Exemption Request, ISE notes that the Exchange Subsidiaries have filed Form 1 Applications and that DECN intends to cease operations as an ECN shortly after any Commission approval of the Form 1 Applications and the Exchange Subsidiaries'

29 17 CFR 240.19b-4(b).

30 See Exemption Request at 1. As discussed above, ISE owns a 31.54% ownership interest in DE Holdings, the sole owner of Merger Sub.

commencement of operations as national securities exchanges.[31] Accordingly, ISE expects that DECN will continue to operate as a facility of ISE for a relatively brief period of time.[32] ISE notes, in addition, that the Commission is reviewing the rules governing the operation of the Exchange Subsidiaries as part of its review of the Form 1 Applications.[33] ISE represents that it has complied with the conditions in the Exemption Order and that it will continue to comply with these conditions during an extension of the relief granted in the Exemption Order.[34]

The Commission believes that it is appropriate to grant a temporary extension of the relief provided in the Exemption Order, subject to the conditions described below, to allow DECN to continue to operate as a facility of ISE without being subject to the rule filing requirements of Section 19(b) of the Exchange Act for a temporary period.[35] Accordingly, the Commission has determined to grant ISE's request for an extension of the relief provided in the Exemption Order, subject to certain conditions, for a period not to exceed 180 days. The Commission finds that the temporary extended conditional exemption from the provisions of Section 19(b) of the Exchange Act is appropriate in the public interest and is consistent with the protection of investors. In particular, the Commission believes that the temporary extended exemption should help promote efficiency and competition in the market by allowing DECN to continue to operate as an ECN for a limited period of time while the Commission considers the Form 1 Applications. In this regard, the Commission notes ISE's belief that it would be unduly burdensome and inefficient to require DECN's operating rules to be separately subjected to the

31 See Exemption Request at 2.

32 Id.

33 Id.

34 See Exemption Request at 2.

35 In granting this relief, the Commission makes no finding regarding whether ISE's operation of DECN as a facility would be consistent with the Exchange Act.

Section 19(b) rule filing and approval process because DECN will operate only temporarily as a facility of ISE while the Commission considers the Form 1 Applications.[36] To provide the Commission with the opportunity to review and act upon any proposal to change DECN's fees or to make material changes to DECN's operations as an ECN during the period covered by the extended temporary exemption, as well as to ensure that the Commission's ability to monitor ISE and DECN is not diminished by the extended temporary exemption, the Commission is imposing the following conditions while the extended temporary exemption is in effect.[37] The Commission believes such conditions are necessary and appropriate in the public interest for the protection of investors. Therefore, the Commission is granting to ISE an extended temporary exemption, pursuant to Section 36 of the Exchange Act, from the rule filing requirements imposed by Section 19(b) of the Exchange Act as set forth above, provided that ISE and DECN comply with the following conditions:

(1) DECN remains a registered broker-dealer under Section 15 of the Exchange Act[38] and continues to operate as an ECN;

(2) DECN operates in compliance with the obligations set forth under Regulation ATS;

(3) DECN and ISE continue to operate as separate legal entities;

(4) ISE files a proposed rule change under Section 19 of the Exchange Act[39] if any material changes are sought to be made to DECN's operations. A material change

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36 In addition, the Commission notes that the rules governing the operation of the Exchange Subsidiaries will be subjected to public comment and Commission review and approval as part of the exchange registration process.

37 See Exemption Request at note 5.

38 15 U.S.C. 78o.

39 15 U.S.C. 78s.

would include any changes to a stated policy, practice, or interpretation regarding the operation of DECN or any other event or action relating to DECN that would require the filing of a proposed rule change by an SRO or an SRO facility;[40]

(5) ISE files a proposed rule change under Section 19 of the Exchange Act if DECN's fee schedule is sought to be modified; and

(6) ISE treats DECN the same as other ECNs that participate in the Facility, and, in particular, ISE does not accord DECN preferential treatment in how DECN submits orders to the Facility or in the way its orders are displayed or executed.[41]

In addition, the Commission notes that the Financial Industry Regulatory Authority is currently the Designated Examining Authority for DECN.

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40 See Section 19(b) of the Exchange Act and Rule 19b-4 thereunder. The Commission notes that a material change would include, among other things, changes to DECN's operating platform; the types of securities traded on DECN; DECN's types of subscribers; or the reporting venue for trading that takes place on DECN. The Commission also notes that any rule filings must set forth the operation of the DECN facility sufficiently so that the Commission and the public are able to evaluate the proposed changes.

41 See Exemption Request at note 5.

For the reasons discussed above, the Commission finds that the extended temporary conditional exemptive relief requested by ISE is appropriate in the public interest and is consistent with the protection of investors.

IT IS ORDERED, pursuant to Section 36 of the Exchange Act,[42] that the application for an extended temporary conditional exemption is granted for a period of 180 days, effective immediately.

By the Commission.

Elizabeth M. Murphy
Elizabeth M. Murphy
Secretary

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42 15 U.S.C. 78mm.

Commissioner Aguilar and Commissioner Paredes not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60149 / June 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13524

In the Matter of RAM CAPITAL RESOURCES, LLC, MICHAEL E. FEIN, and STEPHEN E. SALTZSTEIN Respondents.	ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Ram Capital Resources, LLC ("Ram"), Michael E. Fein, and Stephen E. Saltzstein (collectively "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the "Offers") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b) and 21C of the

Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds[1] that:

Summary

1. These proceedings arise out of Respondent Ram's role as an intermediary in the PIPEs (an acronym for "private investments in public equities") market. Specifically, from 2001 through early 2005, Respondent Ram -- through its principals, Respondents Michael E. Fein and Stephen E. Saltzstein -- engaged in the business of identifying investors for PIPE offerings. Upon identifying a PIPE offering or a potential PIPE offering, Ram solicited investors -- a majority of which were hedge funds -- to invest in the offering. The investors then compensated Ram by paying to it a certain percentage of the gross amount invested and, in most instances, allocated to Ram a certain percentage of any warrants they received as part of their investment. Ram also engaged in structuring PIPE offerings and negotiating the terms of such offerings with investors and issuers.

2. Although Respondents Fein and Saltzstein knew or should have known that Ram was required to register with the Commission as a securities broker or dealer, at no point in time did Ram register while engaging in the conduct alleged herein.

3. While acting as unregistered principals of Ram, Respondents Fein and Saltzstein were responsible for controlling the operations of Ram and were directly compensated out of the proceeds of those operations.

4. By engaging in this course of conduct, Respondents willfully violated the broker-dealer registration provisions of Section 15(a) of the Exchange Act.

Respondents

5. **Ram Capital Resources, LLC** is a New York limited liability company formed by Fein, with its principal place of business in New York, New York. During the relevant time, Fein and Saltzstein controlled and operated Ram and at no point in time was Ram registered with the Commission as a broker or dealer.

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

6. **Michael E. Fein**, age 41, is a resident of Port Washington, New York. During the relevant time, Fein served as a principal of Ram.

7. **Stephen E. Saltzstein**, age 40, is a resident of New York, New York. During the relevant time, Saltzstein served as a principal of Ram.

Background

8. Fein formed Ram in 1997 as a joint venture with a wealthy investor to identify PIPE offerings on his behalf.

9. Later in 1997, Saltzstein joined Ram as a consultant and became a principal of the firm during 2001. During the relevant time period, Saltzstein and Fein were primarily responsible for operating and controlling Ram.

10. Ram's business model focused on seeking investment opportunities within the PIPEs market and soliciting hedge funds and other investors to invest in PIPE offerings.

11. Certain participants in the PIPEs market knew of Ram's business model and its ability to gather investors that wanted to invest in PIPE offerings. Consequently, Ram was notified about pending PIPE offerings by, among others, PIPE issuers, registered broker-dealers acting as placement agents on behalf of the PIPE issuers, and interested investors.

12. In addition to learning about PIPE offerings that were already in the market or about to come to market, Ram also sought out certain issuers it believed were likely candidates for raising capital through a PIPE offering and made inquiries as to whether these issuers were interested in conducting a PIPE offering. If an issuer were interested, Ram contacted investors to see whether they wanted to participate in the PIPE. If an investor expressed interest, Ram alerted the issuer to the investor's interest and served as an intermediary between the issuer and the investor.

13. While acting as an intermediary, Ram's activities on certain occasions went beyond identifying potential PIPE opportunities for both issuers and investors. In connection with certain PIPE offerings, Ram also played a significant role in structuring, and negotiating the terms of, the PIPE offering. For example, Fein and Saltzstein often drafted and distributed to issuers and investors the initial term sheet outlining the terms of the PIPE offering.

14. Ram also advised issuers and investors about the structure of the PIPE offering, including, for example, whether the offering should be structured as a convertible debt offering or a common stock offering. Ram continued to remain involved in the offering by negotiating the terms of the relevant documents, including the securities purchase agreement.

15. Ram's sole source of revenue was generated from services it provided to PIPE investors. Typically, Ram received 3.5% of the gross amount invested by each investor it solicited, in addition to 25% percent of all warrants allocated to such investors.

16. As co-principals of Ram, Fein's and Saltzstein's compensation was directly derived from the fees Ram earned for services it provided to investors.

17. At some point during the relevant time period, Fein and Saltzstein knew or were reckless in not knowing that Ram's compensation structure for its services required Ram to register as a broker-dealer. In fact, others in the industry questioned Fein about whether Ram should be registered based on the services Ram was providing and how it was compensated for such services.

Ram, Fein, and Saltzstein Acted as Unregistered Brokers

18. Section 15(a)(1) of the Exchange Act requires a "broker" to be registered with the Commission or, if a natural person, to be associated with a registered broker-dealer, in order "to induce or attempt to induce the purchase or sale of[] any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills)" while making use of the mails or any means or instrumentality of interstate commerce. Section 3(a)(4) of the Exchange Act defines a "broker" as any person, other than a bank, "engaged in the business of effecting transactions in securities for the account of others."

19. As principals of Ram, Fein and Saltzstein played a role in providing services to PIPE investors. Specifically, through their relationships and communications with both PIPE issuers and investors, Fein and Saltzstein had involvement in structuring certain PIPE offerings and negotiating the terms of the offerings. Furthermore, they were actively involved in soliciting investors to invest in PIPE offerings. Their salaries were paid from the fees that Ram received for the services it provided to PIPE investors.

20. Based on the conduct described above, Ram acted as a broker without being registered with the Commission in connection with dozens of PIPE offerings.

21. Fein and Saltzstein acted as brokers without being registered or associated with a registered broker-dealer.

22. As a result of the conduct described above, Respondents willfully violated Section 15(a) Exchange Act.

Undertakings

23. Respondent Fein shall provide to the Commission, within thirty days after the end of the twelve (12) month suspension period described below, an affidavit that he has complied fully with the sanctions described in Section IV below.

24. Respondent Saltzstein shall provide to the Commission, within thirty days after the end of the six (6) month suspension period described below, an affidavit that he has complied fully with the sanctions described in Section IV below.

IV.

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

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondents Ram, Fein, and Saltzstein cease and desist from committing or causing any violations and any future violations of Section 15(a) of the Exchange Act.

B. Respondent Ram is censured.

C. Respondent Fein be, and hereby is, suspended from association with any broker or dealer for a period of twelve (12) months, effective on the first Monday following the entry of this Order.

D. Respondent Saltzstein be, and hereby is, suspended from association with any broker or dealer for a period of six (6) months, effective on the first Monday following the entry of this Order.

E. Respondent Fein shall pay disgorgement of $364,721, prejudgment interest of $83,657 and a civil penalty of $90,000 to the United States Treasury. Fein's payment shall be made in the following installments: (i) $82,000 within ten days of entry of this Order; (ii) $151,000 within 120 days of entry of this Order; (iii) $151,000 within 240 days of entry of this Order; and (iv) $154,378 within 364 days of entry of this Order. Respondent Saltzstein shall pay disgorgement of $364,721, prejudgment interest of $83,657 and a civil penalty of $60,000 to the United States Treasury. Saltzstein's payment shall be made in the following installments: (i) $75,000 within ten days of entry of this Order; (ii) $144,000 within 120 days of entry of this Order; (iii) $144,000 within 240 days of entry of this Order; and (iv) $145,378 within 364 days of entry of this Order. If any payment is not made by the date the payment is required by this Order, the entire outstanding balance of disgorgement, prejudgment interest, and civil penalties, plus any additional interest accrued pursuant to SEC Rule of Practice 600 or pursuant to 31 U.S.C. § 3717, shall be due and payable immediately, without further application. 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 letters that identify Michael E. Fein and Stephen E. Saltzstein as Respondents in these proceedings, the file number of these proceedings, a copy of which cover letters and money orders or checks shall be sent to Scott

Friestad, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549.

F. Respondent Fein shall comply with the undertakings enumerated in Section III, paragraph 23 above.

G. Respondent Saltzstein shall comply with the undertakings enumerated in Section III, paragraph 24 above.

By the Commission.

Elizabeth M. Murphy
Secretary

By: J. Lynn Taylor
Assistant Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60155 / June 22, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2996 / June 22, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13525

In the Matter of **ANTHONY R. RUSSO, CPA** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e)(3)(i) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Anthony R. Russo, CPA ("Respondent" or "Russo") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

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 Rule 102(e) of the Commission's Rules of Practice, 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. Russo, age 66, was a certified public accountant licensed to practice in the State of New York until his license became inactive during 2006. From August 2002 through approximately December 2003, Russo was Certified Services, Inc.'s ("Certified") Chief Executive Officer and Chief Financial Officer.

2. On March 6, 2008, the Commission filed a complaint against Russo and others in the United States District Court, Southern District of Florida. [SEC v. Anthony R. Russo, et al., Civil Action No. 08-60315-Zloch]. On May 15, 2009, the court entered an order permanently enjoining Russo, by consent, from future violations of Sections 10(b) and 13(b)(5) of the Securities Exchange Act of 1934 ("Exchange Act") and Rules 10b-5, 13a-14, 13b2-1 and 13b2-2 thereunder, and aiding and abetting violations of Sections13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 thereunder. The Court also required Russo to pay disgorgement, prejudgment interest thereon and a civil money penalty and barred him from participating in an offering of penny stock.

3. The Commission's complaint alleged, among other things, that from approximately August 2002 through at least December 2003, Respondent and others violated the anti-fraud and the books and records provisions of the federal securities laws. These violations allowed Certified and others to overstate Certified's financial condition in filings made with the Commission. In addition, Certified and others failed to disclose related party transactions. Moreover, the Commission's complaint alleged that this scheme allowed tens of millions of dollars of Certified's funds to be siphoned into shells, which were controlled by related parties.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that:

Respondent Russo is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

June 24, 2009

In the Matter of **Paivis Corp.,** **Peabodys Coffee, Inc.,** **Penge Corp.,** **Petrol Industries, Inc.** **(n/k/a Caddo International, Inc.),** **Phantom Entertainment, Inc.,** **Phoenix Medical Technology, Inc.,** **Phoenix Metals USA II, Inc.,** **(a/k/a TM Media Group, Inc.)** **Phymed, Inc.,** **Pico Products, Inc., and** **Piemonte Foods, Inc.** **File No. 500-1**	**ORDER OF SUSPENSION OF TRADING**

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Paivis Corp. because it has not filed any periodic reports since the period ended June 30, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Peabodys Coffee, Inc. because it has not filed any periodic reports since the period ended December 31, 2004.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Penge Corp. because it has not filed any periodic reports since the period ended March 31, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Petrol Industries, Inc. (n/k/a Caddo International, Inc.) because it has not filed any periodic reports since the period ended September 30, 2005.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Phantom Entertainment, Inc. because it has not filed any periodic reports since the period ended March 31, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Phoenix Medical Technology, Inc. because it has not filed any periodic reports since the period ended July 2, 2000.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Phoenix Metals USA II, Inc. (a/k/a TM Media Group, Inc.) because it has not filed any periodic reports since the period ended December 31, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Phymed, Inc. because it has not filed any periodic reports since the period ended December 31, 1999.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Pico Products, Inc. because it has not filed any periodic reports since the period ended April 30, 1999

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Piemonte Foods, Inc. because it has not filed any periodic reports since the period ended February 27, 1999.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed companies.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed companies is suspended for the period from 9:30 a.m. EDT on June 24, 2009, through 11:59 p.m. EDT on July 8, 2009.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 24, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13527

In the Matter of **Paivis Corp.,** **Peabodys Coffee, Inc.,** **Penge Corp.,** **Petrol Industries, Inc.** **(n/k/a Caddo International, Inc.),** **Phantom Entertainment, Inc.,** **Phoenix Medical Technology, Inc.,** **Phoenix Metals USA II, Inc.,** **Phymed, Inc.,** **Pico Products, Inc., and** **Piemonte Foods, Inc.** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Paivis Corp., Peabodys Coffee, Inc., Penge Corp., Petrol Industries, Inc. (n/k/a Caddo International, Inc.), Phantom Entertainment, Inc., Phoenix Medical Technology, Inc., Phoenix Metals USA II, Inc., Phymed, Inc., Pico Products, Inc., and Piemonte Foods, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Paivis Corp. (CIK No. 1076607) is a defaulted Nevada corporation located in Atlanta, Georgia with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Paivis is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 2007, which reported a net loss of over $1.55 million for the prior

nine months. As of June 16, 2009, the company's stock (symbol "PAVC") was quoted on Pink Sheets of the Pink OTC Markets, Inc. ("Pink Sheets"), had sixteen market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. Peabodys Coffee, Inc. (CIK No. 1046998) is a defaulted Nevada corporation located in Roseville, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Peabodys is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 2004, which reported a net loss of $410,342 for the prior nine months. As of June 16, 2009, the company's stock (symbol "PBDY") was quoted on the Pink Sheets, had nine market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

3. Penge Corp. (CIK No. 1222557) is a void Delaware corporation located in Midland, Texas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Penge is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 2007, which reported a net loss of over $1.59 million for the prior nine months. As of June 16, 2009, the company's stock (symbol "PNGC") was quoted on the Pink Sheets, had seven market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

4. Petrol Industries, Inc. (n/k/a Caddo International, Inc.) (CIK No. 77864) is a Nevada corporation located in Oil City, Louisiana with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Petrol Industries is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB/A for the period ended September 30, 2005. As of June 16, 2009, the company's stock (symbol "CADD") was quoted on the Pink Sheets, had sixteen market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

5. Phantom Entertainment, Inc. (CIK No. 1145019) is a Delaware corporation located in Port Chester, New York with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phantom is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 2007, which reported a net loss of over $72 million since the company's December 9, 2002 inception. As of June 16, 2009, the company's stock (symbol "PHEI") was quoted on the Pink Sheets, had fourteen market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

6. Phoenix Medical Technology, Inc. (CIK No. 745167) is a void Delaware corporation located in Andrews, South Carolina with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phoenix Medical is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended July 2, 2000, which reported a net loss of $261,249 for the prior six months. On August 21, 2000, the company filed a Chapter 11

petition in the U.S. Bankruptcy Court for the District of South Carolina, which was converted to Chapter 7, and the case was terminated on September 15, 2008. As of June 16, 2009, the company's stock (symbol "PHXT") was quoted on the Pink Sheets, had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

7. Phoenix Metals USA II, Inc. (CIK No. 1104816) is a defaulted Nevada corporation located in Carson City, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phoenix Metals is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 2001, which reported a net loss of over $7.1 million since the company's July 1, 1993 inception. On May 22, 2006, the company filed a Form 15 to voluntarily deregister its securities, but the form was invalid on its face because it was not properly signed.

8. Phymed, Inc. (CIK No. 353904) is a suspended Oklahoma corporation located in Dallas, Texas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phymed is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-KSB/A for the period ended December 31, 1999, which reported a net loss of $972,606 for the prior twelve months. As of June 16, 2009, the company's stock (symbol "PYMD") was quoted on the Pink Sheets, had three market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

9. Pico Products, Inc. (CIK No. 352994) is an inactive New York corporation located in Lakeview Terrace, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Pico is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended April 30, 1999, which reported a net loss of over $1.24 million for the prior nine months. As of June 16, 2009, the company's stock (symbol "PPIP") was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

10. Piemonte Foods, Inc. (CIK No. 813765) is a forfeited South Carolina corporation located in Greenville, South Carolina with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Piemonte is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended February 27, 1999, which reported a net loss of over $3.39 million for the prior nine months. As of June 16, 2009, the company's stock (symbol "PIFI") was quoted on the Pink Sheets, had three market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

B. DELINQUENT PERIODIC FILINGS

11. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1), have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of

Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

12. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

13. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

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

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities of the Respondents identified in Section II registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened 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 HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, 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, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

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.

Elizabeth M. Murphy
Secretary

Attachment

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

Appendix 1

Chart of Delinquent Filings
In the Matter of Paivis Corp., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Paivis Corp.					
	10-KSB	09/30/07	12/31/07	Not filed	18
	10-QSB	12/31/07	2/14/08	Not filed	16
	10-QSB	03/31/08	5/15/08	Not filed	13
	10-QSB	06/30/08	8/14/08	Not filed	10
	10-KSB	09/30/08	12/29/08	Not filed	6
	*10-Q**	12/31/08	2/17/09	Not filed	4
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**7**				
Peabodys Coffee, Inc.					
	10-KSB	03/31/05	06/29/05	Not filed	48
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-QSB	12/31/05	02/14/06	Not filed	40
	10-KSB	03/31/06	06/29/06	Not filed	36
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-QSB	12/31/06	02/14/07	Not filed	28
	10-KSB	03/31/07	06/29/07	Not filed	24
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	02/14/08	Not filed	16
	10-KSB	03/31/08	06/30/08	Not filed	12
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-Q**	12/31/08	02/17/09	Not filed	4
Total Filings Delinquent	**16**				
Penge Corp.					
	10-KSB	06/30/07	9/28/07	Not filed	21
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	2/14/08	Not filed	16
	10-QSB	03/31/08	5/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Penge Corp.	*10-KSB*	06/30/08	9/29/08	Not filed	9
(continued)	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-Q**	12/31/08	2/17/09	Not filed	4
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**8**				
Petrol Industries, Inc. (n/k/a Caddo International, Inc.)					
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**14**				
Phantom Entertainment, Inc.					
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	04/01/09	Not filed	2
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**5**				
Phoenix Medical Technology, Inc.					
	10-QSB	09/30/00	11/14/00	Not filed	103
	10-KSB	12/31/00	04/02/01	Not filed	98
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Phoenix Medical Technology, Inc.	*10-QSB*	09/30/01	11/14/01	Not filed	91
(continued)	*10-KSB*	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75
	10-QSB	03/31/03	05/15/03	Not filed	73
	10-QSB	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**35**				
Phoenix Metals USA II, Inc.					
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-KSB	06/30/02	09/30/02	Not filed	81
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-QSB	12/31/02	02/14/03	Not filed	76
	10-QSB	03/31/03	05/15/03	Not filed	73

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Phoenix Metals USA II, Inc.	*10-KSB*	06/30/03	09/29/03	Not filed	69
(continued)	*10-QSB*	09/30/03	11/14/03	Not filed	67
	10-QSB	12/31/03	02/17/04	Not filed	64
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-KSB	06/30/04	09/28/04	Not filed	57
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-QSB	12/31/04	02/14/05	Not filed	52
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-KSB	06/30/05	09/28/05	Not filed	45
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-QSB	12/31/05	02/14/06	Not filed	40
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-KSB	06/30/06	09/28/06	Not filed	33
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-QSB	12/31/06	02/14/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-KSB	06/30/07	09/28/07	Not filed	21
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-QSB	12/31/07	02/14/08	Not filed	16
	10-QSB	03/31/08	05/15/08	Not filed	13
	10-KSB	06/30/08	09/29/08	Not filed	9
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-Q**	12/31/08	02/17/09	Not filed	4
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**29**				
Phymed, Inc.					
	10-QSB	03/31/00	05/15/00	Not filed	109
	10-QSB	06/30/00	08/14/00	Not filed	106
	10-QSB	09/30/00	11/14/00	Not filed	103
	10-KSB	12/31/00	04/02/01	Not filed	98
	10-QSB	03/31/01	05/15/01	Not filed	97
	10-QSB	06/30/01	08/14/01	Not filed	94
	10-QSB	09/30/01	11/14/01	Not filed	91
	10-KSB	12/31/01	04/01/02	Not filed	86
	10-QSB	03/31/02	05/15/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	79
	10-KSB	12/31/02	03/31/03	Not filed	75

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Phymed, Inc.	*10-QSB*	03/31/03	05/15/03	Not filed	73
(continued)	*10-QSB*	06/30/03	08/14/03	Not filed	70
	10-QSB	09/30/03	11/14/03	Not filed	67
	10-KSB	12/31/03	03/30/04	Not filed	63
	10-QSB	03/31/04	05/17/04	Not filed	61
	10-QSB	06/30/04	08/16/04	Not filed	58
	10-QSB	09/30/04	11/15/04	Not filed	55
	10-KSB	12/31/04	03/31/05	Not filed	51
	10-QSB	03/31/05	05/16/05	Not filed	49
	10-QSB	06/30/05	08/15/05	Not filed	46
	10-QSB	09/30/05	11/14/05	Not filed	43
	10-KSB	12/31/05	03/31/06	Not filed	39
	10-QSB	03/31/06	05/15/06	Not filed	37
	10-QSB	06/30/06	08/14/06	Not filed	34
	10-QSB	09/30/06	11/14/06	Not filed	31
	10-KSB	12/31/06	04/02/07	Not filed	26
	10-QSB	03/31/07	05/15/07	Not filed	25
	10-QSB	06/30/07	08/14/07	Not filed	22
	10-QSB	09/30/07	11/14/07	Not filed	19
	10-KSB	12/31/07	03/31/08	Not filed	15
	*10-Q**	03/31/08	05/15/08	Not filed	13
	*10-Q**	06/30/08	08/14/08	Not filed	10
	*10-Q**	09/30/08	11/14/08	Not filed	7
	*10-K**	12/31/08	03/31/09	Not filed	3
	*10-Q**	03/31/09	05/15/09	Not filed	1
Total Filings Delinquent	**37**				
Pico Products, Inc.					
	10-K	07/31/99	10/29/99	Not filed	116
	10-Q	10/31/99	12/15/99	Not filed	114
	10-Q	01/31/00	03/16/00	Not filed	111
	10-Q	04/30/00	06/14/00	Not filed	108
	10-K	07/31/00	10/30/00	Not filed	104
	10-Q	10/31/00	12/15/00	Not filed	102
	10-Q	01/31/01	03/19/01	Not filed	99
	10-Q	04/30/01	06/14/01	Not filed	96
	10-K	07/31/01	10/29/01	Not filed	92
	10-Q	10/31/01	12/17/01	Not filed	90
	10-Q	01/31/02	03/18/02	Not filed	87

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Pico Products, Inc.	*10-Q*	04/30/02	06/14/02	Not filed	84
(continued)	*10-K*	07/31/02	10/29/02	Not filed	80
	10-Q	10/31/02	12/16/02	Not filed	78
	10-Q	01/31/03	03/17/03	Not filed	75
	10-Q	04/30/03	06/16/03	Not filed	72
	10-K	07/31/03	10/29/03	Not filed	68
	10-Q	10/31/03	12/15/03	Not filed	66
	10-Q	01/31/04	03/16/04	Not filed	63
	10-Q	04/30/04	06/14/04	Not filed	60
	10-K	07/31/04	10/29/04	Not filed	56
	10-Q	10/31/04	12/15/04	Not filed	54
	10-Q	01/31/05	03/17/05	Not filed	51
	10-Q	04/30/05	06/14/05	Not filed	48
	10-K	07/31/05	10/31/05	Not filed	44
	10-Q	10/31/05	12/15/05	Not filed	42
	10-Q	01/31/06	03/17/06	Not filed	39
	10-Q	04/30/06	06/14/06	Not filed	36
	10-K	07/31/06	10/30/06	Not filed	32
	10-Q	10/31/06	12/15/06	Not filed	30
	10-Q	01/31/07	03/19/07	Not filed	27
	10-Q	04/30/07	06/14/07	Not filed	24
	10-K	07/31/07	10/29/07	Not filed	20
	10-Q	10/31/07	12/17/07	Not filed	18
	10-Q	01/31/08	03/17/08	Not filed	15
	10-Q	04/30/08	06/16/08	Not filed	12
	10-K	07/31/08	10/29/08	Not filed	8
	10-Q	10/31/08	12/15/08	Not filed	6
	10-Q	01/31/09	03/17/09	Not filed	3
	10-Q	04/30/09	06/15/09	Not filed	0
Total Filings Delinquent	**40**				
Piemonte Foods, Inc.					
	10-K	05/29/99	8/27/99	Not filed	118
	10-Q	08/28/99	10/12/99	Not filed	116
	10-Q	11/27/99	1/11/00	Not filed	113
	10-Q	02/26/00	4/11/00	Not filed	110
	10-K	06/03/00	9/1/00	Not filed	105
	10-Q	09/02/00	10/17/00	Not filed	104
	10-Q	12/02/00	1/16/01	Not filed	101

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Piemonte Foods, Inc.	*10-Q*	03/03/01	4/17/01	Not filed	98
(continued)	*10-K*	06/02/01	8/31/01	Not filed	94
	10-Q	09/02/01	10/17/01	Not filed	92
	10-Q	12/01/01	1/15/02	Not filed	89
	10-Q	03/02/02	4/16/02	Not filed	86
	10-K	06/01/02	8/30/02	Not filed	82
	10-Q	08/31/02	10/15/02	Not filed	80
	10-Q	11/30/02	1/14/03	Not filed	77
	10-Q	03/01/03	4/15/03	Not filed	74
	10-K	05/31/03	8/29/03	Not filed	70
	10-Q	08/30/03	10/14/03	Not filed	68
	10-Q	11/29/03	1/13/04	Not filed	65
	10-Q	02/28/04	4/13/04	Not filed	62
	10-K	05/29/04	8/27/04	Not filed	58
	10-Q	08/28/04	10/12/04	Not filed	56
	10-Q	11/27/04	1/11/05	Not filed	53
	10-Q	02/26/05	4/12/05	Not filed	50
	10-K	05/28/05	8/26/05	Not filed	46
	10-Q	08/27/05	10/11/05	Not filed	44
	10-Q	11/26/05	1/10/06	Not filed	41
	10-Q	02/25/06	4/11/06	Not filed	38
	10-K	05/27/06	8/25/06	Not filed	34
	10-Q	08/26/06	10/10/06	Not filed	32
	10-Q	11/25/06	1/9/07	Not filed	29
	10-Q	02/24/07	4/10/07	Not filed	26
	10-K	06/02/07	8/31/07	Not filed	22
	10-Q	09/01/07	10/16/07	Not filed	20
	10-Q	12/01/07	1/15/08	Not filed	17
	10-Q	03/01/08	4/15/08	Not filed	14

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Piemonte Foods, Inc. (Continued)	*10-K*	05/31/08	8/29/08	Not filed	10
	10-Q	08/30/08	10/14/08	Not filed	8
	10-Q	11/29/08	1/13/09	Not filed	5
	10-Q	02/28/09	4/15/09	Not filed	2
Total Filings Delinquent	**40**				

*Regulation S-B and its accompanying forms, including Forms 10-QSB and 10-KSB, have been removed from the federal securities laws. *See* Release No. 34-56994 (Dec. 19, 2007). The removal took effect over a transition period that concluded on March 15, 2009. All reporting companies that previously filed their periodic reports on Forms 10-QSB and 10-KSB are now required to use Forms 10-Q and 10-K instead. Forms 10-QSB and 10-KSB will no longer be available, though issuers that meet the definition of a "smaller reporting company" (generally, a company that has less than $75 million in public equity float as of the end of its most recently completed second fiscal quarter) have the option of using new, scaled disclosure requirements that Regulation S-K now includes.

Chairman Schapiro and Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60170 / June 25, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3000 / June 25, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13528

In the Matter of **CHRISTI R. SULZBACH,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Christi R. Sulzbach ("Respondent" or "Sulzbach") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any attorney . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

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 her and the subject matter of these proceedings, and the findings contained in Section III.3. below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Sulzbach, age 54, is and has been an attorney licensed to practice in the State of California. She served as chief compliance officer, executive vice president and general counsel of Tenet Healthcare Corporation ("Tenet") from February 1999 until her termination in September 2003.

2. Tenet was, at all relevant times, a Nevada corporation which maintained its principal executive offices in Santa Barbara, California. At all relevant times, its common stock was registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the New York and Pacific Stock Exchanges.

3. On June 18, 2009, a final judgment was entered against Sulzbach, permanently enjoining her 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, and aiding and abetting violations of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13 thereunder, in the civil action entitled Securities and Exchange Commission v. Tenet Healthcare Corp., et. al, Civil Action Number CV-07-2144 RSWL (RZx), in the United States District Court for the Central District of California. Sulzbach was also ordered to pay $1 in disgorgement of ill-gotten gains and a $120,000 civil money penalty.

4. The Commission's first amended complaint ("complaint") alleges, among other things, that from 1999 through 2002, Tenet and certain of its officers engaged in an unsustainable strategy to improve Tenet's earnings by deliberately exploiting a loophole in Medicare's reimbursement system which allowed Tenet to obtain significantly greater Medicare outlier payments by aggressively increasing its gross charges. The complaint further alleges that Tenet's failure to disclose its unsustainable pricing strategy and its impact on Tenet's Medicare revenues resulted in Tenet filing a materially false and misleading annual report on Form 10-K for its fiscal year ended May 31, 2002, and materially false and misleading quarterly reports on Form 10-Q for the third quarter of its fiscal year 2002 ending February 28, 2002, and the first quarter of its fiscal year 2003 ending August 31, 2002; and a materially false and misleading prospectus supplement on June 21, 2002, in connection with an offering of $400 million of debt securities registered pursuant to a Form S-3 registration statement that had been filed by Tenet in December 2001, which prospectus supplement incorporated by reference, among other filings, Tenet's false and misleading third quarter 2002 Form 10-Q. The complaint further alleges that Sulzbach was substantially involved in preparing, reading, reviewing and approving Tenet's

public reports with the Commission and the prospectus supplement. The complaint further alleges that Sulzbach knew, or was reckless in not knowing, about Tenet's unsustainable strategy to aggressively increase its gross charges in order to inflate its Medicare outlier revenues. In particular, the complaint alleges that as early as 1999, Tenet personnel approached Sulzbach with questions and concerns regarding the legality of implementing the gross charge increases that triggered additional outlier payments, and that by 2002, Sulzbach had requested, received, and discussed data showing that Tenet's outlier payments were a significant portion of its Medicare revenue.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that:

Sulzbach is suspended from appearing or practicing before the Commission as an attorney.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Commissioner Casey not participating

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 60180 / June 26, 2009

Admin. Proc. File No. 3-13096

In the Matter of the Application of

HUSKY TRADING LLC,
EUGENE O'BRIEN,
MICHAEL INEMER,
and
STEPHEN FLOIRENDO

c/o Paula D. Shaffner, Esq.
Stradley Ronon Stevens & Young, LLP
2600 One Commerce Square
Philadelphia, PA 19103

For Review of Disciplinary Action Taken by the

PHILADELPHIA STOCK EXCHANGE, INC.

OPINION OF THE COMMISSION

NATIONAL SECURITIES EXCHANGE – REVIEW OF DISCIPLINARY PROCEEDING

Trading Through Quotations

Failure to Honor Priority

National securities exchange member organization and its president and two employees were charged with trading through the NBBO and the PBBO and with failing to allocate trades to parties with established price and/or time priority. *Held*, disciplinary action of the exchange *set aside*.

APPEARANCES:

Paula D. Shaffner, of Stradley Ronon Stevens & Young, LLP, for Husky Trading LLC, Eugene O'Brien, Michael Inemer, and Stephen Floirendo.

Mark Schepps and *Eustace T. Francis*, for NASDAQ OMX PHLX, Inc. (f/k/a Philadelphia Stock Exchange, Inc.).[1]

Appeal filed: July 24, 2008
Last brief received: October 21, 2008

I.

Husky Trading LLC ("Husky"), a member organization of the Philadelphia Stock Exchange, Inc. (the "PHLX" or the "Exchange"); Eugene O'Brien, Husky's principal, president, and a floor broker; and Michael Inemer and Stephen Floirendo, floor brokers employed by Husky (collectively, "Applicants"), appeal from PHLX disciplinary action. The PHLX found that, on 172 occasions during the period from January 1, 2005 to November 20, 2006 (the "Relevant Period"), Husky violated Exchange Rules 1014, 1067, and 119 or 120, as applicable, which also constituted conduct inconsistent with just and equitable principles of trade, in violation of Exchange Rule 707.[2] Specifically, the PHLX found that, during the Relevant Period, O'Brien executed fifty-two option transactions, Inemer six option transactions, and Floirendo twenty-nine

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[1] On July 24, 2008, the Philadelphia Stock Exchange, Inc. was acquired by the NASDAQ OMX Group, Inc. and renamed NASDAQ OMX PHLX, Inc. *See* Press Release, Philadelphia Stock Exchange, NASDAQ OMX Group to Complete Acquisition of The Philadelphia Stock Exchange (Jul. 24, 2008), *available at http://www.phlx.com/news/pr2008/08pr072408.asp*. Because the disciplinary action taken here was instituted before that date, we continue to use the designation PHLX. References to Exchange rules herein are to the applicable PHLX rules.

[2] Exchange Rule 1014 sets forth the obligations and restrictions applicable to specialists and registered options traders and addresses, among other things, how option contracts are to be allocated in the crowd among market participants who are on parity.

Exchange Rule 1067 provides that the "highest bid and lowest offer shall have precedence in all cases."

Exchange Rule 119 provides that the "highest bid shall have precedence in all cases" and sets forth rules for determining the priority and precedence of bids that have been made at the same price.

Exchange Rule 120 provides that the "lowest offer shall have precedence in all cases" and that, where offers are made at the same price, the priority and precedence are to be determined in the same manner as specified in the case of bids in Rule 119.

Exchange Rule 707 prohibits conduct inconsistent with just and equitable principles of trade.

option transactions in which the execution price traded through the Philadelphia Best Bid or Offer ("PBBO")[3] and/or the National Best Bid or Offer ("NBBO").[4] The PHLX also found that, during the Relevant Period, O'Brien executed twenty option orders, Inemer five option orders, and Floirendo six option orders that traded ahead of customer orders on the Limit Order Book (the "Book").[5] The PHLX found further that, during the Relevant Period, O'Brien executed thirty-four option transactions, Inemer eleven option transactions, and Floirendo nine option transactions that traded ahead of Streaming Quote Traders ("SQT")[6] and/or Remote Streaming Quote Traders ("RSQT")[7] with established priority.[8] The PHLX held that Husky, as a member organization, was liable for the violations of its employees, O'Brien, Inemer, and Floirendo.[9] The PHLX found that O'Brien, as president and the principal of Husky, and as the supervisor of

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[3] The PBBO is the highest bid and lowest offer disseminated by the Exchange at any given time in a particular option class and constitutes the prevailing bid-offer spread for each security trading on the PHLX at a given time. *See* PHLX Rules 119-120, and 1067. *See generally* Securities Exchange Act Release No. 58,099 (July 3, 2008), 73 Fed. Reg. 39,769 (July 10, 2008) (notice of filing of File No. SR-PHLX-2008-5) ("July 2008 Notice").

[4] The NBBO is the highest bid and lowest offer disseminated by all the options exchanges at any given time in a particular option class and constitutes the prevailing highest bid and lowest offer for each security across all exchanges at a given time. *See* PHLX Rule 1085; *see generally* July 2008 Notice, *supra* note 3, at 39,770.

[5] The Book is the Exchange's automated limit order book. The Book automatically routes all unexecuted AUTOM (the Exchange's electronic order delivery, routing, execution, and reporting system) orders to the Book and displays orders real-time in order of price-time priority. *See* Exchange Act Release No. 50997 (Jan. 7, 2005), 70 Fed. Reg. 2444 (Jan. 13, 2005) (order approving File No. SR-PHLX 2003-40 at n.13). Orders not delivered through AUTOM also may be entered onto the Book. *Id.*

[6] "Streaming" is the electronic delivery of bids and offers. An SQT is a Market Maker or Registered Options Trader who generates and delivers quotations electronically.

[7] An RSQT is an SQT who is not located on the Exchange floor.

[8] Husky and O'Brien were also charged with supervisory failure under Exchange Rule 748, but the Hearing Panel found that the Exchange failed to satisfy its burden of proof with respect to this charge.

[9] As relevant here, Exchange Rule 960.1(b) permits a member organization to be charged with any violation within the Exchange's disciplinary jurisdiction committed by the member organization's officers, employees, or associated persons, "as though such violation were its own."

Inemer and Floirendo, was liable for the violations of Husky, Inemer, and Floirendo, respectively.[10]

The PHLX imposed fines of (a) $106,000 on Husky and O'Brien, jointly and severally, based upon the 106 transactions charged to O'Brien; (b) $22,000 on Inemer, Husky, and O'Brien, jointly and severally, based upon the twenty-two transactions charged to Inemer; and (c) $44,000 on Floirendo, Husky, and O'Brien, jointly and severally, based upon the forty-four transactions charged to Floirendo.

The PHLX also suspended O'Brien for two months, Inemer for two weeks, and Floirendo for two weeks, with the suspensions to run consecutively, first Inemer, next Floirendo, and then O'Brien. The PHLX specified that O'Brien's suspension was to continue until the monetary penalties had been paid in full to the Exchange.[11]

We base our findings on an independent review of the record. For the reasons set forth more fully below, we set aside PHLX's action.

II.

A. Background

O'Brien, who has worked in the securities industry for more than twenty-three years, started Husky. Husky's client base consists of large financial institutions and over-the-counter broker dealers. During the Relevant Period, Husky's trades averaged 1,000 options contracts per trade. Husky's trading volume at the Exchange was approximately 2.5 million options per month, or 100,000 - 150,000 options per day.

B. Delta Neutral Stock-Tied Option Transactions

Approximately ninety-five percent of Husky's business involved delta neutral stock-tied option transactions, which are the type of transaction at issue in this proceeding. A stock-tied option transaction is a type of contingent trade. A contingent trade is a "multi-component trade involving orders for a security and a related derivative . . . that are executed at or near the same

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[10] As relevant here, Exchange Rule 960.1(b) permits a person employed by or associated with a member organization to be charged with any violation within the Exchange's disciplinary jurisdiction committed by employees under his supervision or by the member organization with which he is associated, "as though such violations were his own."

[11] The Commission stayed Applicants' sanctions. *Husky Trading LLC*, Order Granting Stay, Admin. Proc. File No. 3-13096 (July 30, 2008).

time."[12] In a stock-tied option order, the ratio of option to stock depends on the number of shares necessary to offset the option position, and may vary. The economics of a contingent trade are based on the relationship between the prices of the underlying security and the related derivative.[13] The sought-after spread or ratio between the relevant instruments is known and specified at the time of the order, and that ratio remains fixed regardless of the prevailing price of each instrument at the time of execution.[14] Thus, the parties to a contingent trade will not execute one side of the trade without the other component or components being executed in full and at the specified spread or ratio.[15] Husky executed delta neutral stock-tied option transactions at various ratios of option to stock.

During the Relevant Period, the PHLX, unlike other options exchanges, had no rules addressing the trading of delta neutral stock-tied option orders. Instead, PHLX's rules referred to "synthetic options," a type of stock-tied option order defined as an order to buy or sell options and the underlying stock or Exchange-Traded Fund Share ("ETF share") such that the stock or ETF shares would offset the option position on a one-to-one basis, *i.e.*, one option contract to 100 shares of the underlying stock or ETF.[16] Less than one percent of Husky's business involved synthetic options, as defined by PHLX.

At the hearing, the parties stipulated to the manner in which each trade at issue was handled:

> Husky floor broker enters the PHLX options trading crowd with an options order tied to stock. Husky communicates the terms of the order to trading crowd participants, which contain an options leg price ("OLP") tied to a stock leg price ("SLP"), the Delta, that results in a net debit or credit ratio. Members of the crowd who wish to participate in the options tied to stock trade reach agreement. Husky promptly submits the stock leg of the trade to a non-PHLX stock execution venue. The stock execution venue executes the

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[12] *See* Exchange Act Rel. No. 54389 (Aug. 31, 2006), 71 Fed. Reg. 52,829 (Sept. 7, 2006) (order exempting qualified contingent trades from Exchange Act Rule 611(a)).

[13] *Id.*

[14] *Id.*

[15] *Id.*

[16] *See* former PHLX Rule 1066(g) (defining synthetic options); *see also* PHLX Rules 1066(g), 1033(e), and OFPA F-14 (rules applicable to synthetic options). In November 2007, the PHLX revised the definition of "Synthetic Option" in PHLX Rule 1066(g) to accommodate delta neutral stock-option orders. *See* Exchange Act Rel. No. 56,760 (Nov. 7, 2007), 72 Fed. Reg. 64,268 (Nov. 15, 2007) (order approving File No. SR-PHLX-2007-40) ("2007 Order").

stock portion of the trade and reports back the stock execution price to Husky. If the price differs from the SLP, an adjustment to the OLP is required. Husky reports the options leg price to the tape, and at the time of the tape report the options leg price was, on the occasions alleged by the Exchange, either: 1.) at a price that is at or outside the NBBO or PBBO of the options, or 2.) at a price that is at or below the price of a booked limit order to buy the options, or at or above the price of a booked limit order to sell the options, or 3.) at a price that is at or below the price of a remote streamer's bid price, or at or above a remote streamer's offer price, in the options.

O'Brien testified that he consulted with Floor Officials or Option Committee Members about how to conduct certain trades. He testified that, for the execution of stock-tied option transactions, a PHLX Head Floor Official "directed" him to PHLX Rule OFPA F-14 ("Rule F-14"), which provides in part:

> In the case of a synthetic option order, the trade may be immediately executed at a single credit or debit which is superior to the aggregate price of the established market for the individual legs (on a buy-on-the-offer and sell-on-the-bid basis), provided that the option leg is executed at a price better than the established bid/offer for that option contract . . . .
>
> [O]nce the credit or debit execution price to a hedge or synthetic option order is agreed upon, the stock portion of the order, if any, must be effected prior to the execution of the option portion and participants must promptly match the individual option legs for trade reporting.

O'Brien testified that Husky patterned the execution of its delta neutral stock-tied option transactions after Rule F-14. O'Brien analogized his reliance on Rule F-14 to a "sporting event . . . like the Phillies game, even though there is a red light, there is a cop outside waving you through, it is the same structure." O'Brien did not state when he sought the advice, did not identify the floor officials, did not explain what he told the floor officials about the transaction, and did not elaborate on the advice that he received.[17] No floor official testified.

C. The Options Floor Brokerage Management System

In 2000, the Commission ordered the options exchanges, including the PHLX, to design and implement an accurate, time-sequenced, consolidated audit trail system to enable the Exchange to reconstruct markets promptly, effectively monitor them, and enforce order handling,

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[17] O'Brien's testimony suggests that some of these conversations may have occurred after PHLX Market Surveillance challenged Husky transactions.

firm quote, trade reporting, and other rules.[18] In response, the PHLX created the Options Floor Broker Management System ("FBMS").[19] FBMS is designed to enable floor brokers and/or their employees to enter, route, and report transactions stemming from option orders received on the Exchange.[20] Upon the execution of an order, the floor broker is required to enter the time of execution of the trade into the FBMS.[21] The resulting trading records comprise the electronic order audit trail. Applicants stipulated to the accuracy of the FBMS data.

D. Proceedings Below

On December 12, 2006, the PHLX issued a statement of charges against Husky only, charging a single count of failure to honor order priority. On March 19, 2007, the PHLX amended its statement of charges to include O'Brien, Inemer, and Floirendo as individual applicants. This new statement charged Applicants with trading through the NBBO and/or the PBBO and with failure to honor order priority, and also charged Husky and O'Brien with supervisory failures.[22]

The Hearing Panel's decision was based largely on FBMS trading records documenting the trades at issue in the proceeding. The Hearing Panel found that, based on the execution times provided to FBMS by Applicants, Applicants executed eighty-seven transactions that traded through the PBBO and/or the NBBO and that seventy-six of those trade-through violations were based on execution times provided by Applicants. The Hearing Panel concluded that, because Exchange rules require floor brokers or their employees to enter the time of execution of the trade promptly into the FBMS, it was "reasonable to conclude that the execution time entered into the FBMS was at or about the time of actual execution of the trade." The Hearing Panel

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18 *See* Order Instituting Public Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Exchange Act Rel. No. 43268 (Sept. 11, 2000), 73 SEC Docket 697, 709.

19 FBMS is a component of AUTOM. AUTOM provides for the automatic entry and routing of equity option and index option orders to the Exchange trading floor. *See* Order Relating to the Options Floor Broker Management System, 84 SEC Docket 2473, 2474 n.10. Equity option and index option specialists are required by the Exchange to participate in AUTOM. *Id.*

20 *See id.* at 2474. The PHLX issues to floor brokers "Handhelds," portable electronic devices that function as FBMS terminals, on which they are required to enter such option order information as the order type, the option symbol, and the nature of the transaction – buy, sell, cross, or cancel.

21 *Id.*

22 *See supra,* note 8.

noted further that, because Applicants chose not to provide the execution times in the FBMS for four of the remaining eleven trade through violations, the Exchange was forced to rely on the tape report time to establish the time of trade execution. In addition, the Hearing Panel observed that, for the remaining seven of those eleven trade-through violations, the market for the options at issue never traded at any time during the life of the order at the price at which the option was executed and reported to the tape.

The Hearing Panel found that on thirty-one occasions Applicants traded ahead of customer orders on the Book. The Hearing Panel noted that, in 2006, Husky settled allegations that Husky had traded ahead of a customer order on the Book in violation of Exchange rules during the period of January 13, 2004 through June 30, 2005.[23] The Hearing Panel concluded that this settlement put Applicants on notice of the Exchange's position that floor brokers have an independent obligation to not execute transactions that trade ahead of booked customer orders.

The Hearing Panel also concluded that on fifty-four occasions, Applicants traded ahead of SQT and/or RSQT orders. In thirty-seven of those instances, SQTs or RSQTs had already posted their quotes and therefore established priority before Applicants had received the applicable orders from their clients. The Hearing Panel observed that, for ten of the remaining transactions, the streamers posted their quotes after Applicants' receipt of orders but before Applicants reported the transactions to the tape. The Hearing Panel noted that in each of those ten instances, Applicants had failed to record the actual execution time. The Hearing Panel concluded that, as a result, the tape report time of those ten trades constituted the best available evidence of the time of execution for purposes of evaluating priority. In addition, the Hearing Panel noted that, for the remaining seven transactions, some streamers posted their quotes before, and some after, Husky received the orders for representation. For the sum of these violations, the Hearing Panel imposed the monetary sanctions described above and suspensions of six months on O'Brien, three weeks on Inemer, and six weeks on Floirendo.

On appeal, the Board affirmed the Hearing Panel's findings of fact and conclusions of law and the monetary sanctions it had imposed, but reduced the length of the suspensions to two months on O'Brien, two weeks on Inemer, and two weeks on Floirendo. The Board's Advisory Committee, which had heard oral argument, had noted that the Hearing Panel decision did not explain how the suspensions would protect the trading public from harm, and the Board accordingly found that the suspensions were "not supported by substantial evidence and are arbitrary, capricious, or an abuse of discretion on the part of the [Hearing] Panel." However, the Board also did not explain the basis for the length of the suspensions it imposed.

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[23] *In the Matter of Husky Trading LLC*, Enf. No. 2006-02 (June 22, 2006). The trading ahead charge at issue in this settled proceeding also involved a delta neutral stock-tied transaction.

III.

A. Regulatory Framework

In general, PHLX rules require that all trades at the Exchange be executed at a price that is at or better than the highest bid or lowest offer.[24] Execution of a trade at a price that is inferior to the highest available bid or the lowest available offer is called a "trade through." Exchange Rule 1085 generally prohibits trade throughs of the NBBO "[a]bsent reasonable justification" and during normal market conditions, although it sets forth ten exceptions to the prohibition against trading through the NBBO.[25] There are no exceptions under PHLX rules that permit trading through the PBBO.

Pursuant to Exchange Rules 119 and 120, bids (or offers), including SQT and RSQT quotations, that are made at the same price generally are prioritized according to the time they are made, with the earliest-entered bids (or offers) taking precedence. Trades that disregard these priority and precedence restrictions are said to "trade ahead" of those orders with established priority. Exchange Rule 1014(g)(i)(A) further prohibits broker-dealer orders from trading ahead of customer orders.

Applicants do not dispute that, at the time the execution of the option leg of each delta neutral stock-tied option transaction was reported to the tape, the trades at issue entered by Applicants traded through and/or traded ahead. Applicants, however, argue that their trades should nonetheless not be deemed violative of PHLX rules. We address their arguments in turn.

B. Trading Through

1. Applicants argue that their delta neutral stock-tied options were a kind of synthetic option. They contend that the trading of synthetic options is covered by Rule F-14, and thus their trades were permitted. However, as discussed earlier, during the Relevant Period, former Exchange Rule 1066(g) limited the term "synthetic option" to stock-tied options with option-to-stock ratios of one-to-one. Since the delta neutral stock-tied option transactions at issue were not synthetic options as defined by former Rule 1066(g), Rule F-14 did not apply to Applicants' trades during the Relevant Period.

Applicants assert in their brief that, if Husky's delta neutral stock-tied options are not deemed synthetic options, "Husky's millions of delta neutral stock-tied options trades – ninety-five percent of Husky's business – are entirely beyond the scope of the business permitted by the PHLX. This is not, and cannot be, correct." However, the exclusion of delta neutral stock-tied

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24 *See* PHLX Rules 119-120, and 1067.

25 *See* PHLX Rule 1085(b). Applicants do not argue that any of these exceptions are applicable to their transactions.

option orders from the definition of "synthetic option" did not place delta neutral orders "entirely beyond the scope of business permitted by the PHLX." It merely excluded them from PHLX rules applicable to synthetic options, including Rule F-14.[26]

2. In the alternative, Applicants assert that Husky "reasonably relied on the guidance of PHLX floor officials to apply Rule F-14" for the execution of Husky's delta neutral trades. As noted, O'Brien testified that he sought advice from unidentified Exchange floor officials during the Relevant Period regarding how to effect Husky's stock-tied option transactions, and that the floor officials "waved them through," directing Applicants to follow Rule F-14.

The record includes no evidence of who O'Brien may have spoken with when the conversations occurred, or what O'Brien told them about the structure of the trades for which he sought guidance. Beyond stating that he was "directed" to Rule F-14, O'Brien did not describe what the floor officials said to him. Nor did Applicants call floor officials to testify on this point. Thus, for example, if O'Brien asserted to floor officials then, as Applicants insist now, that the trades were synthetic options, then directing Applicants to Rule F-14 would have been an appropriate response, albeit not the correct one for the delta neutral transactions at issue.[27] The record is insufficient to permit a conclusion as to the reasonableness of any reliance Applicants may have placed on any advice of floor officials. In any event, O'Brien did not suggest that he had been told that he could trade through the established PBBO.

Moreover, even if Rule F-14 applied to these transactions, Applicants did not comply with the rule's requirements. Rule F-14(d) provides a three-step process: first, there is agreement in the crowd as to the terms of the tied transaction, *i.e.*, the price of both the stock and the options legs, which determines the net debit or credit of the tied trade; second, the stock trade is

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[26] Applicants also suggest that the PHLX disciplinary action against them is tantamount to a denial of access to the Exchange's services, citing *William J. Higgins*, 48 S.E.C. 713 (1987) (setting aside Exchange's denial of request to install telephones to enable communications with non-members away from the trading floor). Of the nearly 76,000 trades involving over 57 million options contracts conducted by Husky during the Relevant Period, the PHLX charged and found that only 172 trades were in violation of PHLX rules. The PHLX has not denied Applicants access to PHLX services for any delta neutral trade; it has sanctioned Applicants because a small minority of their trades did not comply with PHLX's rules.

[27] The Exchange's witnesses both testified that floor officials do not have the authority to make prospective rulings on the applicability of Exchange rules to transactions on the floor. We previously have held that erroneous advice from self-regulatory organization ("SRO") officials does not relieve regulated persons of their duty to comply with SRO rules. *B.R. Stickle & Co.*, 51 S.E.C. 1022, 1025 (1994). We have also stated that members and their associated persons cannot shift their compliance obligations to SRO officials. *See Schon-Ex, LLC*, Exchange Act Rel. No. 57857 (May 23, 2008), 93 SEC Docket 6195, 6204 n.21 and authorities cited therein.

executed; and third, the option leg is executed. As Applicants note, between the time crowd agreement is reached and the time the option leg is executed, the market may have moved. If this happens, and the stock leg has been executed, the only way to preserve the agreed-upon net debit or credit would be to adjust the price of the option. However, Rule F-14 states that the option leg of a synthetic option order must be "executed at a price better than the established bid/offer for that option contract." Accordingly, Rule F-14, by its terms, does not authorize any adjustment to the option price if such an adjustment would result either in a trade through of the PBBO at the time the options order is executed or in trading ahead of an order with priority.

3. Applicants argue that:

> Husky could not refuse to execute half of a tied trade and ignore the option piece of the trade if the stock price had changed. The PHLX had no cancellation rule that would have permitted cancellation of the entire trade after market movement in the stock price . . . . Without a cancellation rule, the operation of Rule F-14 made adjusting the option the only reasonable alternative.

Assuming that Applicants are correct that they could not cancel the option leg of the transaction in the absence of a PHLX rule permitting a cancellation, that absence does not justify non-compliance with existing applicable PHLX rules. Applicants could have structured the stock leg as a contingent trade or asked the contra-party to cancel voluntarily. If those remedies were not adequate, Applicants should have sought to change the PHLX's rules, not to violate them.

4. Rule 1085(a) prohibits trading through the NBBO unless there is "reasonable justification." Applicants contend that the "reasonable justification" language provides an additional exception to the ten exceptions enumerated in Rule 1085(b) because, in their view, the term "reasonable justification" otherwise would be rendered meaningless.

> They claim their trading through was reasonably justified because it was a virtually inevitable result of executing a large delta neutral trade with multiple components on different exchanges . . . . [I]n a delta neutral trade the net debit or credit ratio must be maintained. Husky reasonably believed that Rule F-14 . . . applied. Husky reasonably believed . . . that the stock component was executed first The PHLX had no cancellation rule applicable to these trades. Consequently . . . if the option leg "traded through" when posted to the tape, there was reasonable justification.

However, as noted above, the absence of a cancellation rule does not justify their conduct. Further, on the record before us, Applicants have failed to demonstrate that their reliance on Rule F-14(d) was reasonable. In any event, Rule 1085 does not permit trading through the PBBO.

Applicants note that current Rule 1083 now defines "complex trades" to include delta neutral transactions such as theirs.[28] Applicants assert that, accordingly, the enumerated exception for "complex trades" in Rule 1085(b) is now applicable to delta neutral transactions. However, the enumerated exceptions in Rule 1085(b) are only for trading through the NBBO. The proscription against trading through the PBBO is sacrosanct, and no exemption is provided anywhere in the PHLX rules. Of the eighty-seven trading-through transactions at issue, seventy would still have traded through the PBBO and only seventeen would have been exempted from trading through the NBBO pursuant to the amended rules.

Applicants also argue that PHLX justified this amendment of its rules to the Commission as "modernizing" the rule to "reflect actual practice."[29] They claim this language shows that the PHLX has recognized that Applicants' trades were occurring on the PHLX and were reasonable. In approving the amendment, however, we noted that the new definition of "Complex Trade" was "consistent with the definition of Complex Trade adopted by other Linkage Plan Participants" and could "increas[e] the number of markets in which customers may execute such orders,"[30] suggesting that the actual practice to which the PHLX intended to conform its rules was that of other Linkage Plan Paricipants.

C. Trading Ahead

1. Applicants assert that PHLX's decision that they traded ahead of SQTs and RSQTs is unsupported by evidence because its electronic audit trail does not show whether the SQT or RSQT "stepped aside" or yielded priority to Applicants. The audit trail evidence indicates that SQT and RSQT orders had priority over theirs for the trades alleged, establishing a *prima facie* case that they violated Rules 119 and 120.

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[28] The PHLX amended Rule 1083 in November 2007 to include within the definition of Complex Trade "the execution of a stock option order ('synthetic option order') to buy or sell a stated number of units of an underlying stock . . . coupled with the purchase or sale of option contract(s) on the other side of the market representing," among other things, "the number of units of the underlying stock . . . necessary to create a delta neutral position . . . ." *See* 2007 Order, *supra* note 16.

[29] *Id.*

[30] Exchange Act Rel. No. 56760 (Nov. 7, 2007), 91 SEC Docket 3101, 3101. *See, e.g.*, Chicago Board Options Exchange Rule 6.80 (including delta neutral transactions in definition of "Complex Trade"). The Linkage Plan is a national market system plan for the operation of the Intermarket Option Linkage.

Applicants had the burden going forward to establish any affirmative defense.[31] O'Brien testified at the hearing that Husky had "gone out of [its] way in numerous situations to find[] streamers, to find the representation of the Market Maker who's streaming, and asking him if he wants to do the trade." O'Brien stated that he was not aware that any SQT or RSQT had complained either that its priority had not been honored or that O'Brien traded ahead of its orders without an agreement to do so. However, O'Brien conceded that he did not document what occurred with SQTs or RSQTs with respect to any of the transactions at issue. Although witnesses testified that the audit trail would reflect step asides, there is no other evidence in the record that SQTs or RSQTs yielded priority to Husky. We find that PHLX's findings are supported by a preponderance of the evidence.

2. Applicants do not dispute PHLX's findings that they traded ahead of public customer orders as alleged. Rather, they attempt to avoid liability by shifting blame to the specialist. O'Brien testified that he did not see whether there were customer orders on the Book and that he "would have to think that the specialist would have a responsibility, since he is charging the order on the [B]ook, to tell us whether it is a bid or offer by a customer," and that the specialist "has a fiduciary responsibility to honor that best bid and that best offer for that customer if it is on the [B]ook."

Rule 1014(g)(i)(A) states that accounts under common control with a broker-dealer "are required to yield priority to customer orders when competing at the same price." The rule thus places an onus on the broker-dealer to yield priority to a public customer. Moreover, we agree with PHLX that the 2005 settlement of disciplinary charges involving findings that Husky traded ahead of customer orders on the Book put Applicants on notice of this obligation.

D. Notice of Applicability of Rules to the Transactions at Issue

Applicants argue that there was "rampant confusion about when the trade was actually 'executed,'" *i.e.*, whether the trade was executed (for purposes of determining trade through and trading ahead issues) at the time of crowd agreement, or at the time of the execution of the option leg of the transaction. Applicants note that, during the hearing, there was disagreement among the witnesses on this point. Moreover, while the Hearing Panel majority concluded that the relevant time was the execution of the option leg, one member dissented and expressed the view that the time of crowd agreement controlled, although the basis of his dissent is not clear from the Hearing Panel decision.

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[31] *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953) (stating that "imposition of the burden of proof" on a party "who would plead the exemption seems for us fair and reasonable" (internal citations omitted)); *Donald T. Sheldon*, 51 S.E.C. 59, 77 n.70 (1992), *aff'd*, 45 F. 3d 1515 (11th Cir. 1995).

As an initial matter, we note that the PHLX Board affirmed the Hearing Panel majority. Thus, that majority view was the final decision of the PHLX. We review the final decision.[32] We agree with PHLX that it was appropriate to separate the elements of Husky's delta neutral transactions and deem execution to occur upon entry of the option leg on AUTOM. The view rejected by PHLX that the time of crowd agreement should control may have been useful historically, when trading on exchanges occurred solely in open outcry auctions, and exchanges may have recognized the existence of binding oral contracts formed when the crowd reached agreement but before the agreement was reported or recorded. However, with the implementation of automated trading systems such as AUTOM, and the need to integrate an exchange's open outcry market with such systems, the rules governing the use of trading using these systems have evolved. We believe PHLX reasonably construed its rules as requiring the execution time of the options leg of the delta neutral transactions to be the basis for determining trade through and trading ahead liability.

We are concerned, however, that the disagreement among the witnesses testifying at the hearing, and among the Hearing Panel members, indicates that some level of uncertainty may have existed during the Relevant Period concerning the correct interpretation of PHLX's rules. These circumstances raise a question whether, during the Relevant Period, Applicants were properly on notice that their conduct was violative. While the proper application of PHLX rules is now clarified with the issuance of this opinion, under the circumstances of this case we believe that it is appropriate to set aside the PHLX's action.

An appropriate order will issue.[33]

By the Commission (Chairman SCHAPIRO and Commissioners WALTER, AGUILAR, and PAREDES); Commissioner CASEY not participating.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

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[32] *See, e.g., Schon Ex*, 93 SEC Docket at 6206 n.25 (noting the Exchange board had affirmed sanctions choice of the majority of hearing panel, and that Commission reviewed that final decision).

[33] 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. 60180 / June 26, 2009

Admin. Proc. File No. 3-13096

In the Matter of the Application of

HUSKY TRADING LLC,
EUGENE O'BRIEN,
MICHAEL INEMER,
and
STEPHEN FLOIRENDO

c/o Paula D. Shaffner, Esq.
Stradley Ronon Stevens & Young, LLP
2600 One Commerce Square
Philadelphia, PA 19103

For Review of Disciplinary Action Taken by the

PHILADELPHIA STOCK EXCHANGE, INC.

ORDER SETTING ASIDE DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES EXCHANGE

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

ORDERED that the disciplinary action of the Philadelphia Stock Exchange, Inc. against Husky Trading LLC, Eugene O'Brien, Michael Inemer, and Stephen Floirendo be, and it hereby is, set aside.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 2896 / June 26, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13530

In the Matter of MARK R. HAMLIN, Respondent.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO 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 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against Mark R. Hamlin ("Hamlin" 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 203(f) of the 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. Hamlin is 28 years old and resides in Okemos, Michigan. Hamlin is the owner and President of Kingdom First Corp. and Kingdom First Trading, LLC ("KFT"). From approximately April 2005 through June 2008, Hamlin, individually, and through Kingdom First Corp., offered and sold securities to at least 90 investors and raised approximately $2 million. From April 2005 through June 2008, Hamlin acted as an unregistered investment adviser in connection with these activities.

2. On May 29, 2009, a final judgment was entered by consent against Hamlin, permanently enjoining him from future violations of Sections 5(a), 5(c) and 17(a) of the Securities Act of 1933 ("Securities Act"), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") 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. Mark R. Hamlin, Kingdom First Trading, LLC, and Kingdom First Corp., Civil Action Number 1:09-cv-483, in the United States District Court for the Western District of Michigan.

3. The Commission's complaint alleged, among other things, that Hamlin represented to investors that he was a day trader and that he would invest their funds, along with other investors' funds, in the stock market, and that he would send the investors weekly reports of his trading and their profits or losses. The complaint also alleged that in the weekly trading reports, Hamlin represented that the investors earned profits in all but seven weeks of trading. The complaint alleged that, contrary to his representations, among other things, Hamlin invested only $1,248,370 of the approximately $2 million that he received from the investors. The complaint further alleged that Hamlin subsequently transferred approximately $627,000 from his and KFT's brokerage accounts into his bank accounts and used this money, along with the $759,000 in investor funds that he never invested, to meet $755,000 in investor withdrawal requests and to pay $668,000 in personal expenses. The complaint also alleged that from April 2005 through June 2008, Hamlin's trading resulted in losses of approximately $644,862. The complaint alleged that Hamlin's trading was profitable during only nine of the 39 months of the offering, and generated a total of only $22,150 in profit.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act, that Respondent Hamlin be, and hereby is barred from association with any investment adviser.

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.

Elizabeth M. Murphy
Secretary

By: J. Lynn Taylor
Assistant Secretary

Commissioner Aguilar and Commissioner Paredes not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60181 / June 26, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3002 / June 26, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13529

In the Matter of **WARREN B. SCHMIDGALL,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, 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 against Warren B. Schmidgall ("Respondent" or "Schmidgall") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

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.3. below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, 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. Schmidgall, age 58, is a resident of Oakbrook Terrace, IL 60181. Schmidgall served as chief financial officer of American Italian Pasta Company ("AIPC") from November 1998 until August 2004. Schmidgall also served as an executive vice president of AIPC from September 2004 until September 2005, when he left the company. Schmidgall passed the Uniform Certified Public Accountant ("CPA") exam and has held a CPA certificate from Illinois since 1980, but has never held a CPA license.

2. At all relevant times, AIPC was a Delaware corporation with its principal place of business in Kansas City, Missouri. AIPC is a producer and marketer of dry pasta. At all relevant times, AIPC's common stock was registered pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"). The company filed annual, quarterly, and current reports with the Commission on Forms 10-K, 10-Q, and 8-K, respectively. AIPC stock was traded on the New York Stock Exchange ("NYSE") until December 20, 2006, when the NYSE suspended trading based on AIPC's failure to keep current its Commission filings. The NYSE filed a Form 25 on April 23, 2007 and, as a result, AIPC's common stock was deregistered from Section 12(b) effective April 23, 2007. In June 2008, AIPC filed the quarterly and annual reports that it had failed to timely file and has been current in its filings with the Commission since that time.

3. On October 22, 2008, the Commission filed its amended complaint against Schmidgall in United States District Court for the Western District of Missouri (Civil Action No. 4:08-cv-0067). On June 22, 2009, the court entered an order permanently enjoining Schmidgall, by consent, from future violations of Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5, 13a-14, 13b2-1, and 13b2-2 thereunder, and from aiding and abetting violations of Sections 13(a) and 13(b)(2) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11, and 13a-13 thereunder. The court further ordered that Schmidgall pay $28,500 in disgorgement; $9,788 in prejudgment interest; and a $100,000 civil money penalty. The court further ordered that Schmidgall be barred from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act.

4. The Commission's amended complaint alleged, among other things, that Schmidgall and others at AIPC engaged in a fraudulent scheme that hid from the investing public the true financial state of the company by filing materially false and misleading statements in the company's annual reports on Forms 10-K, quarterly reports on Forms 10-Q, and current reports on Forms 8-K for AIPC's fiscal years 2002, 2003, and 2004. The complaint alleged that to meet aggressive external targets, Schmidgall and others engaged in numerous fraudulent accounting practices that departed from generally accepted accounting principles ("GAAP"), including, among other things, capitalizing improperly millions of dollars of normal operating costs; understating improperly millions of dollars of trade promotion expenses; overstating improperly by millions of dollars the company's spare parts inventory; recognizing improperly millions of dollars of current period revenue on sales of products that were not shipped until after the end of the current periods; structuring round-trip cash transactions; eliminating improperly the company's vacation and paid time off liability; failing improperly to expense operating costs; and failing improperly to expense manufacturing variances.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that Schmidgall is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-60194; International Series Release No. 1311)

June 30, 2009

Order under Section 36 of the Securities Exchange Act of 1934 Granting an Exemption from Exchange Act Section 6(h)(1) for Certain Persons Effecting Transactions in Foreign Security Futures and under Exchange Act Section 15(a)(2) and Section 36 Granting Exemptions from Exchange Act Section 15(a)(1) and Certain Other Requirements

I. Introduction and Background

The Commodity Futures Modernization Act of 2000 ("CFMA")[1] authorized the trading of futures on individual stocks and narrow-based stock indexes, i.e., security futures.[2] The CFMA defined security futures products[3] as "securities" under the Exchange Act,[4] the Securities Act of 1933 ("Securities Act"),[5] the Investment Company Act of 1940,[6] and the Investment Advisers Act of 1940,[7] and as contracts of sale for future delivery under the CEA.[8] Accordingly, the regulatory framework established by the CFMA provides the Securities and Exchange Commission ("Commission") and the Commodity Futures Trading Commission ("CFTC") with joint jurisdiction over security futures products. Futures on broad-based security indexes

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1 Pub. L. No. 106-554, 114 Stat. 2763 (2000).

2 A security future is defined in Section 3(a)(55)(A) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. 78c(a)(55)(A), and Section 1a(31) of the Commodity Exchange Act ("CEA"), 7 U.S.C. 1a(31).

3 A security futures product is defined as a security future or any put, call, straddle, option, or privilege on any security future. See Section 3(a)(56) of the Exchange Act, 15 U.S.C. 78c(a)(56), and Section 1a(32) of the CEA, 7 U.S.C. 1a(32).

4 Section 3(a)(10) of the Exchange Act, 15 U.S.C. 78c(a)(10).

5 Section 2(a)(1) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. 77b(a)(1).

6 Section 2(a)(36) of the Investment Company Act of 1940, 15 U.S.C. 80a-2(a)(36).

7 Section 202(a)(18) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-2(a)(18).

8 Section 1a(31) of the CEA, 7 U.S.C. 1a(31).

(security indexes that are not narrow-based), and options on such futures, remain under the exclusive jurisdiction of the CFTC. To distinguish between futures on narrow-based security indexes and futures on broad-based security indexes, the CFMA also amended the CEA and the Exchange Act to add an objective definition of a narrow-based security index.[9] This definition applies both to security indexes that underlie futures contracts listed and traded in the United States and those that underlie futures contracts traded on or subject to the rules of a foreign board of trade.[10]

The CFMA also added Section 6(h)(1) to the Exchange Act,[11] which makes it unlawful for any person to effect transactions in security futures products that are not listed on a national securities exchange or a national securities association registered pursuant to Section 15A(a) of the Exchange Act.[12] Because of this prohibition, U.S. persons are currently unable to enter into

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9 See Section 1a(25) of the CEA, 7 U.S.C. 1a(25), and Section 3(a)(55)(B) and (C) of the Exchange Act, 15 U.S.C. 78c(a)(55)(B) and (C). See also Rules 3a55-1 and 3a55-2 under the Exchange Act, 17 CFR 240.3a55-1 and 240.3a55-2; Rules 41.11, 41.12, and 41.13 under the CEA, 17 CFR 41.11, 41.12, and 41.13; and Securities Exchange Act Release No. 44724 (August 20, 2001), 66 FR 44490 (August 23, 2001).

10 See Rule 3a55-3 under the Exchange Act, 17 CFR 240.3a55-3; Rule 41.13 under the CEA, 17 CFR 41.13; and Securities Exchange Act Release No. 44724, supra note 9.

11 15 U.S.C. 78f(h)(1).

12 15 U.S.C.78o-3(a). The Exchange Act and the CEA also require that any security underlying a security future listed on a national securities exchange or national securities association, including each component security of a narrow-based security index, be registered under Section 12 of the Exchange Act. See Section 6(h)(3)(A) of the Exchange Act, 15 U.S.C. 78f(h)(3)(A), and Section 2(a)(1)(D)(i)(I) of the CEA, 7 U.S.C. 2(a)(1)(D)(i)(I). Accordingly, if the securities that compose foreign security indexes listed on or subject to the rules of a foreign board of trade are not registered under Section 12 of the Exchange Act, absent relief, a national securities exchange or national securities association would not be able to list and trade a security future based on such an index. The Exchange Act and CEA also require that securities underlying security futures be equity securities. Section 6(h)(3)(D) of the Exchange Act, 15 U.S.C. 78f(h)(3)(D), and Section 2(a)(1)(D)(i)(III) of the CEA, 7 U.S.C. 2(a)(1)(D)(i)(III). The Commission and the CFTC have exercised their authority pursuant to Sections 1a(25)(B)(vi) and 2(a)(1)(D) of the CEA and Sections 3(a)(55)(C)(vi), 3(b), 6(h), 23(a),

contracts for narrow-based index or single stock futures traded on or subject to the rules of a foreign board of trade.

The Food, Conservation and Energy Act of 2008 requires the Commission, the CFTC, or both, as appropriate, to take action under their existing authorities to permit, by June 30, 2009, the trading of futures on certain security indexes by resolving issues related to foreign security indexes.[13] The exemption the Commission is issuing today fulfills this statutory directive on the part of the Commission.

The Commission understands that institutional investors could use futures on foreign securities and foreign security indexes for, among other things, risk management and asset allocation. In particular, in connection with the Commission's rulemaking in 2001 relating to the definition of narrow-based security index and exclusions from that definition,[14] commenters expressed strong views that U.S. investors, particularly institutional investors, need to be able to trade in futures on foreign security indexes for risk management, asset allocation, and other purposes, and would suffer substantial adverse impact and competitive disadvantage with respect to non-U.S. investors if they could not trade such products.[15]

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and 36 of the Exchange Act, to adopt rules to allow security futures on debt securities and debt securities indexes under certain conditions. 7 U.S.C. 1a(25)(B)(vi) and 2(a)(1)(D) and 15 U.S.C. 78c(a)(55)(C)(vi), 78c(b), 78f(h), 78w(a), and 78mm. See Securities Exchange Act Release No. 54106 (July 6, 2006), 71 FR 39534 (July 13, 2006).

13 Pub. L. No. 110-246, Sec. 13, 106, 122 Stat. 1651, 2197 (2008), reprinted in Notes to 7 U.S.C.A. Sec. 2.

14 See Securities Exchange Act Release Nos. 44288 (May 9, 2001), 66 FR 27560 (May 17, 2001), and 44724, supra note 9.

15 See e.g., Comment Letters from Barclay's Global Investors, N.A., dated July 17, 2001; Futures Industry Association, dated July 18, 2001; General Motors Investment Management Corporation, dated June 11, 2001; The Goldman Sachs Group and its subsidiaries, dated July 18, 2001; and The Montreal Exchange, dated June 14, 2001 (cited in Securities Exchange Act Release No. 44724, supra note 9).

Under the federal securities laws, a primary mandate of the Commission is investor protection. In the Commission's view, the federal securities laws are intended to protect U.S. investors and capital markets (including purchasers in those markets, whether U.S. or foreign).[16] For instance, in protecting the U.S. capital markets and investors purchasing in those markets, Congress and the Commission have recognized that the ongoing dissemination of accurate information by issuers about themselves and their securities is essential to the effective operation of the trading markets. The Exchange Act and underlying rules have established a system of ongoing disclosure about issuers that have offered securities to the public, or that have securities that are listed on a national securities exchange or are broadly held by the public.[17] A public issuer's Exchange Act record provides the basic source of information to the market and to potential purchasers regarding the issuer and its management, business, financial condition, and prospects.[18]

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16 For example, under the "territorial approach" to Section 5 of the Securities Act, the registration of securities under the Securities Act is intended to provide that protection to U.S. markets and U.S. investors. Further, in order to "protect investors and securities markets," under the Commission's territorial approach to Section 15 of the Exchange Act, absent an exemption, broker-dealer registration is generally required by "foreign broker-dealers that, from outside the United States, induce or attempt to induce trades by any person in the United States." See Registration Requirements for Foreign Broker-Dealers, Securities Exchange Act Release No. 27017 (July 11, 1989), 54 FR 30013 (July 18, 1989) at 30017.

17 The Exchange Act rules require public issuers to make periodic disclosures at annual and quarterly intervals, with other important information reported on a more current basis. Because of the enactment of the Sarbanes-Oxley Act, 15 U.S.C. 7201 et seq., and the Commission's subsequent rulemaking and interpretive actions, the disclosure included in issuers' Exchange Act filings has been enhanced significantly. See, e.g., Securities Act Release Nos. 8124 (August 28, 2002), 67 FR 57276 (September 9, 2002); 8220 (April 9, 2003), 68 FR 18788 (April 16, 2003); 8238 (June 5, 2003), 68 FR 36636 (June 18, 2003); and 8400 (March 16, 2004), 69 FR 15594 (March 25, 2004). See also Foreign Issuer Reporting Enhancements, Securities Exchange Act Release No. 58620 (September 23, 2008), 73 FR 58300 (October 6, 2008).

18 Because an issuer's Exchange Act reports and other publicly available information form the basis for the market's evaluation of the issuer and the pricing of its securities,

In many circumstances, however, the reasonable expectation of participants in the global markets justifies reliance on laws applicable in jurisdictions outside the U.S. to establish requirements for transactions effected offshore. In this context, this "territorial approach" generally recognizes the primacy of the laws in which a market is located.[19] Thus, the Exchange Act periodic reporting requirements for issuers, including foreign issuers, with securities traded in U.S. markets, do not extend to securities of foreign issuers traded only in foreign markets if such issuers are not otherwise subject to Exchange Act reporting requirements. The Commission historically has sought to balance the information needs of investors with the public interest served by opportunities to invest in a variety of securities, including foreign securities, and believes that such an approach is appropriate in the context of permitting certain persons to engage in security futures transactions involving foreign securities.

Generally, Section 36 of the Exchange Act[20] authorizes the Commission – by rule, regulation, or order – to conditionally or unconditionally exempt any person, security, transaction (or any class or classes of persons, securities, or transactions) from any provision or provisions of the Exchange Act or any rule or regulation thereunder, to the extent such exemption is necessary or appropriate in the public interest and is consistent with the protection

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investors in the secondary market use that information in making their investment decisions.

19 See Securities Act Release No. 6863 (April 24, 1990), 55 FR 18306 (May 2, 1990) ("Regulation S Adopting Release"). This territorial approach to the application of the registration provisions, however, does not affect the broad reach of the antifraud provisions of the federal securities laws. As the Commission noted in the Regulation S Adopting Release, "[t]he antifraud provisions have been broadly applied by the courts to protect U.S. investors and investors in U.S. markets where either significant conduct occurs within the United States ....or the conduct occurs outside the United States but has a significant effect within the United States or on the interests of U.S. investors...." Id. at 18308-18309.

20 15 U.S.C. 78mm.

of investors. As discussed more fully below, pursuant to Section 36 the Commission is exempting, under certain conditions, from Section 6(h)(1) of the Exchange Act certain persons that effect transactions in security futures overlying foreign securities traded on or subject to the rules of a foreign board of trade. All other applicable provisions of the federal securities laws, including the antifraud provisions, will continue to apply to such transactions.

In addition, as discussed more fully below, the Commission is exempting certain foreign brokers or dealers from the registration requirements of Section 15(a)(1) of the Exchange Act and certain other requirements. Such foreign brokers or dealers remain subject to all other applicable provisions of the federal securities laws, including, without limitation, Section 10(b) of the Exchange Act[21] and Rule 10b-5 thereunder.[22] The Commission is granting the exemption pursuant to Section 15(a)(2) of the Exchange Act (which authorizes the Commission, by rule or order, as it deems consistent with the public interest and the protection of investors, to conditionally or unconditionally exempt from Section 15(a)(1) of the Exchange Act any broker or dealer or class of brokers or dealers specified in such rule or order) and Section 36 of the Exchange Act, in order to facilitate transactions contemplated by the exemption from Section 6(h)(1) of the Exchange Act.

II. Exemption from Section 6(h)(1) of the Exchange Act

The Commission finds that it is appropriate in the public interest and consistent with the protection of investors to grant an exemption from Section 6(h)(1) of the Exchange Act to permit certain persons to effect transactions in certain foreign security futures on foreign boards of trade. Specifically, the exemption permits, under certain conditions specified below, the following persons to effect transactions in security futures that are traded on or subject to the

21 15 U.S.C. 78j(b).

22 17 CFR 240.10b-5.

rules of a foreign board of trade: (1) qualified institutional buyers ("QIBs") as defined in Rule 144A under the Securities Act;[23] (2) persons that are not U.S. persons under Rule 902 of Regulation S of the Securities Act ("non-U.S. persons");[24] (3) registered brokers or dealers that effect transactions on behalf of QIBs or non-U.S. persons; and (4) banks, as defined in Section 3(a)(6) of the Exchange Act,[25] acting pursuant to an exception or exemption from the definition of "broker" or "dealer" in Sections 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Exchange Act or the rules thereunder ("Eligible Bank"),[26] to effect transactions on behalf of QIBs or non-U.S. persons.

As described more fully below, the exemption permits such persons to effect transactions in security futures that are not listed on a national securities exchange or a national securities association registered pursuant to Section 15A(a) of the Exchange Act, under the following conditions:

<u>Types of Security Futures.</u>

- If the security future is on a single security:
    - The underlying security must be (1) issued by a foreign private issuer and have its primary trading market outside the U.S., or (2) a note, bond, debenture, or evidence of indebtedness ("debt") security issued or guaranteed by a foreign government that is eligible to be registered with the Commission under Schedule B of the Securities Act.[27]

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23 See Rule 144A(a)(1), 17 CFR 230.144A(a)(1).

24 See Rule 902(k) of Regulation S, 17 CFR 230.902(k).

25 15 U.S.C. 78c(a)(6).

26 15 U.S.C. 78c(a)(4)(B), 15 U.S.C. 78c(a)(4)(E), or 15 U.S.C. 78c(a)(5)(C).

27 See Schedule B, 15 U.S.C. 77aa.

- If the security future is on a narrow-based security index:
  - At least 90 percent of the underlying securities in the index, at the time of the transaction, both in terms of the number of underlying securities and their weighting in the index, must be (1) issued by foreign private issuers where the primary trading market of each such underlying security is outside the U.S., or (2) debt securities issued or guaranteed by a foreign government that are eligible to be registered with the Commission under Schedule B of the Securities Act;[28] and
  - No more than 10 percent of the number and weighting of securities in the index at the time of the transaction can fail to meet the above criteria, and the issuers of such securities must be required to file reports with the Commission pursuant to Section 13 or Section 15(d) of the Exchange Act.[29]

Foreign Exchange.

- The transaction must be effected on, or be subject to the rules of, an exchange or contract market that is not required to register with the Commission under Section 5 of the Exchange Act.[30]

Clearance and Settlement Outside the U.S.

- The security future must not result in physical delivery in the U.S. of the securities underlying the contract and must be cleared and settled outside the U.S.; and
- A position in the security future must not be able to be closed or liquidated by effecting an offsetting transaction on or through the facility of any exchange or association registered in the U.S. under Section 6 or 15A of the Exchange Act, respectively.

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28 Id. See also infra notes 46-51 and accompanying text.

29 15 U.S.C. 78m and 78o(d).

30 See infra notes 52-53 and accompanying text.

A. Types of Persons Covered by the Exemption

The Commission believes that it is necessary and appropriate in the public interest and for the protection of investors to limit the persons who may rely on this exemption because it is possible that the securities underlying a foreign security future may not be registered under Section 12 of the Exchange Act. For this reason, only the following persons are exempt from Section 6(h)(1) of the Exchange Act:

- QIBs;
- Non-U.S. persons;
- Brokers or dealers registered under Section 15(b) of the Exchange Act[31] to the extent that they effect transactions on behalf of QIBs or non-U.S. persons; and
- Eligible Banks[32] to the extent that they effect transactions on behalf of QIBs or non-U.S. persons.[33]

For purposes of this exemption, a broker or dealer or Eligible Bank that effects transactions on behalf of a QIB or a non-U.S. person engaged in trading security futures must reasonably believe that such person is a QIB or a non-U.S. person.[34]

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31 A broker or dealer registered with the Commission pursuant to Section 15(b)(11) of the Exchange Act may rely on this exemption to engage in transactions in foreign security futures to the same extent as a broker or dealer registered with the Commission pursuant to Section 15(b)(1) of the Exchange Act. <u>See</u> <u>infra</u> notes 57-68 and accompanying text.

32 <u>See</u> <u>supra</u> note 26 and accompanying text.

33 A broker or dealer or Eligible Bank acting for its own account would not be able to rely on the exemption in this order unless such broker, dealer, or Eligible Bank is a QIB in its own right.

34 <u>See</u> Rule 144A under the Securities Act, 17 CFR 230.144A, for certain non-exclusive means to satisfy this condition for QIBs.

As discussed above,[35] the registration requirements under Section 12 of the Exchange Act, together with the reporting requirements under Section 13 of the Exchange Act, underlie the full disclosure regime administered by the Commission. These registration and reporting requirements are intended to benefit and protect all investors, both institutions and individual investors.

The Commission nevertheless believes that subject to certain conditions, it is appropriate to permit certain sophisticated investors to trade security futures based on securities of foreign private issuers that are not subject to the reporting requirements of the Exchange Act. In particular, the Commission believes that, with regard to transactions in security futures based on foreign security indexes that may include unregistered securities of foreign private issuers, some of which may be non-reporting issuers, QIBs are sufficiently sophisticated and have enough resources to identify the information that they require to make their investment decisions and to obtain that information, and to engage in transactions not subject to the registration requirements of the U.S. securities laws.[36] The Commission also believes it is appropriate to exempt non-U.S. persons from Section 6(h)(1) of the Exchange Act because such persons do not have the expectation that the U.S. securities laws would apply to their transactions in such security futures traded on non-U.S. boards of trade.

The Commission reminds market participants that, absent registration under the Securities Act, when a QIB or non-U.S. person engages in a transaction pursuant to this

35 See supra notes 16-19 and accompanying text.

36 For certain purposes, QIBs have been deemed to be within the classes of persons that have such knowledge and experience that they are capable of fending for themselves and thus do not need the full protections of the registration provisions of the Securities Act nor the benefits of the full issuer reporting provisions of the Exchange Act. See Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities under Rules 144 and 145, Securities Act Release No. 6862 (April 23, 1990), 55 FR 17933 (April 30, 1990) ("Rule 144A Adopting Release"). See also infra note 39.

exemption, the offer and sale of the security future must be exempt from such registration.[37] The statutory exemption from registration in Section 3(a)(14) of the Securities Act is unavailable for offers and sales of security futures that are not cleared by a registered clearing agency or listed on a registered national securities exchange.[38] The offer and sale of the security future must, therefore, be made in reliance on another exemption from registration, such as the exemption in Section 4(2) of the Securities Act for offerings not involving public offerings[39] or the safe harbor provisions of Regulation D or Regulation S, provided the conditions of those safe harbors, including the restrictions on general solicitation and general advertising, are satisfied.[40]

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37 In addition, if the offer or sale of a security future is by or on behalf of the issuer of the underlying security, an affiliate of the issuer of the underlying security, or an underwriter, the offer or sale of the security future would be an offer or sale of the underlying security as well, as to which the registration provisions of the Securities Act would apply, unless an available exemption existed. See Section 2(a)(3) and Section 5 of the Securities Act, 15 U.S.C. 77b(a)(3) and 77e. See also Commission Guidance on the Application of Certain Provisions of the Securities Act of 1933, the Securities Exchange Act of 1934, and Rules thereunder to Trading in Security Futures Products, Securities Act Release No. 8107 (June 21, 2002), 67 FR 43234 (June 27, 2002).

38 15 U.S.C. 77c(a)(14).

39 Transactions that do not involve any public offering are exempt from federal registration under Section 4(2) of the Securities Act. The Securities Act does not define these transactions. The U.S. Supreme Court, however, set the basic criteria for the Section 4(2) exemption in SEC v. Ralston Purina Co., 346 U.S. 119 (1953). The Court indicated that the application of the non-public offering exemption depended on whether the offerees were able to fend for themselves and had access to the same kind of information that would be disclosed in registration. The Court noted that such persons, by virtue of their knowledge, would not need to rely on the protections afforded by registration. See Securities Act Release No. 8041 (December 19, 2001), 66 FR 66839 (December 29, 2001) at text accompanying note 22. In adopting Rule 144A (which is a resale exemption from registration) in 1990, the Commission determined that QIBs were in the category of persons able to fend for themselves and had access to the same kind of information that would be disclosed in registration. See Rule 144A Adopting Release, supra note 36.

40 See Regulation D, 17 CFR 230.501 et seq., and Regulation S, 17 CFR 230.901 et seq. While the exemption in this order applies to transactions in foreign security futures by QIBs, as defined in Rule 144A, as well as non-U.S. persons, as defined in Regulation S, the exemption or safe harbor relied on in offering or selling a foreign security future to such persons may, but need not, be Regulation S. Rule 144A would not apply to the offer

B. Types of Security Futures in Which Transactions May Be Effected

The exemption is conditioned on the type of security or securities underlying the security futures. In particular, the security future must overlie a single security of, or security index predominantly composed of securities of, foreign private issuers where the securities' primary trading market is outside the U.S., or debt securities of a government or political subdivision of a foreign country. This condition is intended to exclude from the exemption security futures based on unregistered securities that are more appropriately considered under the federal securities laws as securities of U.S. companies that should be registered under the federal securities laws. Moreover, the Commission intends this condition, which requires the security or securities underlying the security future to be foreign securities, to prevent this exemption from being used to avoid U.S. federal securities laws or facilitating a secondary market in the U.S. in securities that may not have been registered under the Securities Act or the Exchange Act.[41]

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and sale of a security future because Rule 144A only applies to resale transactions (see 17 CFR 230.144A), whereas, the offer or sale of a security future is an offering by the clearing agency on or through the facilities of the exchange, not a resale transaction.

In analyzing the availability of an exemption or safe harbor from such registration requirements, the Commission provided some guidance in the General Statement in Regulation S by providing that any offer, offer to sell, sale, or offer to buy that occurs within the United States is subject to Section 5 of the Securities Act, while any such offer or sale that occurs outside the United States is not subject to Section 5. The determination as to whether a transaction is outside the United States will be based on the facts and circumstances of each case. As the Commission stated in adopting Regulation S, "[i]f it can be demonstrated that an offer or sale of securities occurs 'outside the United States,' the registration provisions of the Securities Act will not apply, regardless of whether the conditions of [Regulation S] are met. For a transaction to qualify … both the sale and the offer pursuant to which it was made must be outside the United States." See Regulation S Adopting Release, supra note 19. Regulation S also contains restrictions on, among other matters, directed selling efforts into the U.S. – those activities that could reasonably be expected, or are intended, to condition the market with respect to the securities being offered in reliance on Regulation S. Id.

41 See supra notes 37-40 and accompanying text.

1. Futures on Single Securities

There are two types of foreign securities that may underlie a future on a single security within the terms of this exemption. First, a security future may overlie a security of a "foreign private issuer," as defined under the Commission's rules,[42] where such security's primary trading market is outside the U.S.[43] These security futures are based on the securities of companies that are not considered under the federal securities laws as U.S. companies and that may not be reporting under the Exchange Act. Second, a security future may overlie a debt security issued or guaranteed by a foreign government[44] that is eligible to be registered with the Commission under Schedule B of the Securities Act.[45]

2. Futures on Indexes

If a foreign security future is based on a security index, the exemption is conditioned on at least 90 percent of the securities in the index, at the time of the transaction, both in terms of the number of underlying securities and their weighting in the index, being (1) securities issued by foreign private issuers, where each such security's primary trading market is outside the

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42 See Securities Act Rule 405, 17 CFR 230.405, and Exchange Act Rule 3b-4, 17 CFR 240.3b-4.

43 See infra notes 50-51 and accompanying text.

44 Rule 405 under the Securities Act defines "foreign government" as the government of a foreign country or political subdivision of a foreign country. 17 CFR 230.405.

45 See Schedule B, 15 U.S.C. 77aa. Existing exemptions for futures on foreign government debt do not cover all foreign governments. See Rule 3a12-8, 17 CFR 240.3a12-8. Under Section 7 of the Securities Act, Schedule B may be used by foreign governments and political subdivisions to register securities under the Securities Act. Certain entities that are closely associated with foreign governments may also be eligible to use Schedule B. The Commission intends that the exemption be available for all security futures on foreign government debt. As a result, for foreign government debt securities, the Commission has included the condition that the security be eligible to be registered pursuant to Schedule B so that security futures on foreign government debt that may be acquired pursuant to this exemption include all foreign government securities that are eligible to be registered with the Commission pursuant to Schedule B.

U.S.,[46] or (2) debt securities issued or guaranteed by a foreign government that are eligible to be registered with the Commission under Schedule B of the Securities Act.[47] The exemption permits up to 10 percent of the number and weighting of securities in the index to be securities of issuers that do not meet the above conditions[48] – i.e., the issuers either are not foreign private issuers or are foreign private issuers but the securities' primary trading market is in the U.S. – if such securities are issued by companies that are required to file reports pursuant to Section 13 or 15(d) of the Exchange Act.[49] The Commission believes that 10 percent is an appropriate portion of an index that will allow an index to be considered "foreign" notwithstanding that a small proportion of securities of issuers in the index do not satisfy the criteria to be considered foreign under this exemption.[50]

The Commission's intent is for the exemption to permit transactions in security futures trading on foreign markets that overlie securities of foreign issuers that, in many cases, are not subject to the Exchange Act reporting provisions. The exemption, however, does allow transactions in foreign security futures on foreign security indexes that contain a limited number and weighting of securities of issuers that either are not foreign private issuers or that do not have their primary trading market outside the U.S, provided such issuers are subject to the

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46 See infra notes 50-51 and accompanying text for a discussion of "primary trading market."

47 15 U.S.C. 77aa.

48 For other contexts in which a 10 percent threshold exists under the federal securities laws see, e.g., Exchange Act Section 16(a)(1), 15 U.S.C. 78p(a)(1), and Regulation AB (Rule 1101(k), 17 CFR 229.1101(k)).

49 15 U.S.C. 78m and 78o(d).

50 For example, if the foreign index contains 30 securities, up to three securities could be the securities of an issuer that is not a foreign private issuer or that does not meet the primary market trading test (as discussed below), as long as the aggregate weighting of those securities also is no more than 10 percent of the index.

reporting requirements of the Exchange Act. Allowing a limited number and weighting of securities that do not satisfy the foreign private issuer or primary trading market condition will not result in a distribution of unregistered securities in the U.S. of non-reporting issuers.

3. Primary Trading Market

The exemption also is conditioned on the primary trading market of any foreign private issuer's security being outside the U.S. For purposes of this condition, a security's primary trading market will be deemed to be outside the U.S. if at least 55 percent of the worldwide trading volume in the security took place in, on, or through the facilities of a securities market or markets located either (i) in a single foreign jurisdiction, or (ii) in no more than two foreign jurisdictions during the issuer's most recently completed fiscal year. If the trading in the foreign private issuer's security is in two foreign jurisdictions, the trading for the issuer's security in at least one of the two foreign jurisdictions must be greater than the trading in the U.S. for the same class of the issuer's securities in order for such security's primary trading market to be considered outside the U.S.[51] Where a security's primary trading market is in the U.S., the Commission believes it is more appropriate, for these purposes, to require that the issuer of such security be subject to the reporting requirements under the Exchange Act. If 55 percent or more

51 Security futures can be surrogates for the underlying security. Thus, for purposes of the exemption, the 55-percent test is important to ensure that the majority of trading in the foreign private issuer's securities occurs offshore. Under this exemption, for purposes of determining whether the 55-percent test is met, trading volume is measured by the foreign private issuer's most recently completed fiscal year. The Commission uses this same test to assess U.S. market interest in a foreign private issuer's securities. See Foreign Private Issuer's Exemption from Registration, Securities Exchange Act Release No. 58465 (September 5, 2008), 73 FR 52752 (September 10, 2008) ("Release No. 34-58465"). The Commission has previously adopted similar tests to assess U.S. market interest in a foreign private issuer's securities in other contexts. See Regulation S, Rule 902(j)(1)(ii), 17 CFR 230.902(j)(1)(ii), and Termination of a Foreign Private Issuer's Registration of a Class of Securities Under Section 12(g) and Duty to File Reports Under Section 13(a) or 15(d), Securities Exchange Act Release No. 55540 (March 27, 2007), 72 FR 16934 (April 5, 2007).

of the trading volume in a foreign private issuer's securities occurs through the facilities of a securities market or markets located outside the U.S., there is a greater likelihood that the foreign private issuer will be subject to a body of reporting and other securities regulatory requirements in a foreign jurisdiction and that the principal pricing determinants for the issuer's securities will be on a market within the jurisdiction of such other regulator.[52]

4. Closing Transactions Only

A security or securities underlying a security future may satisfy the conditions in this exemption described above at the time a transaction is effected, but may cease to satisfy such conditions while a security future position remains open. The exemption would allow persons who entered into positions in foreign security futures in compliance with this exemption to close such positions. For example, a person that opened a position in a foreign security future in compliance with the exemption could close such position even if the underlying index, because of changes in the value of the securities that compose the index, is now less than 90 percent composed of foreign private issues.

C. Exchange Registration

The Commission is not granting an exemption from Section 5 of the Exchange Act for transactions pursuant to this exemption. To the extent exchanges are required to register in the U.S., the listing standards in Section 6(h) of the Exchange Act would apply to any security future trading on that exchange. This exemption is not intended to exempt a U.S. exchange from having to satisfy these listing standards. As a result, the only exchanges that can trade security futures that do not meet these listing standards are those not registered, or required to register, in the U.S.

52 See Release No. 34-58465, supra note 51.

Accordingly, this exemption is conditioned on any transaction effected pursuant to this exemption being on an exchange that is not required to register with the Commission under Section 5 of the Exchange Act.[53] Specifically, for purposes of this exemption, a transaction must be effected on, or subject to the rules of, an exchange or contract market that has its principal place of business outside the U.S. and that is regulated as an exchange or contract market in a country other than the U.S. The Commission believes that an exchange or contract market would be required to register under Section 5 of the Exchange Act if it provides direct electronic access to persons located in the U.S.[54]

D. Issuance, Clearance and Settlement Outside the United States

A clearing agency is the issuer of the security future.[55] Any offer or sale by the clearing agency would have to be registered or exempt under the Securities Act. The purpose of the exemption from Section 6(h)(1) of the Exchange Act is to allow certain persons to effect transactions in security futures overlying securities traded outside the U.S. Therefore, as a condition to this exemption, any transaction in a security future must be cleared and settled on a foreign exchange or contract market located outside the U.S., or, if transactions on such foreign exchange or contract market are cleared and settled through a separate clearing entity, the transaction must be cleared and settled with the clearing entity, which must be located outside the U.S.

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53 15 U.S.C. 78e.

54 Activities of a foreign exchange or contract market in the U.S. relating to security futures also will be subject to applicable Securities Act provisions regarding the offer or sale of securities. See supra notes 37-40 and accompanying text.

55 A clearing organization interposes itself in each transaction and adopts the position of buyer to every seller and seller to every buyer. Robert W. Kolb, Futures, Options, & Swaps, 16 (3d ed. 2000).

In addition, as a condition to the exemption, it must not be possible to close or liquidate a position in the foreign security future entered into on an exchange or contract market located outside the U.S. by effecting an offsetting transaction on or through the facility of any exchange or association registered in the U.S. under Section 6 or 15A of the Exchange Act, respectively.[56]

To limit the potential for an indirect distribution and development of a secondary market in the U.S. in securities that have not been registered under the Securities Act or the Exchange Act, this exemption is also conditioned on persons not taking delivery in the U.S. of the security or securities underlying the foreign security future in connection with settlement. Positions in foreign security futures cannot be transferred to another investor in the same manner as the underlying security, but can be disposed of only in an offsetting transaction on an exchange or contract market outside the U.S. This fact, together with the restriction on physical delivery in the U.S., is intended to help safeguard against development of a public market in the U.S. with respect to unregistered securities as a result of the ability to effect transactions in foreign security futures pursuant to this exemption.

III. Exemptions from Section 15(a)(1) of the Exchange Act and Certain Other Requirements

A foreign broker or dealer effecting transactions in foreign security futures with persons exempt from Section 6(h)(1) of the Exchange Act under this order will need to determine whether it is required to register as a broker or dealer in the U.S. Such foreign broker or dealer can rely on any of the exemptions from U.S. broker-dealer registration provided by Rule 15a-6 under the Exchange Act.[57] The Commission is today also issuing alternative exemptions, on

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56 15 U.S.C. 78f and 15 U.S.C. 78o-3.

57 17 CFR 240.15a-6. By way of background, Rule 15a-6 provides conditional exemptions from U.S. broker-dealer registration requirements for foreign brokers or dealers that: (1) effect unsolicited transactions; (2) provide research reports to certain institutional

which a foreign broker or dealer can rely, from Section 15(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)),[58] and the rules and regulations thereunder, that apply specifically to a broker or dealer whether or not registered with the Commission, as discussed below.[59]

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investors; (3) effect transactions for certain institutional investors through a U.S. registered broker or dealer; and (4) execute transactions directly with registered brokers or dealers and certain specified other persons. Because the Commission construes solicitation broadly, it would expect few transactions effected in reliance on this exemptive order to qualify for the unsolicited exemption. See Registration Requirements for Foreign Broker-Dealers, Securities Exchange Act Release No. 27017 (July 11, 1989), 54 FR 30013 (July 18, 1989). See also Statement of the Commission Regarding Use of Internet Web Sites to Offer Securities, Solicit Securities Transactions, or Advertise Investment Services Offshore, Securities Exchange Act Release No. 39779 (March 23, 1998), 63 FR 14806 (March 27, 1998) at 14813 ("Foreign broker-dealers that have Internet Web sites and that intend to rely on Rule 15a-6's 'unsolicited' exemption should ensure that the 'unsolicited' customer's transactions are not in fact solicited, either directly or indirectly, through customers accessing their Web sites.") Foreign brokers or dealers relying on the other exemptions in Rule 15a-6 should take care to ensure that they meet all of the related conditions. In addition, foreign brokers or dealers should be aware of potential Securities Act implications arising from the distribution of research reports pursuant to Rule 15a-6(a)(2). Specifically, in connection with the distribution of the research report in the U.S., it is important to evaluate whether such distribution may affect the availability of an exemption from registration for the offer or sale of a foreign security future to a QIB or non-U.S. person pursuant to the terms of this order. For example, the research report may be an offer of the securities discussed in the report, a general solicitation of investors, or a directed selling effort for such securities for purposes of the Securities Act. A research report on the underlying security of a foreign security future can be distributed under the Securities Act without being considered a directed selling effort (for Regulation S purposes) or a general solicitation (for Rule 144A purposes) if the conditions of Rule 138 or Rule 139 under the Securities Act, 17 CFR 230.138 and 17 CFR 230.139, are satisfied. Distributing a research report on the foreign security future itself in the U.S. would not, however, satisfy the conditions of those safe harbors.

58 15 U.S.C. 78o(b)(4) and 78o(b)(6).

59 The Commission has issued a proposing release discussing possible amendments to Exchange Act Rule 15a-6. See Exchange Act Release No. 58047 (June 27, 2008), 73 FR 39182 (July 8, 2008). To date, the Commission has not taken final action with respect to the proposed amendments. Accordingly, the Commission is basing the exemption provided herein on the current requirements under Exchange Act Rule 15a-6.

A. Background

Paragraph (a)(3) of Rule 15a-6 permits a foreign broker or dealer to effect certain transactions for institutional investors through a registered broker or dealer. A "registered broker or dealer" is defined in the rule as "a person that is registered with the Commission under Sections 15(b), 15B(a)(2), or 15C(a)(2) of the [Exchange] Act."[60] This term includes a broker or dealer registered with the Commission pursuant to Section 15(b)(11) of the Exchange Act ("Notice BD").[61] Rule 15a-6(a)(3) sets forth conditions that the foreign broker or dealer and the registered broker or dealer must meet in order for the foreign broker or dealer to rely on the rule. Because a Notice BD is subject to a specialized regulatory scheme, however, a foreign broker or dealer may find it difficult to rely on the rule if the registered broker or dealer through which it effects transactions in accordance with Rule 15a-6(a)(3) is a Notice BD.

B. The Exemptions

The Commission finds that it is consistent with the public interest, the protection of investors, and the purposes of the Exchange Act to provide a conditional exemption for foreign brokers or dealers from the registration requirement of Section 15(a)(1) of the Exchange Act. The Commission also finds that it is necessary and appropriate, in the public interest, and is consistent with the protection of investors to provide conditional exemptions for foreign brokers or dealers from the reporting and other requirements of the Exchange Act (other than Sections

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60 Rule 15a-6(b)(5) under the Exchange Act, 17 CFR 240.15a-6(b)(5).

61 A "Notice BD" is a futures commission merchant or introducing broker that registers with the Commission as a broker or dealer pursuant to Section 15(b)(11) of the Exchange Act, 15 U.S.C. 78o(b)(11), and the rules adopted by the Commission. See Securities Exchange Act Release No. 44730 (August 21, 2001), 66 FR 45138 (August 27, 2001).

15(b)(4) and 15(b)(6)),[62] and the rules and regulations thereunder, that apply specifically to a broker or dealer whether or not registered with the Commission.

The conditional exemptions would be available to foreign brokers or dealers that induce or attempt to induce the purchase or sale of any foreign security futures by a QIB[63] that is exempt from Section 6(h)(1) of the Exchange Act under this order. The conditional exemptions also would extend exemptive relief to transactions that are intermediated by Notice BDs, recognizing the role that Notice BDs play with respect to security futures and the specialized regulatory scheme that applies to these particular brokers and dealers.

A foreign broker or dealer may rely on the conditional exemptions to induce or attempt to induce the purchase or sale of any foreign security future by a QIB exempt from Section 6(h)(1), so long as the foreign broker or dealer and the registered broker or dealer, through which any resulting transactions are effected, comply with the requirements of paragraphs (a)(3)(i) through

62 15 U.S.C. 78o(b)(4) and 78o(b)(6).

63 The conditional exemptions in this order from the registration requirements in Section 15(a)(1) of the Exchange Act and related requirements cover foreign brokers' or dealers' transactions with QIBs. The exemption in this order from Section 6(h)(1) of the Exchange Act is applicable to persons that are QIBs. The Rule 15a-6(a)(3) exemption applies to a foreign broker's or dealer's transactions with U.S. institutional investors (see Rule 15a-6(b)(7) under the Exchange Act, 17 CFR 240.15a-6(b)(7)) and major U.S. institutional investors (see Rule 15a-6(b)(4) under the Exchange Act, 17 CFR 240.15a-6(b)(4)). There is substantial overlap, however, between the definitions of major U.S. institutional investor and QIB. Therefore, the conditional exemptions in this order from the registration requirements in Section 15(a)(1) of the Exchange Act and related requirements should simplify the process for engaging in transactions in foreign security futures without substantially altering the class of persons with which foreign brokers or dealers (intermediated by registered brokers or dealers) may transact.

(iii)[64] of Rule 15a-6 under the Exchange Act, except as otherwise provided below.[65] If the registered broker or dealer through which any resulting transactions with QIBs are effected is a Notice BD, then the Notice BD must comply with the alternative requirements, discussed below, in lieu of the requirements of paragraphs (a)(3)(iii)(A)(5) and (a)(3)(iii)(A)(6) of Rule 15a-6.[66]

Paragraphs (a)(3)(iii)(A)(5) and (a)(3)(iii)(A)(6) of Rule 15a-6 require the registered broker or dealer to be responsible for (1) complying with Rule 15c3-1 under the Exchange Act[67] with respect to the transaction, and (2) receiving, delivering, and safeguarding funds and securities in connection with the transaction in compliance with Rule 15c3-3 under the Exchange Act.[68] However, Section 15(b)(11)(B)(iii) of the Exchange Act, exempts Notice BDs from

64 For purposes of this exemption, references in paragraphs (a)(3)(i) through (iii) and paragraph (b)(2) of Rule 15a-6 to major U.S. institutional investors shall be deemed to be references to QIBs. In addition, for purposes of this exemption, the reference in paragraph (a)(3)(iii)(D) to Form BD shall be deemed a reference to Form BD-N with respect to Notice BDs.

65 In view of the experience and capabilities QIBs are likely to possess, the chaperoning requirement under paragraph (a)(3)(ii)(A)(1) may provide only limited benefits with respect to QIBs. Therefore, notwithstanding paragraph (a)(3)(ii)(A)(1) of the rule, in this context, foreign broker-dealers may engage in unchaperoned contacts with QIBs to the same extent as described in a 1997 staff no-action letter. See Letter re: Certain Securities Activities of U.S. Affiliated Foreign Dealers, from Giovanni P. Prezioso, Cleary, Gottlieb, Steen & Hamilton, to Richard R. Lindsey, Director, Division of Market Regulation, Securities and Exchange Commission (Apr. 9, 1997). Specifically, foreign associated persons of the foreign broker or dealer may have in-person contacts (without the participation of an associated person of a registered broker or dealer) during visits to the United States with QIBs, so long as the number of days on which such in-person contacts occur does not exceed 30 per year and the foreign associated persons engaged in such in-person contacts do not accept orders to effect securities transactions while in the United States.

66 A Notice BD intermediating a foreign broker or dealer that is relying on the exemption under Exchange Act Rule 15a-6(a)(3) would need to comply with the requirements in paragraphs (a)(3)(iii)(A)(5) and (a)(3)(iii)(A)(6) in a similar manner as any other registered broker or dealer even if the requirements in such paragraphs would not otherwise be applicable.

67 17 CFR 240.15c3-1.

68 17 CFR 240.15c3-3.

Section 15(c)(3) of the Exchange Act and the rules thereunder. Instead, Notice BDs are subject to analogous requirements of the CEA. Accordingly, for purposes of this exemption, a Notice BD, in lieu of compliance with paragraphs (a)(3)(iii)(A)(5) and (a)(3)(iii)(A)(6) of Rule 15a-6, would need to comply with the analogous CEA requirements, including being responsible for receiving, delivering, and safeguarding funds and securities in connection with transactions on behalf of the QIB in compliance with the CEA segregation[69] and net capital requirements.[70] Consistent with the regulatory framework established by the CFMA, this relief will permit a foreign broker or dealer to be intermediated by a Notice BD without subjecting the Notice BD to duplicative regulatory requirements.

IV. Rule 15c6-1 under the Exchange Act (Settlement Cycle)

Rule 15c6-1 under the Exchange Act[71] prohibits a broker or dealer from effecting or entering into a contract for the purchase or sale of a security (other than an exempted security, government security, municipal security, commercial paper, bankers' acceptances, or commercial bills) that provides for payment of funds and delivery of securities later than the third business day after the date of the contract, unless otherwise expressly agreed to by the parties at the time of the transaction. The rule does not distinguish between U.S. securities and foreign securities. Thus, because security futures are considered securities under the Exchange

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69 For a discussion regarding analogous CEA provisions, see Applicability of CFTC and SEC Customer Protection, Recordkeeping, Reporting, and Bankruptcy Rules and the Securities Investor Protection Act of 1970 to Accounts Holding Security Futures Products, Joint Release by SEC and CFTC, Securities Exchange Act Release No. 46473 (September 9, 2002), 67 FR 58284 (September 13, 2002) ("Joint September 2002 Release") (noting that transactions involving a futures account shall be subject to the segregation requirements of the CEA and that transactions involving a securities account shall be subject to Rule 15c3-3 under the Exchange Act and Securities Investor Protection Act of 1970).

70 17 CFR 1.17.

71 17 CFR 240.15c6-1.

Act,[72] this rule by its terms would apply to transactions in foreign security futures. The Commission has, however, previously exempted from the scope of Rule 15c6-1 under the Exchange Act all transactions that do not have transfer or delivery facilities in the U.S.[73] In addition, the Commission has granted an exemption to make it clear that Rule 15c6-1 does not apply to transactions that occur outside the U.S.[74] Therefore, transactions in foreign security futures pursuant to the exemption from Section 6(h)(1) of the Exchange Act in this order would fall within the scope of the Commission's prior exemption from Rule 15c6-1 under the Exchange Act.

V. Conditional Exemptions from Sections 6(h)(1) and 15(a)(1) of the Exchange Act and Certain Other Requirements

A. Conditional Exemption from Section 6(h)(1) of the Exchange Act

For these reasons stated in, and by, this order, the Commission is exempting from Section 6(h)(1) of the Exchange Act[75] any qualified institutional buyer (as defined in Rule 144A under the Securities Act) ("QIB");[76] any person who is not a "U.S. person," as the term is defined in Rule 902(k) of Regulation S under the Securities Act ("non-U.S. person");[77] any

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72 See the definition of "security" in Section 3(a)(10) of the Exchange Act, 15 U.S.C. 78c(a)(10).

73 See Securities Exchange Act Release No. 35750 (May 22, 1995), 60 FR 27994 (May 26, 1995).

74 Id. In particular, the Commission stated that if a U.S. broker-dealer were to execute a trade on a foreign exchange with a U.S. or foreign broker-dealer, the contract would not be subject to the rule. This exemption applies, however, only to the contract between the U.S. broker-dealer and the foreign broker-dealer. If the U.S. broker-dealer is executing the trade on a foreign exchange to satisfy its obligations to a U.S. customer, the contract with the U.S. customer is still subject to T+3 settlement unless that contract also is exempted. Id. At n. 9 and accompanying text.

75 15 U.S.C. 78f(h)(1).

76 17 CFR 230.144A.

77 17 CFR 230.902(k).

broker or dealer registered under Section 15(b) of the Exchange Act[78] to the extent such broker or dealer effects transactions on behalf of a QIB or a non-U.S. person; and any bank, as defined in Section 3(a)(6) of the Exchange Act,[79] acting pursuant to an exception or exemption from the definition of "broker" or "dealer" in sections 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Exchange Act[80] or the rules thereunder ("Eligible Bank") to effect transactions on behalf of a QIB or a non-U.S. person; provided that any transaction effected:

(1)(a) Is for a contract of sale for future delivery of:

(i) (A) a security issued by a foreign private issuer (as defined in Rule 3b-4(c) of the Exchange Act and Rule 405 under the Securities Act)[81] for which at least 55 percent of the worldwide trading volume in the security took place in, on, or through the facilities of a securities market or markets in a single foreign jurisdiction or in no more than two foreign jurisdictions during the issuer's most recently completed fiscal year. If the trading in the foreign private issuer's security is in two foreign jurisdictions, the trading for the issuer's securities in at least one of the two foreign jurisdictions must be greater than the trading in the U.S. for the same class of the issuer's securities in order for such security's primary trading market to be considered outside the U.S.; or

(B) a security that is a note, bond, debenture or evidence of indebtedness ("debt security") issued or guaranteed by a foreign government as defined

78 15 U.S.C. 78o(b).

79 15 U.S.C. 78c(a)(6).

80 15 U.S.C. 78c(a)(4)(B), 15 U.S.C. 78c(a)(4)(E), or 15 U.S.C. 78c(a)(5)(C).

81 17 CFR 240.3b-4(c) and 17 CFR 230.405.

in Rule 405 of the Securities Act[82] that is eligible to be registered with the Commission under Schedule B of the Securities Act;[83] or

(ii) a "narrow-based security index" of which:

(A) At least 90 percent of the underlying securities in the index, at the time of the transaction, both in terms of the number of underlying securities and their weighting in the index, are: (1) securities issued by a foreign private issuer for which at least 55 percent of the worldwide trading volume in the security took place in, on, or through the facilities of a securities market or markets located in a single foreign jurisdiction, or in no more than two foreign jurisdictions during the issuer's most recently completed fiscal year. If the trading in the foreign private issuer's security is in two foreign jurisdictions, the trading for the issuer's security in at least one of the two foreign jurisdictions must be greater than the trading in the U.S. for the same class of the issuer's securities in order for such security's primary trading market to be considered outside the U.S.; or (2) debt securities issued or guaranteed by a foreign government as defined in Rule 405 of the Securities Act[84] that are eligible to be registered with the Commission under Schedule B of the Securities Act;[85] and

(B) no more than 10 percent of the underlying securities in the index, at the time of the transaction, both in terms of the number of underlying

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[82] 17 CFR 230.405. Rule 405 defines "foreign government" as the government of a foreign country or political subdivision of a foreign country.

[83] See Schedule B, 15 U.S.C. 77aa.

[84] 17 CFR 230.405.

[85] See Schedule B, 15 U.S.C. 77aa.

securities and their weighting in the index, do not meet the criteria in (1)(a)(ii)(A) above and, as to any such security, the issuer of such security is required to file reports with the Commission pursuant to Section 13 or Section 15(d) of the Exchange Act;[86]

(b) Is a closing transaction to offset a position in a contract of sale for future delivery that satisfied the conditions in paragraph (1)(a) of this order at the time such position was opened.

(2) Is executed on, or subject to the rules of, an exchange or contract market that has its principal place of business outside the U.S., that is regulated as an exchange or contract market in a country other than the U.S., and that is not required to register with the Commission under Section 5 of the Exchange Act;[87]

(3) Is cleared and settled on, and with respect to such clearance and settlement subject to the rules of, an exchange, contract market, or clearing entity that is regulated as an exchange, contract market, or clearing entity in a country other than the U.S. and that is not required to register with the Commission under Section 5 or Section 17A of the Exchange Act;[88]

(4) Is for a security future, that cannot be closed or liquidated by effecting an offsetting transaction on or through the facility of any exchange or association registered in the U.S. under Section 6 or Section 15A of the Exchange Act,[89] respectively; and

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86 15 U.S.C. 78m and 78o(d).

87 15 U.S.C. 78e.

88 15 U.S.C. 78e and 78q-1.

89 15 U.S.C. 78f and 15 U.S.C. 78o-3.

(5) Does not result in such person taking physical delivery of the underlying security in the U.S. in connection with settlement;

B. Conditional Exemptions from Section 15(a)(1) of the Exchange Act and Certain Other Requirements

For the reasons stated in, and by, this order, the Commission is exempting foreign brokers or dealers (as defined in Rule 15a-6(b)(3) under the Exchange Act)[90] that induce or attempt to induce the purchase or sale of any foreign security futures by a QIB that is subject to the exemption from Section 6(h)(1) of the Exchange Act, from the registration requirements of Section 15(a)(1) of the Exchange Act[91] and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)),[92] and the rules and regulations thereunder, that apply specifically to a broker or dealer whether or not registered with the Commission; provided that the foreign broker or dealer and the registered broker or dealer (as defined in Rule 15a-6(b)(5) under the Exchange Act), through which any resulting transactions with QIBs are effected, comply with the requirements of paragraphs (a)(3)(i) through (iii)[93] of Rule 15a-6 under the Exchange Act, except as otherwise provided below.[94] If the registered broker or dealer

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90 17 CFR 240.15a-6(b)(3).

91 15 U.S.C. 78o(a)(1).

92 15 U.S.C. 78o(b)(4) and 78o(b)(6).

93 For purposes of this exemption, references in paragraphs (a)(3)(i) through (iii) and paragraph (b)(2) of Rule 15a-6 to major U.S. institutional investors shall be deemed to be references to QIBs. In addition, for purposes of this exemption, the reference in paragraph (a)(3)(iii)(D) to Form BD shall be deemed a reference to Form BD-N with respect to Notice BDs.

94 Notwithstanding paragraph (a)(3)(ii)(A)(1) of the rule, foreign associated persons of the foreign broker or dealer may have in-person contacts (without the participation of an associated person of a registered broker or dealer) during visits to the United States with QIBs, so long as the number of days on which such in-person contacts occur does not exceed 30 per year and the foreign associated persons engaged in such in-person contacts do not accept orders to effect securities transactions while in the United States. See supra note 65.

through which any resulting transactions with QIBs are effected is a broker or dealer registered with the Commission pursuant to Section 15(b)(11) of the Exchange Act ("Notice BD"), then:

(1) in lieu of the requirement in paragraph (a)(3)(iii)(A)(5) of Rule 15a-6, the Notice BD shall be responsible for complying with Rule 1.17 under the Commodity Exchange Act ("CEA") (17 CFR 1.17) with respect to the transactions; and

(2) in lieu of the requirement in paragraph (a)(3)(iii)(A)(6) of Rule 15a-6, the Notice BD shall be responsible for receiving, delivering, and safeguarding funds and securities in connection with transactions on behalf of the QIB in compliance with the segregation requirements of the CEA and the regulations thereunder.

Accordingly,

IT IS HEREBY ORDERED, pursuant to Section 36 of the Exchange Act,[95] that certain persons are exempt from the provisions of Section 6(h)(1) of the Exchange Act[96] that prohibit persons from effecting transactions in security futures products that are not listed on a national securities exchange or a national securities association registered pursuant to Section 15A(a) of the Exchange Act,[97] subject to the conditions set forth above.

IT IS HEREBY FURTHER ORDERED, pursuant to Section 15(a)(2) of the Exchange Act,[98] that a foreign broker or dealer as defined in Rule 15a-6(b)(3)[99] is exempt, with respect only to the activities described above in Section V.B. of this order, from the registration

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95 15 U.S.C. 78mm.

96 15 U.S.C. 78f(h)(1).

97 15 U.S.C.78o-3(a).

98 15 U.S.C. 78o(a)(2).

99 17 CFR 240.15a-6(b)(3).

requirements of Section 15(a)(1) of the Exchange Act, subject to the conditions set forth above.[100]

IT IS HEREBY FURTHER ORDERED, pursuant to Section 36 of the Exchange Act,[101] that a foreign broker or dealer as defined in Rule 15a-6(b)(3)[102] is exempt, with respect only to the activities described above in Section V.B. of this order, from the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)),[103] and the rules and regulations thereunder, that apply specifically to a broker or dealer whether or not registered with the Commission, subject to the conditions set forth above.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

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100 15 U.S.C. 78o(a)(1).

101 15 U.S.C. 78mm.

102 17 CFR 240.15a-6(b)(3).

103 15 U.S.C. 78o(b)(4) and 78o(b)(6).

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 270 and 274

[Release No. IC-28807; File No. S7-11-09]

RIN 3235-AK33

Money Market Fund Reform

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission ("Commission" or "SEC") is proposing amendments to certain rules that govern money market funds under the Investment Company Act. The amendments would: (i) tighten the risk-limiting conditions of rule 2a-7 by, among other things, requiring funds to maintain a portion of their portfolios in instruments that can be readily converted to cash, reducing the weighted average maturity of portfolio holdings, and limiting funds to investing in the highest quality portfolio securities; (ii) require money market funds to report their portfolio holdings monthly to the Commission; and (iii) permit a money market fund that has "broken the buck" (*i.e.*, re-priced its securities below $1.00 per share) to suspend redemptions to allow for the orderly liquidation of fund assets. In addition, the Commission is seeking comment on other potential changes in our regulation of money market funds, including whether money market funds should, like other types of mutual funds, effect shareholder transactions at the market-based net asset value, *i.e.*, whether they should have "floating" rather than stabilized net asset values. The proposed amendments are designed to make money market funds more resilient to certain short-term market risks, and to provide greater protections for investors in a money market fund that is unable to maintain a stable net asset value per share.

DATES: Comments should be received on or before September 8, 2009.

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.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-11-09 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 Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-11-09. 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 website (http://www.sec.gov/rules/proposed.shtml). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. 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: Office of Regulatory Policy, at (202) 551-6792, Division of Investment Management, Securities and Exchange Commission, 100 F

Street, NE, Washington, DC 20549-8549.

SUPPLEMENTARY INFORMATION: The Commission is proposing for public comment amendments to rules 2a-7 [17 CFR 270.2a-7], 17a-9 [17 CFR 270.17a-9], and 30b1-5 [17 CFR 270.30b1-5], new rules 22e-3 [17 CFR 270.22e-3] and 30b1-6 [17 CFR 270.30b1-6], and new Form N-MFP under the Investment Company Act of 1940 ("Investment Company Act" or "Act").[1]

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[1] 15 U.S.C. 80a. Unless otherwise noted, all references to statutory sections are to the Investment Company Act, and all references to rules under the Investment Company Act, including rule 2a-7, will be to Title 17, Part 270 of the Code of Federal Regulations [17 CFR 270].

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I. BACKGROUND

A. Money Market Funds

Money market funds are open-end management investment companies that are registered under the Investment Company Act and regulated under rule 2a-7 under the Act. They invest in high-quality, short-term debt instruments such as commercial paper, Treasury bills and repurchase agreements.[2] Money market funds pay dividends that reflect prevailing short-term interest rates and, unlike other investment companies, seek to maintain a stable net asset value

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[2] Money market funds are also sometimes called "money market mutual funds" or "money funds."

per share, typically $1.00 per share.[3]

This combination of stability of principal and payment of short-term yields has made money market funds one of the most popular investment vehicles for many different types of investors. Commonly offered features, such as check-writing privileges, exchange privileges, and near-immediate liquidity, have contributed to the popularity of money market funds. More than 750 money market funds are registered with the Commission, and collectively they hold approximately $3.8 trillion of assets.[4] Money market funds account for approximately 39 percent of all investment company assets.[5]

Individual (or "retail") investors use money market funds for a variety of reasons. For example, they may invest in money market funds to hold cash temporarily or to take a temporary "defensive position" in anticipation of declining equity markets. Money market funds also play an important role in cash management accounts for banks, broker-dealers, variable insurance products, and retirement accounts. As of December 2008, about one-fifth of U.S. households' cash balances were held in money market funds.[6]

Different types of money market funds have been introduced to meet the differing needs of retail money market fund investors. Historically, most retail investors have invested in "prime money market funds," which hold a variety of taxable short-term obligations issued by

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3 *See generally* Valuation of Debt Instruments and Computation of Current Price Per Share by Certain Open-End Investment Companies (Money Market Funds), Investment Company Act Release No. 13380 (July 11, 1983) [48 FR 32555 (July 18, 1983)] ("1983 Adopting Release"). Most money market funds seek to maintain a stable net asset value per share of $1.00, but a few seek to maintain a stable net asset value per share of a different amount, *e.g.*, $10.00. For convenience, throughout this release, the discussion will simply refer to the stable net asset value of $1.00 per share.

4 *See* Investment Company Institute, *Trends in Mutual Fund Investing*, April 2009, *available at* http://www.ici.org/highlights/trends_04_09 ("ICI Trends").

5 *See id.*

6 *See* INVESTMENT COMPANY INSTITUTE, REPORT OF THE MONEY MARKET WORKING GROUP, at 21 (Mar. 17, 2009), *available at* http://www.ici.org/pdf/ppr_09_mmwg.pdf ("ICI REPORT").

corporations and banks, as well as repurchase agreements and asset backed commercial paper secured by pools of assets.[7] Prime money market funds typically have paid higher yields than other types of money market funds available to retail investors.[8] "Government money market funds" principally hold obligations of the U.S. Government, including obligations of the U.S. Treasury and federal agencies and instrumentalities, as well as repurchase agreements collateralized by Government securities. Some government money market funds limit themselves to holding only Treasury obligations. Compared to prime funds, government funds generally offer greater safety of principal but historically have paid lower yields. "Tax exempt money market funds" primarily hold obligations of state and local governments and their instrumentalities, and pay interest that is generally exempt from federal income taxes.

Institutional investors account for a growing portion of investments in money market funds. These investors include corporations, bank trust departments, securities lending operations of brokerage firms, state and local governments, hedge funds and other private funds. Many corporate treasurers of large businesses have essentially "outsourced" cash management operations to money market funds, which may be able to manage cash more efficiently due both to the scale of their operations and their expertise. As of January 2008, approximately 80 percent of U.S. companies used money market funds to manage at least a portion of their cash balances.[9] At year-end 2008, U.S. non-financial businesses held approximately 32 percent of their cash balances in money market funds.[10] According to the Investment Company Institute, about 66

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7 *See* INVESTMENT COMPANY INSTITUTE, 2009 INVESTMENT COMPANY FACT BOOK, at 147, Table 38 (May 2009), *available at* http://www.ici.org/pdf/2009_factbook.pdf ("2009 FACT BOOK").

8 *See, e.g., iMoneyNet Money Fund Report* (Mar. 20, 2009), *available at* http://www.imoneynet.com/files/Publication_News/mfr.pdf.

9 *See* ICI REPORT, *supra* note 6, at 28-29, Figure 3.7.

10 *See id.* at 28-29, Figure 3.6.

percent of money market fund assets are held in money market funds or share classes intended to be sold to institutional investors ("institutional money market funds").[11]

Institutional money market funds hold securities similar to those held by prime funds and government funds. They typically have large minimum investment amounts (*e.g.*, $1 million), and offer lower expenses and higher yields due to the large account balances, large transaction values, and smaller number of accounts associated with these funds. As we will discuss in more detail below, institutional money market funds also tend to have greater investment inflows and outflows than retail money market funds.

B. Market Significance

Due in large part to the growth of institutional funds, money market funds have grown substantially over the last decade, from approximately $1.4 trillion in assets under management at the end of 1998 to approximately $3.8 trillion in assets under management at the end of 2008.[12] During this same period, retail taxable money market fund assets grew from approximately $835 billion to $1.36 trillion, or 63 percent, while institutional taxable money market fund assets grew from approximately $516 billion to $2.48 trillion, or 380 percent.[13]

One implication of the growth of money market funds is the increased role they play in the capital markets. They are by far the largest holders of commercial paper, owning almost 40 percent of the outstanding paper.[14] The growth of the commercial paper market has generally

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11 *See* Investment Company Institute, *Money Market Mutual Fund Assets*, June 11, 2009, *available at* http://www.ici.org/highlights/mm_06_11_09.

12 *See* INVESTMENT COMPANY INSTITUTE, 1999 MUTUAL FUND FACT BOOK, at 4 (May 1999), *available at* http://www.ici.org/pdf/1999_factbook.pdf; Investment Company Institute, *Trends in Mutual Fund Investing*, May 28, 2009, *available at* http://www.ici.org/highlights/trends_04_2009.

13 *See* INVESTMENT COMPANY INSTITUTE, 2008 INVESTMENT COMPANY FACT BOOK, at 144, Table 35 (May 2008) ("2008 FACT BOOK"); 2009 FACT BOOK, *supra* note 7, at 147, Table 38.

14 FEDERAL RESERVE BOARD, STATISTICAL RELEASE Z.1: FLOW OF FUNDS ACCOUNTS OF THE

followed the growth of money market funds over the last three decades.[15] Today, money market funds provide a substantial portion of short-term credit extended to U.S. businesses.

Money market funds also play a large role in other parts of the short-term market. They hold approximately 23 percent of all repurchase agreements, 65 percent of state and local government short-term debt, 24 percent of short-term Treasury securities, and 44 percent of short-term agency securities.[16] They serve as a substantial source of financing in the broader capital markets, holding approximately 22 percent of all state and local government debt, approximately nine percent of U.S. Treasury securities and 15 percent of agency securities.[17]

As a consequence, the health of money market funds is important not only to their investors, but also to a large number of businesses and state and local governments that finance current operations through the issuance of short-term debt. A "break in the link [between borrowers and money market funds] can lead to reduced business activity and pose risks to

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UNITED STATES: FLOWS AND OUTSTANDINGS FOURTH QUARTER 2008, at 86, Table L.208 (Mar. 12, 2009), *available at* http://www.federalreserve.gov/releases/z1/Current/z1.pdf ("FED. FLOW OF FUNDS REPORT").

15 *See* INSTRUMENTS OF THE MONEY MARKET, at 121, Table 2 (Timothy Q. Cook & Robert K. Laroche eds., 1993), *available at* http://www.richmondfed.org/publications/research/special_reports/instruments_of_the_money_market/pdf/full_publication.pdf; FED. FLOW OF FUNDS REPORT, *supra* note 14, at Tables L.206 and L.208. One commenter has called the growth of these two markets "inextricably linked." *See* Leland Crabbe & Mitchell A. Post, *The Effect of SEC Amendments to Rule 2a-7 on the Commercial Paper Market*, at 4 (Federal Reserve Board, Finance and Economics Discussion Series #199, May 1992) ("Crabbe & Post").

16 These securities include securities issued or guaranteed by the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac") and the Federal Home Loan Banks. *See* ICI REPORT, *supra* note 6, at 19, Figure 2.3. *See generally* U.S. Treasury Department, FAQs on Fixed Income Agency Securities, *available at* http://www.treas.gov/education/faq/markets/fixedfederal.shtml.

17 *See* Fed. Flow of Funds Report, *supra* note 14 (percentages derived from flow of funds data). Foreign banks also have relied substantially on U.S. money market funds for dollar-denominated funding. *See* Naohiko Baba, Robert N. McCauley, & Srichander Ramaswamy, *U.S. Dollar Money Market Funds and non-U.S. Banks*, BIS QUARTERLY REVIEW, Mar. 2009, *available at* http://www.bis.org/publ/qtrpdf/r_qt0903g.htm ("U.S. Dollar Money Market Funds").

economic growth."[18] The regulation of money market funds, therefore, is important not only to fund investors, but to a wide variety of operating companies as well as state and local governments that rely on these funds to purchase their short-term securities.

C. Regulation of Money Market Funds

The Commission regulates money market funds under the Investment Company Act and pursuant to rule 2a-7 under the Act. We adopted rule 2a-7 as an exemptive rule in 1983 and amended it in 1986 to facilitate the development of tax exempt money market funds.[19] We also amended it substantially in 1991 (taxable funds) and 1996 (tax exempt funds) to provide for a more robust set of regulatory conditions and to expand the rule to apply it to any investment company holding itself out as a money market fund.[20]

The Investment Company Act and applicable rules generally require that mutual funds price their securities at the current net asset value per share by valuing portfolio instruments at market value or, if market quotations are not readily available, at fair value determined in good faith by the board of directors.[21] As a consequence, the price at which funds will sell and redeem shares ordinarily fluctuates daily with changes in the value of the fund's portfolio securities. These valuation and pricing requirements are designed to prevent investors' interests from being

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18 *See* Mike Hammill & Andrew Flowers, *MMMF, and AMLF, and MMIFF*, MACROBLOG (Federal Reserve Bank of Atlanta), Oct. 30, 2008, *available at* http://www.macroblog.typepad.com/macroblog/2008/10/index.html.

19 *See* 1983 Adopting Release, *supra* note 3; Acquisition and Valuation of Certain Portfolio Instruments by Registered Investment Companies, Investment Company Act Release No. 14983 (Mar. 12, 1986) [51 FR 9773 (Mar. 21, 1986)] ("1986 Adopting Release").

20 *See* Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 18005 (Feb. 20, 1991) [56 FR 8113 (Feb. 27, 1991)] ("1991 Adopting Release"); Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 21837 (Mar. 21, 1996) [61 FR 13956 (Mar. 28, 1996)] ("1996 Adopting Release").

21 *See* section 2(a)(41) of the Act (defining "value" of fund assets); rule 2a-4 (defining "current net asset value" for use in computing the current price of a redeemable security); and rule 22c-1 (generally requiring open-end funds to sell and redeem their shares at a price based on the funds' current net asset value as next computed after receipt of a redemption, purchase, or sale order).

diluted or otherwise adversely affected if fund shares are not priced fairly.[22]

Rule 2a-7, however, permits money market funds to use the amortized cost method of valuation and penny-rounding method of pricing instead, which facilitate money market funds' ability to maintain a stable net asset value.[23] Under the amortized cost method, portfolio securities generally are valued at cost plus any amortization of premium or accumulation of discount ("amortized cost").[24] The basic premise underlying money market funds' use of the amortized cost method of valuation is that high-quality, short-term debt securities held until maturity will eventually return to the amortized cost value, regardless of any current disparity between the amortized cost value and market value, and would not ordinarily be expected to fluctuate significantly in value.[25] Therefore, the rule permits money market funds to value portfolio securities at their amortized cost so long as the deviation between the amortized cost and current market value *remains* minimal and results in the computation of a share price that represents fairly the current net asset value per share of the fund.[26]

To reduce the likelihood of a material deviation occurring between the amortized cost value of a portfolio and its market-based value, the rule contains several conditions (which we

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22 *See* Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 17589 at n.7 and accompanying text (July 17, 1990) [55 FR 30239 (July 25, 1990)] ("1990 Proposing Release").

23 The penny-rounding method of pricing means the method of computing a fund's price per share for purposes of distribution, redemption and repurchase whereby the current net asset value per share is rounded to the nearest one percent. *See* rule 2a-7(a)(18).

24 *See* rule 2a-7(a)(2) (defining the amortized cost method as calculating an investment company's net asset value whereby portfolio securities are valued at the fund's acquisition cost as adjusted for amortization of premium or accretion of discount rather than at their value based on current market factors).

25 *See* 1983 Adopting Release, *supra* note 3, at nn.3-7 and accompanying text; Valuation of Debt Instruments and Computation of Current Price Per Share by Certain Open-End Investment Companies, Investment Company Act Release No. 12206, at nn.3-4 and accompanying text (Feb. 1, 1982) [47 FR 5428 (Feb. 5, 1982)] ("1982 Proposing Release").

26 *See* rule 2a-7(c)(1), (c)(7)(ii)(C).

refer to as "risk-limiting conditions") that limit the fund's exposure to certain risks, such as credit, currency, and interest rate risks.[27] In addition, the rule includes certain procedural requirements overseen by the fund's board of directors. One of the most important is the requirement that the fund periodically "shadow price" the amortized cost net asset value of the fund's portfolio against the mark-to-market net asset value of the portfolio.[28] If there is a difference of more than ½ of 1 percent (or $0.005 per share), the fund's board of directors must consider promptly what action, if any, should be taken, including whether the fund should discontinue the use of the amortized cost method of valuation and re-price the securities of the fund below (or above) $1.00 per share, an event colloquially known as "breaking the buck."[29]

D. Recent Developments

Money market funds have had a record of stability during their more than 30 years of operation. Before last fall, only one money market fund had ever broken the buck.[30] This record appears to be due primarily to three factors. First, the short-term debt markets generally were relatively stable during this period. Second, many fund advisers (and their portfolio managers

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[27] For example, the rule requires, among other things, that a money market fund's portfolio securities meet certain credit quality requirements, such as being rated in the top one or two rating categories by nationally recognized statistical rating organizations ("NRSROs"), and by limiting the portion of the fund's portfolio that may be invested in securities rated in the second highest rating category. *See* rule 2a-7(c)(3). The rule also places limits on the remaining maturity of securities in the fund's portfolio. A fund generally may not acquire, for example, any securities with a remaining maturity greater than 397 days, and the dollar-weighted average maturity of the securities owned by the fund may not exceed 90 days. *See* rule 2a-7(c)(2).

[28] *See* rule 2a-7(c)(7); *see also supra* note 21 and accompanying text.

[29] *See* rule 2a-7(c)(7)(ii)(B). Regardless of the extent of the deviation, rule 2a-7 imposes on the board of a money market fund a duty to take appropriate action whenever the board believes the extent of any deviation may result in material dilution or other unfair results to investors or current shareholders. Rule 2a-7(c)(7)(ii)(C). *See* 1983 Adopting Release, *supra* note 3, at nn.51-52 and accompanying text.

[30] In September 1994, a series of a small institutional money market fund re-priced its shares below $1.00 as a result of loss in value of certain floating rate securities. The fund promptly announced that it would liquidate and distribute its assets to its shareholders. *See* 1996 Adopting Release, *supra* note 20, at n.162.

and credit analysts) were skillful in analyzing the risks of portfolio securities and thereby largely avoiding significant losses that could force a fund to break the buck.[31] Finally, fund managers and their affiliated persons have had significant sources of private capital that they were willing to make available to support the stable net asset value of a money market fund when it experienced losses in one or more of its portfolio securities.

Since the late 1980s, fund managers from time to time have sought to prevent a money market fund from breaking the buck by voluntarily purchasing distressed portfolio securities from the fund, directly or through an affiliated person, at the higher of market price or amortized cost.[32] These events occurred irregularly and involved a limited number of funds.[33] In response to these events, the Commission tightened the risk-limiting conditions of the rule for taxable funds in 1991 and for tax exempt funds in 1996.[34] Among other things, we added diversification requirements to the rule, which limited the exposure of a fund to any one issuer of securities, thus reducing the consequences of a credit event affecting the value of a portfolio holding.[35] We repeatedly emphasized the responsibility of fund managers to manage, and fund boards to oversee that the fund is managed, in a manner consistent with the investment objective of

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[31] We made similar observations last year. *See* Temporary Exemption for Liquidation of Certain Money Market Funds, Investment Company Act Release No. 28487, at text accompanying nn.6-7 (Nov. 20, 2008) [73 FR 71919 (Nov. 26, 2008)] ("Rule 22e-3T Adopting Release").

[32] These transactions implicate section 17(a) of the Investment Company Act, which prohibits an affiliated person of a fund or an affiliated person of such a person from knowingly purchasing a security from the fund, except in limited circumstances. Under section 17(b) of the Act, such persons can apply to the Commission for an exemption from these prohibitions. In 1996, the Commission adopted rule 17a-9, which permits affiliated persons of funds and affiliated persons of such persons to purchase distressed securities in funds' portfolios subject to certain conditions, without the need to first obtain an individual exemption. We are proposing certain amendments to rule 17a-9 in this release, as well as an amendment to rule 2a-7 that would require money market funds to notify us of any transactions under rule 17a-9. *See infra* Section II.H.

[33] *See* 1990 Proposing Release, *supra* note 22, at nn.16-18 and accompanying text; 1996 Adopting Release, *supra* note 20, at nn.22-23 and accompanying text.

[34] *See* 1991 Adopting Release, *supra* note 20; 1996 Adopting Release, *supra* note 20.

[35] *See* rule 2a-7(c)(4).

maintaining a stable net asset value.[36]

In 2007, however, losses in the subprime mortgage markets adversely affected a significant number of money market funds. These money market funds had invested in asset backed commercial paper issued by structured investment vehicles ("SIVs"), which were off-balance sheet conduits sponsored mostly by certain large banks and money managers.[37] Although we understand that most SIVs had little exposure to sub-prime mortgages, they suffered severe liquidity problems and significant losses when risk-averse short-term investors (including money market funds), fearing increased exposure to liquidity risk and residential mortgages, began to avoid the commercial paper the SIVs issued.[38] Unable to roll over their short-term debt, SIVs were forced to liquidate assets to pay off maturing obligations and began to wind down operations.[39] In addition, NRSROs rapidly downgraded SIV securities, increasing downward price pressures already generated by these securities' lack of liquidity. The value of the commercial paper fell, which threatened to force several money market funds to break the buck.

Money market funds weathered this storm. In some cases, bank sponsors of SIVs provided support for the SIVs.[40] In other cases, money market fund affiliates voluntarily

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36 *See* 1983 Adopting Release, *supra* note 3, at nn.41-42 and accompanying text; 1996 Adopting Release, *supra* note 20, at nn.22-29 and accompanying text.

37 *See* Neil Shah, *Money Market Funds Cut Exposure to Risky SIV Debt—S&P*, REUTERS, Nov. 21, 2007, *available at* http://www.reuters.com/article/bondsNews/idUSN2146813220071121.

38 We know of at least 44 money market funds that were supported by affiliates because of SIV investments. In many of these cases the affiliate support was provided in reliance on no-action assurances provided by Commission staff. Many of these no-action letters are available on our website. *See* http://www.sec.gov/divisions/investment/im-noaction.shtml#money. Unlike other asset backed commercial paper, SIV debt was not backed by an external liquidity provider.

39 *See, e.g.*, Alistair Barr, *HSBC's Bailout Puts Pressure on Citi, "Superfund,"* MARKETWATCH, Nov. 26, 2007, *available at* http://www.marketwatch.com/story/hsbcs-35-bln-siv-bailout-puts-pressure-on-citi-superfund.

40 *See, e.g.*, *id.*

provided support to the funds by purchasing the SIV investments at their amortized cost or providing some form of credit support.[41] Money market funds also benefited from strong cash flows into money market funds, as investors fled from riskier markets. During the period from July 2007 to August 2008, more than $800 billion in new cash was invested in money market funds, increasing aggregate fund assets by one-third.[42] Eighty percent of these investments came from institutional investors.[43]

As financial markets continued to deteriorate in 2008, however, money market funds came under renewed stress. This pressure culminated the week of September 15, 2008 when the bankruptcy of Lehman Brothers Holdings Inc. ("Lehman Brothers") led to heavy redemptions from about a dozen money market funds that held Lehman Brothers debt securities. On September 15, 2008, The Reserve Fund, whose Primary Fund series held a $785 million position in commercial paper issued by Lehman Brothers, began experiencing a run on its Primary Fund, which spread to the other Reserve funds. The Reserve funds rapidly depleted their cash to satisfy redemptions, and began offering to sell the funds' portfolio securities into the market, further depressing their valuations. Unlike the other money market funds that held Lehman Brothers debt securities (and SIV commercial paper), The Reserve Primary Fund ultimately had no affiliate with sufficient resources to support the $1.00 net asset value. On September 16, 2008, The Reserve Fund announced that as of that afternoon, its Primary Fund would break the

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41 *See, e.g.*, Shannon D. Harrington & Christopher Condon, *Bank of America, Legg Mason Prop Up Their Money Funds*, BLOOMBERG, Nov. 13, 2007, *available at* http://www.bloomberg.com/apps/news?pid=20601087&sid=aWWjLp8m3J1I&refer=home. Under rule 17a-9, funds are not required to report to us all such transactions. *See infra* Section II.H.

42 *See* ICI REPORT, *supra* note 6, at 49.

43 *Id.*

buck and price its securities at $0.97 per share.[44] On September 22, 2008, in response to a request by The Reserve Fund, the Commission issued an order permitting the suspension of redemptions in certain Reserve funds, to permit their orderly liquidation.[45]

These events led many investors, especially institutional investors, to redeem their holdings in other prime money market funds and move assets to Treasury or government money market funds.[46] This trend was intensified by turbulence in the market for financial sector securities as a result of the bankruptcy of Lehman Brothers and the near failure of American International Group, whose commercial paper was held by many prime money market funds.

During the week of September 15, 2008, investors withdrew approximately $300 billion from prime (taxable) money market funds, or 14 percent of the assets held in those funds.[47] Most of the heaviest redemptions were from institutional funds, which depleted cash positions and threatened to force a fire sale of portfolio securities that would have placed widespread pressure

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44 *See* Press Release, The Reserve Fund, A Statement Regarding The Primary Fund (Sept. 16, 2008). The Reserve Fund subsequently stated that the fund had broken the buck earlier in the day on September 16. *See* Press Release, The Reserve Fund, Important Notice Regarding Reserve Primary Fund's Net Asset Value (Nov. 26, 2008) ("The Fund is announcing today that, contrary to previous statements to the public and to investors, the Fund's net asset value per share was $0.99 from 11:00 a.m. Eastern time to 4:00 p.m. Eastern time on September 16, 2008 and *not* $1.00.").

45 *See* In the Matter of The Reserve Fund, Investment Company Act Release No. 28386 (Sept. 22, 2008) [73 FR 55572 (Sept. 25, 2008)] (order). Several other Reserve funds also obtained an order from the Commission on October 24, 2008 permitting them to suspend redemptions to allow for their orderly liquidation. *See* Reserve Municipal Money-Market Trust, et al., Investment Company Act Release No. 28466 (Oct. 24, 2008) [73 FR 64993 (Oct. 31, 2008)] (order).

46 *See* U.S. Dollar Money Market Funds, *supra* note 17, at 72; BLACKROCK, THE CREDIT CRISIS: U.S. GOVERNMENT ACTIONS AND IMPLICATIONS FOR CASH INVESTORS (Nov. 2008), *available at* https://www2.blackrock.com/webcore/litService/search/getDocument.seam?venue=PUB_INS&ServiceName=PublicServiceView&ContentID=50824 ("THE CREDIT CRISIS"); Standard & Poor's, *Money Market Funds Tackle 'Exuberant Irrationality,'* RATINGS DIRECT, Sept. 30, 2008, *available at* http://www2.standardandpoors.com/spf/pdf/media/MoneyMarketFunds_Irrationality.pdf.

47 *See* ICI REPORT, *supra* note 6, at 62 (analyzing data from iMoneyNet); *see also* Investment Company Institute, *Money Market Mutual Fund Assets Historical Data*, Apr. 30, 2009, *available at* http://www.ici.org/pdf/mm_data_2009.pdf ("ICI Mutual Fund Historical Data").

on fund share prices.[48] Fearing further redemptions, money market fund (and other cash) managers began to retain cash rather than invest in commercial paper, certificates of deposit or other short-term instruments.[49] In the final two weeks of September 2008, money market funds reduced their holdings of top-rated commercial paper by $200.3 billion, or 29 percent.[50]

As a consequence, short-term markets seized up, impairing access to credit in short-term private debt markets.[51] Some commercial paper issuers were only able to issue debt with overnight maturities.[52] The interest rate premium (spread) over three-month Treasury bills paid

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48 *See* ICI Mutual Fund Historical Data, *supra* note 47.

49 *See* Philip Swagel, "The Financial Crisis: An Inside View," Brookings Papers on Economic Activity, at 31 (Spring 2009) (conference draft), *available at* http://www.brookings.edu/economics/bpea/~/media/Files/Programs/ES/BPEA/2009_spring_bpea_papers/2009_spring_bpea_swagel.pdf.

50 *See* Christopher Condon & Bryan Keogh, *Funds' Flight from Commercial Paper Forced Fed Move*, BLOOMBERG, Oct. 7, 2008, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a5hvnKFCC_pQ.

51 *See Minutes of the Federal Open Market Committee*, FEDERAL RESERVE BOARD, Oct. 28-29, 2008, at 5, *available at* http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081029.pdf ("*FRB Open Market Committee Oct. 28-29 Minutes*") (stating that following The Reserve Fund's announcement that the Primary Fund would break the buck, "risk spreads on commercial paper rose considerably and were very volatile" and "[c]onditions in short-term funding markets improved somewhat following the announcement of...a number of mutual initiatives by the Federal Reserve and the Treasury to address the pressures on money market funds and the commercial paper market"). *See also* Press Release, Federal Reserve Board Announces Creation of the Commercial Paper Funding Facility (CPFF) to Help Provide Liquidity to Term Funding Markets (Oct. 7, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20081007c.htm ("The commercial paper market has been under considerable strain in recent weeks as money market mutual funds and other investors, themselves often facing liquidity pressures, have become increasingly reluctant to purchase commercial paper, especially at longer-dated maturities. As a result, the volume of outstanding commercial paper has shrunk, interest rates on longer term commercial paper have increased significantly, and an increasingly high percentage of outstanding paper must now be refinanced each day. A large share of outstanding commercial paper is issued or sponsored by financial intermediaries, and their difficulties placing commercial paper have made it more difficult for those intermediaries to play their vital role in meeting the credit needs of businesses and households.").

52 *See* Matthew Cowley, *Burnt Money Market Funds Stymie Short-Term Debt*, DOW JONES INTERNATIONAL NEWS, Oct. 1, 2008; Anusha Shrivastava, *Commercial-Paper Market Seizes Up*, THE WALL STREET JOURNAL, Sept. 19, 2008, at C2.

by issuers of three-month commercial paper widened significantly from approximately 25-100 basis points before the September 2008 market events to approximately 200-350 basis points, and issuers were exposed to the costs and risks of having to roll over increasingly large amounts of commercial paper each day.[53] Many money market fund sponsors took extraordinary steps to protect funds' net assets and preserve shareholder liquidity by purchasing large amounts of securities at the higher of market value or amortized cost and by providing capital support to the funds.[54]

On September 19, 2008, the U.S. Department of the Treasury and the Board of Governors of the Federal Reserve System ("Federal Reserve Board") announced an unprecedented market intervention by the federal government in order to stabilize and provide liquidity to the short-term markets. The Department of the Treasury announced its Temporary Guarantee Program for Money Market Funds ("Guarantee Program"), which temporarily guaranteed certain investments in money market funds that decided to participate in the program.[55] The Federal

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53 *See* Federal Reserve Board data, *available at* http://www.frbatlanta.org/econ_rd/macroblog/102808b.jpg (charting three-month commercial paper spreads over three-month Treasury bill); *see also* Federal Reserve Board Chairman Ben S. Bernanke, Testimony before the Committee on Financial Services, U.S. House of Representatives (Nov. 18, 2008), *available at* http://www.federalreserve.gov/newsevents/testimony/bernanke20081118a.htm.

54 Commission staff provided no-action assurances allowing 100 money market funds in 18 different fund complexes to enter into such arrangements during the period from September 16, 2008 to October 1, 2008. *See, e.g.*, http://www.sec.gov/divisions/investment/im-noaction.shtml#money.

55 *See* Press Release, U.S. Department of the Treasury, Treasury Announces Guaranty Program for Money Market Funds (Sept. 19, 2008), *available at* http://www.treas.gov/press/releases/hp1147.htm. The Program insures investments in money market funds, to the extent of their shareholdings as of September 19, 2008, if the fund has chosen to participate in the Program. The Guarantee Program is due to expire on September 18, 2009. We adopted, on an interim final basis, a temporary rule, rule 22e-3T, to facilitate the ability of money market funds to participate in the Guarantee Program. The rule permits a participating fund to suspend redemptions if it breaks a buck and liquidates under the terms of the Program. *See* Rule 22e-3T Adopting Release, *supra* note 31. The temporary rule will expire on October 18, 2009. We discuss this rule in more detail in *infra* Section II.I.

Reserve Board announced the creation of its Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility ("AMLF"), through which it extended credit to U.S. banks and bank holding companies to finance their purchases of high-quality asset backed commercial paper from money market funds.[56] In addition, the Federal Reserve Board's Commercial Paper Funding Facility ("CPFF") provided support to issuers of commercial paper through a conduit that purchased commercial paper from eligible issuers, although the CPFF did not purchase commercial paper from money market funds.[57] The Commission and its staff worked closely with the Treasury Department and the Federal Reserve Board to help design these programs, most of which relied in part on rule 2a-7 to tailor the program and/or condition the terms of a fund's participation in the program, and we also assisted in administering the Guarantee Program.[58] Our staff also worked with sponsors of money market funds to provide regulatory

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56 *See* Press Release, Federal Reserve Board, Federal Reserve Board Announces Two Enhancements to its Programs to Provide Liquidity to Markets (Sept. 19, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20080919a.htm. The AMLF will expire on February 1, 2010, unless extended. *See* Press Release, Federal Reserve Board, Federal Reserve Announces Extensions of and Modifications to a Number of Its Liquidity Programs (June 25, 2009), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20090625a.htm ("2009 Federal Reserve Extension and Modification Announcement").

57 *See* Press Release, Federal Reserve Board, Board Announces Creation of the Commercial Paper Funding Facility (CPFF) to Help Provide Liquidity to Term Funding Markets (Oct. 7, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20081007c.htm. At one point the Federal Reserve had purchased about one-fifth of all commercial paper outstanding in the U.S. market. *See* Bryan Keogh, *GE Leads Commercial Paper "Test" as Fed's Buying Ebbs*, BLOOMBERG, Jan. 27, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aHWA87Aa2aQQ. The CPFF will expire on February 1, 2010, unless extended. *See* 2009 Federal Reserve Extension and Modification Announcement, *supra* note 56. Although the CPFF did not directly benefit money market funds, it did indirectly benefit them by stabilizing the commercial paper market. *See, e.g.*, Richard G. Anderson, *The Success of the CPFF?* (Economic Synopses No. 18, Federal Reserve Bank of St. Louis, 2009), at 2, *available at* http://www.research.stlouisfed.org/publications/es/09/ES0918.pdf.

58 *See, e.g.*, Guarantee Agreement that money market funds participating in the Treasury's Guarantee Program were required to sign, at 2, 10, *available at* http://www.treas.gov/offices/domestic-finance/key-initiatives/money-market-docs/Guarantee-Agreement_form.pdf (under which money market funds were required to state that they operated

relief they requested to participate fully in these programs.[59]

These steps helped to stanch the tide of redemptions from institutional prime money market funds,[60] and provided liquidity to money market funds that held asset backed commercial paper. Commercial paper markets remained illiquid, however, and, as a result, money market funds experienced significant problems pricing portfolio securities. Institutional as well as retail money market funds with little redemption activity and no distressed securities reported to our staff that they nevertheless faced the prospect of breaking the buck as a consequence of their reliance on independent pricing services that reported prices based on models with few reliable inputs. The Commission's Office of Chief Accountant and the Financial Accounting Standards Board provided funds and others guidance on determining fair value of securities in turbulent markets,[61] but it appeared that fund boards remained reluctant to deviate from the prices received from their vendors. On October 10, 2008, our Division of Investment Management issued a letter agreeing not to recommend enforcement action if money market funds met the "shadow pricing" obligations of rule 2a-7 by pricing certain of their portfolio securities with a remaining

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in compliance with rule 2a-7 to be eligible to initially participate in the program and must continue to comply with rule 2a-7 to continue to participate in the program); *see also* http://www.sec.gov/divisions/investment/mmtempguarantee.htm.

59 *See* Investment Company Institute, SEC Staff No-Action Letter (Sept. 25, 2008) (relating to the AMLF); Investment Company Institute, SEC Staff No-Action Letter (Oct. 8, 2008) (relating to the Guarantee Program). These no-action letters are available on our website at http://www.sec.gov/divisions/investment/im-noaction.shtml#money.

60 During the week ending September 18, 2008, taxable institutional money market funds experienced net outflows of $165 billion. *See Money Fund Assets Fell to $3.4T in Latest Week*, ASSOCIATED PRESS, Sept. 18, 2008. Almost $80 billion was withdrawn from prime money market funds even after the announcement of the Guarantee Program on September 19, 2008. *See* Diana B. Henriques, *As Cash Leaves Money Funds, Financial Firms Sign Up for U.S. Protection*, N.Y. TIMES, Oct. 2, 2008, at C10. However, by the end of the week following the announcement, net outflows from taxable institutional money market funds had ceased. *See Money Fund Assets Fell to $3.398T in Latest Week*, ASSOCIATED PRESS, Sept. 25, 2008.

61 *See* Press Release No. 2008-234, Securities and Exchange Commission, Office of the Chief Accountant and FASB Staff Clarifications on Fair Value Accounting (Sept. 30, 2008), *available at* http://www.sec.gov/news/press/2008/2008-234.htm.

final maturity of less than 60 days by reference to their amortized cost.[62]

Over the four weeks after The Reserve Fund's announcement, assets in institutional prime money market funds shrank by 30 percent, or approximately $418 billion (from $1.38 trillion to $962 billion).[63] No money market fund other than The Reserve Primary Fund broke the buck, although money market fund sponsors or their affiliated persons in many cases committed extraordinary amounts of capital to support the $1.00 net asset value per share. Our staff estimates that during the period from August 2007 to December 31, 2008, almost 20 percent of all money market funds received some support from their money managers or their affiliates.[64]

During this time period, short-term credit markets became virtually frozen as market participants hoarded cash and generally refused to lend on more than an overnight basis.[65] Interest rate spreads increased dramatically.[66] After shrinking to historically low levels as credit markets boomed in the mid-2000s, interest rate spreads surged upward in the summer of 2007

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62 Investment Company Institute, SEC Staff No-Action Letter (Oct. 10, 2008). This letter is available on our website at http://www.sec.gov/divisions/investment/noaction/2008/ICI101008.htm. The letter by its terms did not apply, however, to shadow pricing if particular circumstances (such as the impairment of the creditworthiness of the issuer) suggested that amortized cost was not appropriate. The staff position also was limited to portfolio securities that were "first tier securities" under rule 2a-7 and that the fund reasonably expected to hold to maturity. The letter applied to shadow pricing procedures through January 12, 2009.

63 On September 10, 2008, six days prior to The Reserve Fund's announcement, approximately $1.38 trillion was invested in institutional prime (taxable) money market funds. *See* ICI Mutual Fund Historical Data, *supra* note 47. On October 8, 2008, approximately $962 billion was invested in those funds. *See id.* In addition, between September 10 and September 17, the assets of these funds fell by approximately $193 billion. *See id.*

64 This estimate is based on no-action requests and other conversations with our staff during this time period.

65 THE CREDIT CRISIS, *supra* note 46, at 1 ("After experiencing more than $400 billion in outflows over a short period of time, money funds had little appetite for commercial paper; even quality issuers discovered they could not access the commercial paper market ....").

66 An interest rate spread measures the difference in interest rates of debt instruments with different risk. *See* Markus K. Brunnermeier, *Deciphering the Liquidity and Credit Crunch 2007-2008*, 23 J. ECON. PERSPECTIVES 77, 85, Winter 2009 ("Brunnermeier").

and peaked after the bankruptcy of Lehman Brothers in September 2008.[67] Money market funds shortened the weighted average maturity of their portfolios to be better positioned in light of increased liquidity risk to the funds.[68]

Although the crisis money markets faced last fall has abated, the problems have not disappeared. Today, while interest rate spreads have recently declined considerably, they remain above levels prior to the crisis,[69] and short-term debt markets remain fragile.[70] Although the average weighted average maturity of taxable money market funds (as a group) had risen to 53 days as of the week ended June 16, 2009,[71] we understand that the long-term securities that

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67 *See id.*; David Oakley, *LIBOR Hits Record Low as Credit Fears Ease*, FIN. TIMES, May 5, 2009. For example, the "TED" spread (the difference between the risk-free U.S. Treasury Bill rate and the riskier London Inter-bank Offering Rate ("LIBOR")), normally around 50 basis points, reached a high of 463 basis points on October 10, 2008. *See* David Serchuk, *Banks Led by the TED*, FORBES, Jan. 12, 2009.

68 Taxable money market fund average weighted average maturities shortened to 40-42 days during October 2008 from 45-46 days shortly prior to this period based on analysis of data from the iMoneyNet Money Fund Analyzer database.

69 The TED spread was 52 basis points on May 29, 2009. The LIBOR-OIS spread (the difference between three-month dollar London Interbank Offered Rate and the overnight index swap rate) was 45 basis points. *See* Lukanyo Mnyanda, *Libor Declines for Second Day on Signs Economic Slump is Easing*, BLOOMBERG, May 29, 2009, *available at* http://www.bloomberg.com/apps/news?pid=20670001&sid=agpZArg2paJE. Prior to the start of the financial turbulence in the summer of 2007, the TED spread averaged approximately 25-50 basis points and the three-month LIBOR-OIS spread averaged 7-9 basis points. *See* historical chart of TED spread *available at* http://www.bloomberg.com/apps/cbuilder?ticker1=.TEDSP%3AIND; Simon Kwan, *Behavior of LIBOR in the Current Financial Crisis*, FRBSF ECONOMIC LETTER (Federal Reserve Bank of San Francisco), Jan. 23, 2009, at 2-3, *available at* http://www.frbsf.org/publications/economics/letter/2009/el2009-04.pdf.

70 *See* Bryan Keogh, John Detrixhe & Gabrielle Coppola, *Coca-Cola Flees Commercial Paper for Safety in Bonds*, BLOOMBERG, Mar. 17, 2009, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=atxKQSJUp6RE (noting that certain companies are issuing long-term debt to replace commercial paper to avoid the risk of not being able to roll over their commercial paper, given the instability in short-term credit markets); Michael McKee, *Fed Credit Has Stabilized Markets, Not Fixed Them, Study Says*, BLOOMBERG, Mar. 6, 2008, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aRGBZuGYE78Y.

71 This information is based on analysis of data from the iMoneyNet Money Fund Analyzer database.

account for the longer weighted average maturity are not commercial paper and corporate medium term notes (as they were before the crisis), but instead are predominantly government securities, which suggests that money market funds may still be concerned about credit risk.

The Treasury Guarantee Program has been extended twice, but is set to expire on September 18, 2009.[72] Programs established by the Federal Reserve Board to support liquidity in the short-term market are set to expire early next year.[73] Total money market fund assets have continued to grow and now amount to approximately $3.8 trillion.[74] However, the composition of those assets has changed dramatically. Between September 10 and October 8, 2008, government money market fund assets *increased* by about 47 percent compared to a *decrease* of about 21 percent in taxable prime money market fund assets.[75] Since that time, prime money market fund assets have begun to grow again, although they remain below pre-September 2008 levels and government money market fund assets remain elevated.[76]

Finally, The Reserve Primary Fund has yet to distribute all of its remaining assets to shareholders, many of whom were placed in financial hardship as a result of losing access to

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72 *See* Press Release, U.S. Department of the Treasury, Treasury Announces Extension of Temporary Guarantee Program for Money Market Funds (Nov. 24, 2008), *available at* http://www.treas.gov/press/releases/hp1290.htm; Press Release, U.S. Department of the Treasury, Treasury Announces Extension of Temporary Guarantee Program for Money Market Funds (Mar. 31, 2009), *available at* http://www.treas.gov/press/releases/tg76.htm.

73 The AMLF and the CPFF will expire on February 1, 2010. *See* Press Release, Federal Reserve (June 25, 2009), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20090625a.htm. The use of the AMLF peaked on October 1, 2008, with holdings of $152.1 billion. *See* FEDERAL RESERVE BOARD, STATISTICAL RELEASE H.4.1: FACTORS AFFECTING RESERVE BALANCES (Oct. 2, 2008), *available at* http://www.federalreserve.gov/releases/h41/20081002. AMLF holdings as of April 29, 2009 stood at $3.699 billion. *See* FEDERAL RESERVE BOARD, STATISTICAL RELEASE H.4.1: FACTORS AFFECTING RESERVE BALANCES (Apr. 30, 2009), *available at* http://www.federalreserve.gov/releases/h41/20090430.

74 *See* ICI Trends, *supra* note 4.

75 *See* ICI Mutual Fund Historical Data, *supra* note 47.

76 *See id.*

their investments.[77] The dissolution of the fund has been affected by several factors, including operational difficulties and lack of liquidity in the secondary markets, and by legal uncertainties over the disposition of the remaining assets. We recently instituted an action in federal court seeking to ensure that the liquidation is effected on a fair and equitable basis,[78] and propose in this release regulatory changes designed to protect investors in a fund that breaks a dollar in the future.[79]

II. Discussion

The severe problems experienced by money market funds since the fall of 2007 and culminating in the fall of 2008 have prompted us to review our regulation of money market funds. Based on that review, including our experience with The Reserve Fund, we today are proposing for public comment a number of significant amendments to rule 2a-7 under the Investment Company Act.

In formulating these proposals, Commission staff has consulted extensively with other members of the President's Working Group on Financial Markets, and in particular the Department of Treasury and the Federal Reserve Board, which provided support to money market funds and the short-term debt markets last fall, and which continue to administer programs from which money market funds and their shareholders benefit. We have consulted

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77 The Reserve Primary Fund did not make an initial partial pro rata distribution of assets until October 30, 2008. *See* Press Release, The Reserve Fund, Reserve Primary Fund Makes Initial Distribution of $26 Billion to Primary Fund Shareholders (Oct. 30, 2008). The fund has distributed approximately 90 percent of its assets. *See* Press Release, The Reserve Fund, Court Issues Order Setting Objection and Hearing Dates on Securities and Exchange Commission's Proposed Plan for Distribution of Reserve Primary Fund's Assets (June 15, 2009).

78 *See* SEC v. Reserve Management Co., Inc., *et al.*, Litigation Release No. 21025 (May 5, 2009), *available at* http://www.sec.gov/litigation/litreleases/2009/lr21025.htm. We note that we also have filed fraud charges against several entities and individuals who operate The Reserve Primary Fund alleging that they failed to provide key material facts to investors and trustees about the fund's vulnerability as Lehman Brothers sought bankruptcy protection. *See id.*

79 *See infra* Section II.I.

with managers of money market funds and other experts to develop a deeper understanding of the stresses experienced by funds and the impact of our regulations on the readiness of money market funds to cope with market turbulence and satisfy heavy demand for redemptions. In March, we received an extensive report from a "Money Market Working Group" assembled by the Investment Company Institute ("ICI Report"), which recommended a number of changes to our rule 2a-7 that it believes could improve the safety and oversight of money market funds.[80] We have also drawn from our experience as a regulator of money market funds under rule 2a-7 for more than 25 years and particularly since autumn 2007.

Our proposals, which we discuss in more detail below, are designed to increase the resilience of money market funds to market disruptions such as those that occurred last fall. The proposed rules would reduce the vulnerability of money market funds to breaking the buck by, among other things, improving money market funds' ability to satisfy significant demands for redemptions. If a particular fund does break the buck and determines to liquidate, the proposed rules would facilitate the orderly liquidation of the fund in order to protect the interests of all fund shareholders. These changes together should make money market funds (collectively) less susceptible to a run by diminishing the chance that a money market fund will break a dollar and, if one does, provide a means for the fund to orderly liquidate its assets. Finally, our proposals would improve our ability to oversee money market funds by requiring funds to submit to us current portfolio information.

Our proposals represent the first step in addressing issues we believe merit immediate attention.[81] Throughout this release, we ask comment on other possible regulatory changes

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80 ICI REPORT, *supra* note 6.

81 We note that we accomplished the reforms of money market fund regulation we initiated in 1990 in two steps. *See* 1990 Proposing Release, *supra* note 22 (taxable money market funds);

aimed at further strengthening the stability of money market funds. In addition, we ask comment on some more far-reaching changes that could transform the business and regulatory model on which money market funds have operated for more than 30 years, including whether money market funds should move to a floating net asset value.[82] We expect to benefit from the comments we receive before deciding whether to propose further changes.

A. Portfolio Quality

To limit the amount of credit risk to which money market funds can be exposed, rule 2a-7 limits them to investing in securities that a fund's board of directors (or its delegate pursuant to written guidelines) determines present minimal credit risks.[83] In addition, securities must at the time of acquisition be "eligible securities," which means in part that they must have received the highest or second highest short-term debt ratings from the "requisite NRSROs."[84] Because of the additional credit risk that generally is represented by securities rated in the second highest, rather than the highest, NRSRO rating category, a taxable money market fund may not invest more

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Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 19959 (Dec. 17, 1993) [58 FR 68585 (Dec. 28, 1993)] (tax exempt money market funds) ("1993 Proposing Release").

82 *See infra* Section III.A.

83 Rule 2a-7(c)(3)(i). Although rule 2a-7 refers to determinations to be made by a fund or its board, many of these determinations under the rule may be delegated to the investment adviser or fund officers pursuant to written guidelines that the board establishes and oversees to assure that the applicable procedures are being followed. Rule 2a-7(e).

84 Rule 2a-7(a)(10)(i) (defining "eligible security"). If the securities are unrated, they must be of comparable quality. Rule 2a-7(a)(10)(ii). The term "requisite NRSROs" is defined in paragraph (a)(21) of the rule to mean "(i) Any two NRSROs that have issued a rating with respect to a security or class of debt obligations of an issuer; or (ii) If only one NRSRO has issued a rating with respect to such security or class of debt obligations of an issuer at the time the fund Acquires the security, that NRSRO." Thus, a security can satisfy the ratings requirement in one of four ways: (1) it is rated in the same (top two) category by any two NRSROs; (2) if it is rated by at least two NRSROs in either of the top two categories, but no two NRSROs assign the same rating, the lower rating is assigned; (3) it is rated by only one NRSRO, in one of the top two categories; or (4) it is an unrated security that the board or its delegate determines to be of comparable quality to securities satisfying the rating criteria. The terms "rated security" and "unrated security" are defined in paragraphs (a)(19) and (a)(28) of rule 2a-7, respectively.

than five percent of its total assets in "second tier securities."[85] Tax exempt money market funds are limited in the same manner only with respect to second tier "conduit securities," *i.e.*, municipal securities backed by a private issuer.[86]

We are also proposing a change to the provisions of rule 2a-7 that limit money market funds to investing in high quality securities. We propose to generally limit money market fund investments to securities rated in the highest NRSRO ratings category. In addition, we are seeking comment on whether to modify provisions of the rule that incorporate minimum ratings by NRSROs to reflect changes made to the federal securities laws by the Credit Rating Agency Reform Act of 2006 ("Rating Agency Reform Act").[87]

1. Second Tier Securities

We propose to amend rule 2a-7 to allow money market funds to invest only in first tier securities. Under the proposed amendments, money market funds could "acquire" only "eligible securities," which would be re-defined to include securities receiving only the highest (rather than the highest two) short-term debt ratings from the "requisite NRSROs."[88] Funds would not

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[85] Rule 2a-7(c)(3)(ii)(A). *See also* rule 2a-7(a)(10) (defining "eligible security"), (a)(22) (defining "second tier security" as any eligible security that is not a first tier security), and (a)(12) (defining "first tier security" as, among other things, any eligible security that, if rated, has received the highest short-term term debt rating from the requisite NRSROs or, if unrated, has been determined by the fund's board of directors to be of comparable quality). *See also* 1990 Proposing Release, *supra* note 22, at Section II.1.b.

[86] Rule 2a-7(c)(3)(ii)(B). *See also* rule 2a-7(a)(7) (defining "conduit security").

[87] Credit Rating Agency Reform Act of 2006, Pub. L. No. 109-291, 120 Stat. 1327.

[88] *See* rule 2a-7(a)(1) (defining acquisition (or acquire) as any purchase or subsequent rollover, but not including the failure to exercise a demand feature); proposed rule 2a-7(a)(11)(iii) (defining eligible security); proposed rule 2a-7(c)(3) (portfolio quality). Because eligible securities would no longer be divided into first tier and second tier securities, both of those terms would be deleted from the rule, as would provisions relating specifically to second tier securities. *See* rule 2a-7(a)(12), (a)(22), (c)(3)(ii), (c)(4)(i)(C), (c)(4)(iii)(B), (c)(6)(i)(A), and (c)(6)(i)(C). We would therefore amend the definition of eligible security to require that securities receive "the highest," as opposed to "one of the two highest" short-term rating categories, as the current definition provides, and delete other references in the rule to the second highest rating category. *See* proposed rule 2a-7(a)(11)(iii). The definition of eligible security also would be expanded to

have to immediately dispose of a security that was downgraded by the requisite NRSROs but, under existing provisions of rule 2a-7, the fund would have to dispose of the security "as soon as practicable consistent with achieving an orderly disposition of the security" unless the fund's board of directors finds that such disposal would not be in the best interest of the fund.[89]

We have considered previously the extent to which money market funds should be permitted to invest in second tier securities. In 1991, following distress at several money market funds that held defaulted commercial paper, the Commission, among other things, limited a taxable money market fund's total investment in second tier securities to five percent of the fund's portfolio assets and limited the investment in any particular issuer of second tier securities to no more than the greater of one percent of the fund's portfolio assets or $1 million.[90] At that time, commenters in favor of eliminating money market funds' investment in second tier securities argued that such securities may undergo a rapid deterioration and thus may pose risks to the fund holding such securities as well as to investor confidence in money market funds in general.[91] On the other hand, issuers of second tier securities urged the Commission not to limit money market funds' holdings of second tier securities, arguing that the Commission's concerns regarding the creditworthiness of second tier securities were misplaced and that restrictions would raise issuers' borrowing costs and discourage money market funds from holding any

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include two types of securities, securities issued by a money market fund and "Government securities," that were formerly part of the definition of first tier securities. *See* proposed rule 2a-7(a)(11)(i) and (ii); *see also* rule 2a-7(a)(14) (defining Government security). Unrated securities determined by the board of directors of the fund or its delegate to be of comparable quality also would still be eligible securities. *See* proposed rule 2a-7(a)(11)(iv).

89 *See* rule 2a-7(c)(6)(ii); proposed rule 2a-7(c)(7)(ii).

90 *See* rule 2a-7(c)(3)(ii)(A), (c)(4)(i)(C)(1). *See also* 1991 Adopting Release, *supra* note 20.

91 *See* 1991 Adopting Release, *supra* note 20, at n.36 and accompanying text. Most commenters representing the mutual fund industry supported or did not oppose the limitations we proposed. *Id.* at n.35 and accompanying text.

second tier securities.[92] Based principally on the potential risk to money market funds of holding second tier securities, we adopted the five percent and one percent limitations to limit (but not eliminate) exposure of money market funds to second tier securities and any one issuer of second tier securities.[93]

Second tier securities were not directly implicated in the recent strains on money market funds. The ICI's Money Market Working Group expressed concern to us, however, that these securities may present an "imprudent" risk to the stable value of money market funds because they present "weaker credit profiles, smaller overall market share, and smaller issuer program sizes ...."[94] Our examination of the data discussed below suggests support for their recommendation that money market funds no longer be permitted to invest in these securities.[95]

Compared to the market for first tier securities, the market for second tier securities is relatively small. As of June 24, 2009, there was $1082.5 billion in rule 2a-7-eligible commercial paper outstanding, consisting of $1035.8 billion (95.7 percent) of first tier and $46.7 billion (4.3 percent) of second tier.[96] The size of the second tier market has remained consistently small over time.[97]

In addition, second tier securities present potentially substantially more risk than first tier

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92 *See id.* at text following n.35.

93 *See id.* at n.35-37 and accompanying text; 1990 Proposing Release, *supra* note 22, at n.33 and accompanying text.

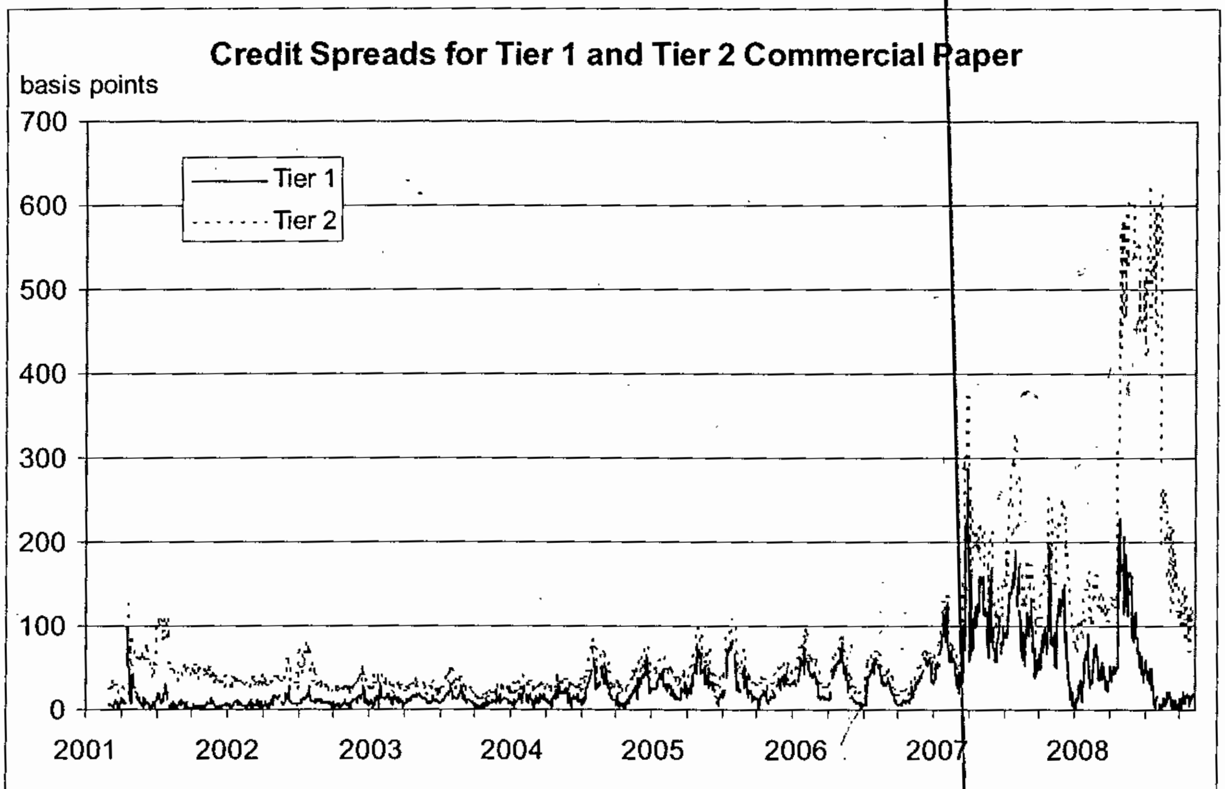
94 ICI REPORT, *supra* note 6, at 101.

95 *Id.* at 100.

96 *See* Federal Reserve Board Commercial Paper Outstanding Chart, *available at* http://www.federalreserve.gov/releases/cp/outstandings.htm (showing weekly levels of rule 2a-7-eligible commercial paper outstanding).

97 *See* Federal Reserve Board Commercial Paper Data Download Program, *available at* http:www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP (select year-end outstandings from the preformatted data package menu and follow the instructions for download). Over the last eight years, the market for second tier securities on average has represented only 4.6 percent of the rule 2a-7-eligible commercial paper market.

securities. As the following chart shows, during the market disruptions of last fall, second tier securities experienced significantly wider credit spreads than first tier securities.[98]



Source of Data: Federal Reserve, *available at* http://www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP.

Second tier securities as an asset class also are of weaker credit quality in terms of interest coverage ratios, debt coverage ratios, and debt to equity ratios.[99] These data strongly suggest that

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98 *See* Federal Reserve Board Commercial Paper Rates Chart, *available at* http://www.federalreserve.gov/releases/cp/default.htm. *See also* FRANK J. FABOZZI, THE HANDBOOK OF FIXED INCOME SECURITIES, at 4 (7^{th} ed. 2005) ("Default risk or credit risk refers to the risk that the issuer of a bond may be unable to make timely payment of principal or interest payments .... The spread between Treasury securities and non-Treasury securities that are identical in all respects except for quality is referred to as a *credit spread* or *quality spread*.").

99 *See* STANDARD & POOR'S, CREDITSTATS: 2007 ADJUSTED KEY U.S. INDUSTRIAL AND UTILITY FINANCIAL RATIOS, at 6, Table 3 (Sept. 10, 2008), *available at* http://www2.standardandpoors.com/spf/pdf/fixedincome/CreditStats_2007_Adjusted_Key_Financial_Ratios.pdf (showing A-2 rated commercial paper had EBIT interest coverage of 7.2x, free operating cash flow to debt of 16.7%, and debt to debt plus equity of 45.1%, compared to A-1 averages of 11.5x, 31.3%, and 37.1%, respectively, represented as three-year (2005-2007) averages).

second tier securities generally present additional risks to a money market fund. This is a conclusion that may have been reached by money market fund managers, most of which (as described below) do not invest in second tier securities. In light of the risks that second tier securities generally present to money market funds, and the consequences to funds and fund investors of breaking a dollar, we are proposing to limit funds to investing in first tier securities. We believe such a limitation would make it less likely that a money market fund would hold a problematic security, or a security that would lose significant value as a result of market disruptions.

It does not appear that amending rule 2a-7 to eliminate money market funds' ability to acquire second tier securities would be materially disruptive to funds. Prior to our amendments to rule 2a-7 in 1991, non-government money market funds held more than eight percent of their assets in second tier securities.[100] After we restricted the amount of second tier securities money market funds could buy, the funds soon reduced their holdings to almost zero.[101] Our staff's review of money market fund portfolios in September 2008 found that second tier securities represented only 0.4 percent of the $3.6 trillion held by the funds (approximately $14.6 billion).

We request comment on our proposal to eliminate the ability of money market funds to invest in second tier securities. What would be the impact on funds? Would the benefit of reducing credit risk by eliminating the ability of money market funds to invest in second tier securities outweigh any potential diversification benefits that second tier securities may otherwise provide to money market funds? What, if any, diversification benefits do money market funds currently receive from investing in second tier securities? Would this change have a significant effect on yields?

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100 *See* Crabbe & Post, *supra* note 15, at 11, Table 2.

101 *See id*, at 11-12.

Would there be a proportionately greater impact of eliminating second tier securities on smaller or less established money market funds or on particular types of funds (*e.g.*, single-state tax exempt funds)? If the proposal to eliminate funds' ability to hold second tier securities is adopted, what transition period should we provide money market funds to dispose of their existing second tier holdings in an orderly manner? Should we allow funds that hold second tier securities after the amended rule becomes effective to continue to hold such securities until maturity?

Are there alternatives to eliminating entirely the ability of a money market fund to invest in second tier securities? For example, should money market funds instead be limited to investing in second tier securities (i) with a maximum maturity of, for example, 45 days, or (ii) as a smaller portion of fund assets, such as two percent of the total assets, or (iii) a combination of both? A security with a shorter maturity presents less credit risk to a fund (because the exposure is shorter) and less liquidity risk (because cash will be available sooner). Would such an approach address, or at least partly address, the concerns raised by the ICI Report and in this Release?[102] Could additional credit risk analysis or other procedures be imposed with respect to second tier securities to address these concerns?

2. Eligible Securities

a. Use of NRSROs

As discussed above, rule 2a-7 currently requires a money market fund to limit its portfolio investments to eligible securities, *i.e.*, short-term securities that at the time of acquisition have received ratings from the "requisite NRSROs" in one of the two highest short-

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[102] *See* ICI REPORT, *supra* note 6, at 100-101.

term debt rating categories and securities that are comparable to rated securities.[103]

A determination that a security is an eligible security as a result of its NRSRO ratings is a necessary but not sufficient finding in order for a fund to acquire the security.[104] References to NRSRO ratings in rule 2a-7 and other regulations were designed to provide a clear reference point to regulators and market participants. The reliability of credit ratings, however, has been questioned, in particular in light of developments during the recent financial crisis. As a result, there have been calls to produce higher quality ratings. Last year, we proposed to eliminate the use of NRSRO ratings in rules under the Investment Company Act, including rule 2a-7, and instead to rely solely on the fund manager's credit risk determination.[105] In 2003, in a concept release seeking comment on various issues relating to credit rating agencies, we also asked whether credit ratings should be used as a minimum objective standard in rule 2a-7. Most commenters who addressed the specific question in 2003 supported retaining the ratings requirement in rule 2a-7.[106] One commenter asserted that "[t]he combination of this objective test with the 'subjective test' (credit analysis performed by the adviser to the money market

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103 *See supra* note 84 and accompanying text. A "rated security" generally means a security that (i) has received a short-term rating from an NRSRO, or whose issuer has received a short-term rating from an NRSRO with respect to a class of debt obligations that is comparable in priority and security with the security; or (ii) is subject to a guarantee that has received a short-term rating from an NRSRO, or a guarantee whose issuer has received a short-term rating from an NRSRO with respect to a class of debt obligations that is comparable in priority and security with the guarantee. Rule 2a-7(a)(19).

104 The rule also requires fund boards (which typically rely on the fund's adviser) to determine that the security presents minimal credit risks, and specifically requires that determination "be based on factors pertaining to credit quality in addition to any ratings assigned to such securities by an NRSRO." Rule 2a-7(c)(3)(i).

105 *See, e.g.*, References to Ratings of Nationally Recognized Statistical Rating Organizations, Investment Company Act Release No. 28327 (July 1, 2008) [73 FR 40124 (July 11, 2008)] ("NRSRO References Proposal").

106 *See, e.g.*, Comment Letter of Fidelity Investments (July 25, 2003) (File No. S7-12-03). Comment letters on File No. S7-12-03 are available at http://www.sec.gov/rules/concept/s71203.shtml.

fund) provides an important complementary rating structure under Rule 2a-7."[107] Similarly, in our proposal last year, a substantial majority of commenters disagreed with the proposed elimination of the ratings requirement.[108] The ICI Report summed up the views of many of these commenters, asserting that elimination of the NRSRO ratings' "floor ... would remove an important investor protection from Rule 2a-7, introduce new uncertainties and risks, and abandon a regulatory framework that has proven to be highly successful."[109] A few commenters supported removing the ratings requirement in 2003 and as proposed in 2008, however. One of these commenters noted that "one of the core causes of the sub-prime crisis was dependence on inaccurate and unsupportable credit ratings."[110]

In light of recent market developments, we request that commenters again address whether or not the approach we proposed last year would provide safeguards with respect to credit risk that are comparable to the continued inclusion of NRSRO references in the rule. What other alternatives could we adopt to encourage more independent credit risk analysis and meet the regulatory objectives of rule 2a-7's requirement of NRSRO ratings? Are there additional factors that we should consider with respect to last year's proposal? Should we consider establishing a roadmap for phasing in the eventual removal of NRSRO references from the rule? We are also considering an approach under which a money market fund's board would designate three (or more) NRSROs that the fund would look to for all purposes under rule 2a-7

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107 Comment Letter of Denise Voigt Crawford, Securities Commissioner, Texas State Securities Board (July 28, 2003) (File No. S7-12-03).

108 *See, e.g.,* Comment Letter of T. Rowe Price Family of Funds (Sept. 5, 2008) (File No. S7-19-08). Comment letters on File No. S7-19-08 are available at http://www.sec.gov/comments/s7-19-08/s71908.shtml.

109 *See* ICI REPORT, *supra* note 6, at 81.

110 *See* Comment Letter of Professor Frank Partnoy (received Sept. 5, 2008) (File No. S7-19-08).

in determining whether a security is an eligible security.[111] In addition, the board would be required to determine at least annually that the NRSROs it has designated issue credit ratings that are sufficiently reliable for that use.[112] We request comment on an approach in which the fund board designates NRSROs. Would the inclusion of a number of "designated NRSROs" improve rule 2a-7's use of NRSRO ratings as a threshold investment criterion and be consistent with the goals of Congress in passing the Rating Agency Reform Act?[113] What are the advantages and disadvantages of such an approach? Should funds be required to designate a minimum number of NRSROs to use in determining thresholds for Eligible Securities or in monitoring ratings? If so, would at least three be the appropriate number, as some have suggested?[114] Would more be appropriate to address these purposes (*e.g.*, four, five or six)? Should we permit fund boards to designate different NRSROs with respect to different types of issuers of securities in which the fund invests? Should the funds be required to disclose these designated NRSROs in their

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111 Commenters on our NRSRO References Proposal and the ICI Report recommended similar approaches. *See* Comment Letter of Federated Investors, Inc. (Sept. 5, 2008) (File No. S7-19-08) (suggesting that rule 2a-7 require the board or its delegate to select by security type at least three NRSROs on which the fund would rely under the rule); Comment Letter of OppenheimerFunds, Inc. (Sept. 4, 2008) (File No. S7-19-08) (suggesting the rule allow fund boards to designate (presumably after considering any recommendations of the investment manager) the identity and number of NRSROs whose ratings will be used to determine eligible portfolio securities); ICI REPORT, *supra* note 6, at 82 (recommending the fund designate three or more NRSROs that the fund would use in determining the eligibility of portfolio securities). *See also* Comment Letter of Stephen A. Keen on behalf of Federated Investors, Inc. (Mar. 12, 2007) (File No. S7-04-07) (in response to our 2007 proposal on oversight of NRSROs, asserting that investment advisers should be free to choose which NRSROs they will rely upon and monitor only their ratings).

112 The only time that funds would be required to look to all NRSROs under this approach would be, as under the current rule, in determining whether a long-term security with a remaining maturity of 397 calendar days or less that does not, and whose issuer does not, have a short-term rating is an eligible security. *See infra* section II.A.2.b.

113 *See* Senate Committee on Banking, Housing, and Urban Affairs, Credit Rating Agency Reform Act of 2006, S. Rep. No. 109-326, at 2 (2006) ("Senate Report 109-326") (purposes of the Act include improving the quality of NRSRO credit ratings by fostering accountability, transparency, and competition in the credit rating industry).

114 *See supra* note 111.

statements of additional information?[115]

What impact would a requirement that the fund board designate NRSROs have on competition among NRSROs? Would NRSROs compete through ratings to achieve designation by money market funds? Given that the staff believes it is reasonable to assume that the three NRSROs that issued almost 99 percent of all outstanding ratings across all categories that were issued by the 10 registered NRSROs as of June 2008,[116] also issued well over 90 percent of all outstanding ratings of short term debt, and in light of concerns about enhancing competition among NRSROs, should the minimum number of designated NRSROs be greater than three, such as four, five, or six?[117] What are the advantages and disadvantages of requiring boards to monitor the ratings issued by all NRSROs? Should rule 2a-7 specify certain minimum policies and procedures for monitoring NRSROs? Should money market fund boards be permitted to designate credit rating agencies or credit evaluation providers that are not registered as NRSROs with the Commission under the Securities Exchange Act of 1934 and the rules we have adopted under those provisions?[118] Should a board be solely responsible for designating and annually reviewing a designated NRSRO or should we permit delegation of this responsibility? How many NRSROs would money market fund boards be likely to evaluate before making their designations? After a fund board had designated NRSROs, what incentives would the board have to change the designated NRSROs?

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115 *See* Part B of Form N-1A.

116 The staff's belief is based on its report that three NRSROs issued almost 99 percent of all the outstanding ratings across all categories that were issued by the 10 registered NRSROs as of June 2008. *See* SEC, ANNUAL REPORT ON NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS at 35 (June 2008) ("2008 NRSRO REPORT").

117 According to the ICI Report, requiring money market funds to designate at least three NRSROs whose ratings the fund would use in determining eligible portfolio securities could encourage competition among NRSROs to achieve designation by money market funds. *See* ICI REPORT, *supra* note 6, at 82.

118 *See* 15 U.S.C. 78o-7; 17 CFR 240.17g-1 (rules governing the registration of NRSROs).

We request comment on the impact of any of these approaches on funds and their ability to maintain a stable net asset value. Would any particular requirement help funds to better determine whether a security is an eligible security? We also request comment on the potential impact on competition among NRSROs.

b. Long-Term Unrated Securities

Rule 2a-7 permits money market funds to invest in a long-term security with a remaining maturity of 397 calendar days or less ("stub security") that is an unrated security (*i.e.*, neither the security nor its issuer or guarantor has a short-term rating) *unless* the security has received a long-term rating from any NRSRO that is not within the NRSRO's three highest categories of long-term ratings.[119] Under rule 2a-7, the measure of quality is the rating given to the issuer's short-term debt. In the absence of a short-term rating, the minimum long-term rating is designed to provide an independent check on a fund's quality determination.[120] In light of the changes we are proposing above to increase the portfolio quality standards of the rule, we propose to permit money market funds to acquire such securities only if they have received long-term ratings in the highest two ratings categories to more narrowly limit the credit risk to which a money market fund may be exposed.[121] As under the current rule, fund boards would continue to be required to determine that such a security is "of comparable quality" to a rated security if it met these

119 Rule 2a-7(a)(10)(ii)(A). Nonetheless, the security may be an eligible security if it has received a long-term rating from the requisite NRSROs in one of the three highest long-term rating categories and (as with any unrated security that is an eligible security) is of comparable quality to a rated security. *Id.*

120 *See* 1991 Adopting Release, *supra* note 20, at text accompanying nn.65-68.

121 Proposed rule 2a-7(a)(11)(iv)(A). Similar to the provision in the current rule, the security might be an eligible security even if it received a long-term rating below the two highest long-term rating categories if the requisite NRSROs rate the security in one of the two highest long-term rating categories. *Id.*

proposed conditions.[122]

We request comment on this proposed change. Given our proposal to increase the quality standards of the rule, is the proposed change appropriate? Should we consider permitting funds to acquire these stub securities only if they have received long-term ratings in the highest rating category? What impact would the proposed amendment have on money market funds' current portfolio holdings? We request commenters expressing views on this change to provide us with data identifying the relationship between the long-term ratings on these stub securities and short-term ratings.

3. *Credit Reassessments*

Rule 2a-7 currently requires a money market fund's board of directors to promptly reassess whether a portfolio security continues to present minimal credit risks if, subsequent to its acquisition by the fund, (i) the security has ceased to be a first tier security (*e.g.*, the security is downgraded to second tier by one of the requisite NRSROs), or (ii) the fund's adviser *becomes aware* that an unrated or second tier security has received a rating from *any* NRSRO below the second highest short-term rating category.[123] In light of the proposed elimination of second tier securities from the definition of eligible security, we propose to amend rule 2a-7 so the only circumstance in which the fund's board of directors would be required to reassess whether a security continues to present minimal credit risks would be if, subsequent to its acquisition by the fund, the fund's money market fund adviser becomes aware that an unrated security has received a rating from any NRSRO below the highest short-term rating category.[124]

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122 Proposed rule 2a-7(a)(11)(iv).

123 Rule 2a-7(c)(6)(i)(A)(1) and (2).

124 Proposed rule 2a-7(c)(7)(i)(A). As under the current rule, the proposed rule amendment would not require, and we would not expect, investment advisers to subscribe to every rating service publication in order to comply with the requirement that the board reassess when the fund's

We request comment on whether these are appropriate circumstances under which to require a reassessment in light of our proposal to eliminate the ability of money market funds to invest in second tier securities.

4. *Asset Backed Securities*

Rule 2a-7 contains provisions that specifically address asset backed securities ("ABSs"),[125] including the circumstances under which an ABS is an eligible security,[126] the maturity of an ABS,[127] and how a fund must treat such an investment under the diversification provisions.[128] The rule, however, does not specifically address how a fund board (or its delegate) should determine that an investment in an ABS (or other potential portfolio investment) presents minimal credit risks, nor does it specifically address liquidity issues presented by a money market fund's investment in an ABS.

Both such matters were raised in 2007 by money market funds' investment in SIVs, which we discussed briefly above. SIVs issued commercial paper to finance a portfolio of longer term, higher yielding investments, including residential mortgages. Unlike other commercial paper programs, SIVs typically did not have access to liquidity facilities to protect commercial paper investors (including money market funds) against the risk of the issuer's inability to reissue (or "rollover") commercial paper caused by either a credit event of the issuer or a

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adviser becomes aware that any NRSRO has rated an unrated security below its highest rating. We would expect an investment adviser to become aware of a subsequent rating if it is reported in the national financial press or in publications to which the adviser subscribes. *See* 1991 Adopting Release, *supra* note 20, at n.71.

125 An asset backed security is defined very generally to mean a fixed income security that entitles its holders to receive payments that depend primarily on the cash flow from financial assets underlying the asset backed security. *See* rule 2a-7(a)(3).

126 *See* rule 2a-7(a)(10)(ii)(B).

127 *See* rules 2a-7(a)(8)(ii) and 2a-7(d).

128 *See* rule 2a-7(c)(4)(ii)(D).

disruption in the commercial paper market.[129] When they could no longer rollover their debt beginning in 2007, those SIVs, unable to secure liquidity support from sponsoring banks, were forced to begin selling the vehicles' assets into depressed markets to pay maturing debt and to begin winding down their operations. SIV credit ratings deteriorated rapidly as they deleveraged, placing pressure on valuations of SIV securities held by money market funds. We understand that eventually most funds holding SIV securities not supported by a large bank entered into agreements with affiliates of the fund to support the fund's stable net asset value per share.

We request comment on whether, and if so how, we should amend rule 2a-7 to address risks presented by SIVs or similar ABSs. As discussed above, rule 2a-7 requires that money market funds only invest in securities that the board of directors or its delegate determines present minimal credit risks.[130] The Commission has stated that "[d]etermining that an ABS presents minimal credit risks requires an examination of the criteria used to select the underlying assets, the credit quality of the put providers, and the conditions of the contractual relationships among the parties to the arrangement. When an ABS consists of a large pool of financial assets, such as credit card receivables or mortgages, it may not be susceptible to conventional means of credit risk analysis because credit quality is based not on a single issuer but on an actuarial analysis of a pool of financial assets."[131] We also said, however, that we were concerned that "fund credit analysts may be unable to perform the thorough legal, structural and credit analyses required to determine whether a particular ABS involves inappropriate risks for money market

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129 For a discussion of the evolution of the asset backed commercial paper market and SIV securities during this period, *see generally* Jim Croke, *New Developments in Asset-Backed Commercial Paper* (2008), at 2-4, *available at* http://www.orrick.com/fileupload/1485.pdf.

130 Rule 2a-7(c)(3)(i).

131 1993 Proposing Release, *supra* note 81, at text accompanying nn.108-109.

funds" and, as a result, required that any ABS in which a money market fund invested be rated by an NRSRO because of NRSROs' role in assuring that the underlying ABS assets are properly valued and provide adequate asset coverage for the cash flows required to fund ABSs.[132]

As discussed above, beginning in 2007, SIV securities were rapidly downgraded by NRSROs revealing money market funds' varying minimal credit risk determinations with respect to these securities. In light of this experience, should we provide additional guidance to money market funds on the required minimal credit risk evaluation with respect to ABSs? We believe that part of this analysis, when evaluating any security, should include an evaluation of the issuer's ability to maintain its promised cash flows which, in the case of an asset backed security, would entail an analysis of the underlying assets, their behavior in various market conditions, and the terms of any liquidity or other support provided by the sponsor of the security.[133] Should we amend rule 2a-7 to remove the requirement that any ABS be rated by an NRSRO in order to be an eligible security for money market funds in light of the NRSROs' recent rapid downgrading of these securities? Under our proposed liquidity requirements (discussed below), the liquidity features of an ABS would have to be considered in determining whether the fund holds sufficiently liquid assets to meet shareholder redemptions.[134]

We request comment on whether rule 2a-7 should explicitly require fund boards of directors (or their delegates) to evaluate whether the security includes any committed line of credit or other liquidity support. Are there other factors that we should require money market

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132 *Id.* at nn.110-112 and accompanying text.

133 The ICI Report recommended that we amend rule 2a-7 to require money market fund advisers to adopt a "new products committee." *See* ICI REPORT, *supra* note 6, at 79-80. Although such committees may be useful, their usefulness would turn on what might be a "new product" as well as the judgment of its members, whose judgment is today required to be brought to bear on whether the security presents minimal credit risks.

134 *See infra* Section II.C.

fund boards to evaluate when determining whether SIV investments or other new financial products pose minimal credit risks? We note that some money market funds invested more significantly in SIV securities while other money market funds avoided such investments entirely. Are there facets of the credit analysis that led certain money market funds to avoid such investments that should be incorporated explicitly into rule 2a-7?[135] Should we limit money market funds to investing in ABSs that the manager concludes can be paid upon maturity with existing cash flow, *i.e.*, the payment upon maturity is not dependent on the ability of the special purpose entity to rollover debt? Alternatively, should the rule itself require ABSs to be subject to unconditional demand features to be eligible securities?[136]

B. Portfolio Maturity

Rule 2a-7 restricts the maximum remaining maturity of a security that a money market fund may acquire, and the weighted average maturity of the fund's portfolio, in order to limit the exposure of money market fund investors to certain risks, including interest rate risk. The Commission is proposing changes to the rule's maturity limits to further reduce such risks, as discussed below. First, we propose to reduce the maximum weighted average portfolio maturity permitted by the rule. Second, we propose a new maturity test that would limit the portion of a

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135 The staff's recent examinations of money market funds indicate that credit analysts for money market funds that invested in SIVs that subsequently defaulted appear to have had access to the same basic set of information on SIVs as did analysts at money market funds that did not and that the judgment of these credit analysts regarding minimal creditworthiness of the SIVs that subsequently defaulted appeared to have been different. The staff's exams also appear to indicate that credit analysts for money market funds that invested in SIVs that subsequently defaulted placed less emphasis on the length of time that payment experience was available on assets in the collateral pool and they were willing to accept sub-prime mortgage credits as a seasoned asset class. In addition, their decision, in part, may have been influenced by the greater amount of over-collateralization of the collateral pools and the high yields paid by notes supported by sub-prime credits.

136 Rule 2a-7(a)(26) defines an "unconditional demand feature" as a "demand feature" that by its terms would be readily exercisable in the event of a default in payment of principal or interest on the underlying security or securities.

fund's portfolio that could be held in longer term variable- or floating-rate securities. Third, we propose to delete a provision in the rule that permits certain money market funds to acquire Government securities with extended maturities of up to 762 calendar days. We are also requesting comment on other ways of adjusting the rule's maturity provisions in order to accomplish our goal of decreasing the risks associated with a money market fund holding longer term investments.

1. Weighted Average Maturity

Rule 2a-7 requires a money market fund to maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable net asset value or price per share, but in no case greater than 90 days.[137] We adopted this provision because securities that have shorter periods remaining until maturity (and are of higher quality) generally exhibit a low level of volatility and thus provide a greater assurance that the money market fund will continue to be able to maintain a stable share price.[138]

Having a portfolio weighted towards securities with longer maturities poses several risks to a money market fund. First, as we have noted in the past, a longer weighted average maturity increases a fund's exposure to interest rate risk.[139] Second, and as we discuss in more detail

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137 *See* rule 2a-7(c)(2)(iii).

138 *See* 1983 Adopting Release, *supra* note 3, at n.7 and accompanying text.

139 *See* 1990 Proposing Release, *supra* note 22, at text accompanying n.60. *See also* STANDARD & POOR'S, MONEY MARKET FUND RATINGS CRITERIA, at 21 (2007) *available at* http://www2.standardandpoors.com/spf/pdf/events/MMX709.pdf ("S&P 2007 RATINGS CRITERIA") ("The portfolio's weighted average maturity (WAM) is a key determinant of the tolerance of a fund's investments to rising interest rates. In general, the longer the WAM, the more susceptible the fund is to rising interest rates. A fund comprised entirely of Treasury securities with a WAM of 45 days could withstand approximately twice the interest rate increase than could a fund with a 90-day WAM, leaving all other factors aside."); FABOZZI, *supra* note 98, at 4 ("[T]he volatility of a bond's price is closely associated with maturity: Changes in the market level of [interest] rates will wrest much larger changes in price from bonds of long maturity than from otherwise similar debt of shorter life.").

below, longer maturities also amplify the effect of widening credit and interest rate spreads on a fund.[140] Finally, a fund holding securities with longer maturities generally is exposed to greater liquidity risk, because fewer securities mature on a daily or weekly basis. Perhaps in recognition of these risks, few fund managers maintain weighted average maturity at or near the maximum permissible 90 days.[141]

In view of the extraordinary market conditions we have witnessed recently, the Commission is concerned that the 90-day maximum weighted average maturity under the rule may be too long. Particularly during the market events of last fall, funds with shorter portfolio maturities were much better positioned to withstand heavy redemptions, because a greater portion of their portfolios matured each week and provided cash to pay to redeeming investors. They also were better able to withstand increased credit spreads in certain financial sector notes because of the shorter period of exposure to such distressed securities. Finally, interest rate spreads on longer maturity securities widened to a much greater degree than interest rate spreads on shorter maturity securities.[142]

The ICI Report recommended reducing the maximum weighted average maturity to 75 days.[143] Historically, however, most funds have maintained shorter maturities. During the last 20 years, the average weighted average maturity of taxable money market funds (as a group) has

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140 *See also supra* notes 65-71 and accompanying text.

141 According to monthly statistics kept by the Investment Company Institute, during the past 10 years, the weighted average maturities of funds in the longest maturity categories (the 90th percentile of all taxable prime money market funds) seldom have exceeded 75 days. As of April 30, 2009, these funds maintained an average weighted maturity of 67 days. These statistics are available in File No. S7-11-09.

142 *See, e.g.*, U.S. Department of the Treasury, *Daily Treasury Yield Curve Rates*, *available at* http://www.treasury.gov/offices/domestic-finance/debt-management/interest-rate/yield_historical_main.shtml.

143 *See* ICI REPORT, *supra* note 6, at 77.

never exceeded 58 days.[144] As of June 16, 2009, it was 53 days.[145] Some money market funds have, from time to time, extended their maturities substantially longer than the average to gain a yield advantage, anticipating declining or stable interest rates. By doing so, these funds assumed greater risk and would be more likely to experience losses that could result in their breaking the buck if interest rates rise, credit markets do not behave as they expect, or they receive substantial redemption requests.

Most European money market funds with stable share prices (many of which are domiciled in Ireland) are limited to 60-day weighted average maturities.[146] So are money market funds rated highly by the NRSROs.[147] In light of these considerations, we believe that a shorter period may be appropriate. Accordingly, we propose that rule 2a-7 be amended to impose a 60-

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144 2008 FACT BOOK, *supra* note 13, at Table 38. In 2009, the ICI Fact Book began presenting this information separately for taxable government and taxable non-government money market funds, which had average maturities of 49 days and 47 days, respectively, in 2008. 2009 FACT BOOK, *supra* note 7, at 150-51, Tables 41 & 42.

145 *See Money Fund Report*, IMONEYNET, May 7, 2008. Average maturity for tax exempt money market funds (as a group) is even lower – 24 days as of June 16, 2009. *Id.*

146 *See* Irish Financial Services Regulatory Authority, *Valuation of Assets of Money Market Funds,* 2008 GUIDANCE NOTE 1/08 (Aug. 2008), *available at* http://www.financialregulator.ie/industry-sectors/funds/Documents/Guidance%20Note%20108%20Valuation%20of%20Assets%20of%20Money%20Market%20Funds.pdf ("Financial Regulator Guidance Note 1/08"). As of April 2009, money market funds registered in Ireland managed approximately €317 billion ($419 billion) in assets. *See* Irish Financial Regulator statistics *available at* http://www.irishfunds.ie/money_marketfunds.htm. In addition, the Institutional Money Market Funds Association ("IMMFA") requires the triple-A rated institutional money market funds sponsored by its members to comply with a Code of Practice that generally limits portfolio maturity to 60 days. *See* IMMFA, CODE OF PRACTICE, Part IV., ¶ 22 (2005), *available at* http://www.immfa.org/about/Codefinal.pdf. As of February 13, 2009, IMMFA-member constant net asset value money market funds managed approximately $493 billion in assets. *See* IMMFA statistics, *available at* http://www.immfa.org/stats/IMFR130209.pdf. *See also* ICI REPORT, *supra* note 6, at 184, Appendix H.

147 *See* S&P 2007 RATINGS CRITERIA, *supra* note 139, at 21; MOODY'S INVESTORS SERVICE, FREQUENTLY ASKED QUESTIONS ABOUT MOODY'S RATINGS OF MANAGED FUNDS, at 4 (July 20, 2005), *available at* http://www.moodys.com/moodys/cust/research/MDCdocs/20/2003600000425726.pdf?search=5&searchQuery=Frequently+Asked+Questions+about+Moody; FITCH RATINGS, U.S. MONEY MARKET FUND RATINGS, at 4 (Mar. 3, 2006), *available at* http://www.fitchresearch.com/creditdesk/reports/report_frame.cfm?rpt_id=266376.

day weighted average maturity limit.[148]

We request comment on the proposed 60-day weighted average maturity limit. Would it decrease portfolio volatility and increase fund liquidity, as we suggest? What would be the anticipated effect on money market fund yields? Would a negative effect on yields make money market funds less attractive to investors? Should a different weighted average maturity limit apply, such as 45 days or 75 days? We request that commenters provide us with data demonstrating the effect that alternative weighted average maturity limits would have had on portfolios of money market funds during the recent economic turmoil.

2. *Weighted Average Life*

We propose to add to rule 2a-7 a new maturity test, which would limit the weighted average life maturity of portfolio securities to 120 days.[149] As explained further below, the weighted average life of a portfolio would be measured without regard to a security's interest rate reset dates, and thus would limit the extent to which a fund could invest in longer term securities that may expose a fund to interest rate spread risk and credit spread risk.[150]

Generally, under rule 2a-7 the maturity of a portfolio security is the period remaining until the date on which the principal must unconditionally be repaid according to its terms (its final "legal" maturity) or, in the case of a security called for redemption, the date on which the redemption payment must be made.[151] The rule contains exceptions from this general approach

148 *See* proposed rule 2a-7(c)(2)(ii).

149 *See* proposed rule 2a-7(c)(2)(iii).

150 While the proposed rule would ignore interest rate resets for purposes of calculating the fund's weighted average life to maturity, a security's demand features could continue to be used in this calculation. *See, e.g.,* rule 2a-7(d)(3) and (d)(5).

151 *See* rule 2a-7(d).

for specific types of securities, which are referred to as the "maturity shortening" provisions.[152] Among these exceptions are three provisions that allow a fund to treat a variable- or floating-rate security as having a maturity equal to the time remaining to the next interest rate reset date.[153] First, a fund may treat a short-term variable-rate security (*i.e.*, one with a remaining maturity of 397 days or less), as having a maturity equal to the *earlier* of the interest rate reset date or the time it would take the fund to recover the principal by exercising a demand feature.[154] Second, a fund may treat a short-term floating-rate security (*i.e.*, one with a remaining maturity of 397 days or less) as having a maturity of one day.[155] Third, a variable- or floating-rate Government security generally may be deemed to have a maturity equal to the next reset date even if it is a long-term security.[156] For purposes of calculating weighted average maturity, the rule effectively treats short-term variable- and floating-rate securities and all adjustable-rate Government securities as if they were a series of short-term obligations that are continually "rolled over" on the reset dates at the current short-term interest rates.

As the ICI Report explains, however, longer term adjustable-rate securities are more sensitive to credit spreads (the amount of additional yield demanded by purchasers above a risk-

152 *Id.* We added maturity shortening provisions to the rule in 1986; they are particularly important for tax exempt funds, which invest in municipal obligations, most of which are issued with longer maturities. *See* 1986 Adopting Release, *supra* note 19, at nn.9-10 and accompanying text.

153 *See* rule 2a-7(a)(13) (defining "floating rate security") and (a)(29) (defining "variable rate security"). The interest rate for a variable-rate security is established on set dates, whereas the interest rate for a floating-rate security adjusts whenever a specified interest rate changes. We also may refer to variable- and floating-rate securities collectively in this Release as "adjustable-rate" securities.

154 *See* rule 2a-7(d)(2). *See also* rule 2a-7(a)(8) (definition of "demand feature").

155 *See* rule 2a-7(d)(4).

156 *See* rule 2a-7(d)(1) (allowing a variable-rate Government security where the variable rate is readjusted no less frequently than every 762 days to be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate, and a floating-rate Government security to be deemed to have a remaining maturity of one day).

free rate of return to compensate for the credit risk of the issuer) than short-term securities with final maturities equal to the reset date of the longer term security.[157] Longer term adjustable-rate securities also are subject for a longer period of time to risk from widening interest rate spreads.[158] As a result, prices of longer term adjustable-rate securities could fall more than prices of comparable short-term securities in times of market turbulence. The ICI Report also notes that while adjustable-rate securities do protect a fund against changes in interest rates, permitting maturity shortening based on interest rate resets does not protect against liquidity risk to the portfolio.[159]

We are concerned that the traditional weighted average maturity measurement of rule 2a-7 does not require that a manager of a money market fund limit these risks. We understand that some money market fund portfolio managers, to protect the fund, have already begun using a weighted average maturity measurement that ignores interest rate resets.

The ICI Report confirms our observations of the behavior of prices for certain securities last fall, when money market funds found it difficult to sell at amortized cost longer term adjustable-rate securities, including securities issued by agencies of the federal government. We believe that the use of the measurement the ICI recommends, which we will call the "weighted average life" to maturity of a money market fund portfolio, appears to be a prudent limitation on the structure of a money market fund portfolio and would limit credit and interest rate spread risks not encompassed by the weighted average maturity restriction of rule 2a-7. As suggested

157 *See* ICI REPORT, *supra* note 6, at 77.

158 Interest rate spreads can widen because a variable-rate note has a fixed period of time to the next interest reset date and during that time the benchmark interest rate will likely change. Interest rate spreads can also widen because market conditions change after the security is issued such that investors may demand a greater margin to hold the security. *See* FABOZZI, *supra* note 98, at 196.

159 *See* ICI REPORT, *supra* note 6, at text accompanying n.140.

by the ICI Report, we are proposing that money market funds maintain a weighted average life of no more than 120 days.[160] The Commission believes that a 120-day weighted average life requirement would provide a reasonable balance between strengthening the resilience of money market funds to market stress (*e.g.*, interest rate increases, widening spreads, and large redemptions) while not unduly restricting the funds' ability to offer a diversified portfolio of short-term, high quality debt securities.

One of the effects of a limit on the weighted average life of a portfolio would appear to be on funds that hold longer term floating-rate Government securities, which are issued by federal agencies. Consider a money market fund with a portfolio consisting 50 percent of overnight repurchase agreements and 50 percent of two-year Government agency floating-rate obligations that reset daily based on the federal funds rate. Using the reset dates as permitted by the rule's maturity shortening provisions, the portfolio would have a weighted average maturity of one day. In contrast, by applying a measurement that does not recognize resets, the portfolio would have a weighted average life of 365.5 days (*i.e.*, half of the portfolio has a one day maturity and half has a two-year maturity), which would be considerably longer than the 120-day limit we are proposing. The weighted average life limitation would provide an extra layer of protection for funds and their shareholders against spread risk, particularly in volatile markets.

We request comment on all aspects of the proposed weighted average life limitation. Is this new maturity test appropriate? Is 120 days an appropriate limit? What would be the effect on yield? Does it place too much of a constraint on the ability of money market fund advisers to effectively manage fund portfolios? Does it permit funds to assume too much risk? Would a

160 The proposed rule would require a money market fund to maintain a weighted average maturity not to exceed 120 days, determined without reference to the exceptions in paragraph (d) of the rule regarding interest rate resets. *See* proposed rule 2a-7(c)(2)(iii).

different limit be more appropriate, such as 90 days or 150 days? Would the proposed weighted average life limitation have a material impact on the issuers of short-term debt and, if so, what would it be?

We request comment on whether there are alternative approaches to measuring these risks. We understand that some fund managers use an alternative maturity test that focuses solely on credit spread risk. Such a test not only disregards interest rate resets, but also excludes Government securities from the weighted average maturity calculation. Would this test provide a clearer indication of the overall credit spread risk of the portfolio? Are there other advantages to such an approach? If so, what would be an appropriate limit? Should it be the same as proposed weighted average life limitation of 120 days, or should it be different, such as 90 days or 150 days? We request that commenters provide us with data demonstrating the effect of such alternative credit limitations and/or weighted average life limitations on their portfolios during the recent economic turmoil.

When the Commission first adopted rule 2a-7, we explained that we were allowing Government securities to use resets for purposes of the maturity limitations under the rule because we understood that the volatility of such instruments would be no greater than the volatility of fixed interest rate instruments having a maturity equal to the period before the security's interest rate reset.[161] The Commission noted, however, that this position was based entirely upon experience with Small Business Administration guaranteed debentures – at the time the only adjustable-rate Government securities of which the Commission was aware.[162] The Commission stated that it would consider amending this provision if market experience indicates

161 *See* 1983 Adopting Release, *supra* note 3, at n.16.

162 *See id.*

that such treatment is inappropriate.[163]

Since 1983, the number and variety of adjustable-rate Government securities have grown and, in particular, the issuance of such securities by Freddie Mac and Fannie Mae increased significantly with the growth in mortgage-backed securities. While adjustable-rate securities historically have maintained market values similar to equivalent short-term fixed-rate securities, last fall these Government securities experienced increased credit and interest rate spreads and greater volatility than Government securities with maturities similar to the reset dates of the adjustable-rate securities.[164] Further, as noted above, other short-term adjustable-rate securities also experienced increased credit and interest rate spreads and greater volatility than securities with maturities similar to the reset dates.

Currently, rule 2a-7 permits funds to rely on these reset provisions to shorten portfolio maturities only if boards or their delegates can reasonably expect that the security's market value will approximate its amortized cost on the reset date.[165] However, recent experience suggests that in times of market stress, this expected performance may not hold true. Would the weighted average life to maturity limitation adequately address this risk? Are there other alternative limitations or tests that would have mitigated this risk last fall? Should we restrict a fund's ability to use the maturity-shortening provisions of the rule to those adjustable-rate securities, including Government securities, with maximum final maturities of no more than two years, three years, or four years? What would be the impact of the weighted average life limitation on longer term adjustable-rate Government securities issuers?

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163 *See id.*

164 *See* Jody Shenn, *Fannie Mae Debt Spreads Hit Records as GMAC Seeks Bank Status*, BLOOMBERG, Nov. 20, 2008; Jody Shenn, *Agency Mortgage-Bond Spreads Head for Worst Month on Record*, BLOOMBERG, Oct. 31, 2008, *available at* http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aSc8k8D7ZMw0.

165 *See* rule 2a-7(a)(13) and (a)(29).

3. Maturity Limit for Government Securities

The Commission is proposing to delete a provision of the rule that permits a fund that relies exclusively on the penny-rounding method of pricing to acquire Government securities with remaining maturities of up to 762 days, rather than the 397-day limit otherwise provided by the rule.[166] We are unaware of money market funds today that rely solely on the penny-rounding method of pricing, and none that hold *fixed-rate* Government securities with remaining maturities of two years, which we are concerned would involve the assumption of a substantial amount of interest rate risk. We request comment on our proposal to delete the provision. Are we correct that funds no longer use it? If not, are there reasons why we should retain it?

4. Maturity Limit for Other Portfolio Securities

Currently, in order to qualify as an eligible security under rule 2a-7, an individual security generally cannot have a remaining maturity that exceeds 397 days.[167] We request comment on whether we should consider reducing the maximum maturity for individual non-Government securities acquired by a money market fund from 397 days to, for example, 270 days.[168]

The length of time remaining before a security matures affects its sensitivity to increases in interest rates. In addition, a shorter maturity decreases the amount of time a fund is exposed to potential investment losses for a particular security. On the other hand, it is less clear that such a change would produce a significant increase in the safety and stability of money market funds if

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166 *See* rule 2a-7(c)(2)(ii). We added this provision in 1991. *See* 1991 Adopting Release, *supra* note 20, at nn.53-57 and accompanying text. In a conforming change, we also propose to revise the maturity-shortening provision of the rule for variable-rate Government securities to require that the variable rate of interest is readjusted no less frequently than every 397 days, instead of 762 days as currently permitted. *See* rule 2a-7(d)(1); proposed rule 2a-7(d)(1).

167 *See* rule 2a-7(a)(10)(i) and (c)(2)(i).

168 A maturity limit of 270 days would be consistent with the exemption for commercial paper under section 3(a)(3) of the Securities Act of 1933 [15 U.S.C. 77c(a)(3)].

we were to adopt it in addition to adopting the proposed 60-day weighted average maturity and 120-day weighted average life limitations. Moreover, unlike the weighted average maturity and weighted average life limitations, a stricter maturity limitation on individual securities could have a substantially greater adverse impact on issuers of short-term obligations other than commercial paper, including issuers of tax exempt municipal securities.

What would be the effects on money market funds and the capital markets of shortening the maturity limit on individual portfolio securities to 270 days? Would there be benefits to funds from shortening the maturities of individual securities beyond the benefits that would be attained through the 60-day weighted average maturity and 120-day weighted average life limitations? What would be the likely impact on money market fund yields? What effect, if any, would shortening the maturity limit have on the supply of rule 2a-7-eligible securities? Should Government securities be excluded from a 270-day maturity limit?[169] If we were to adopt a maximum 270-day maturity for individual securities, should we include or exclude securities issued by municipalities, which typically issue debt securities with maturities of a year or more?

C. Portfolio Liquidity

Rule 2a-7 does not contain any provisions limiting the ability of a money market fund to hold or acquire illiquid assets.[170] Money market funds are, however, subject to section 22(e) of the Act, which requires registered investment companies to satisfy redemption requests in no

[169] We note that, while posing less credit risk, Government securities are subject to much the same risks as corporate securities from rising spreads between their market price and money market benchmarks, whether due to liquidity concerns, changes in interest rates, or other factors. For this reason some rating agencies have imposed limitations on remaining maturities of adjustable-rate Government securities held by money market funds. *See, e.g.*, S&P 2007 RATINGS CRITERIA, *supra* note 139, at 30 (setting a two-year limit for remaining maturities of floating- or variable-rate Government securities held by money market funds for the fund to maintain the highest rating).

[170] *See* 1983 Adopting Release, *supra* note 3 at n.37 and accompanying text ("[Rule 2a-7] does not limit a money market fund's portfolio investments solely to negotiable and marketable instruments ....").

more than seven days – a requirement we have construed as restricting a money market fund from investing more than 10 percent of its assets in illiquid securities.[171] Since rule 2a-7 was first adopted we have emphasized the importance of a money market fund holding sufficiently liquid securities. Money market funds often have a greater, and perhaps less predictable, volume of redemptions than other open-end investment companies.[172] And because many promise to provide redemptions sooner than other types of open-end funds – often on the same day that the redemption request is received – money market funds need sufficient liquidity to meet redemption requests on a more immediate basis.[173]

By holding illiquid securities, a money market fund exposes itself to a risk that it may be unable to satisfy redemption requests promptly, without selling illiquid securities at a loss that could impair its ability to maintain a stable net asset value per share.[174] Illiquid securities also complicate the valuation of the fund's portfolio.[175] Moreover, illiquid securities are subject to greater price volatility, exposing the fund to greater risk of breaking a buck as a result of net asset values eroding in a declining market.[176]

We have not included a specific provision in rule 2a-7 regarding liquidity because, until recently, money market funds had not experienced a severe liquidity shortfall. As discussed above, in September 2008, the markets for both traditional and asset backed commercial paper essentially seized up. Large portions of many money market fund portfolios became illiquid

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171 *See, e.g., id.* at nn.37-38 and accompanying text; 1986 Adopting Release, *supra* note 19, at n.21 and accompanying text.

172 *See, e.g.,* 1986 Adopting Release, *supra* note 19, at text preceding and accompanying n.22; 1983 Adopting Release, *supra* note 3, at text following n.39.

173 *See* 1983 Adopting Release, *supra* note 3, at text following n.39.

174 *Id.* at text preceding, accompanying and following nn.37-39.

175 *Id.* at text preceding section titled "Obligation of the Board to Maintain Stable Price."

176 S&P 2007 RATINGS CRITERIA, *supra* note 139, at 21.

when buyers of asset backed and traditional commercial paper fled the market.[177] At the same time, many money market funds – principally institutional money market funds – received substantial redemption requests.[178] The ability of these funds to maintain a stable net asset value turned on their ability to convert portfolio holdings to cash without selling them at "fire sale" prices.

These events suggest to us that rule 2a-7 should be amended to address liquidity risks that money market funds face. We propose to amend rule 2a-7 to add new risk-limiting conditions designed to improve money market funds' ability to meet significant redemption demands.

1. Limitation on Acquisition of Illiquid Securities

We propose to prohibit money market funds from acquiring securities unless, at the time acquired, they are liquid, *i.e.*, securities that can be sold or disposed of in the ordinary course of business within seven days at approximately their amortized cost value.[179] In light of the risk to

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177 *See* Board of Governors of the Federal Reserve, Report Pursuant to Section 129 of the Emergency Economic Stabilization Act of 2008: Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (undated), *available at* http://www.federalreserve.gov/monetarypolicy/files/129amlf.pdf at 1-2 ("In ordinary circumstances, MMMFs would have been able to meet these redemption demands by selling assets. At the time of the establishment of the AMLF, however, many money markets were extremely illiquid, and the forced liquidation of assets by MMMFs was placing increasing stress on already strained financial markets."); *see generally* Board of Governors of the Federal Reserve, Monetary Policy Report to the Congress (Feb. 24, 2009), Part 2, http://www.federalreserve.gov/monetarypolicy/mpr_20090224_part2.htm.

178 *See* ICI Mutual Fund Historical Data, *supra* note 47 (in the week ending September 17, the day after the Reserve Primary Fund announced that it would break a dollar, institutional money market fund assets fell by more than $119 billion while retail money market fund assets fell by $1.1 billion).

179 Proposed rule 2a-7(c)(5). "Liquid security" would be defined in proposed rule 2a-7(a)(19). Last year in the NRSRO References Proposal, we proposed to define "liquid security" as a security that can be sold or disposed of in the ordinary course of business within seven days at approximately the cost ascribed to it by the money market fund. *See supra* note 105, at n.28 and accompanying text. *See also* 1986 Adopting Release, *supra* note 19, at text following n.21 ("The term 'illiquid security' generally includes any security which cannot be disposed of promptly and in the ordinary course of business without taking a reduced price."). The one comment we received on the proposed definition recommended the definition refer to the "shadow price" rather than the "value" ascribed to the security by the money market fund. Most funds that rely

the fund of securities *becoming* illiquid as a result of market events, such as those that occurred last fall, investing any portion of the fund in securities that are already illiquid may be imprudent and thus should be prohibited by rule 2a-7.

We request comment on our proposal to preclude funds from acquiring illiquid securities. We understand that some funds make very limited investments in securities that, at the time of acquisition, are illiquid, such as insurance company funding agreements, loan participations, and structured notes that have no demand features. Would this proposed provision (which would not prohibit funds from continuing to hold securities that become illiquid after their purchase) have a significant impact on money market funds? What would be the impact on funds of not being able to buy illiquid securities? Would there be a material impact on yield?

2. Cash and Securities that Can Be Readily Converted to Cash

As discussed above, liquidity of a money market fund portfolio is critical to the fund's ability to maintain a stable net asset value. Our traditional notions of liquidity incorporated into our guidelines (discussed above) appear to be inadequate to meet the needs of a money market fund because the guidelines assume that a fund has time (up to seven days) to sell securities and that there will be a market for the securities. As noted above, money market funds typically undertake to pay their investors more quickly (frequently the same or following day). As the events of last fall demonstrated, money market funds may be unable to rely on a secondary or dealer market ready to provide immediate liquidity at amortized cost under all market conditions. Therefore we are proposing new liquidity tests that would be based on the fund's legal right to receive cash rather than its ability to find a buyer of the security.

on rule 2a-7 value their securities using the amortized cost method and thus would be required to acquire securities that can be sold or disposed of in the ordinary course of business within seven days at approximately amortized cost value.

The amount of liquidity a fund will need will vary from fund to fund and will turn on cash flows resulting from purchases and redemptions of shares. As a general matter, a fund that has some large shareholders, any one of which could redeem its entire position in a single day, will have greater liquidity needs than a retail fund that has thousands of relatively small shareholders. A fund that competes for yield-sensitive shareholders (*e.g.*, "hot money") through electronic "portals" will have substantially greater liquidity needs than a fund holding the cash of commercial enterprises that have predictable needs (such as payrolls).[180]

Our proposed formulation of a new liquidity standard is designed to take into consideration each of these factors. The proposed daily and weekly standards, discussed immediately below, would be minimum standards; the proposed general standard (which we discuss after the minimum standards) may require a fund to maintain a higher portion of its portfolios in cash or securities that can readily be converted into cash.

a. Minimum Daily Liquidity Requirement

Taxable Retail Funds. We propose to require each taxable retail money market fund to invest at least five percent of its assets in cash, U.S. Treasury securities, or securities that can provide the fund with daily liquidity, *i.e.,* securities that the fund can reasonably expect to

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180 *See Money Market Funds Tackle "Exuberant Irrationality,"* Standard & Poor's, RatingsDirect (Sept. 30, 2008), *available at* http://www2.standardandpoors.com/spf/pdf/media/MoneyMarketFunds_Irrationality.pdf ("It is likely that certain yield-sensitive institutions commonly referred to as 'hot money' accounts, moved money from one investment to another to capture a higher yielding, or seemingly safer, option. For example, after Lehman Bros. filed for bankruptcy, corporations that issued commercial paper (CP) to fund their business operations were forced to pay a significantly higher premium to obtain funding because of investor concerns with holding debt from any nongovernment issuer. The subsequent 'flight to quality' pushed some overnight and 30-day CP rates up by 0.5% (to approximately 3.5%) for issuers whose credit or financial/risk profile did not seem to change. As a result, these hot money accounts moved their investments from money market funds yielding less than 2.75%.").

convert to cash within a day.[181] Unlike our liquidity guidelines discussed above, which allow for a period during which a fund would be expected to seek buyers in a secondary market, these daily liquidity requirements would be significantly more demanding, requiring a portion of the funds' assets be held in "daily liquid assets," which the rule would define as: (i) cash (including demand deposits); (ii) securities (including repurchase agreements) for which the fund has a contractual right to receive cash within one business day either because the security will mature or the fund can exercise a demand feature;[182] or (iii) U.S. Treasury securities, which have historically traded in deep, liquid markets, even in times of market distress.[183]

Under the proposed amendments, a money market fund that is a "retail fund" could not acquire any securities other than daily liquid assets if, immediately after the acquisition, the fund would have invested less than five percent of its total assets in those assets ("minimum daily

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181 Proposed rule 2a-7(c)(5)(iii).

182 A "demand feature" means a feature permitting (i) the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise, and (ii) the holder of an asset backed security unconditionally to receive principal and interest within 397 calendar days of making demand. Rule 2a-7(a)(8).

183 U.S. Treasury securities were highly liquid last fall. *See, e.g., FRB Open Market Committee Oct. 28-29 Minutes, supra* note 51, at 5 ("Yields on short-term nominal Treasury coupon securities declined over the intermeeting period, reportedly as a result of substantial flight-to-quality flows and heightened demand for liquidity. In contrast, higher term premiums and expectations of increases in the supply of Treasury securities associated with the Emergency Economic Stabilization Act and other initiatives seemed to put upward pressure on longer term nominal Treasury yields. Yields on longer term inflation-indexed Treasury securities, which are relatively illiquid, rose more sharply than did those on nominal securities."); *Minutes of the Federal Open Market Committee*, FEDERAL RESERVE BOARD, Dec. 15-16, 2008, at 5, *available at* http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081029.pdf ("*FRB Open Market Committee Oct. 28-29 Minutes"*) (Dec. 15-16, 2008), at 4, *available at* http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081216.pdf ("Yields on nominal Treasury coupon securities declined significantly over the intermeeting period in response to safe-haven demands as well as the downward revisions in the economic outlook and the expected policy path. Meanwhile, yields on inflation-indexed Treasury securities declined by smaller amounts, leaving inflation compensation lower. Although the decline in inflation compensation occurred amid sharp decreases in inflation measures and energy prices, it was likely amplified by increased investor preference for the greater liquidity of nominal Treasury securities relative to that of inflation-protected Treasury securities.").

liquidity requirement").[184] Compliance with the daily liquidity requirement would be determined at the time each security is acquired, and thus a fund would not have to dispose of less liquid securities (and potentially realize an immediate loss) if the portion of the fund held in highly liquid securities fell below five percent as a result of redemptions.

Retail money market funds experienced relatively modest redemption demands last fall, even in the midst of substantial market turbulence.[185] Thus we believe that a five percent requirement, which was recommended in the ICI Report, may be sufficient.[186] We request comment on our analysis, and whether a five percent standard is appropriate in light of the liquidity needs of retail money market funds (which we distinguish from institutional money market funds in the next section of this release). Should we consider a higher percentage, such as 10 percent or 15 percent, or a lower percentage, such as two percent or three percent? Do our proposed amendments strike the right balance between reducing liquidity risk and limiting the impact on yield? What would be the effect on yields of a lower or higher minimum daily liquidity requirement? There may be a number of factors that influence the lower redemption rates among retail investors, including investment purposes and practices, size of investments and possible differences in the information that retail as opposed to institutional investors obtain

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184 The term "daily liquid assets" is defined in proposed rule 2a-7(a)(8). A "retail fund" would be defined as any fund other than an institutional fund. Proposed rule 2a-7(a)(24). For a discussion of the definition of "institutional fund," *see infra* text preceding, accompanying and following note 196. "Total assets" means with respect to a money market fund using the amortized cost method, the total amortized cost of its assets and, with respect to any other money market fund, the total market-based value of its assets. Rule 2a-7(a)(27).

185 *See supra* note 178. On September 17, 2008, approximately 4% of prime retail money market funds and 25% of prime institutional money market funds had outflows greater than 5%; on September 18, 2008, approximately 5% of prime retail funds and 30% of prime institutional funds had outflows greater than 5%; and on September 19, 2008, approximately 5% of prime retail funds and 22% of prime institutional funds had outflows greater than 5%. This information is based on analysis of data from the iMoneyNet Money Fund Analyzer database.

186 *See* ICI REPORT, *supra* note 6, at 74.

and the time when they obtain the information. We solicit comment on whether these factors did or would in the future influence the level of retail redemptions. If so, how should the proposed rule be revised to address such factors?

We also request comment on the definition of "daily liquid assets." Are there other securities that are sufficiently liquid that should be included in the definition?

A fund's contractual rights to cash will be different if the fund is relying on an unconditional demand feature rather than a conditional demand feature, which the fund may not be able to exercise if there is a default or other credit event with respect to the issuer of the securities.[187] Rule 2a-7 permits both to be used to shorten the maturity of an instrument.[188] For purposes of determining the daily liquidity requirement, should the rule distinguish between securities subject to conditional and unconditional demand features?

As discussed above, compliance with the daily liquidity requirement would be determined at the time each security is acquired. A fund could acquire only daily liquid assets until the portfolio investments met the five percent daily liquidity test.[189] Because the requirement applies only at the time of acquisition, a money market fund would not have to maintain a specified percentage of its assets in daily liquid assets at all times (subject to the general liquidity requirement discussed below), even though the fund is exposed to liquidity risk at all times. We request comment on whether to impose a minimum liquidity maintenance requirement, *i.e.,* require that a money market fund maintain five percent of its portfolio *at all times* in daily liquid assets. What are the advantages and disadvantages of each approach?

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187 *See* rule 2a-7(a)(26) (defining "unconditional demand feature"); rule 2a-7(a)(6) (defining "conditional demand feature").

188 *See* rule 2a-7(d)(3), (5).

189 This is also the approach rule 2a-7 takes with respect to money market fund credit quality and diversification requirements. *See* rule 2a-7(c)(3), (4).

Taxable Institutional Funds. We propose to limit a taxable institutional fund to acquiring daily liquid assets unless, immediately after acquiring a security, the fund holds at least 10 percent of its total assets in daily liquid assets.[190] Institutional money market funds typically maintain a greater portion of their assets in cash and overnight repurchase agreements than retail funds, which reflects the greater liquidity needs of these funds.[191] These greater needs were demonstrated last fall, when (as discussed above) institutional funds were subject to substantially greater redemption pressure than retail funds.[192] We understand that some of these institutional funds had cash positions of almost 50 percent in their portfolios in anticipation of substantial redemptions following the large amount of inflows during 2007 through August 2008.

We request comment on whether institutional money market funds should be subject to a higher daily liquidity requirement (10 percent) than retail funds (five percent). Should we consider a higher percentage, such as 15 or 20 percent? Ten percent daily liquidity could seem high for a money market fund that reserved the right to delay payment of redemptions for seven days. We are not proposing to adjust the appropriate minimum daily liquidity requirement for institutional or retail funds solely by reference to the seven day period, however, because many money market funds undertake to pay redemption proceeds on the same day or the next day, and an announcement by a fund of a delay in payment of redemption could itself precipitate a run on funds. We request comment on whether a five percent daily liquidity requirement for retail funds or a 10 percent daily liquidity requirement for institutional funds should turn on the representations the money market fund has made to its investors regarding the timing of

190 Proposed rule 2a-7(c)(5)(iii).

191 This information is based on analysis of data from the iMoneyNet Money Fund Analyzer database.

192 *See supra* note 178.

payments of redemption proceeds.

We propose to add two new definitions to rule 2a-7 to distinguish between retail and institutional money market funds. Although the ICI and others who compile data about money market funds have traditionally distinguished between retail and institutional money market funds, in practice the distinctions are not always clear.[193] An institutional fund may have investors who invest on behalf of retail investors. For example, institutional money market funds commonly have investors that are bank sweep accounts or master funds in master-feeder arrangements.[194] Although these investors ordinarily provide cash flows to the fund that are more similar to retail funds, a single decision-maker may be in a position to redeem all of the shares of the money market fund and move the sweep account to another money market fund. In addition, some funds have a single portfolio but issue separate classes of shares to retail and institutional investors that bear different expenses. In these cases, the cost of managing the institutional share class's relatively greater cash flow volatility is shared with the retail investors.

Our proposed amendments would require that a money market fund's board determine,

193 *See, e.g.,* ICI, Frequently Asked Questions About Money Market Funds, http://www.ici.org/faqs/faqs_money_funds (describing (i) institutional money market funds as "held primarily by businesses, governments, institutional investors, and high-net worth households" that as of July 2008, held 63 percent of all money market fund assets and (ii) retail money market funds as "offered primarily to individuals with moderate-sized accounts" that as of July 2008, held around 37 percent of all money market fund assets); iMoneyNet home page, http://imoneynet.com/ (separates information and analysis on money market funds into institutional and retail categories); Crane Data, Money Fund Intelligence (June 2009) at 30, http://www.cranedata.us/products/money-fund-intelligence/ (select issue 2009-06-01 (Vol.4, #6)) (classifying money market funds as institutional or individual based on expense ratio, minimum investment and "who they're sold to").

194 A "master-feeder fund" is an arrangement in which one or more funds with identical investment objectives ("feeder funds") invest all their assets in a single fund ("master fund") with the same investment objective. Investors purchase securities in the feeder fund, which is an open-end fund and a conduit to the master fund. *See* H.R. REP. NO. 622, 104TH CONG., 2D SESS., at 41 (1996) ("H.R. REP. NO. 622"); *see generally* Exemption for Open-End Management Investment Companies Issuing Multiple Classes of Shares; Disclosure by Multiple Class and Master Feeder Funds; Voting on Distribution Plans; Final Rules and Proposed Rule, Investment Company Act Release No. 20915 (Feb. 23, 1995) [60 FR 11876, 11876-77 (Mar. 2, 1995)].

no less frequently than once each calendar year, whether the fund is an institutional money market fund for purposes of meeting the liquidity requirements.[195] In particular, the fund's board of directors would determine whether the money market fund is intended to be offered to institutional investors or has the characteristics of a fund that is intended to be offered to institutional investors, based on the: (i) nature of the record owners of fund shares; (ii) minimum amount required to be invested to establish an account; and (iii) historical cash flows, resulting or expected cash flows that would result, from purchases and redemptions.[196] The provision is designed to permit fund directors to evaluate the overall characteristics of the fund based on relevant factors.[197] Under the provision, a fund offered through two classes, a majority of whose shares are held by retail investors, should nonetheless be deemed to be an institutional fund by the fund board if the cash flows from purchases and redemptions and the portfolio management required to meet liquidity needs based on those cash flows are more characteristic of an institutional money market fund.

We request comment on our proposed definitions. The differences today in the liquidity management of institutional and retail money market funds suggest to us that fund managers (and perhaps fund boards) currently distinguish between retail and institutional funds. Would our proposed definition permit them to continue to draw the distinctions they draw today? Are there additional factors the board should consider in determining whether a fund is an institutional fund? Would a different approach result in better distinctions? If we cannot distinguish between retail and institutional funds, should we amend rule 2a-7 to apply the

195 Proposed rule 2a-7(c)(5)(v).

196 Proposed rule 2a-7(a)(18) (defining "institutional fund").

197 Proposed rule 2a-7(a)(24) would define "retail fund" as any money market fund that the board of directors has not determined within the calendar year is an institutional fund.

minimum daily liquidity requirements we propose for institutional funds to all funds? Would setting the same minimum daily liquidity requirement for institutional and retail funds impose unnecessary costs (in terms of lower yields) on retail investors in light of retail funds' reduced liquidity needs?

Might one effect of the proposed amendments be that funds currently offering two classes of shares, one retail and one institutional, would decide to divide the fund into two funds and manage them differently? Would one of the advantages of such a result be that retail investors would not bear the cost of maintaining liquidity for institutional investors? Would a disadvantage be the loss to retail investors of the economies of scale in these multi-class funds? What additional advantages and disadvantages do commenters foresee? Retail investors may not be aware of the higher redemption rates that institutional funds experienced last fall. Should we consider requiring institutional funds to provide additional disclosures regarding the risk to the fund of large redemptions?

Tax Exempt Money Market Funds. We propose to exempt tax exempt funds from the minimum daily liquidity requirements.[198] We understand that most of the portfolios of tax exempt funds consist of longer term floating- and variable-rate securities with seven day demand features from which the fund obtains much of its liquidity. We understand that these funds are unlikely to have investment alternatives that would permit them to meet a daily liquidity requirement.[199] We request comment on whether tax exempt money market funds could meet a daily liquidity requirement, such as we have proposed for taxable retail funds. Do tax exempt retail money market funds nevertheless have similar liquidity requirements as taxable retail

198 Proposed rule 2a-7(c)(5). Rule 2a-7 defines a "tax exempt fund" as a money market fund that holds itself out as distributing income exempt from regular federal income tax. Rule 2a-7(a)(24).

199 *See* ICI REPORT, *supra* note 6, at 74.

funds? If so, should rule 2a-7 treat them differently and how?

b. Minimum Weekly Liquidity Requirement

We propose that all money market funds (including tax exempt funds) also be subject to a minimum weekly liquidity requirement ("minimum weekly liquidity requirement"). Specifically, retail and institutional funds could not acquire any securities other than U.S. Treasury securities or securities (including repurchase agreements) that mature or are subject to a demand feature exercisable and payable in five business days (together with cash, "weekly liquid assets") if, immediately after the acquisition, (i) the retail fund would have invested less than 15 percent of its total assets in weekly liquid assets and (ii) the institutional fund would have invested less than 30 percent of its total assets in weekly liquid assets.[200]

The proposed minimum weekly liquidity requirement would supplement the proposed minimum daily liquidity requirement (discussed above) and give greater assurance that money market funds could meet their statutory obligations to redeem shareholders in times of market turbulence. We estimate that under our proposed minimum weekly liquidity requirement, approximately 93 percent of retail funds and 91 percent of institutional funds would have been able to satisfy the level of redemption demands during the periods of greatest redemption pressure last fall without having to sell portfolio securities.[201]

We request comment on the minimum weekly liquidity requirements. Would a minimum daily liquidity requirement alone be sufficient to allow funds to adequately manage risk in the

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200 Proposed rule 2a-7(c)(5)(iv). The term "weekly liquid assets" would be defined in proposed rule 2a-7(a)(32).

201 During the week of September 15–19, 2008, approximately 6% of retail funds had net redemptions that exceeded 15%, and 9% of institutional money market funds had redemptions that exceeded 30% of assets. In addition, in the 52 weeks preceding September 17, 2008, roughly the same portion of redemption requests in institutional and retail funds (less than 2%) would have exceeded the weekly liquidity requirements. This information is based on analysis of data from iMoneyNet Money Fund Analyzer database.

event of unexpected shareholder redemptions in excess of the daily threshold and market illiquidity? Are the proposed minimums of 15 percent of a retail fund's total assets and 30 percent of an institutional fund's total assets sufficient?[202] Should we, as the ICI Report suggests, adopt the same (20 percent of total assets) test for both retail and institutional funds? As discussed above, we designed our minimum weekly liquidity requirements so that more than 90 percent of retail and institutional funds could have met redemption requests during the week of September 15-19, 2008 without selling portfolio securities. Should we set the threshold lower, such as at 80 percent or 70 percent? Should we set the threshold higher at 95 percent or 100 percent? The weekly liquidity requirement would be essentially the same as the daily liquidity requirement, except that the fund must be able to access cash on a weekly rather than daily basis. Compliance with the test would be determined upon the acquisition of a security, and demand features could be used to determine the maturity of a portfolio security for purposes of the test.

We propose to treat as weekly liquid assets for purposes of the weekly liquidity requirements, the same securities that would be daily liquid assets except that the requirement for maturing securities or demand features would be five business days rather than one.[203] The ICI Report suggests that we ought to treat as a weekly liquid asset a security issued by an agency of the U.S. Government that, when originally issued, had a maturity of 95 days or less.[204] Is there a basis on which to treat these agency securities as weekly liquid assets? If so, why should the maturity of the security be 95 days based on original issue rather than specifying a period remaining to maturity? We urge commenters supporting such treatment to submit market data to

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202 We note that for most weeks during the past year, prime institutional money market funds maintained over 30% of their assets in securities maturing in seven days or less. This information is based on analysis of data from iMoneyNet Money Fund Analyzer database.

203 *Compare* proposed rule 2a-7(a)(8) with proposed rule 2a-7(a)(32).

204 *See* ICI REPORT, *supra* note 6, at 74.

support their views.

c. General Liquidity Requirement

As discussed above, the daily and weekly liquidity requirements would be minimum requirements a fund would have to satisfy upon acquisition of a security. A fund's liquidity needs, however, depending upon the volatility of its cash flows, may be greater. Therefore, we also propose to require that a money market fund at all times hold highly liquid securities sufficient to meet reasonably foreseeable redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders, such as undertaking to pay redemptions more quickly than seven days.[205]

To comply with this condition, we would expect money market funds to consider a number of factors that could affect the fund's liquidity needs. For example, a money market fund would have to understand the characteristics of its investors and their likely liquidity needs. A volatile investor base, *e.g.*, one consisting of a few relatively larger investors that are likely to make significant redemptions, would require a fund to maintain greater liquidity than a stable investor base, which is generally associated with a retail fund with many hundreds or thousands of smaller investors. With this information, a fund manager could take different steps to protect the fund from greater liquidity risk. For example, the fund manager could increase the amount of daily or weekly liquid assets above those required by the daily and weekly requirements, or

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205 Proposed rule 2a-7(c)(5)(ii). Our proposal is similar to the liquidity standard we proposed last year in the proposal on NRSRO references. *See* NRSRO References Proposal, *supra* note 105, at Section III.A.2. Among the commenters that specifically addressed that proposed standard, two suggested that codification of the standard was not needed because money market fund advisers already understand and adhere to the current standards. *See* Comment Letter of Fidelity Management & Research Company (Aug. 29, 2008) (File No. S7-19-2008); Comment Letter of the Securities Industry and Financial Markets Association Credit Rating Agency Task Force (Sept. 4, 2008) (File No. S7-19-2008). A third suggested eliminating the standard because it involves "subjective, forward-looking estimates," while retaining a proposed maximum level for illiquid securities holdings to "preserve a clearer bright-line test"). *See* Comment Letter of Morrison & Foerster (Sept. 5, 2008) (File No. S7-19-2008).

could decline to accept new investments from investors whose liquidity needs are inconsistent with the objectives of the management of the fund.[206]

We request comment on this proposed requirement for liquidity. Should we consider incorporating specific objective standards for liquidity in this requirement? Should we provide guidance regarding the steps fund advisers could take to evaluate the fund's liquidity needs? If so, what should the guidance be?

Because the obligation would be ongoing, we believe a fund should adopt policies and procedures to assure that appropriate efforts are undertaken to identify risk characteristics of shareholders, particularly those that hold their securities through omnibus accounts, or access the fund through "portals" or through other arrangements that provide the fund with little or no transparency with respect to the beneficial shareholder. We are not proposing to amend rule 2a-7 to require that funds adopt specific procedures because we believe those procedures would be required by rule 38a-1, the "compliance rule" under the Investment Company Act, if we adopt the proposed general liquidity requirement.[207] Should the Commission provide guidance to funds to assist them in determining the adequacy of their policies and procedures? Should we consider specifying any particular aspects of the policies and procedures?

In their consideration of these procedures and in their oversight of their implementation, fund directors should understand that fund managers' interest in increasing fund assets, and thus their advisory fees, may lead them to accept investors who present greater risks to the fund than they might otherwise have accepted. We urge directors to consider the need for establishing

206 We do not mean to suggest that each money market fund should minimize the volatility of cash flows, but rather should limit its liquidity risks. Some money market funds with the most volatile shareholder base manage liquidity risk by, for example, investing exclusively in overnight repurchase agreements or Treasury debt.

207 *See* rule 38a-1(a)(1) (requiring funds to adopt and implement written policies and procedures reasonably designed to prevent violation of the federal securities laws by the fund).

guidelines for advisers to money market funds that address this potential conflict. We are aware of more than one occasion in which a fund adviser (or its affiliate that served as the principal underwriter to the fund) has marketed the fund to "hot money" in order to increase fund assets, which has exposed the fund to substantially higher risks.

3. *Stress Testing*

We are also proposing to amend rule 2a-7 to require the board of directors of each money market fund using the amortized cost method to adopt procedures providing for periodic stress testing of the money market fund's portfolio.[208] The procedures would require testing of the fund's ability to maintain a stable net asset value per share based upon certain hypothetical events, including an increase in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on a portfolio security, and widening or narrowing of spreads between yields on an appropriate benchmark selected by the fund for overnight interest rates and commercial paper and other types of securities held by the fund.

Our proposal would require funds to test for certain hypothetical events, but would not specify other details of the stress testing. The proposal would require that stress tests be conducted at intervals that the board of directors determines appropriate and reasonable in light of current market conditions. This is the same approach that rule 2a-7 currently takes with respect to the frequency of shadow pricing.[209]

The proposed amendments also would leave to the money market fund's board of directors (and the fund manager) the specifics of the scenarios or assumptions on which the tests are based. Boards should, for example, consider procedures that require the fund to test for the concurrence of multiple hypothetical events, *e.g.*, where there is a simultaneous increase in

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208 Proposed rule 2a-7(c)(8)(ii)(D)(*1*).

209 Rule 2a-7(c)(7)(ii)(A)(*1*).

interest rates *and* substantial redemptions. The proposed amendments also would require that the board receive a report of the results of the testing at its next regularly scheduled meeting, which report must include: (i) the date(s) on which the fund portfolio was tested; and (ii) the magnitude of each hypothetical event that would cause the money market fund to break the buck.[210] Thus, a fund must test each hypothetical event to a degree of severity that it would result in the market-based per share net asset value of the fund to fall below $0.995 (in the case of a fund that is maintaining a stable net asset value at $1.00). The proposed amendment also would require the written procedures to include the provision of an assessment by the adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably likely to occur within the following year.[211] The adviser's assessment would provide the fund board context within which to evaluate the magnitude of the events that would cause the fund to break the buck. Finally, funds would be required to maintain records of the stress testing for six years, the first two years in an easily accessible place.[212]

We believe that the proposed stress testing procedures would provide money market fund boards a better understanding of the risks to which the fund is exposed and would give managers a tool to better manage those risks. We understand that stress testing is already a best practice followed by many money market funds. The ICI Report recommends that rule 2a-7 require money market funds regularly to "stress test" their portfolios, although it does not suggest a particular means of stress testing.[213] The Institutional Money Market Funds Association provides

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210 Proposed rule 2a-7(c)(8)(ii)(D)(*2*).

211 Proposed rule 2a-7(c)(8)(ii)(D)(*3*).

212 Proposed rule 2a-7(c)(11)(vii).

213 ICI REPORT, *supra* note 6, at 75.

guidance for its members in stress testing money market fund portfolios,[214] and the ratings agencies stress test the portfolios of money market funds they rate.[215]

We request comment on our proposed stress test requirement. Would this requirement allow fund managers to better understand and manage the risks to which the fund is exposed? Have we identified the correct stress events? If not, what additional or alternative scenarios or assumptions should we require the fund to test? Should we specify at least one base-line stress test that would test the fund portfolio against a combination of two or more events? For example, the rule could require that the market value per share of the fund be tested against an assumed 50 basis point increase in LIBOR and a redemption of 15 percent of fund shares. Are there alternative base-line tests we should consider requiring?

We request comment on our proposal to require that the board receive a report on these tests. Would the report help the board identify when a fund adviser is exposing the fund to greater risks? Should the board only receive a report when the tests indicate a particular level of risk? If so, what particular level of risk should the rule identify? Should we consider including additional information in the report, and if so, what should it be? Should the rule provide for a minimum frequency of testing? If so, what should be the frequency (*e.g.,* monthly, weekly, or a shorter period)? Should we consider different intervals for different types of money market funds? If so, what intervals would be appropriate for what types of money market funds?

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214 *See* Institutional Money Market Funds Association, Stress Testing for Money Market Funds (Feb. 2009).

215 *See, e.g.,* STANDARD & POOR'S, FUND RATINGS CRITERIA, at 9 (2007), *available at* http://www2.standardandpoors.com/spf/pdf/events/FundRatingsCriteria.pdf. *See also* Financial Regulator Guidance Note 1/08, *supra* note 146, at 5 (requirements of the Irish Financial Services Authority for money market funds domiciled in Ireland include stress testing: "A money market fund is expected to be subject to monthly portfolio analysis incorporating stress testing to examine portfolio returns under various market scenarios to determine if the portfolio constituents are appropriate to meet pre-determined levels of credit risk, interest rate risk, market risk and investor redemptions.").

Should the frequency depend upon the market-based value of the fund portfolio or other criteria or events?

We note that certain of the hypothetical events we propose funds include in their testing may not be meaningful for some money market funds. For example, U.S. Treasury money market funds (*i.e.*, funds that invest solely in direct obligations of the U.S. government such as U.S. Treasury bills and other short term securities backed by the full faith and credit of the U.S. government) are not likely to experience downgrades of or defaults on those securities. Should these money market funds be exempted from testing certain hypothetical events, such as a downgrade of or default on a portfolio security, that may not present risks to the fund? Are there other money market funds that we should exempt from testing for certain of the proposed hypothetical events? If so, which funds should have exemptions and which events should be exempted from their testing?

The ICI Report suggests that the results of stress testing could be used to evaluate whether a money market fund's liquidity thresholds need to be adjusted.[216] Should we consider imposing minimum liquidity requirements based on the results of a particular stress test? For example, should we require that a fund invest 50 percent of its portfolio in daily or weekly liquid assets if a five percent increase in shareholder redemptions would cause the fund to break the buck? If we considered imposing minimum liquidity requirements, should they be different for retail and institutional funds?

[216] *See* ICI REPORT, *supra* note 6, at 75.

D. Diversification

Rule 2a-7 requires a money market fund's portfolio to be diversified, both as to the issuers of the securities it acquires and to the guarantors of those securities.[217] Generally, money market funds must limit their investments in the securities of any one issuer (other than Government securities), to no more than five percent of fund assets.[218] They must also generally limit their investments in securities subject to a demand feature or a guarantee to no more than ten percent of fund assets from any one provider.[219] The Commission adopted these requirements in order to limit the exposure of a money market fund to any one issuer or guarantor.[220]

The issuer diversification provisions of the rule generally were not implicated by the market turbulence last fall.[221] The Reserve Primary Fund, for example, held only 1.2 percent of its assets in Lehman Brothers commercial paper, well below what rule 2a-7 permits. The market turbulence did, however, implicate the guarantor and demand feature diversification provisions – many funds (particularly tax exempt funds) were heavily exposed to bond insurers, and some

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217 Rule 2a-7(c)(4)(i). The diversification requirements of rule 2a-7 differ in significant respects from the requirements for diversified management investment companies under section 5(b)(1) of the Act. A money market fund that satisfies the applicable diversification requirements of the paragraphs (c)(4) and (c)(5) of the rule is deemed to have satisfied the requirements of section 5(b)(1). Rule 2a-7(c)(4)(v). Subchapter M of the Internal Revenue Code contains other diversification requirements for a money market fund to be a "regulated investment company" for federal income tax purposes. 26 U.S.C. 851 *et seq.* *See also* 1990 Proposing Release, *supra* note 22, at n.25.

218 Rule 2a-7(c)(4)(i)(A). The rule contains a safe harbor where a taxable and national tax exempt fund may invest up to 25 percent of its assets in the first tier securities of a single issuer for a period of up to three business days after acquisition (but a fund may use this exception for only one issuer at a time). Rule 2a-7(c)(4)(i)(A).

219 Rule 2a-7(c)(4)(iii). With respect to 25 percent of total assets, holdings of a demand feature or guarantee provider may exceed the 10 percent limit subject to certain conditions. See rule 2a-7(c)(4)(iii)(A), (B), and (C). *See also* rule 2a-7(a)(8) (definition of "demand feature") and (a)(15) (definition of "guarantee").

220 *See* 1990 Proposing Release, *supra* note 22, at II.1. ("Diversification limits investment risk to a fund by spreading the risk of loss among a number of securities.").

221 The positions held by funds in distressed securities were in almost all cases well below the rule's diversification limits.

were heavily exposed to a few major securities firms that served as liquidity providers.[222]

Should we propose to further restrict the diversification limits of the rule? If so, by how much should we reduce them? Should the five percent diversification limit for issuers be reduced to, for example, three percent? Would it be possible to further reduce the guarantor diversification limits without reducing the quality of portfolio securities? Even a diversification limitation of one percent would not preclude a fund from breaking a buck if the security should sustain sufficient losses as did the securities issued by Lehman Brothers. Moreover, such a diversification limit may force funds to invest in relatively lower quality securities. If so, might lower diversification limits increase the likelihood of a default or other credit event affecting a money market fund while diminishing the impact of such an event on the fund? We request that commenters address the tradeoffs of lower diversification limits for different types of money market funds.

Last fall, money market funds did appear to be extensively exposed to securities issued by participants in the financial sector, which contributed significantly to the difficulties they experienced.[223] Money market funds are not subject to any industry concentration limitations under rule 2a-7. Should we consider proposing such a limitation? If we did, what should the concentration limit be? Are distinctions among industry sectors sufficiently clear that a concentration limitation would be meaningful?[224]

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222 *See, e.g.*, Brunnermeier, *supra note 66*, at 87.

223 *See, e.g.*, U.S. Dollar Money Market Funds, *supra* note 17, at 67 (mid-2008 holdings of 15 largest prime money market funds showed they had invested $1 trillion, or half of their portfolios, with non-U.S. banks).

224 In 1992, our staff observed that "the current [statutory] treatment of 'concentration' suffers from problems of industry definition. There is no clear standard to determine what constitutes an 'industry,' much less 'a group of industries.' Indeed, as the boundaries between different industries erode and the trend toward corporate diversification and conglomeration continues, it is often difficult to fit companies into distinct industry categories ...." DIVISION OF INVESTMENT

E. Repurchase Agreements

Money market funds typically invest a significant portion of their assets in repurchase agreements, many of which mature the following day and provide an immediate source of liquidity.[225] In a typical repurchase agreement, a fund purchases securities from a broker-dealer or a bank ("counterparty"), upon an agreement that the counterparty will repurchase the same securities at a specified price, at a later date. The securities purchased serve as the collateral for the agreement.

Money market funds may treat the acquisition of a repurchase agreement as an acquisition of the collateral underlying the repurchase agreement for purposes of meeting rule 2a-7's diversification requirement, provided that the repurchase agreement is "collateralized fully."[226] A repurchase agreement collateralized fully must, among other things, qualify for an exclusion from any automatic stay of creditors' rights against the counterparty under applicable insolvency law.[227] We propose two amendments to rule 2a-7 affecting a money market fund's

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MANAGEMENT, U.S. SECURITIES AND EXCHANGE COMMISSION, PROTECTING INVESTORS: A HALF CENTURY OF INVESTMENT COMPANY REGULATION, at n.103 (May 1992).

225 In 2008, repurchase agreements accounted for 26.4% of taxable Government money market funds' total net assets and 9.1% of taxable non-Government money market funds' total net assets. *See* 2009 FACT BOOK, *supra* note 7, at 150-51, Tables 41 & 42.

226 *See* rule 2a-7(c)(4)(ii)(A). We have allowed this "look-through" treatment, for diversification purposes, based on the notion that a money market fund looks to the collateral rather than the counterparty as the ultimate source of repayment. *See* Treatment of Repurchase Agreements and Refunded Securities as an Acquisition of the Underlying Securities, Investment Company Act Release No. 25058 (July 5, 2001) [66 FR 36156 (July 11, 2001)] ("2001 Repo Rule Adopting Release"), at Background. Rule 5b-3 allows the same treatment for purposes of section 5 and section 12(d)(3) of the Act. The rule 5b-3(c)(1) definition of collateralized fully, which is cross-referenced by rule 2a-7(a)(5), sets forth the related conditions. Money market funds may enter into repurchase agreements that are not collateralized fully. Any agreement or portion of agreement that is not collateralized fully would be deemed an unsecured loan. As such the loan itself would have to meet the quality requirements set forth in rule 2a-7, both with respect to the minimal credit risk and the high quality rating, as well as the five percent diversification test. *See* 1991 Adopting Release, *supra* note 20, at n.31.

227 *See* rule 5b-3(c)(1)(v).

investment in repurchase agreements.

First, we propose to limit money market funds to investing in repurchase agreements collateralized by cash items or Government securities in order to obtain special treatment under the diversification provisions of rule 2a-7.[228] Such a limitation would make it less likely that, in the event of the default of a counterparty during a period of market turmoil such as last fall, a money market fund would experience losses upon the sale of collateral that had become illiquid. Such a consequence is more likely in the case of a default by a large counterparty when, as a result, many investors in repurchase agreements seek to liquidate similar collateral at the same time.[229]

We request comment on this amendment. We understand that most money market funds that take advantage of the diversification "look-through" provision enter into repurchase agreements that are collateralized by Government securities. Is our understanding correct? If so, would this amendment have a significant impact on money market funds? Would the amendment significantly reduce the risk of losses upon the default of a repurchase agreement counterparty? Would it negatively impact money market funds' yields? Should we apply this

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228 Proposed rule 2a-7(a)(5). Under the current definition of collateralized fully, a money market fund may look through repurchase agreements collateralized with cash items, Government securities, securities with the highest rating or unrated securities of comparable credit quality. Rule 5b-3(c)(1)(iv). Repurchase agreements have traditionally been collateralized with U.S. Treasury and agency securities, but over the years borrowers have increasingly used investment grade corporate bonds, mortgage-backed securities and other potentially illiquid securities. *See* Martin Duffy et al., *supra* note 191, at 3. Our staff's examination of the portfolio holdings in the 15 largest money market fund complexes last spring indicated that approximately 75% of the collateral supporting repurchase agreements held by the funds consisted of Government securities (48.3% agencies and 26.4% U.S. Treasuries). The exam further indicated that the remaining collateral consisted of a variety of instruments, such as equities, commercial paper, corporate notes, and mortgage loan obligations.

229 If the counterparty defaults, a money market fund might be required to dispose of the collateral as soon as possible to the extent that the collateral, now part of the fund's portfolio, does not meet the fund's maturity or liquidity requirements. Such requirements do not apply to the collateral when it is not part of the fund's portfolio. *See* 1991 Adopting Release, *supra* note 20, at n.33 and accompanying text.

limitation to repurchase agreements that are not collateralized fully, and thus do not qualify for the special "look-through" treatment?

Second, we propose to require that the money market fund's board of directors or its delegate evaluate the creditworthiness of the counterparty, regardless of whether the repurchase agreement is collateralized fully.[230] We eliminated this requirement in 2001 in light of amendments to relevant bankruptcy law that protected funds from the automatic stay of creditors' rights under applicable bankruptcy law.[231] The events of last fall, which involved the failure of a large investment bank holding company that served as a counterparty, suggest we should revisit this determination.[232] We are concerned that in the midst of a crisis following the bankruptcy of a counterparty, a money market fund may find it difficult to protect fully its interests in the collateral without incurring losses.[233] A fund should seek to avoid such a crisis by limiting its counterparties to those that are creditworthy. We request comment on this proposed amendment.

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230 Proposed rule 2a-7(c)(4)(ii)(A). It appears that this evaluation is already being made in many fund complexes. *See* ICI REPORT, *supra* note 6, at n.90.

231 *See* 2001 Repo Rule Adopting Release, *supra* note 226, at nn.18-20 and accompanying text.

232 We understand that a number of money market funds discontinued entering into repurchase agreements with The Bear Stearns Companies Inc. ("Bear Stearns") when it was threatened with collapse in March 2008. ICI REPORT, *supra* note 6, at 51.

233 *See* Stephen Morris & Hyun Song Shin, *Financial Regulation in a System Context*, Brookings Papers on Economic Activity, Fall 2008, at 229, 239 (noting that "if Bear Stearns had become illiquid, and the assets pledged as collateral reverted to the money market funds, they would have been forced to sell those assets quickly, possibly at a large loss."). *Cf. Calyon N.Y. Branch v. Am. Home Mortg. Corp. (In re Am. Home Mortg., Inc.)*, 379 B.R. 503, 520-22 (Bankr. D. Del. 2008) (Holding that seller in bankruptcy was not required to transfer to the buyer the right to service the collateral of the repurchase agreement. The court found that the servicing provisions of the agreement were severable from the repurchase provisions, dismissing the buyer's argument that without the servicing rights the buyer's ability to liquidate the collateral would have been impaired.).

F. Disclosure of Portfolio Information

1. Public Website Posting

The Commission is proposing to amend rule 2a-7 to require money market funds to disclose information about their portfolio holdings each month on their websites. Specifically, a fund would be required to disclose the fund's schedule of investments, as prescribed by rules 12-12 to 12-14 of Regulation S-X,[234] identifying, among other things, the issuer, the title of the issue, the principal amount of the security, and its current amortized cost.[235] The fund would be required to post the information no later than the second business day of the month, current as of the last business day of the previous month, and would have to maintain the information on the website for at least twelve months.[236]

Currently, money market funds must report portfolio holdings information to us four times a year, no earlier than within 60 days of the close of the covered period.[237] Many funds today provide this information to their investors much more frequently on their websites, with some funds updating information each day.[238]

We understand that the greater transparency provided by many funds today responds to demands from investors, particularly institutional investors, who wish to have a better

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234 17 CFR 210.12-12 – 12-14.

235 Proposed rule 2a-7(c)(12).

236 *Id.*

237 Money market funds must provide a full schedule of their portfolio holdings in quarterly filings to the Commission. *See* Form N–CSR [17 CFR 274.128] (form used by registered management investment companies to file shareholder reports); Form N-Q [17 CFR 274.130] (form used by registered management investment companies to file quarterly reports of portfolio holdings after the first and third quarters).

238 *See* Colleen Sullivan & Mike Schnitzel, *Money Funds Move to Update Holdings Faster*, FUND ACTION, Sept. 29, 2008, *available at* http://www.fundaction.com/pdf/FA092908.pdf.

understanding of the current risks to which the fund is exposed.[239] Those investors find that the quarterly reports are too infrequent in light of the rapid turnover of money market fund portfolios. We believe that the greater transparency of fund portfolios is a positive development by which investors can exert influence on risk-taking by fund advisers, and thus reduce the likelihood that a fund will break the buck.

We request comment on the proposed monthly portfolio disclosure requirement. Should we require more information from funds than what we have proposed? If so, what additional information should we require? Should we require that money market funds also post their market-based net asset value per share and the market-based prices of their portfolio securities? This information would enable investors to understand the fund's exposure to distressed securities (the market value of which would be less than the amortized cost). In addition, it could help investors understand the risk that the fund may be unable to maintain a $1.00 stable net asset value. Currently, only larger, more sophisticated investors may be able to gauge this risk, by themselves estimating the market value of portfolio securities disclosed on fund websites. Thus, a requirement that funds disclose the market-based values may help to level the playing field for all investors. On the other hand, we acknowledge that disclosure of shadow pricing could cause certain investors to redeem their holdings once the shadow price drops below a certain threshold and thus potentially introduce greater instability.

We request comment on how investors might react to the disclosure of market-based values and the consequences to funds and shareholders if such information were disclosed. Would investors seek to redeem their shares when the fund's market-based net asset value falls below a certain threshold because of concerns that other investors may seek to redeem? Would

239 *See id.*

market analysts follow and report this information and thereby cause investors to redeem if the fund's market-based net asset value falls below a certain threshold? Would the disclosure of market-based values, in addition to amortized cost, confuse investors, particularly retail investors? Are there costs to disclosing this information, and, if so, what are they? Alternatively, would this information provide shareholders with useful information regarding the fund's risk characteristics? Would it enable investors to make better informed investment decisions? Would this information benefit investors, and, if so, how? If the market-based values were required to be disclosed, how frequently should they be disclosed? Would monthly disclosure be frequent enough for investors to understand how often and to what extent a money market fund's market-based share price deviates from the $1.00 stable share price?

Should we omit any of the proposed disclosure requirements? If so, what information should be omitted from the proposed requirement, and why?

Each money market fund would have to update its portfolio schedule as of the end of each month and post the update no later than two business days after the end of the month. Should we provide for a longer delay to prevent cash investors other than shareholders from trading along with the fund, to the possible detriment of the fund and its shareholders? The ICI Report recommended monthly disclosure with a two-day delay, asserting that "front running" concerns are less of a risk for money market funds than other types of mutual funds.[240] We understand that funds that already post portfolio schedules frequently have come to the same conclusion. Should funds be required to provide more frequent disclosure of portfolio holdings (*e.g.*, weekly or biweekly)?

The amendments would require that a fund post the information on its website for at least

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[240] *See* ICI REPORT, *supra* note 6, at 93.

12 months. Should the information be accessible on the website for a longer or shorter time period? Should we require this information somewhere other than on the fund's website? Do all money market funds have websites?

2. Reporting to the Commission

We are also proposing a new rule requiring money market funds to provide the Commission a monthly electronic filing of more detailed portfolio holdings information.[241] The information would enable the Commission to create a central database of money market fund portfolio holdings, which could enhance our oversight of money market funds and our ability to respond to market events.[242]

Our current information on money market fund portfolios is limited to quarterly reports filed with us which, as noted above, quickly become stale. Moreover, the reports are not filed in a format that allows us to search expeditiously across portfolios or within a portfolio to identify securities that may raise concerns. In 2007, our staff was not able to ascertain quickly which money market funds held SIVs, and last fall we had to engage in lengthy and time-consuming inquiries to determine which money market funds held commercial paper issued by Lehman Brothers after it declared bankruptcy. Further, if we had had such data immediately available to us, we could have provided additional assistance to the Treasury Department or the Federal Reserve Board in structuring the programs they put into place to protect investors.[243] In

241 Proposed rule 30b1-6.

242 In 1995, the Commission proposed, but did not adopt, a similar rule that would have required money market funds to file quarterly reports of portfolio holdings. Money Market Fund Quarterly Reporting, Investment Company Act Release No. 21217 (July 19, 1995) [60 FR 38467 (July 26, 1995)]. *See also* Rulemaking Petition from Fund Democracy, *et al.* (Jan. 16, 2008) (File No. 4-554) (recommending that the Commission require money market funds to make nonpublic monthly electronic filings of their portfolio holdings).

243 The Treasury's Guarantee Program requires a participating money market fund to provide a schedule of its portfolio holdings if its market-based net asset value falls below 99.75 percent of its stable net asset value. *See* U.S. Department of the Treasury, "Guarantee Agreement (Stable

preparing this release we have relied in part on data about money market funds available only through industry associations and publications.[244]

Proposed rule 30b1-6 would provide us information that would assist our staff in analyzing the portfolio holdings of money market funds, and thus enhance our understanding of the risk characteristics of individual money market funds and money market funds as a group and industry trends. We would be able to identify quickly those funds that are holding certain types of securities or specific securities, such as distressed securities, and funds that have unusual portfolios that may involve greater risks than are typical (*e.g.*, funds that have higher gross yields).

Although the portfolio reports to the Commission are not primarily designed for individual investors, we would expect to make the information available to the public two weeks after their filing. We anticipate that academic researchers, financial analysts and economic research firms would use this information to study money market fund holdings and evaluate their risk information. Their analyses may further help investors and regulators better understand risks in money market funds. In addition, we believe that delaying the public availability of this information would alleviate possible concerns about the public disclosure of the detailed portfolio holdings information contained in the filing, without compromising its utility.[245]

Proposed rule 30b1-6 would require money market funds to file a monthly portfolio

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Value)," ¶ 5(b), *available at* http://www.treas.gov/offices/domestic-finance/key-initiatives/money-market-docs/Guarantee_Agreement_Stable-Value.pdf.

244 *See, e.g., supra* note 68.

245 As discussed above, we understand the confidentiality of certain portfolio holdings information is not of critical importance to money market funds. Accordingly, the proposed amendments to rule 2a-7 would require money market funds to disclose certain monthly portfolio holdings information on their websites within two days after the end of month. *See also* ICI REPORT, *supra* note 6, at 93 (recommending that funds disclose monthly portfolio holdings information after a two-day delay). Here, however, the more detailed information included in the filing to the Commission may present more significant concerns.

holdings report on new Form N-MFP (for "money fund portfolio" reporting) no later than the second business day of each month, current as of the last business day of the previous month.[246] Proposed Form N-MFP would require the fund to report, with respect to each portfolio security held on the last business day of the prior month, among other things: (i) the name and CIK number of the issuer; (ii) the title of the issue; (iii) the CUSIP number or other unique identifier; (iv) the category of investment (*e.g.*, Treasury debt, government agency debt, corporate commercial paper, structured investment vehicle notes, etc.); (v) the current credit ratings of the issuer and the requisite NRSROs giving the ratings; (vi) the maturity date as determined under rule 2a-7, (vii) the final legal maturity date; (viii) whether the maturity date is extendable; (ix) whether the instrument has certain enhancement features; (x) the identity of any enhancement provider; (xi) the current credit rating of the enhancement provider; (xii) the principal amount; (xiii) the current amortized cost value; (xiv) certain valuation information (*i.e.*, whether the inputs used in determining the value of the securities are Level 1, Level 2 or Level 3,[247] if applicable); and (xv) the percentage of the money market fund's assets invested in the security.[248] In addition, Form N-MFP would require funds to report to us information about the fund's risk characteristics, such as the fund's dollar weighted average maturity of its portfolio and its 7-day gross yield.

Given the rapidly changing composition of money market fund portfolios, which is

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246 The portfolio securities information that money market funds currently must report is more limited in scope, and includes information about the issuer, the title of the issue, the balance held at the close of the period, and the value of each item at the close of the period. *See* Form N-Q, Item 1 [17 CFR 274.130]; Rules 12-12 – 12-14 of Regulation S-X [17 CFR 210.12-12 – 12.14].

247 *See* Financial Accounting Standards Board, *Statement of Financial Accounting Standards No. 157, "Fair Value Measurement," available at* *http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175818754924&blobheader=application%2Fpdf.*

248 In addition, proposed Form N-MFP would include an "Explanatory Notes" item to permit funds to add miscellaneous information that may be material to other disclosure in the form.

largely the result of securities maturing, we believe that monthly reports would improve the timeliness and relevance of portfolio information. Once a money market fund has established a system for tagging and filing a Form N-MFP, we expect the marginal costs of filing additional reports would be minimal.[249]

Under the proposed rule, Form N-MFP would be filed electronically through the Commission's EDGAR system in an eXtensible Markup Language ("XML") tagged data format.[250] We understand that money market funds already maintain the requested information, and therefore would need only to tag the data and file the reports with the Commission.[251] We anticipate that, in the future, many funds may be able to collect, tag, and file this information with the Commission through even more efficient, automated processes, thereby minimizing the related costs and potential for clerical error.

We request comment on the proposed monthly portfolio reporting requirement. Should we require funds to file the portfolio holdings report on a more frequent basis? As discussed above, we intend to make this information publicly available two weeks after the report is filed with the Commission. Would such a delay alleviate concerns about possible front-running or other possible harms that might be caused by making the information public? Should the lag time between the filing of the form and its public availability be longer or shorter? Should the information be immediately available to the public upon filing? Should we instead provide that

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249 *See also infra* Section V.

250 We anticipate that the XML interactive data file would be compatible with a wide range of open source and proprietary information management software applications. Continued advances in interactive data software, search engines, and other web-based tools may further enhance the accessibility and usability of the data.

251 We understand that many funds often provide this type of information in different formats to various information services and third-parties, including NRSROs. Standardizing the data format in proposed Form N-MFP may encourage standardization across the industry, resulting in cost savings for money market funds.

all or a portion of the requested information be submitted in nonpublic reports to the Commission? If so, please identify the specific items that should remain nonpublic and explain why.

Proposed Form N-MFP requires money market funds to disclose certain items that would be relevant to an evaluation of the risk characteristics of the fund and its portfolio holdings. Should we require additional or alternative information, such as the fund's client concentration levels, the percentage of the issue held by the fund, or last trade price and trade volume for each security?[252] Should we require funds to disclose market-based values (including the value of any credit support agreement), which would allow us to identify funds that have market-based net asset values that sufficiently deviate from their amortized cost that they present a risk of breaking the buck? Would the two-week delay in making the information publicly available mitigate any concerns about the disclosure of this information? Alternatively, should we require funds to provide the market-based values information to us on a nonpublic basis?[253] If funds were required to provide market-based values information to us on a nonpublic basis, should we require funds to provide this information more frequently once the fund's net asset value per share falls below a certain threshold? If so, how frequently should funds be required to provide this information (*e.g.*, weekly or daily) and what should be the threshold (*e.g.*, $0.9975)?

Should we omit any proposed disclosure requirement? Are there specific items that the proposed form would require that are unnecessary or otherwise should not be required?

We request comment on feasible alternatives that would minimize the reporting burdens

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252 *See* Rulemaking Petition from Fund Democracy, *supra* note 242 (recommending that the Commission require money market funds to disclose to the Commission, among other things, the percentage of an issue owned by a fund and its affiliates and the last trade price and trade volume for each portfolio security).

253 *See supra* discussion at paragraph following note 239 and paragraph preceding note 240.

on money market funds.[254] We also request comment on the utility of the reports to the Commission in relation to the costs to money market funds of providing the reports.[255] In addition, we request comment on whether funds should be permitted to post a human readable version of their Forms N-MFP on their websites to satisfy the proposed monthly website disclosure requirement.

The Commission anticipates that the data to be required by proposed Form N-MFP would be clearly defined and often repetitive from one month to the next. Therefore, we believe the XML format would provide us with the necessary information in the most timely and cost-effective manner. Should the Commission allow or require the form to be provided in a format other than XML, such as eXtensible Business Reporting Language ("XBRL")? Is there another format that is more widely used or would be more appropriate for the required data? Is there a need for more detailed categories of data? What would be the costs to funds of providing data in the XML format? Would there be a disproportionate cost burden on smaller fund companies? Is there another format that would be less costly but still allow investors and analysts easily to view (or download) and analyze the data from a central database? Should the Commission use the EDGAR database or should it create a new database? Should the Commission consider the implementation of reporting on Form N-MFP initially through a voluntary pilot program?

3. *Amendment to Rule 30b1-5*

To avoid unnecessarily duplicative disclosure obligations, we propose to amend rule

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254 *See* section 30(c)(2)(A) of the Investment Company Act (requiring Commission to consider and seek public comment on feasible alternatives to the required filing of information that minimize reporting burdens on funds).

255 *See* section 30(c)(2)(B) of the Investment Company Act (requiring Commission to consider and seek public comment on the utility of information, documents and reports to the Commission in relation to the associated costs).

30b1-5 to exempt money market funds from the requirement to file their schedules of investments pursuant to Item 1 of Form N-Q, a quarterly schedule of portfolio holdings of management investment companies.[256] We request comment on this exemption. We are not proposing to exempt money market funds from the controls and procedures and certification requirements of Form N-Q. Should we also exempt money market funds from Item 2 of Form N-Q, which requires disclosure of certain information about a fund's controls and procedures, and/or Item 3 of Form N-Q, which requires certain fund officers to file a certification as an exhibit to the form?[257] Should we exempt money market funds from the portions of Items 2 and 3 that pertain to the schedule of investments required by Form N-Q? Alternatively, should we amend Form N-Q and/or rule 30b1-5 to apply similar controls and procedures and certification requirements to the proposed monthly reporting requirement? Should we exempt money market funds from requirements to provide portfolio schedules in Form N-CSR?[258]

G. Processing of Transactions

We are proposing to require that each money market fund's board determine in good faith, at least once each calendar year, that the fund (or its transfer agent) has the capacity to redeem and sell its securities at a price based on the current net asset value per share.[259] This proposed amendment would require money funds to have the operational capacity to "break a dollar" and continue to process investor transactions in an orderly manner.[260]

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256 Item 1 of Form N-Q requires funds to file the schedule of investments, as of the close of the reporting period, in accordance with rules 12-12 – 12-14 of Regulation S-X.

257 17 CFR 274.130.

258 *See supra* note 237.

259 Proposed rule 2a-7(c)(1) (new last two sentences).

260 Once a fund has broken the buck, the fund could no longer use the amortized cost method of valuing portfolio securities, and therefore would have to compute share price by reference to the market values of the portfolio with the accuracy of at least a tenth of a cent. *See* 1983 Adopting Release, *supra* note 3, at n.6 and accompanying text. Thus, a fund whose market-based net asset

Money market funds that seek to maintain a stable net asset value do not guarantee that they will be able to maintain the stable net asset value. Indeed, each money market fund prospectus must disclose that an investor may lose money by investing in the fund.[261] Nonetheless, we understand that some money market funds do not have in place systems to process purchases and redemptions at prices other than the funds' stable net asset value. In other words, the systems of these money market funds and their transfer agents are "hardwired" to process shareholder transactions at only the stable net asset value.

The consequences of such an operational limitation contributed to the delays in redeeming shareholders of The Reserve Primary Fund after that fund broke the buck in September 2008. We understand that all transactions thereafter had to be processed manually, a time-consuming and expensive process that extended the time that shareholders had to wait for the proceeds from their shares.[262]

We believe that money market funds that do not have the operational capacity to price

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value was determined to be $0.994 would, upon ceasing to use the amortized cost method of valuation, begin to redeem shares at $0.994 (rather than at $0.990). *See generally id.*

261 Item 2(c)(1)(ii) of Form N-1A [17 CFR 239.15A, 274.11A]. Similar disclosure is required in money market fund advertisements and sales literature. *See* rule 482(b)(4) under the Securities Act of 1933 [17 CFR 230.482]; rule 34b-1(a).

262 *See* Press Release, The Reserve Fund, Timeframe for Initial Distribution Payment of Reserve Primary Fund (Sept. 30, 2008) (explaining that "[m]oney market management systems … are programmed to accommodate a constant $1.00 NAV [and that making] a distribution to holders that have made redemption requests since September 15, 2008 necessitated a series of system modifications designed to ensure an accurate and equitable distribution of funds"); Press Release, The Reserve Fund, Reserve Primary Fund Disbursement Update (Oct. 15, 2008) (explaining that Reserve Fund investors were "supported by complex technology at The Reserve as well as their own systems, which had to be adjusted due to the decline of the net asset value below $1.00 on September 16 … [and that The Reserve Fund was] working diligently to enhance … existing software and add new programs to hasten the distribution process"). *See also* Press Release, The Reserve Fund, Statement About The Reserve Yield Plus Fund (Oct. 17, 2008) ("apologiz[ing] for the delay in meeting redemption requests" in a short-term bond fund, and explaining that the fund's sponsor needed to "first move the Fund to a different computer platform that's able to account for a share price below $1.00 … [which] wasn't anticipated when the Fund was created").

shares according to market values expose their shareholders to unnecessary risks – risks that may render a money market fund unable to meet its obligations under section 22(e) of the Act to pay the proceeds of a redemption within seven days. Therefore, we propose to amend rule 2a-7 to require that a money market fund's board determine in good faith, no less frequently than once each calendar year, that the fund (or its transfer agent) has the capacity to redeem and sell fund shares at prices based on the current net asset value per share. The proposed amendment also clarifies that this capacity includes the capacity to sell and redeem shares at prices that do not correspond to the stable net asset value or price per share.[263]

We request comment on this proposed amendment. Is it appropriate? Should the board play a role in this determination? Should we instead revise the risk-limiting conditions of the rule to require that the fund simply *have* the capacity to redeem and sell securities at market-based prices? Alternatively, should the rule require that the board determine that the fund has *adopted procedures* adequate to enable the fund to redeem and sell securities at market-based prices? Or should the rule require that the board *approve* such procedures? If the rule requires a determination by the board, is an annual determination appropriate? Should the determination be more frequent (*e.g.*, quarterly) or less frequent (*e.g.*, every three years)?

H. Exemption for Affiliate Purchases

The Commission is proposing to amend rule 17a-9, which provides an exemption from section 17(a) of the Act to permit affiliated persons of a money market fund to purchase distressed portfolio securities from the fund.[264] The amendment would expand the

263 Proposed 2a-7(c)(1) (new third sentence).

264 Absent a Commission exemption, section 17(a)(2) prohibits any affiliated person or promoter of or principal underwriter for a fund (or any affiliated person of such a person), acting as principal, from knowingly purchasing securities from the fund. Rule 17a-9 exempts certain purchases of securities from a money market fund from section 17(a). For convenience, in this Release, we refer to all of the persons who would otherwise be prohibited by section 17(a)(2) from purchasing

circumstances under which affiliated persons can purchase money market fund portfolio securities.[265] The Commission is also proposing a related amendment to rule 2a-7, which would require that funds report all such transactions to the Commission.

1. Expanded Exemptive Relief

In 1996, the Commission adopted rule 17a-9 under the Act to permit affiliated persons to purchase a security from an affiliated money market fund that is no longer an eligible security under rule 2a-7, as long as the purchase price is paid in cash and is equal to the amortized cost of the security or its market price, whichever is greater.[266] The rule codified a series of staff no-action letters in which the staff agreed not to recommend enforcement action to the Commission if affiliated persons of a money market fund purchased portfolio securities from the fund in order prevent the fund from realizing losses on the securities that may otherwise have caused it to break the buck.[267] When we adopted the rule we explained that experience had shown that such transactions appeared to be fair, reasonable, in the best interests of fund shareholders, and consistent with the requirement that money market funds dispose of a defaulted security in an orderly manner as soon as practicable.[268]

The current rule exempts only purchases of securities that are no longer "eligible

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securities of a money market fund as "affiliated persons." "Affiliated person" is defined in section 2(a)(3) of the Act.

265 The proposed expansion of the rule would not include "capital support agreements" supporting the net asset value per share of money market funds, which support fund affiliates provided in several instances in reliance on no-action assurances by our staff. *See supra* note 38. Unlike direct purchases of securities by affiliates, the nature and terms of these agreements are highly customized and terminate after a limited period of time. As a result, these situations do not readily lend themselves to being addressed in a rule of general applicability.

266 Rule 17a-9(a) and (b). *See* 1996 Adopting Release, *supra* note 20, at nn.190-94 and accompanying text.

267 *See* 1996 Adopting Release, *supra* note 20, at nn.190-92 and accompanying text.

268 *See id.*

securities" under rule 2a-7 because, for example, their ratings have been downgraded. This limitation served as a proxy indicating that the market value of the security was likely less than its amortized cost value, and thus the resulting transaction was fair to the fund and did not involve overreaching.[269] Since rule 17a-9 was adopted, our staff has responded to several emergency requests for no-action relief for transactions involving portfolio securities that remained eligible securities. In some cases, the fund's adviser anticipated that the securities would be downgraded and sought to arrange a purchase by an affiliate as a preventive measure before the distressed security could impact the fund's market-based net asset value.[270] In other cases, markets for portfolio securities had become illiquid and the affiliated person sought to provide the fund with cash to satisfy redemptions by purchasing portfolio securities.[271] In all cases, the terms of the transactions met all the requirements of rule 17a-9 except that the securities were eligible securities.

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269 *See id.* at text following n.194 ("The rule, as adopted, is available for transactions involving securities that are no longer eligible securities because they no longer satisfy either the credit quality or maturity limiting provisions (*e.g.*, the securities are long-term adjustable-rate securities whose market values no longer approximate their par values on the interest rate readjustment dates).").

270 *See, e.g.,* Fixed Income Shares – Allianz Dresdner Daily Asset Fund, SEC Staff No-Action Letter (May 5, 2008); First American Funds, Inc. – Prime Obligation Fund, SEC Staff No-Action Letter (Dec. 3, 2007); MainStay VP Series Fund – MainStay VP Cash Management Portfolio, SEC Staff No-Action Letter (Oct. 22, 2008); Institutional Liquidity Trust – Prime Master Series, SEC Staff No-Action Letter (Apr. 30, 2008); Penn Series Funds, Inc. – Money Market Fund, SEC Staff No-Action Letter (Oct. 22, 2008); Phoenix Opportunities Trust – Phoenix Money Market Fund and Phoenix Edge Series Fund – Phoenix Money Market Series, SEC Staff No-Action Letter (Oct. 22, 2008); USAA Mutual Funds Trust – USAA Money Market Fund, SEC Staff No-Action Letter (Oct. 22, 2008). SEC staff no-action letters are available on the SEC website at http://www.sec.gov/divisions/investment/im-noaction.shtml under the hyperlink for the relevant letter.

271 *See, e.g.,* Dreyfus Money Funds, SEC Staff No-Action Letter (Oct. 20, 2008); Mount Vernon Securities Lending Trust, Inc. – Mount Vernon Securities Lending Prime Portfolio, SEC Staff No-Action Letter (Oct. 22, 2008); Morgan Stanley Money Market Funds, SEC Staff No-Action Letter (Oct. 22, 2008); Reserve New York Municipal Money-Market Trust – New York Municipal Money-Market Fund, SEC Staff No-Action Letter (Nov. 18, 2008); Russell Investment Company – Russell Money Market Fund, SEC Staff No-Action Letter (Oct. 20, 2008).

Our staff's experience is that these transactions appear to be similarly fair and reasonable and in the best interest of shareholders. We are therefore proposing to extend the exemption to additional types of transactions, which will eliminate the need for affiliated persons to seek no-action assurances from our staff for these transactions when the delay would not be in the best interests of shareholders.

Currently, under rule 17a-9 a security must no longer be an eligible security for an affiliated person of a money market fund to purchase such security. Under the proposed amendment, a money market fund could sell a portfolio security that has defaulted (other than an immaterial default unrelated to the financial condition of the issuer), to an affiliated person, even though the security continued to be an eligible security.[272] Any such transaction would have to satisfy the existing requirements of rule 17a-9.[273]

In addition, we propose to add a new provision to rule 17a-9 that would permit affiliated persons, for any reason, to purchase other portfolio securities (*e.g.*, eligible securities that have not defaulted) from an affiliated money market fund for cash at the greater of its amortized cost value or market value, provided that such person promptly remits to the fund any profit it realizes from the later sale of the security.[274] Because in these circumstances there may not be an objective indication that the security is distressed (and thus that the transaction is clearly in the interest of the fund), the proposed "claw-back" provision would eliminate incentives for fund advisers and other affiliated persons to buy securities for reasons other than protecting fund

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272 Proposed rule 17a-9(a). Other provisions of rule 2a-7 currently except immaterial defaults unrelated to the financial condition of the issuer. *See* rule 2a-7(c)(6)(ii)(A). As we have noted in the past, this exception is intended to exclude defaults that are technical in nature, such as where the obligor has failed to provide a required notice or information on a timely basis. *See* 1991 Adopting Release, *supra* note 20, at Section II.E.2.

273 Proposed rule 17a-9(a)(1) and (2).

274 Proposed rule 17a-9(b)(2).

shareholders from potential future losses.

We request comment on all aspects of the proposed expansion of rule 17a-9. Should we instead expand the exemption to include only those portfolio securities that fall within enumerated categories (*e.g.,* securities have defaulted, have become illiquid, have been determined by the board of directors to no longer present minimal credit risk)? If so, what would those categories be and why? Would any additional conditions be needed with respect to particular categories of purchases to control for potential conflicts of interest on the part of the adviser? Is so, what conditions should we include? Is it appropriate to subject only eligible securities that have not defaulted to the proposed claw-back provision? Is such a provision necessary and fair? Should we provide a time limit after purchase when the required claw-back provision would no longer apply? Should we exclude from the claw-back requirement potential payments to money market funds that are subsequently liquidated?

2. *New Reporting Requirement*

The Commission is also proposing an amendment to rule 2a-7 that would require a money market fund whose securities have been purchased by an affiliated person in reliance on rule 17a-9 to provide us with prompt notice of the transaction via electronic mail.[275] We proposed a similar amendment last summer in connection with the NRSRO References Proposal.[276] That proposal is superseded by the requirement we propose here, which contains one change.[277] Due to the nature of the proposed amendments to rule 17a-9, which do not restrict the purchase of a portfolio security from a fund to particular categories, we propose to require

[275] Proposed rule 2a-7(c)(7)(iii)(B). The electronic mail notification would be directed to the Director of our Division of Investment Management, or the Director's designee. Proposed rule 2a-7(c)(7)(iii).

[276] *See* NRSRO References Proposal, *supra* note 105, at n.35 and accompanying text.

[277] Proposed rule 2a-7(c)(7)(iii)(B).

not only notice of the fact of the purchase, but also the reasons for the purchase. Such reasons might include, for example, that the fund's adviser expected that the security would be downgraded, that due to the decreased market value of the security the fund was at risk of breaking the buck, or that the fund was experiencing heightened redemption requests and wished to avoid a "fire sale" of assets to satisfy such requests.

We continue to believe that the current notice requirement in rule 2a-7, which is triggered when a security over a threshold amount of the fund's assets defaults, provides us with incomplete information about money market fund holdings of distressed securities, particularly those that have engaged in affiliated transactions.[278] We also continue to believe that this proposed notice requirement, which is a concept supported by some commenters last summer,[279] would impose little burden on money market funds or their managers, and would enhance our oversight of money market funds especially during times of economic stress. We request comment on this proposed notice requirement. Is the proposed requirement that the notice include the reasons for the purchase by the affiliate sufficiently clear? Should we require that any additional information be included in the notice and should the notice take a particular form?

I. Fund Liquidation

1. Proposed Rule 22e-3

The Commission is proposing a new rule 22e-3, which would exempt money market funds from section 22(e) to permit them to suspend redemptions in order to facilitate an orderly liquidation of the fund. The new rule would replace rule 22e-3T, a temporary rule that provides

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278 *See* NRSRO References Proposal, *supra* note 105, at Section III.A.4.

279 *See, e.g.,* Comment Letters of the Investment Company Institute (Sept. 5, 2008); Commenter Letter of the Mutual Fund Directors Forum (Sept. 5, 2008); Comment Letter of OppenheimerFunds, Inc. (Sept. 4, 2008); Comment Letter of Charles Schwab Co., Inc. (Sept. 5, 2008). Comment letters may be accessed on the Commission's website at http://www.sec.gov/comments/s7-19-08/s71908.shtml.

a similar exemption for money market funds participating in the Treasury Department's Guarantee Program.[280]

Section 22(e) of the Act generally prohibits funds, including money market funds, from suspending the right of redemption, and from postponing the payment or satisfaction upon redemption of any redeemable security for more than seven days. The provision was designed to prevent funds and their investment advisers from interfering with the redemption rights of shareholders for improper purposes, such as the preservation of management fees.[281] Although section 22(e) permits funds to postpone the date of payment or satisfaction upon redemption for up to seven days, it does not permit funds to suspend the right of redemption, absent certain specified circumstances or a Commission order.

As discussed above, on September 22, 2008, we issued an order under section 22(e) to permit two series of The Reserve Fund to suspend redemptions and postpone payments in the midst of a run on the fund. In November 2008, we adopted rule 22e-3T to permit money market funds participating in the Treasury's Guarantee Program to suspend redemptions and postpone the payment of redemption proceeds if a fund breaks the buck and begins liquidation proceedings under the Guarantee Program.[282]

The temporary rule was intended to facilitate the orderly disposal of assets in a manner that would protect the interests of all shareholders. Absent the exemption provided by rule 22e-3T, a fund participating in the Guarantee Program that faces a run would be compelled by

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280 The Treasury's Guarantee Program guarantees that shareholders of a participating money market fund will receive the fund's stable share price for each share owned as of September 19, 2008, if the fund liquidates under the terms of the Program. *See supra* note 55 and accompanying text.

281 *See Investment Trusts and Investment Companies: Hearings on S. 3580 Before a Subcomm. of the Senate Comm. on Banking and Currency*, 76th Cong., 3d Sess. 291 (1940) (statement of David Schenker, Chief Counsel, Investment Trust Study, SEC).

282 *See* Rule 22e-3T Adopting Release, *supra* note 31.

section 22(e) to continue to redeem shares. In order to raise the money to pay redemption proceeds to shareholders, a fund may have to sell portfolio securities. Massive redemption requests could thus force a fund to liquidate positions in a fire sale, further depressing the fund's market value share price. Earlier redeeming shareholders would receive higher share prices (at or near the amortized cost) but, as a result of the fund's diminishing asset base, later redeeming shareholders may receive lower prices.[283] Moreover, as demonstrated by the events of last fall, a run on a single fund can quickly spread to other funds and, as multiple funds attempt to meet redemption requests, seriously deplete the value of portfolio holdings and drain the availability of cash and more liquid securities.

We believe that rule 22e-3T, which will expire on October 18, 2009 in conjunction with the Guarantee Program, should be replaced with a rule that would provide for a similar exemption independent of the Guarantee Program.[284] Proposed rule 22e-3 would permit all money market funds to suspend redemptions upon breaking a buck, if the board, including a majority of independent directors, approves liquidation of the fund, in order to liquidate in an orderly manner. The proposed rule is intended to reduce the vulnerability of investors to the

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[283] *Id.*

[284] One commenter on rule 22e-3T recommended that we make the rule a permanent rule for any fund preparing to liquidate, independent of the Guarantee Program. *See* Comment Letter of the Investment Company Institute (Dec. 24, 2008). Two other comment letters related to matters unique to the Guarantee Program. *See* Comment Letter of the Coalition of Mutual Fund Investors (Dec. 14, 2008) (recommending that any fund that liquidates and relies on the Guarantee Program be required to provide information obtained pursuant to rule 22c-2 under the Investment Company Act); Comment Letter of Michael F. Johnson (Nov. 20, 2008) (requesting information concerning the applicability of the Guarantee Program to a particular fund). The only other comment letter that the Commission received concerning interim final rule 22e-3T was a letter from the Committee of Annuity Insurers, discussed below. *See infra* note 288 and accompanying text. Comments on interim final rule 22e-3T, File No. S7-32-08, are available at http://www.sec.gov/comments/s7-32-08/s73208.shtml.

Once rule 22e-3T expires, the Commission would stand ready to consider applications for exemptive relief under section 22(e).

harmful effects of a run on a fund, and minimize the potential for disruption to the securities markets.

Proposed rule 22e-3(a) would permit a money market fund to suspend redemptions if: (i) the fund's current price per share, calculated pursuant to rule 2a-7(c), is less than the fund's stable net asset value per share; (ii) its board of directors, including a majority of directors who are not interested persons, approves the liquidation of the fund; and (iii) the fund, prior to suspending redemptions, notifies the Commission of its decision to liquidate and suspend redemptions, by electronic mail directed to the attention of our Director of the Division of Investment Management or the Director's designee.[285] These proposed conditions are intended to ensure that any suspension of redemptions will be consistent with the underlying policies of section 22(e). We understand that suspending redemptions may impose hardships on investors who rely on their ability to redeem shares. Accordingly, our proposal is limited to permitting suspension of this statutory protection only in extraordinary circumstances. Thus, the proposed conditions, which are similar to those of the temporary rule, are designed to limit the availability of the rule to circumstances that present a significant risk of a run on the fund. Moreover, the exemption would require action of the fund board (including the independent directors), which would be acting in its capacity as a fiduciary.[286]

The proposed rule contains an additional provision that would permit us to take steps to protect investors. Specifically, the proposed rule would permit us to rescind or modify the relief provided by the rule (and thus require the fund to resume honoring redemptions) if, for example, a liquidating fund has not devised, or is not properly executing, a plan of liquidation that protects

285 Proposed rule 22e-3(a).

286 We also note that the potential for abuse may be mitigated because the impending liquidation of the fund would ultimately eliminate a source of advisory fees for the adviser. *See* Rule 22e-3T Adopting Release, *supra* note 31, at text accompanying nn.19-20.

fund shareholders.[287] Under this provision, the Commission may modify the relief "after appropriate notice and opportunity for hearing," in accordance with section 40 of the Act.

Paragraph (b) of the proposed rule would provide a limited exemption from section 22(e) for certain conduit funds that invest, pursuant to section 12(d)(1)(E) of the Act, all of their assets in a money market fund that suspends redemption in reliance on paragraph (a) of the proposed rule.[288] Without this exemption, these conduit funds may be placed in the position of having to honor redemption requests while being unable to liquidate shares of money market funds held as portfolio securities. We anticipate that this provision would be used principally by insurance company separate accounts issuing variable insurance contracts and by funds participating in master-feeder arrangements.[289]

We request comment generally on all aspects of proposed rule 22e-3. Is it appropriate to permit money market funds that break the buck to suspend redemptions during liquidation? Should the exemption be available to other types of open-end investment companies? Should there be additional or alternative conditions with regard to the exemption (*e.g.*, should the fund be required to disclose its liquidation plan to shareholders)? Should there be a limit on the suspension period so that shareholder assets are not "locked up" for an unduly lengthy period? If so, what should be the maximum length of the suspension period (*e.g.*, 60 or 90 days)?

2. *Request for Comment on Other Regulatory Changes*

We also request comment on certain additional changes that we are considering but are

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287 Proposed rule 22e-3(c). We adopted a similar provision in rule 22e-3T. Rule 22e-3T(b); *see also* Rule 22e-3T Adopting Release, *supra* note 31.

288 Proposed rule 22e-3(b). This provision is based on a suggestion we received in a comment letter submitted in connection with rule 22e-3T. *See* Comment Letter of the Committee of Annuity Insurers (Dec. 23, 2008) (requesting that the Commission extend the application of rule 22e-3T to insurance company separate accounts). Proposed rule 22e-3(b) also would require a fund to promptly notify the Commission that it has suspended redemptions in reliance on the rule.

289 For a discussion of master-feeder arrangements, *see supra* note 194.

not currently proposing, relating to the suspension of redemptions that may provide additional protections to money market fund investors.

a. Temporary Suspensions for Exigent Circumstances

Should we include a provision in rule 22e-3 that would permit fund directors to temporarily suspend redemptions during certain exigent circumstances other than liquidation of the fund? The ICI Report recommends that we permit a fund's directors to suspend temporarily the right of redemption if the board, including a majority of its independent directors, determines that the fund's net asset value is "materially impaired."[290] Under this approach, the fund could suspend redemptions for up to five days, during which time the fund could attempt to restore its net asset value (*e.g.*, by securing credit support agreements). In the event that the fund could not restore its net asset value within that period, the fund would be required to begin the liquidation process. A fund would be permitted to exercise this option only once every five years. This "time out" could give money market funds some time during turbulent periods to assess the viability of the fund.[291]

We request comment generally on whether we should provide this additional relief. Would it make money market funds less appealing to investors? Would it provide time for directors to find a solution? Or might it accelerate redemptions from shareholders once the suspension period ends, regardless of any action taken by the board of directors?[292] Could the

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290 ICI REPORT, *supra* note 6, at 85-89.

291 Similarly, the Treasury's Guarantee Program and rule 22e-3T effectively provide funds with the ability to temporarily suspend redemptions. The Guarantee Program requires funds that break the buck to commence liquidation proceedings within five days, unless the fund restores its net asset value to a level equal to or above $0.995 within that period. Meanwhile, rule 22e-3T permits funds to suspend redemptions if a fund breaks the buck and has not yet "cured" the event.

292 In other situations, temporary restrictions on redemptions may have exacerbated the situation and increased the rate of redemptions. *See* Svea Herbst-Bayliss, *"Gates" May Have Hurt More Than Helped Hedge Funds*, REUTERS, Mar. 26, 2009, *available at* http://www.reuters.com/article/PrivateEquityandHedgeFunds09/idUSTRE52P4JJ20090326.

accumulating redemptions "hanging over the fund" place pressure on the prices of fund portfolio securities? How could we ensure that directors would use this authority only in exigent circumstances? When is a money market fund's net asset value "materially impaired"? Would this term include circumstances in which the fund has overvalued securities, which, if sold to satisfy redemptions, would have to be marked down?

We also request comment on how a temporary suspension should operate. What disclosures should a money market fund be required to make, and when and where should the fund make them? Should a fund be required to calculate its net asset value during the suspension period, and, if so, should the net asset value be publicly disclosed? Should the suspension period be longer or shorter than five days? What factors should the board of directors take into consideration when deciding whether to suspend redemptions temporarily? How would directors weigh the various and possibly competing interests of shareholders?

b. Options for Shareholders in Liquidating Funds

If a fund suspends redemptions in order to liquidate, the directors would likely distribute money to investors as it becomes available from the sale of portfolio securities, while maintaining a reserve to cover expenses and potential liabilities. As we have seen, this process can be lengthy. Should we include conditions in any rule regarding the treatment of shareholders in a liquidation?[293] For example, should we require that fund assets be distributed on a pro rata basis? Should there be a limit on allowable reserves?

293 The Investment Company Act does not contain any provisions governing the liquidation of an investment company, including a money market fund; rather, liquidations are primarily effected in accordance with applicable state law. The Act does include, however, a provision authorizing Federal district courts to enjoin a plan of reorganization upon a proceeding initiated by the Commission on behalf of security holders, if the court determines that the plan of reorganization is not "fair and equitable to all security holders." Section 25(c) of the Act. A plan of "reorganization" includes a voluntary dissolution or liquidation of a fund. Section 2(a)(33) of the Act.

Alternatively, should we permit or require a fund board to recognize that investors will have different preferences for liquidity and capital preservation? For example, a fund that decides to liquidate and suspend redemptions could be allowed to offer shareholders the choice of redeeming their shares immediately at a reduced net asset value per share that reflects the fair market value of fund assets, *i.e.*, at a price below the fund's stable net asset value. Remaining shareholders would receive their redemption proceeds at the end of the liquidation process and may receive the economic benefit of an orderly disposal of assets. Would such an approach be fair to all fund shareholders? What conditions would be necessary and appropriate to ensure that shareholders are treated fairly? Specifically, how would such a mechanism operate? Should funds be able to deduct an additional discount or "haircut" from earlier redeeming shareholders to provide additional protection for later redeeming shareholders? Should we permit boards to decide the amount of the haircut? If so, what factors should boards use to decide such haircuts? What disclosures and information would be necessary to permit shareholders to make an informed decision between the options?

Should investors be required to choose their preferences at the time they purchase fund shares? Should investors be able to change their preferences? If so, how and when? Should they be able to choose their preferences when a fund announces its intention to liquidate and suspend redemptions under the rule? If so, should we (or the fund board) establish a default assumption for investors that fail to respond to the inquiry?

III. REQUEST FOR COMMENT

The Commission requests comment on the rules and amendments proposed in this release. Commenters are requested to provide empirical data to support their views. The Commission also requests suggestions for additional changes to existing rules or forms, and comments on other matters that might have an effect on the proposals contained in this release.

We recognize that the events of the last two years raise the question of whether further and perhaps more fundamental changes to the regulatory structure governing money market funds may be warranted. Therefore we are exploring other ways in which we could improve the ability of money market funds to weather liquidity crises and other shocks to the short-term financial markets. We invite interested persons to submit comments on the advisability of pursuing any or all of the following possible reforms, as well as to provide other approaches that we might consider to achieve our goals. We expect to benefit from the comments we receive before deciding whether to propose these changes.[294]

A. Floating Net Asset Value

When the Commission adopted rule 2a-7 in 1983,[295] it facilitated money market funds' maintenance of a stable net asset value by permitting them to use the amortized cost method of valuing their portfolio securities. As discussed above, section 2(a)(41) of the Act, in conjunction with rules 2a-4 and 22c-1, normally require a registered investment company to calculate its current net asset value per share by valuing its portfolio securities for which market quotations are readily available at current market value and its other securities at their fair value as determined, in good faith, by the board of directors. Therefore, using the amortized cost method of valuation is an exception to the general requirement under the Act that investors in investment companies should pay and receive market value or fair value for their shares.[296] The Commission

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294 In addition, we note that the U.S. Department of the Treasury's white paper on Financial Regulatory Reform calls for the President's Working Group on Financial Markets to prepare a report by September 15, 2009 assessing whether more fundamental changes are necessary to further reduce the money market fund industry's susceptibility to runs, such as eliminating the ability of a money market fund to use a stable net asset value or requiring money market funds to obtain access to reliable emergency liquidity facilities from private sources. *See* DEPARTMENT OF THE TREASURY, FINANCIAL REGULATORY REFORM, A NEW FOUNDATION: REBUILDING FINANCIAL SUPERVISION AND REGULATION, at 38-39 (June 2009).

295 *See* 1983 Adopting Release, *supra* note 3.

296 Rule 2a-7 is not the only exception permitting open-end investment companies to value short-

did not take lightly its decision to permit money market funds to use the amortized cost method of valuation. Rule 2a-7 essentially codified several of the Commission's exemptive orders relating to money market funds, and these orders were issued only after an administrative hearing in the late 1970s at which the use of the amortized cost method of valuation was a matter of considerable debate.[297]

The balance the Commission struck was that, in exchange for permitting this valuation method, it would impose certain conditions on money-market funds designed to ensure that these funds invested only in instruments that would tend to promote a stable net asset value per share and would impose on the funds' boards of directors an ongoing obligation to determine that it remains in the best interest of the funds and their shareholders to maintain a stable net asset value. Further, money market funds are permitted to use the amortized cost method of valuation only so long as their boards believe that it fairly reflects the funds' market-based net asset value per share.[298]

The $1.00 stable net asset value per share has been one of the trademark features of money market funds. It facilitates the funds' role as a cash management vehicle, provides tax and administrative convenience to both money market funds and their shareholders,[299] and promotes money market funds' role as a low-risk investment option. Many investors may hold

term debt securities in their portfolios on an amortized cost basis. Subject to certain conditions, the amortized cost method of valuation may be used by open-end investment companies to value investments with a remaining maturity of 60 days or less in accordance with the Commission's interpretation set forth in Valuation of Debt Instruments by Money Market Funds and Certain Other Open-End Investment Companies, Investment Company Act Release No. 9786 (May 31, 1977) [42 FR 28999 (June 7, 1977)].

297 *See* 1982 Proposing Release, *supra* note 25, at text preceding, accompanying, and following nn.2-4.

298 *See* rule 2a-7(c)(1).

299 A $1.00 stable net asset value per share relieves shareholders of the administrative task of tracking the timing and price of purchase and sale transactions for capital gain and wash sale purposes under tax laws.

shares in money market funds in large part because of these features.[300] We are mindful that if we were to require a floating net asset value, a substantial number of investors might move their investments from money market funds to other investment vehicles.

However, a stable $1.00 net asset value per share also creates certain risks for a money market fund and its investors. These risks are a consequence of the amortized cost method of valuation and the resulting insensitivity of the $1.00 net asset value per share to market valuation changes. It may create an incentive for investors to redeem their shares when a fund's market-based net asset value per share falls between $0.995 and $1.00 because they will obtain $1.00 in exchange for their right to fund assets worth less than $1.00 per share. Regardless of the motivation underlying the redemptions, the unrealized losses attributable to redeeming shareholders are now borne by the remaining money market fund shareholders.

Further, particularly in times of market turbulence and illiquidity, regardless of the motivation behind the redemptions, redemptions at $1.00 in a money market fund whose market-based net asset value is below $1.00 can further depress the fund's market-based net asset value, exacerbating the impact on remaining shareholders. It can create a level of unfairness in permitting the remaining fund shareholders to pay for the liquidity needs and unrealized losses of redeeming fund shareholders. Because there is a limited window where only so many shareholders can redeem at $1.00 in a fund with a portfolio under threat (because of holding distressed securities or facing significant shareholder redemptions) before the board of the fund must consider whether to re-price the fund's shares or take other action, there can be an incentive

300 Some institutional investors are prohibited by board-approved guidelines or firm policies from investing certain assets in money market funds unless they have a stable net asset value per share. *See* ICI REPORT, *supra* note 6, at 109. One survey also reported that 55% of institutional cash managers would substantially decrease their investments in money market funds if the funds had a floating value. *See id.* at 110 (citing a January 2009 survey by Treasury Strategies, Inc.).

to be the first shareholder to place a redemption request upon any hint of stress at a money market fund. Generalized market dislocations or illiquidity can create this stress on a number of money market funds simultaneously, leading to runs on money market funds similar to those we witnessed in September 2008. Even further, a run may result in fire sales of securities, placing pressure on market prices and transmitting problems that may be originally associated with a single money market fund to other money market funds. Finally, larger, institutional money market fund investors, especially those with fiduciary responsibilities for managing their clients' assets, are more likely to recognize negative events potentially affecting the money market fund and to be in a position to quickly redeem shares of the money market fund and thus protect their money market investments and those of their clients, leaving other smaller, more passive money market investors to bear their losses.

When we determined to permit money market funds to use amortized cost valuation in 1983, money market funds held only about $180 billion in assets[301] and played a minor role in the short-term credit markets. Their principal benefit was to provide *retail* investors with a cash investment alternative to bank deposits, which at the time paid fixed rates substantially below short-term money market rates. Since that time, money market funds have grown tremendously and have developed into an industry driven in large part by *institutional* investors, who hold approximately 67 percent of the over $3.7 trillion in money market fund assets.[302] As noted earlier, with the ability of institutional investors today to make hourly redemption requests to money market funds, these investors have the ability to move substantial amounts of money in and out of money market funds (or between money market funds), with potentially detrimental effects on the funds, their remaining shareholders, and the marketplace.

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301 *See* ICI REPORT, *supra* note 6, at 1.

302 *See* ICI Mutual Fund Historical Data, *supra* note 47 (data for week ended June 10, 2009).

The influx of institutional investments in money market funds, the increased transparency of fund holdings, and the speed with which large shareholders can buy and redeem shares may have increased the possibility that the value of some fund investors' shares will be diluted as a result of the fund's use of the amortized cost valuation method.[303] When short-term interest rates decrease, the fund's portfolio holdings (with their now above-market yields) become more valuable. Institutional investors may pay $1.00 per share to purchase fund shares whose market value is, for example, $1.002 per share. Such institutional inflows would be invested by the fund in securities offering the new, reduced market yields, diluting the yield advantage that existing fund shareholders would otherwise enjoy. These institutional investors, in effect, are able to earn a yield through a money market fund above the market rate they could earn on a direct investment. They achieve this yield advantage by capturing a portion of the benefit from declining interest rates that otherwise would benefit existing money market fund investors.[304] Similarly, when interest rates increase, institutional investors could sell shares of money market funds, obtaining $1.00 per share for a fund that all things being equal likely will be worth less, *e.g.*, $0.997 per share.[305] If instead the institutional investor sells commercial paper in the market

303 We have considered the impact of dilution in money market funds using the amortized cost method of valuation in the past. *See, e.g.*, 1982 Proposing Release, *supra* note 25, at n.6 and accompanying text.

304 This benefit would otherwise be paid out to money market fund shareholders in the form of greater dividend payments from the increased yield.

305 *See* S&P 2007 RATINGS CRITERIA, *supra* note 139, at 27. Standard and Poor's gives the example of an investor holding $1 million in 90-day U.S. Treasury bills yielding 5%. If interest rates increased 150 basis points, the value of the investment would drop by approximately $3700 and the investor's yield would remain at 5%. Compare this to an investor holding one million shares of a money market fund holding exclusively Treasury bills yielding 5% (setting aside fund expenses). If interest rates rose 150 basis points, the investor could sell the fund investment for $1.00 per share and not experience any loss. The investor could then purchase 90-day Treasury bills yielding 6.5%, instantaneously increasing its return by 1.5%. If the fund is forced to sell these securities to meet redemption requests, the $3700 unrealized loss would be borne by the fund and its remaining shareholders.

under the same conditions, it could only sell such securities at a discount.

In stable markets and with small shareholdings, amortized cost pricing at most results in shareholders who purchase or redeem shares receiving slightly more or less (in shares or in redemption proceeds) than they otherwise would if the fund's net asset value were to fluctuate according to market-based pricing. Net redemptions generally are funded by cash on hand. Any deviation between the market-based net asset value per share of the fund and its amortized cost value is small enough to have an immaterial effect on the fund, and no effect on investors. It could be compared to a rounding convention in a billing system.

In a market under significant stress and with institutions holding billions of dollars of money market fund shares, however, a real arbitrage opportunity can arise, and a race or threat of a potential race for redemptions may become a real possibility. For example, during last fall's market turbulence, as credit spreads on many money market fund portfolio securities widened and the market value of these securities fell, we understand that the market-based net asset value of some money market funds dropped low enough that redemptions by a few large shareholders in the fund at $1.00 per share alone could have caused the fund to break the buck.

We recognize that a floating net asset value would not necessarily eliminate the incentive to redeem shares during a liquidity crisis—shareholders still would have an incentive to redeem before the portfolio quality deteriorated further from the fund selling securities into an illiquid market to meet redemption demands. But a floating net asset value may lessen the impact of any portfolio deterioration by eliminating the ability of shareholders to redeem their shares for more than the current market value per share of the fund's portfolio. It also might better align investors' expectations of risk with the actual risks posed by money market fund investments. We expect that, at least under stable market conditions, the other risk-limiting conditions of rule

2a-7 would tend to promote a relatively stable net asset value per share even if we eliminated the ability of money market funds to rely on the amortized cost method of valuation.

We request comment on the possibility of eliminating the ability of money market funds to use the amortized cost method of valuation. Would such a change render money market funds a more stable investment vehicle? Would it lessen systemic risk by making money market funds less susceptible to runs? Would it make the risks inherent in money market funds more transparent? Many money market funds' stable net asset value was supported voluntarily by fund affiliates over the last two years, and shareholders may not have understood that this support was provided on a voluntary basis and may not be provided in the future.

On the other hand, would such a change make money market funds more susceptible to runs because investors might respond quickly to small changes in net asset value? As discussed above, a stable net asset value per share creates certain administrative, tax, and cash management conveniences for fund investors. Accordingly, would prohibiting the use of the amortized cost method of valuation in money market funds encourage investors to shift assets from money market funds to unregulated offshore funds, bank accounts, or other investments? Would it result in some institutional money market funds deregistering with the Commission (in reliance on section 3(c)(7) of the Act) in order to continue to maintain a stable net asset value? Is this a result with which the Commission should be concerned?

What impact would this have on investors' cash management activities? What impact might such a change have on the short-term credit markets and issuers of short-term debt securities? How would money market funds whose share prices were based on market-based net asset values differ from current short-term bond funds? Should any rule amendment eliminating the ability of money market funds to rely on the amortized cost method of valuation to create a stable net asset value be limited to institutional money market funds? As discussed above, institutional money market funds are at greater risk of instability, runs and the dilutive effect of large redemptions.

B. In-Kind Redemptions

As noted above, one of our concerns relates to the ability of large institutional shareholders to rapidly redeem substantial amounts of fund assets, which can pose a threat to the stable net asset value of the fund and can advantage one group of shareholders over another by requiring remaining shareholders to pay for the liquidity needs of large redeeming shareholders.[306] While the liquidity requirements we are proposing today may ameliorate pressures created by redeeming shareholders, during severe market dislocations even more steps may be necessary to help ensure the stability of a stable net asset value money market fund. Accordingly, if we retain a stable net asset value for money market funds, we are interested in exploring other methods of reducing the risks and unfairness posed by significant sudden redemptions.

One possible way of addressing these issues would be to require that funds satisfy redemption requests in excess of a certain size through in-kind redemptions.[307] Money market funds currently are permitted to and many money market funds disclose in their prospectuses that they may satisfy redemption requests through in-kind redemptions.[308] In the wake of last fall's

306 This situation to some extent could be analogized to the situation that can be created by market timing in which selling shareholders receive benefits to the detriment of remaining mutual fund shareholders.

307 An in-kind redemption occurs when a shareholder's redemption request to a fund is satisfied by distributing to that shareholder portfolio assets of that fund instead of cash.

308 *See* section 2(a)(32) of the Act (defining a redeemable security as a security where the holder "is entitled ... to receive approximately his proportionate share of *the issuer's current net assets*, or the cash equivalent thereof" (italics added)). *See also* rule 18f-1, which provides an exemption from certain prohibitions of section 18(f)(1) of the Act with regard to redemptions in kind and in cash.

redemption pressures on money market funds, however, only one announced that it would do so.[309] In-kind redemptions would lessen the impact of large redemptions on remaining money market fund shareholders and would require the redeeming investor to bear part of the cost of its liquidity needs. If shareholders did not immediately sell these securities, requiring in-kind redemptions in such circumstances may mitigate the impact of large redemptions on short-term credit markets by reducing the likelihood of large fire sales of short-term securities into the market. Finally, it also may encourage large investors to diversify their money market fund holdings among a variety of funds, perhaps lessening the risk that any individual fund would be threatened by a few redemptions.[310] If proposed, we would expect to set a threshold for requiring in-kind redemptions sufficiently high that we could reasonably assume that such an investor would be in the position to assume ownership of such securities.

We request comment on requiring money market funds to satisfy redemption requests in excess of a certain size through in-kind redemptions. What would be the advantages and disadvantages of this approach? What type of threshold redemption request should trigger this requirement? Should there be a different threshold for third-party shareholders versus affiliated shareholders of a money market fund? Should there be other restrictions on affiliate redemptions (*e.g.*, prioritizing non-affiliate redemptions over affiliate redemption requests that are submitted on the same day)? How should the fund determine the value of the securities to be distributed as

[309] On September 19, 2008, the American Beacon Money Market Portfolio announced it would honor redemption requests exceeding $250,000 in a 90-day period through pro rata payments of cash and "in-kind" distributions of securities held by the fund, to prevent redemptions from "forcing" the sale of fund assets. *See* American Beacon Funds, Prospectus Supplement for BBH ComSet Class, Institutional Class, Cash Management Class, and PlanAhead Class (Sept. 30, 2008), *available at* http://www.sec.gov/Archives/edgar/data/809593/000080959308000045/sep3008_prosuppbeacon.txt.

[310] Large investors that did not wish to receive in-kind redemptions could avoid this risk by spreading their investments among several money market funds such that no single money market fund investment was large enough to possibly trigger the in-kind redemption requirement.

a result of such a redemption request? The securities' amortized cost value? The securities' fair value, as determined based on current market quotations or, if no such quotations are readily available, as determined in good faith by the fund's board of directors? Would these shareholders be able to assume ownership of such securities?

We note that a board of directors alternatively could cause a money market fund to impose a redemption fee under rule 22c-2 to impose some of the fund's costs from shareholders' liquidity needs on the redeeming shareholders.[311] What would be the advantages and disadvantages of this alternative approach to addressing our concerns regarding significant shareholder redemptions?

IV. Paperwork Reduction Act Analysis

Certain provisions of the proposed amendments to rules 2a-7 and 30b1-5 and proposed new rules 22e-3 and 30b1-6 and Form N-MFP under the Investment Company Act contain "collections of information" within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[312] The titles for the existing collections of information are: (1) "Rule 2a-7 under the Investment Company Act of 1940, Money market funds" (OMB Control No. 3235-0268); (2) "Rule 30b1-5 under the Investment Company Act of 1940, Quarterly filing of schedule of portfolio holdings of registered management investment companies" (OMB Control No. 3235-0577); and (3) "Form N-Q under the Investment Company Act of 1940, Quarterly Schedule of Portfolio Holdings of Registered Management Investment Company" (OMB Control No. 3235-0578). The titles for the new collections of information are: (1) "Rule 22e-3 under the Investment Company Act of 1940, Exemption for liquidation of money market funds;" (2) "Rule 30b1-6 under the Investment Company Act of 1940, Monthly report for money market funds;"

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311 The redemption fee cannot exceed two percent of the value of the shares redeemed.

312 44 U.S.C. 3501-3521.

and (3) "Form N-MFP under the Investment Company Act of 1940, Portfolio Holdings of Money Market Funds." The Commission is submitting these collections of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. Our proposed amendments and new rules are designed to make money market funds more resilient to risks in the short-term debt markets, and to provide greater protections for investors in a money market fund that is unable to maintain a stable net asset value per share. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

A. Rule 2a-7

Rule 2a-7 under the Investment Company Act exempts money market funds from the Act's valuation requirements, permitting money market funds to maintain stable share pricing, subject to certain risk-limiting conditions. As discussed above, we are proposing to amend rule 2a-7 in several respects. Our proposal would amend the rule by: revising portfolio quality and maturity requirements; introducing liquidity requirements; requiring money market fund boards to adopt procedures providing for periodic stress testing of the fund's portfolio; requiring funds to disclose monthly on their websites information on portfolio securities; and finally, requiring money market fund boards to determine, at least once each calendar year, that the fund has the capability to redeem and issue its securities at prices other than the fund's stable net asset value per share.[313] Three of the proposed amendments would create new collection of information requirements. The respondents to these collections of information would be money market funds or their advisers, as noted below.

[313] *See supra* Section II.A-G.

1. Stress Testing

The proposed amendments would require money market fund boards to adopt written procedures that provide for the periodic testing of the fund's ability to maintain a stable net asset value per share based on certain hypothetical events.[314] These procedures also would have to provide for a report of the testing results to be submitted to the board of directors at its next regularly scheduled meeting, and an assessment by the fund's adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably likely to occur within the following year.[315] Compliance with this proposed disclosure requirement would be mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. The information when provided to the Commission in connection with staff examinations or investigations would be kept confidential to the extent permitted by law.

We anticipate that stress testing would give fund advisers a better understanding of the effect of potential market events and shareholder redemptions on their funds' ability to maintain a stable net asset value, the fund's exposure to that risk, and actions the adviser may need to take to mitigate the possibility of the fund breaking the buck.

Commission staff believes that in light of the events of last fall most, if not all, money market funds currently conduct some stress testing of their portfolios as a matter of routine fund

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314 Proposed rule 2a-7(c)(8)(ii)(D). These events would include, but would not be limited to, a change in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on portfolio securities, and the widening or narrowing of spreads between yields on an appropriate benchmark the fund has selected for overnight interest rates and commercial paper and other types of securities held by the fund.

315 Proposed rule 2a-7(c)(8)(ii)(D)(2), (3). The report to the board would include the dates on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value calculated using available market quotations (or appropriate substitutes that reflect current market conditions) from its net asset value per share calculated using amortized cost to exceed ½ of 1 percent.

management and business practice.[316] These procedures likely vary depending on the fund's investments. For example, a prime money market fund that is offered to institutional investors may test for hypothetical events such as potential downgrades or defaults in portfolio securities while a U.S. Treasury money market fund may not. Some funds that currently conduct testing may be required to include additional hypothetical events under our proposed amendments. These funds likely provide regular reports of the test results to senior management. We expect, however, that most funds do not have written procedures documenting the stress testing, do not report the results of testing to their boards of directors, and do not provide an assessment from the fund's adviser regarding the fund's ability to withstand the hypothetical events reasonably likely to occur in the next year.

Commission staff believes that the stress testing procedures are or would be developed for all the money market funds in a fund complex by the fund adviser, and would address appropriate variations for individual money market funds within the complex. Staff estimates that it would take a fund adviser an average of 21 hours for a portfolio risk analyst initially to draft procedures documenting the complex's stress testing, and 3 hours for the board of directors to consider and adopt the written procedures. We estimate that 171 fund complexes with money market funds are subject to rule 2a-7. We therefore estimate that the total burden to draft these procedures initially would be 4104 hours.[317] Amortized over a three-year period, this would result in an average annual burden of 8 hours for an individual fund complex and a total of 1368

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316 The estimates of hour burdens and costs provided in the PRA and cost benefit analyses are based on staff discussions with representatives of money market funds and on the experience of Commission staff. We expect that the board of directors would be the same for all the money market funds in a complex, and thus could adopt the stress test procedures for all money market funds in the complex at the same meeting.

317 This estimate is based on the following calculation: (21 hours + 3 hours) x 171 fund complexes = 4104 hours.

hours for all fund complexes.[318] Staff estimates that a risk analyst also may spend an average of 6 hours per year revising the written procedures to reflect changes in the type or nature of hypothetical events appropriate to stress tests and the board would spend 1 hour to consider and adopt the revisions, for a total annual burden of 1197 hours.[319] Commission staff estimates further that it would take an average of 10 hours of portfolio management time to draft each report to the board of directors, 2 hours of an administrative assistant's time to compile and copy the report and 15 hours of the fund adviser's time to provide an assessment of the funds' ability to withstand reasonably likely hypothetical events in the coming year. The report must be provided at the next scheduled board meeting, and we estimate that the report would cover all money market funds in a complex. We also believe that the fund adviser would provide an assessment each time it provided a report. Finally, we assume that funds would conduct stress tests no less than monthly. With an average of 6 board meetings each year, we estimate that the annual burden would be 162 hours for an individual fund complex with a total annual burden for all fund complexes of 27,702 hours.[320]

The proposed amendment would require the fund to retain records of the reports on stress tests and the assessments for at least 6 years (the first two in an easily accessible place).[321] The retention of these records would be necessary to allow the staff during examinations of funds to determine whether a fund is in compliance with the stress test requirements. We estimate that

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318 These estimates are based on the following calculations: (21 + 3) ÷ 3 = 8 hours; 8 x 171 fund complexes = 1368 hours. PRA submissions for approval are made every three years. To estimate an annual burden for a collection of information that occurs one time, the total burden is amortized over the three year period.

319 This estimate is based on the following calculation: (6 hours (analyst) + 1 hour (board)) x 171 fund complexes = 1197 hours.

320 These estimates are based on the following calculations: (10 hours + 2 hours + 15 hours) x 6 meetings = 162 hours; 162 hours x 171 fund complexes = 27,702 hours.

321 Proposed rule 2a-7(c)(11)(vii).

the burden would be 10 minutes per fund complex per meeting to retain these records for a total annual burden of 171 hours for all fund complexes.[322]

Thus, we estimate that for the three years following adoption, the average annual burden resulting from the stress testing requirements would be 178 hours for each fund complex with a total of 30,438 hours for all fund complexes.[323]

We request comment on these estimates of hourly burdens. Would funds develop stress tests on a complex-wide basis for money market funds? Would the adviser prepare one report regarding stress tests for all the money market funds in a complex, or prepare a separate report for each money market fund?

2. *Public Website Posting*

The proposed amendments would require money market funds to post monthly portfolio information on their websites.[324] We believe that greater transparency of fund portfolios may allow investors to exert influence on risk-taking by fund advisers, and thus reduce the likelihood that a fund will break the buck. Information will be posted on a public website, and compliance with this requirement would be mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. We estimate that there are approximately 750 money market funds that would be affected by this proposal. We understand, based on interviews with industry representatives, that most money market funds already post portfolio information on their

322 This estimate is based on the following calculation: 0.1667 hours x 6 meetings x 171 fund complexes = 171 hours.

323 These estimates are based on the following calculations: 8 hours (draft procedures) + 7 hours (revise procedures) + 72 hours (6 reports) + 90 hours (assessments) + 1 hour (record retention) = 178 hours; 1368 hours (draft procedures) + 1197 hours (revise procedures) + 12,312 hours (6 reports) + 15,390 (6 assessments) + 171 hours (record retention) = 30,438 hours.

324 Proposed rule 2a-7(c)(12).

webpages at least quarterly.[325] To be conservative, the staff estimates that 20 percent of money market funds, or 150 funds, do not currently post this information at least quarterly, and therefore would need to develop a webpage to comply with the proposed rule. We estimate that a money market fund would spend approximately 24 hours of internal money market fund staff time initially to develop the webpage. We further estimate that a money market fund would spend approximately 4 hours of professional time to maintain and update the relevant webpage with the required information on a monthly basis. Based on an estimate of 750 money market funds posting their portfolio holdings on their webpages, including 150 funds incurring start-up costs to develop a webpage, we estimate that, in the aggregate, the proposed amendment would result in a total of 37,200 average burden hours for all money market funds for each of the first three years.[326]

3. *Reporting of Rule 17a-9 Transactions*

We are proposing to amend rule 2a-7 to require a money market fund to promptly notify the Commission by electronic mail of the purchase of a money market fund's portfolio security by an affiliated person in reliance on the rule and to explain the reasons for such purchase.[327] The proposed reporting requirement is designed to assist Commission staff in monitoring money market funds' affiliated transactions that otherwise would be prohibited. The new collection of

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325 Certain of the required information is currently maintained by money market funds for regulatory reasons, such as in connection with accounting, tax and disclosure requirements. We understand that the remaining information is retained by funds in the ordinary course of business. Accordingly, for the purposes of our analysis, we do not ascribe any time to producing the required information.

326 The estimate is based on the following calculations. The staff estimates that 150 funds would require a total of 3600 hours initially to develop a webpage (150 funds x 24 hours per fund = 3600 hours). In addition, each of the 750 funds would require 48 hours per year to update and maintain the webpage, for a total of 36,000 hours per year (4 hours per month x 12 months = 48 hours per year; 48 hours per year x 750 funds = 36,000). The average annual hour burden for each of the first three years would thus equal 37,200 hours ([3600 + (36,000 x 3)] ÷ 3).

327 *See* proposed rule 2a-7(c)(7)(iii).

information would be mandatory for money market funds that rely on rule 2a-7 and that rely on rule 17a-9 for an affiliated person to purchase a money market fund's portfolio security. Information submitted to the Commission related to a rule 17a-9 transaction would not be kept confidential.[328]

We estimate that fund complexes will provide one notice for all money market funds in a particular fund complex holding a distressed security purchased in a transaction under rule 17a-9. As noted above, Commission staff estimates that there are 171 fund complexes with money market funds subject to rule 2a-7. Of these fund complexes, Commission staff estimates that an average of 25 per year would be required to provide notice to the Commission of a rule 17a-9 transaction, with the total annual response per fund complex, on average, requiring 1 hour of an in-house attorney's time. Given these estimates, the total annual burden of this proposed amendment to rule 2a-7 for all money market funds would be approximately 25 hours.[329]

4. *Total burden*

The currently approved burden for rule 2a-7 is 1,348,000 hours. In a recent renewal submission to OMB, we estimated the collection of information burden for the rule is 310,983 hours. The additional burden hours associated with the proposed amendments to rule 2a-7 would increase the renewal estimate to 378,646 hours annually.[330]

B. Rule 22e-3

Proposed rule 22e-3 would permit a money market fund to suspend redemptions and

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328 Commission rules provide, however, for a procedure under which persons submitting notices under the proposed amendment would be able to request that the information not be disclosed under a Freedom of Information Act request. *See* 17 CFR 200.83.

329 The estimate is based on the following calculation: (25 fund complexes x 1 hour) = 25 hours.

330 This estimate is based on the following calculation: 310,983 (estimated in 2a-7 renewal submission) + 30,438 (stress testing) + 37,200 (website posting) + 25 hours (reporting 17a-9 transactions) = 378,646 hours.

postpone the payment of proceeds pending board-approved liquidation proceedings, provided that the fund notifies the Commission by electronic mail of its decision to do so.[331] The proposed rule is intended to reduce the vulnerability of investors to the harmful effects of a run on a fund, and minimize the potential for disruption to the securities markets. The proposed notification requirement is a collection of information under the PRA, and is designed to assist Commission staff in monitoring a money market fund's suspension of redemptions, which would otherwise be prohibited. Only money market funds that break the buck and begin board-approved liquidation proceedings would be able to rely on the rule. The respondents to this information collection therefore would be money market funds that break the buck and elect to rely on the exemption afforded by the rule. Compliance with the notification requirements of rule 22e-3 would be necessary for money market funds that seek to rely on rule 22e-3 to suspend redemptions and postpone payment of proceeds pending a liquidation, and would not be kept confidential.

We estimate that, on average, one money market fund would break the buck and liquidate every six years.[332] Staff estimates that a fund providing the required electronic mail notice under proposed rule 22e-3 would spend approximately 1 hour of an in-house attorney's time to prepare and submit the notice. Given these estimates, the total annual burden of proposed rule 22e-3 for all money market funds would be approximately 10 minutes.[333]

C. Monthly Reporting of Portfolio Holdings

1. Rule 30b1-6 and Form N-MFP

Proposed rule 30b1-6 would require money market funds to file an electronic monthly

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331 *See* proposed rule 22e-3(c).

332 As discussed above, since the adoption of rule 2a-7 in 1983, only two money market funds have broken the buck.

333 These estimates are based on the following calculations: (1 hour ÷ 6 years) = 10 minutes per year.

report on proposed Form N-MFP within two business days after the end of each month. The proposed rule is intended to improve transparency of information about money market funds' portfolio holdings and facilitate oversight of money market funds. The information required by the proposed form would be data-tagged in XML format and filed through EDGAR. The respondents to rule 30b1-6 would be investment companies that are regulated as money market funds under rule 2a-7. Compliance with proposed rule 30b1-6 would be mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. Responses to the disclosure requirements would not be kept confidential.

We estimate that 750 money market funds would be required by rule 30b1-6 to file, on a monthly basis, a complete Form N-MFP disclosing certain information regarding the fund and its portfolio holdings. For purposes of this PRA analysis, the burden associated with the requirements of proposed rule 30b1-6 has been included in the collection of information requirements of proposed Form N-MFP.

Based on our experience with other interactive data filings, we estimate that money market funds would require an average of approximately 40 burden hours to compile, tag and electronically file the required portfolio holdings information for the first time and an average of approximately 8 burden hours in subsequent filings.[334] Based on these estimates, we estimate the average annual burden over a three-year period would be 107 hours per money market fund.[335] Based on an estimate of 750 money market funds submitting Form N-MFP in interactive data

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334 We understand that the required information is currently maintained by money market funds pursuant to other regulatory requirements or in the ordinary course of business. Accordingly, for the purposes of our analysis, we do not ascribe any time to producing the required information.

335 The staff estimates that a fund would make 36 filings in three years. The first filing would require 40 hours and subsequent filings would require 8 hours each, for an average annual burden of 107 hours (1 filing x 40 hours = 40 hours; 35 filings x 8 hours = 280 hours; 40 hours + 280 hours = 320 hours; 320 hours ÷ 3 years = 107 hours). Thereafter, filers generally would not incur the start-up burdens applicable to the first filing.

format, each incurring 107 hours per year on average, we estimate that, in the aggregate, Form N-MFP would result in 80,250 burden hours, on average, for all money market funds for each of the first three years.

2. *Rule 30b1-5 and Form N-Q*

Our proposed amendments to rule 30b1-5 would exempt money market funds from the requirement to file a schedule of investments pursuant to Item 1 of Form N-Q. The proposed amendment is intended to eliminate unnecessarily duplicative disclosure requirements. The proposed amendment would only affect investment companies that are regulated as money market funds under rule 2a-7.

We estimate that 750 money market funds would be affected by the proposed amendment to rule 30b1-5. For the purposes of this PRA analysis, the decrease in burden hours resulting from the proposed amendment is reflected in the collection of information requirements for Form N-Q.

We estimate that money market funds would require an average of approximately 4 hours to prepare the schedule of investments required pursuant to Item 1 of Form N-Q. Based on these estimates, we estimate that the average annual burden avoided would be 8 hours per fund.[336] Based on an estimate of 750 money market funds filing Form N-Q, each incurring 8 burden hours per year on average, we estimate that, in the aggregate, our proposed exemption would result in a decrease of 6000 burden hours associated with Form N-Q.[337]

D. Request for Comments

We request comment on whether these estimates are reasonable. Pursuant to 44 U.S.C.

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336 Funds are required to file a quarterly report on Form N-Q after the close of the first and third quarters of each fiscal year.

337 The estimate is based on the following calculation: 750 money market funds x 8 hours per money market fund = 6000 hours.

3506(c)(2)(B), the Commission solicits comments in order to: (i) evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) determine whether there are ways to minimize the burden of the collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons wishing to submit comments on the collection of information requirements of the proposed amendments should direct them to the Office of Management and Budget, Attention Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Room 10102, New Executive Office Building, Washington, DC 20503, and should send a copy to Elizabeth Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090, with reference to File No. S7-11-09. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this Release; therefore a comment to OMB is best assured of having its full effect if OMB receives it within 30 days after publication of this Release. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-11-09, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, 100 F Street, NE, Washington, DC 20549-0213.

V. Cost Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules. We have identified certain costs and benefits of the proposed amendments and new rules, and we request comment on all aspects of this cost benefit analysis, including identification and assessment of any costs and benefits not discussed in this analysis. We seek comment and data on the value of the benefits identified. We also welcome comments on the accuracy of the cost estimates in each section of this analysis, and request that commenters provide data that may be relevant to these cost estimates. In addition, we seek estimates and views regarding these costs and benefits for particular covered institutions, including small institutions, as well as any other costs or benefits that may result from the adoption of these proposed amendments and new rules.

A. Rule 2a-7

1. Second Tier Securities, Portfolio Maturity and Liquidity Requirements

We are proposing several changes to the risk-limiting conditions of rule 2a-7. While we believe that these changes would impart substantial benefits to money market funds, we recognize that they also may impose certain costs.

First, we would limit money market fund investments to first tier securities, *i.e.*, securities receiving the highest short-term debt ratings from the requisite NRSROs or securities that the fund's board of directors or its delegate determines are of comparable quality.[338] We also are proposing to limit money market funds to acquiring long-term securities that have received long-term ratings in the highest two ratings categories.[339]

Second, we are proposing certain changes to rule 2a-7's portfolio maturity limits. We are proposing to reduce the maximum weighted average maturity of a money market fund permitted by rule 2a-7 from 90 days to 60 days.[340] We also are proposing a new maturity limitation based on the "weighted average life" of fund securities that would limit the portion of a fund's portfolio

338 *See* proposed rule 2a-7(a)(11)(iii); proposed rule 2a-7(a)(11)(iv); proposed rule 2a-7(c)(3).

339 *See* proposed rule 2a-7(a)(11)(iv)(A).

340 *See* proposed rule 2a-7(c)(2)(ii).

that could be held in longer term floating- or variable-rate securities. This restriction would require a fund to calculate the weighted average maturity of its portfolio without regard to interest rate reset dates. The weighted average life of a fund's portfolio would be limited to 120 days.[341] Finally, we are proposing to delete a provision in rule 2a-7 that permits money market funds not relying on the amortized cost method of valuation to acquire Government securities with a remaining maturity of up to 762 calendar days. Under the amended rule, money market funds could not acquire any security with a remaining maturity of more than 397 days, subject to the maturity shortening provisions for floating- and variable-rate securities and securities with a Demand Feature.[342]

Third, we are proposing new liquidity requirements on money market funds. Under the proposed amendments, money market funds would be prohibited from acquiring securities unless, at the time acquired, they are liquid, *i.e.*, securities that can be sold or disposed of in the ordinary course of business within seven days at approximately the value ascribed to it by the money market fund.[343] We also propose to limit taxable retail money market funds and taxable institutional money market funds to acquiring Daily Liquid Assets unless five percent of a retail fund's and 10 percent of an institutional fund's assets are Daily Liquid Assets.[344]

In addition, our proposed amendments to rule 2a-7 would impose weekly liquidity requirements on money market funds. Specifically, retail and institutional money market funds would not be permitted to acquire any securities other than weekly liquid assets if, after the acquisition, (i) the retail fund would hold less than 15 percent of its total assets in weekly liquid

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341 *See* proposed rule 2a-7(c)(2)(iii).

342 *See* proposed rule 2a-7(c)(2)(i); rule 2a-7(d)(1)-(5).

343 *See* proposed rule 2a-7(c)(5)(i).

344 *See* proposed rule 2a-7(c)(5)(iii). This restriction would not apply to tax exempt money market funds.

assets and (ii) the institutional fund would hold less than 30 percent of its total assets in weekly liquid assets.[345] Finally, we are proposing to require that a money market fund at all times hold daily and weekly liquid assets sufficient to meet reasonably foreseeable redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders.[346]

Our proposed amendments would rely on a money market fund's board of directors to determine, no less frequently than once each calendar year, whether the money market fund is intended to be offered to institutional investors or has the characteristics of a fund that is intended to be offered to institutional investors, based on the: (i) nature of the record owners of fund shares; (ii) minimum amount required to be invested to establish an account; and (iii) historical cash flows resulting, or expected cash flows that would result, from purchases and redemptions.[347]

a. *Benefits*

We believe that the proposed amendments to rule 2a-7's risk-limiting conditions would be likely to produce broad benefits for money market fund investors. First, they should reduce money market funds' exposure to certain credit, interest rate, and spread risks. For example, precluding money market funds from investing in second tier securities would decrease money market funds' exposure to credit risk. Reducing the maximum weighted average maturity of money market funds' portfolios would further decrease their interest rate sensitivity, as well as reduce their exposure to credit risk. Introducing the weighted average life limitation on money market funds' portfolios would limit credit spread risk and interest rate spread risk to funds from

345 *See* proposed rule 2a-7(c)(5)(iv).

346 *See* proposed rule 2a-7(c)(5)(ii).

347 *See* proposed rule 2a-7(a)(18) (defining "Institutional Fund").

longer term floating- or variable-rate securities.

We expect that the proposed amendments also would bolster the ability of money market funds to maintain a stable net asset value during times when the level of shareholder redemption demand is high. Fund portfolios with a lower weighted average maturity that include a limited amount of longer term floating- or variable-rate securities would turn over more quickly and the fund would be better able to increase its holdings of highly liquid securities in the face of illiquid markets than funds that satisfy current maturity requirements. The proposed liquidity requirements are designed to increase a money market fund's ability to withstand illiquid markets by ensuring that the fund acquires only liquid securities and that a certain percent of its assets are held in daily and weekly liquid assets. These requirements also should decrease the likelihood that a fund would have to realize losses from selling portfolio securities into an illiquid market to satisfy redemption requests. Because the proposed amendments would require a fund to have a contractual right to receive cash for the daily and weekly liquid assets, rather than the current standard, which assumes that a fund would be able to find a buyer for its securities within seven days, we believe that the proposed required liquidity requirements would allow money market fund advisers to more easily adjust the funds' portfolios to increase liquidity when needed.

We believe that a reduction of these credit, interest rate, spread, and liquidity risks would better enable money market funds to weather market turbulence and maintain a stable net asset value per share. The proposed amendments are designed to reduce the risk that a money market fund will break the buck and therefore prevent losses to fund investors. To the extent that money market funds are more stable, they also would reduce systemic risk to the capital markets and provide a more stable source of financing for issuers of short-term credit instruments, thus promoting capital formation. If money market funds become more stable investments as a result of the proposed rule amendments, they may attract further investment, increasing their role as a source of capital formation.

b. Costs

We recognize that there are potential costs that would result if we adopted our proposed changes regarding second tier securities, portfolio maturity, and liquidity. Second tier securities, less liquid securities, and longer term credit instruments typically pay a higher interest rate and, therefore, the proposed amendments may decrease money market funds' yields.

Precluding ownership of second tier securities also may deprive money market funds of some benefits of reduced risk through diversification. We invite comment on whether the benefits of reducing credit risk through precluding purchases of second tier securities justifies the costs of the lost diversification benefits that second tier securities may provide.

If, as a result of the proposed amendments, there is a smaller set of Eligible Securities for a money market fund to choose from, that may increase the cost of those securities if their supply is limited. In particular, to the extent that the proposed liquidity requirements increase demand for highly liquid securities that is not countered by increased supply, the cost of those securities may rise as well. Increased costs of portfolio securities will have a negative impact on money market fund yield. Finally, to the extent that actual investor redemptions are significantly lower than our proposed liquidity requirements, money market funds may achieve lower yields as a result of complying with these liquidity requirements.

Although the impact on individual funds would vary significantly, we estimate that the proposed changes to rule 2a-7's requirements regarding portfolio quality, portfolio maturity, and liquidity would decrease the yield that a money market fund is able to achieve in the range of 2 to 4 basis points. We understand that the majority of money market funds are already in compliance with these proposed requirements due either to their own risk-limiting actions or to their voluntary compliance with the recommendations contained in the ICI Report. Accordingly, we expect that the decrease in yield from these changes to rule 2a-7's risk-limiting conditions would have a relatively minor impact on current money market fund yields.

However, this decreased yield may limit the range of choices that individual money market fund investors currently have to select their desired level of investment risk. This might cause some investors to shift their assets to, among other places, offshore or other enhanced cash funds unregulated by rule 2a-7 that are able to offer a higher yield. Alternatively, some investors may choose to shift their assets to bank deposits. When markets come under stress, investors may be more likely to withdraw their money from these offshore or private funds due to their perceived higher risk[348] and substantial redemptions from those funds and accompanying sales of their portfolio securities could increase systemic risk to short-term credit markets, which would impact money market funds. In addition, the proposed stricter portfolio quality, maturity, and liquidity requirements may result in some money market funds having fewer issuers from which to select securities if some issuers only offer second tier securities, less liquid securities or a larger percentage of longer term securities.

Our proposed portfolio quality, maturity, and liquidity restrictions also may impact issuers. Issuers may experience increased financing costs to the extent that they are unable to find alternative purchasers of their second tier securities, less liquid securities, longer term securities, or floating- and variable-rate securities at previous market rates. As noted earlier in the release, we do not believe that money market funds currently hold a significant amount of

348 During the recent financial crisis, investors redeemed substantial amounts of assets from ultra-short bond funds and certain offshore money market funds. *See* ICI REPORT, *supra* note 6, at 106-07.

second tier securities, or securities that are illiquid at acquisition.[349] Thus, we expect that the proposed amendment's impact on issuers of these securities would be minimal. If the proposed amendments result in companies or governments issuing shorter maturity securities, those issuers may be exposed to an increased risk of insufficient demand for their securities and adverse credit market conditions because they must roll over their short-term financing more frequently. We note that this impact could be mitigated if money market funds sufficiently staggered or "laddered" the maturity of the securities in their portfolios. The markets for longer term or floating- and variable-rate securities may become less liquid if the proposed rule amendments cause issuance of these instruments to decline. We generally expect that issuers of floating- or variable-rate securities would respond to the proposed amendments by issuing a greater proportion of their securities with shorter final maturities.

Our proposed requirement that fund boards distinguish between retail and institutional money market funds would require boards to make a determination based on an understanding of the investors in the fund and their behavior. Our proposed liquidity requirements also would require money market funds to "know their customers," including their expected redemption behavior. We expect that most money market funds already have methods to understand their customers and their redemption needs because "knowing your customer" is already a best practice. As a result, we also do not expect that these requirements would impose any material costs on funds.

We do not believe that eliminating the provision in rule 2a-7 that allowed money market funds relying solely on the penny-rounding method of pricing to hold Government securities with remaining maturities of up to 762 days would have a material impact on money market

349 *See supra* note 101 and accompanying and following text, and Section II.C.1.

funds, investors, or issuers of longer term Government securities because we believe that substantially all money market funds rely on the amortized cost method of valuation, and not exclusively on the penny-rounding method of pricing, and thus are not eligible to rely on this exception.

We request comment on these costs and benefits. Would money market fund investors benefit from the proposed portfolio quality, maturity and liquidity requirements? Would money market funds experience a significant yield and diversification impact from the proposed changes to rule 2a-7's second tier security, portfolio maturity, and liquidity requirements? We note that the highest rated money market funds currently must have a weighted average maturity of 60 days or less, the average weighted average maturity for taxable money market funds as of June 16, 2009 was 53 days, and very few money market funds hold second tier securities.[350] What other impacts would these changes have on money market funds? What effect would such changes have on the short-term credit market and issuers of longer term or debt instruments held to satisfy the daily or weekly liquidity requirements? How would the proposed amendments impact issuers of, and the market for, longer term variable- or floating-rate debt securities? We encourage commenters to provide empirical data to support their analysis.

2. Use of NRSROs

As discussed above, we are considering an approach that would require a money market fund's board of directors to designate NRSROs whose credit ratings the fund would use in determining the eligibility of portfolio securities under rule 2a-7 and that the board would annually determine issue credit ratings that are sufficiently reliable for that use. As we also

[350] *See supra* text accompanying note 101, note 145 and accompanying text, and note 147.

noted above, we proposed eliminating references to NRSROs in rule 2a-7 last year.[351] For a discussion of the costs and benefits of that proposal, please see Section VI of the NRSRO References Release.[352] Are there additional factors we should consider since that release was published?

We request comment on the approach we are considering. We specifically request comment regarding the standard we are considering for the board's annual determination, *i.e.*, that the designated NRSROs issue ratings that are sufficiently reliable for use in determining the eligibility of portfolio securities. Is this standard appropriate, and if not, what would be a more appropriate standard? We expect that in making their initial designation and their annual determination, fund boards would review a presentation by the fund's adviser regarding the relative strength of relevant NRSROs' ratings and ratings criteria. What kind of guidance, if any, should the Commission provide with respect to such a standard?

According to the ICI Report, a requirement that funds designate three or more NRSROs to use in determining the eligibility of portfolio securities could encourage competition among NRSROs to achieve designation by money market funds.[353] We anticipate that the approach we are considering, which would require fund boards annually to determine that the designated NRSROs issue credit ratings sufficiently reliable to use in determining the eligibility of portfolio securities, may promote competition among NRSROs to produce the most reliable ratings in order to obtain designation by money market funds. In addition to the potential for competition among existing NRSROs, the proposed amendment might encourage new NRSROs that issue ratings specifically for money market fund instruments to enter the market. As we noted above,

351 *See* NRSRO References Proposal, *supra* note 105.

352 *See id.*

353 *See* ICI REPORT, *supra* note 6, at 82.

however, the staff believes it is reasonable to assume that the three NRSROs that issued almost 99 percent of all outstanding ratings across all categories that were issued by the 10 registered NRSROs as of June 2008, also issued well over 90 percent of all outstanding ratings of short term debt.[354] If fund boards were required to designate a minimum of three NRSROs and all money market fund boards chose to designate these three NRSROs, the requirement could result in decreased competition among NRSROs. We request comment on the impact that the approach we are considering, particularly the minimum number of NRSROs, might have on competition among NRSROs. We also request comment on the impact, if any, of this approach with respect to the efficiency of fund managers. Finally, we request comment on any potential benefits this approach might have with respect to money market funds or NRSROs.

We recognize that there could be costs associated with the approach we are considering. Staff estimates that the costs of this approach would include: initial costs for the board to designate NRSROs, as well as an annual cost to determine that designated NRSROs continue to issue ratings that are sufficiently reliable for use in determining the eligibility of portfolio securities. We expect that fund advisers currently evaluate the strength of NRSRO ratings and ratings criteria as part of the analysis they perform (under delegated authority from the board) in determining the eligibility of portfolio securities, and that this evaluation includes consideration of whether an NRSRO's rating is sufficient for that use. Accordingly, we anticipate that fund advisers would not incur additional time to perform an evaluation that would be the basis for their recommendations to the board when it makes its initial designation and annual determination, but the adviser would incur costs to draft those recommendations in a presentation or report for board review.

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[354] *See supra* note 116 and accompanying text.

Under the current rule, if a money market fund invests in unrated or second tier securities, the adviser must monitor all NRSROs in case an unrated or second tier security has received a rating from *any* NRSRO below the second highest short-term rating category.[355] Because fund advisers currently monitor NRSROs, we do not expect that limiting the number of NRSROs that a fund would have to monitor to a number designated by the fund board would result in increased costs to fund advisers to monitor NRSROs.

We request comment on our analysis of the potential costs and benefits of a requirement to designate NRSROs. Do funds currently evaluate NRSRO ratings for reliability? Would there be benefits to funds and their advisers if the board designates three or more NRSROs? Would fund advisers benefit from having fewer NRSROs to monitor? Would fund advisers incur significant costs to make presentations to the board recommending which NRSROs to designate? What would be involved, including specific costs, for fund management to evaluate whether an NRSRO "issues credit ratings that are sufficiently reliable" for the fund's determination of whether a security is an eligible security? Would funds incur costs if we required them to disclose designated NRSROs in the statement of additional information?

We do not anticipate that the designation of NRSROs would have an adverse impact on capital formation. We request comment on whether requiring fund boards to designate NRSROs would have an impact on capital formation.

3. *Stress Testing*

We are proposing to require that money market fund boards of directors adopt written procedures that provide for the periodic stress testing of each money market fund's portfolio.[356] The procedures would require testing of the fund's ability to maintain a stable net asset value per

[355] *See* rule 2a-7(c)(6)(i)(A)(2).

[356] Proposed rule 2a-7(c)(8)(ii)(D).

share based upon certain hypothetical events.[357] The procedures also would have to provide for a report to be delivered to the fund's board of directors at its next regularly scheduled meeting on the results of the testing and an assessment by the fund's adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably likely to occur within the following year.[358]

We anticipate that stress testing would give fund advisers a better understanding of the effect of potential market events and shareholder redemptions on their funds' ability to maintain a stable net asset value, the fund's exposure to the risk that it would break the buck, and actions the adviser may need to take to mitigate the possibility of the fund breaking the buck. We believe that many funds currently conduct stress testing as a matter of routine fund management and business practice. We anticipate, however, that funds that do not currently perform stress testing and funds that may revise their procedures in light of the proposed rule amendments would give their managers a tool to better manage those risks. For fund boards of directors that do not currently receive stress test results, we believe that the regular reports and assessments would provide money market fund boards a better understanding of the risks to which the fund is exposed.

We understand that today rigorous stress testing is a best practice followed by many

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[357] The proposed provision includes as hypothetical events a change in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on a portfolio security, and widening or narrowing of spreads between yields on a benchmark selected by the fund and securities held by the fund. *See* proposed rule 2a-7(c)(8)(ii)(D)(*1*).

[358] Proposed rule 2a-7(c)(8)(ii)(D)(*2*), (*3*). The report must include dates on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value calculated using available market quotations (or appropriate substitutes that reflect current market conditions) from its net asset value per share, calculated using amortized cost, to exceed ½ of 1%.

money market funds.[359] We understand that the fund complexes that conduct stress tests include smaller complexes that offer money market funds externally managed by advisers experienced in this area of management.[360] Accordingly, staff estimates that as a result of the proposed amendments to adopt stress testing procedures, (i) funds that currently conduct rigorous stress testing, including tests for hypothetical events listed in the proposed amendment (and concurrent occurrences of those events) would incur some cost to evaluate whether their current test procedures would comply with the proposed rule amendment, but would be likely to incur relatively few costs to revise those procedures or continue the stress testing they currently perform, (ii) funds that conduct less rigorous stress testing, or that do not test for all the hypothetical events listed in the proposed rule amendment, would incur somewhat greater expenses to revise those procedures in light of the proposed amendments and maintain the revised testing, and (iii) funds that do not conduct stress testing would incur costs to develop and adopt stress test procedures and conduct stress tests. As noted above, we believe that there is a range in the extent and rigor of stress testing currently performed by money market funds. We also expect that stress test procedures are or would be developed by the adviser to a fund complex for all money market funds in the complex while specific stress tests are performed for each individual money market fund. We estimate that a fund complex that currently does not conduct stress testing would require approximately 1 month for 2 risk management analysts and 2 systems analysts to develop stress test procedures at a cost of approximately $155,000, 21

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359 As noted above, the ratings agencies stress test the portfolios of money market funds they rate. In addition, the Irish Financial Services Authority requires stress testing of money market funds domiciled in Ireland, and the Institutional Money Market Funds Association provides guidance for its members in stress testing money market fund portfolios. *See supra* notes 214-215 and accompanying text.

360 These complexes do not, however, meet the definition of "small entities" under the Investment Company Act for purposes of the Regulatory Flexibility Act of 1980. 5 U.S.C. 603(a). *See infra* note 417.

hours for a risk management analyst to draft the procedures, and 3 hours of board of directors' time to adopt the procedures for a total of approximately $173,000.[361] Costs for fund complexes that would have to revise or fine-tune their stress test procedures would be less. For purposes of this cost benefit analysis, we estimate that these funds would incur half the costs of development, for a total of approximately $95,000.[362] Funds that would not have to change their test procedures would incur approximately $20,000 to determine compliance with the proposed amendment, and to draft and adopt the procedures.[363] We also would anticipate that if there is a demand to develop stress testing procedures, third parties may develop programs that funds could purchase for less than our estimated cost to develop the programs themselves.

As with the development of stress test procedures, the costs funds would incur each year as a result of the proposed amendments to update test procedures, conduct stress tests and provide reports on the tests and assessments to the board of directors would vary. Funds that currently conduct stress tests already incur costs to perform the tests. In addition, some of those funds may currently provide reports to senior management (if not the board) of their test results. We assume, however, that few, if any, fund advisers provide a regular assessment to the board of the fund's ability to withstand the events reasonably likely to occur in the following year. For that reason, we estimate that all fund complexes would incur costs of $3000 to provide a written report on the test results to the board, $4000 to provide an assessment to the board and $10 to retain records of the reports and assessments for a total annual cost to a fund complex of

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361 This estimate is based on the following calculations: $275/hour x 280 hours (2 senior risk management specialists) + ($244/hour x 320 hours (2 senior systems analysts) = $155,080; $275/hour (1 senior risk management specialist) x 21 hours = $5775; $4000/hour x 3 hours = $12,000; $155,080 + $5775 + $12,000 = $172,855.

362 This estimate is based on the following calculation: (155,080 x 0.5) (revise procedures) + $5775 (draft procedures) + $12,000 (board approval) = $93,315.

363 This estimate is based on the following calculation: $275/hour (senior risk management specialist) x 8 hours = $2200; $2200 + $5775 + $12,000 = $19,975.

approximately $42,000.[364] We estimate that a portion of funds would incur additional costs each year to perform stress tests and update their procedures each year, up to a maximum of approximately $113,000.[365]

For purposes of this cost benefit analysis, Commission staff has estimated that 25 percent of fund complexes (or 43 complexes) would have to develop stress test procedures, 50 percent (or 85) would have stress test procedures, but have to revise those procedures, and 25 percent of complexes (or 43 complexes) would review the procedures without having to change them. Based on these estimates, staff further estimates that the total one time costs for fund complexes to develop or refine existing stress test procedures would be approximately $19 million.[366] In addition, staff estimates that the annual costs to all funds to conduct stress tests, update test procedures, provide reports and assessments to fund boards and retain records of the reports and assessments would be approximately $17 million.[367]

We request comment on our estimates. We are particularly interested in comments regarding how many funds currently conduct stress testing, the extent and nature of that testing, including whether the procedures can be adopted on a complex wide basis, and the costs to develop rigorous stress testing procedures. For those money market funds that have stress test

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364 This estimate is based on the following calculation: *Report:* $275/hour x 10 hours (senior risk management specialist) + $62 x 2 hours (administrative assistant) = $2874; *Assessment:* $275/hour x 15 hours (senior risk management specialist) = $4125; *Record retention:* $62/hour x 0.1667 hours (administrative assistant) = $10.33; ($2874 + $4125 +$10) x 6 (board meetings per year) = $42,054.

365 This estimate is based on the following calculations: *Tests:* $275/hour x 15 hours (senior risk management specialist) + $244/hour x 20 hours (senior systems analyst) = $9,005; $9,005 x 12 (monthly testing) = $108,060; *Update procedures:* $275/hour x 5 hours (senior risk management specialist) + $4000/hour x 1 hour = $5375; $108,060 + $5375 = $113,435.

366 This estimate is based on the following calculation: (43 x $173,000) + (85 x $95,000) + (43 x $20,000) + (171 x $5775) + (171 x $12,000) = $19,413,525.

367 This estimate is based on the following calculation: (43 x $113,000) + (85 x $113,000 x 0.5) + (171 x $42,054 (reports and assessments)) = $16,852,734.

procedures, how significantly would they have to change those procedures in light of the proposed rule amendment? What costs would they incur, including specific costs for personnel that would be involved in changes?

4. Repurchase Agreements

We are proposing to modify the conditions under which a money market fund may treat the acquisition of a repurchase agreement collateralized fully to be an acquisition of the repurchase agreement's collateral for purposes of rule 2a-7's diversification requirement.[368] Money market funds would be able to adopt this "look-through" treatment only with respect to repurchase agreements collateralized by cash items or Government securities[369] and as to which the board of directors or its delegate has evaluated the creditworthiness of the counterparty.[370]

We believe that the proposed changes would limit money market funds' exposure to credit risk. Collateral other than cash items and Government securities might not adequately protect money market funds because the funds may be unable to liquidate the collateral without incurring a loss if the counterparty defaults. The creditworthiness evaluation, moreover, would make it less likely that a money market fund enters into repurchase agreements with counterparties that will default and be exposed to risks related to the collateral. As discussed above, we believe that the reduction of credit risk would better enable money market funds to weather market turbulence and maintain a stable net asset value per share.

We recognize that these proposed changes could result in costs to money market funds.

368 *See* rule 2a-7(c)(4)(ii)(A). The rule 5b-3(c)(1) definition of collateralized fully, which is cross-referenced by rule 2a-7(a)(5), sets forth the related conditions. Under the current definition, a money market fund may look through repurchase agreements collateralized with cash items, Government securities, securities with the highest rating or unrated securities of comparable credit quality.

369 Proposed rule 2a-7(a)(5).

370 Proposed rule 2a-7(c)(4)(ii)(A).

The limitation on money market funds' ability to invest in repurchase agreements collateralized with securities other than cash items and Government securities may result in lower yields for money market funds to the extent that other investment opportunities do not provide the same returns as those agreements. The limitation also could lead to an increase in the counterparties' short-term financing costs. Counterparties may have to substitute such repurchase agreements with other sources of financing linked to the same type of collateral. If counterparties limited their own investments in securities that are no longer permissible collateral, the issuers of such securities could also be indirectly affected by our proposed change. The restrictions on repurchase agreements held by money market funds might potentially affect the functioning of these important markets. We invite comment on what effects, if any, these restrictions might have on the markets for repurchase agreements.

The creditworthiness evaluation would also impose additional costs. A credit risk evaluation, however, is required with respect to other portfolio securities and to repurchase agreements for which money market funds do not adopt a look-through treatment.[371] We understand, moreover, that many money market fund complexes already perform a creditworthiness evaluation for all repurchase agreement counterparties. Accordingly, we believe that the additional cost imposed on money market funds, if any, would be minimal.

We request comment on any potential costs and benefits. Would the proposed amendments significantly reduce the risk that money market funds incur losses upon the default of their repurchase agreement counterparties? What effect would the limitation on permissible collateral have on counterparties' ability to obtain short-term financing? How would the proposed change impact issuers of securities that would no longer be permissible collateral?

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371 *See* rule 2a-7(c)(3)(i).

Would the required creditworthiness evaluation impose any material cost on money market funds? We encourage commenters to provide empirical data to support their analysis.

5. Public Website Posting

The proposed amendments to rule 2a-7 would require money market funds to post monthly portfolio information on their websites.[372] The rule is intended to provide shareholders with timely information about the securities held by the money market fund.

We anticipate that the proposal to require funds to post monthly portfolio information on their websites would benefit investors by providing them a better understanding of their own risk exposure and thus enabling them to make better informed investment decisions. The proposed rule may thus instill more discipline into portfolio management and reduce the likelihood of a money market fund breaking the buck. Finally, any increased costs to money market funds from monthly reporting may be offset to a degree by the proposal to exclude them from current requirements to file quarterly portfolio holdings information on Form N-Q. For the purposes of the PRA analysis, we estimate that money market funds would realize, in the aggregate, a decrease of 6000 burden hours, or $470,880, from this exclusion.[373]

The proposed website posting requirement would also impose certain costs on funds. We estimate that, for the purposes of the PRA, money market funds would be required to spend 24 hours of internal money market fund staff time initially to develop a webpage, at a cost of $4944 per fund.[374] We also estimate that all money market funds would be required to spend 4 hours of professional time to maintain and update the webpage each month, at a total annual cost of

[372] Proposed rule 2a-7(c)(12).

[373] This estimate is based on our experience with other filings and an estimated hourly wage rate of $78.48 (6000 hours x $78.48 = $470,880).

[374] The staff estimates that a webmaster at a money market fund would require 24 hours (at $206 per hour) to develop and review the webpage (24 hours x $206 = $4944).

$9888 per fund.[375] We believe, however, that our estimates may overstate the actual costs that would be incurred to comply with the website posting requirement because many funds currently post their portfolio holdings on a monthly, or more frequent, basis.[376] For purposes of this cost benefit analysis, Commission staff estimates that 20 percent of money market portfolios (150 portfolios) do not currently post portfolio holdings information on their websites. Based on these estimates, we estimate that the total initial costs for the proposed website disclosure would be $741,600.[377] In addition, we estimate that the annual costs for all money market funds to maintain and update their webpages would be $7.4 million.[378]

In addition, monthly website disclosure may impose other costs on funds and their shareholders. For example, more frequent disclosure of portfolio holdings may arguably expand the opportunities for professional traders to exploit this information by engaging in predatory trading practices, such as front-running. However, given the short-term nature of money market fund investments and the restricted universe of eligible portfolio securities, we believe that the risk of trading ahead is severely curtailed in the context of money market funds.[379] For similar reasons, we believe that the potential for "free riding" on a money market fund's investment strategies, *i.e.*, obtaining for free the benefits of fund research and investment strategies, is minimal. Given that shares of money market funds are ordinarily purchased and redeemed at the stable price per share, we believe that there would be relatively few opportunities for profitable arbitrage. Thus, we estimate that the costs of predatory trading practices under this proposal

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375 The staff estimates that a webmaster would require 4 hours (at $206 per hour) to maintain and update the relevant webpages on a monthly basis (4 hours x $206 x 12 months = $9888).

376 *See supra* note 325 and accompanying text.

377 This calculation is based on the following estimate: ($4944 x 150 portfolios) = $741,600.

378 This calculation is based on the following estimate: ($9888 x 750 portfolios) = $7,416,000.

379 *See* ICI REPORT, *supra* note 6, at 93.

would be minimal. We request comment on the analysis above, and on any other potential costs and benefits of the proposed website disclosure requirement.

6. Processing of Transactions

Our proposal would require that a money market fund's board determine in good faith, on an annual basis, that the fund (or its transfer agent) has the capacity to redeem and sell securities at prices that do not correspond to the fund's stable net asset value per share.[380] As discussed above, the aftermath of 2008 market events revealed that some funds had not implemented systems to calculate redemptions at prices other than the funds' stable net asset value per share.[381] Because of this failure, transactions were processed manually, which extended the time that investors had to wait for the proceeds from their redeemed shares.

As noted in Section II.G above, money market funds may be required to process transactions at a price other than the fund's stable share price and pay the proceeds of redemptions within seven days (or a shorter time that the fund has represented). We believe that funds that do not have the operational capacity to price shares at other than the stable share price risk being unable to meet their obligations under the Act. We expect that the proposed amendments would help eliminate the risk that money market funds would not be able to meet these obligations in the event the fund breaks a buck. Shareholders would benefit from the proposed amendments because they would be more likely to receive the proceeds from their investments in the event of a liquidation.

Because funds are obligated to redeem at other than stable net asset value per share, there should be no new cost associated with the requirement for the funds (or their transfer agents) to have the systems that can meet these requirements. To the extent that funds and transfer agents

380 Proposed rule 2a-7(c)(1).

381 *See supra* note 262 and accompanying text.

have to change their systems, however, these changes will likely entail costs. If a fund complex were to require one month of a senior systems analyst's time in assuring that the required systems are in place, the total cost for the fund complex would be $39,040.[382] Based on this estimate we estimate that, if one-third of the fund complexes are not currently able to redeem at prices other than stable net asset value, the total cost to all money market funds would be $2,225,280.[383] We also anticipate that the board's determination would result in costs. We anticipate that the board's determination would be based on a review at a regularly scheduled board meeting of the fund adviser's or the transfer agent's certification that the operational systems have the requisite capacity. Commission staff estimates that this review would take about 15 minutes of board time at a cost of $1000.[384] Based on this estimate we estimate that the total cost to all money market funds of board determinations would be $171,000.[385] We request comment on the analysis above, and on any other potential costs and benefits of this proposed rule amendment.

B. Rule 17a-9

The Commission is proposing to amend rule 17a-9 to expand the circumstances under which affiliated persons can purchase money market fund portfolio securities. Under the proposed amendment, a money market fund could sell a portfolio security that has defaulted (other than an immaterial default unrelated to the financial condition of the issuer) to an affiliated person for the greater of the security's amortized cost value or market value (plus accrued and

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382 This estimate is based on the following calculation: $244/hour x 160 hours (senior systems analyst) = $39,040.

383 This is based on the following calculation: (171 (fund complexes) ÷ 3) x $39,040 = $2,225,280.

384 This is based on the following calculation: $4000/hour (board time) x 0.25 hours = $1000.

385 This is based on the following calculation: $1000 x 171 (fund complexes) = $171,000.

unpaid interest), even though the security continued to be an eligible security.[386]

The proposed amendment essentially would codify past Commission staff no-action letters[387] and should benefit investors by enabling money market funds to dispose of troubled securities (*e.g.*, securities depressed in value as a result of market conditions) from their portfolios quickly without any loss to fund shareholders. It also would benefit money market funds by eliminating the cost and delay of requesting no-action assurances in these scenarios and the uncertainty whether such assurances will be granted.[388] We do not believe that there are any costs associated with this amendment, but we request comment on this analysis.

In addition, we are proposing to permit affiliated persons to purchase other portfolio securities from an affiliated money market fund, for any reason, provided that such person would be required to promptly remit to the fund any profit it realizes from the later sale of the security.[389] Our staff provided temporary no-action assurances last fall to certain funds facing extraordinary levels of redemption requests for affiliated persons of such funds to purchase eligible securities from the funds at the greater of amortized cost or market value (plus accrued and unpaid interest).[390] In these circumstances, money market funds may need to obtain cash quickly to avoid selling securities into the market at fire sale prices to meet shareholder redemption requests, to the detriment of remaining shareholders. The staff also provided no-action assurances to money market funds last fall for affiliated persons of the fund to purchase at the greater of amortized cost or market value (plus accrued and unpaid interest) certain distressed

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386 *See* proposed rule 17a-9(a).

387 *See supra* Section II.H.1.

388 Commission staff estimates that the costs to obtain staff no-action assurances range from $50,000 to $100,000.

389 *See* proposed rule 17a-9(b)(2).

390 Many of the no-action letters can be found on our website. *See* http://www.sec.gov/divisions/investment/im-noaction.shtml#money.

securities that were depressed in value due to market conditions potentially threatening the stable share price of the fund, but that remained eligible securities and had not defaulted.[391] Money market funds and their shareholders would benefit if affiliated persons were able to purchase securities from the fund at the greater of amortized cost or market value (plus accrued and unpaid interest) in such circumstances without the time, expense, and uncertainty of applying to Commission staff for no-action assurances.

Affiliated persons purchasing such securities would have costs in creating and implementing a system for tracking the purchased securities and remitting to the money market fund any profit ultimately received as a result. We estimate that creating such a system on average would require 5 hours of a senior programmer's time, at a cost of $1460 for each of the 171 fund complexes with money market funds and a total cost of $249,660.[392] After the initial creation of this system, we expect that the time spent noting in this system that a security was purchased under rule 17a-9 would require a negligible amount of compliance personnel's time. Based on our experience, we do not anticipate that there would be many instances, if any, in which an affiliated person would be required to repay profits in excess of the purchase price paid to the fund. However, if there is a payment, it would be made to the fund. If the payment is sufficiently large, we believe that funds are likely to include it with the next distribution to shareholders, which would not result in any additional costs to the fund. We request comment on this analysis. Are our cost estimates accurate? Are there other costs in allowing an affiliated person of a money market fund to purchase portfolio securities from the fund? Are there incentives that might encourage an affiliated person to purchase securities that are not distressed

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391 *Id.*

392 This estimate is based on the following calculation: $292/hour x 5 hours x 171 fund complexes = $249,660.

in any way? If so, would such purchases result in any cost to the fund and its investors?

The Commission also is proposing a related amendment to rule 2a-7, which would require that funds report all transactions under rule 17a-9 to the Commission. We believe that this reporting requirement would benefit fund investors by allowing the Commission to monitor the purchases for possible abuses and conflicts of interest on the part of the affiliates. It also would allow the Commission to observe what types of securities are distressed and which money market funds are holding distressed securities or are subject to significant redemption pressures. This information would better enable the Commission to monitor emerging risks at money market funds. For purposes of the Paperwork Reduction Act analysis, we estimate this amendment would impose relatively small reporting costs on money market funds of $7625 per year.[393] We request comment on whether these cost estimates are reasonable. We also request comment on our analysis of the costs and benefits of this proposed rule amendment.

C. Rule 22e-3

Proposed rule 22e-3 would permit money market funds that break the buck to suspend redemptions and postpone payment of proceeds pending board-approved liquidations. The rule would thus facilitate orderly liquidations, which would protect value for fund shareholders and minimize disruption to financial markets. The rule would also enable funds to avoid the expense and delay of obtaining an exemptive order from the Commission, which we estimate would otherwise cost about $75,000,[394] and would provide legal certainty to funds that wish to suspend

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393 This estimate is based on the following calculations: 25 (notices) + $305/hour (attorney) x 1 hour = $7625. *See supra* note 329 and accompanying text.

394 *See* Exchange Traded Funds, Investment Company Act Release No. 28913 (Mar. 11, 2008) [73 FR 14618 (Mar. 18, 2008)] at n.301 (estimating a cost range between $75,000 and $350,000 to submit an application for relief to operate an ETF). We assume that the costs associated with an application for exemptive relief from section 22(e) would be on the low end of this range because section 22(e) exemptive applications are often less involved than ETF exemptive applications.

redemptions during a liquidation in the interest of fairness to all shareholders.

Proposed rule 22e-3 would impose certain minimal costs on funds relying on the rule by requiring them to provide prior notice to the Commission of their decision to suspend redemptions in connection with a liquidation. We estimate that, for the purposes of the PRA, the annual burden of the notification requirement would be 10 minutes for a cost of $51.[395] The proposed rule may also impose costs on shareholders who seek to redeem their shares, but are unable to do so. In those circumstances, shareholders might have to borrow funds from another source, and thereby incur interest charges and other transactional fees. We believe the potential costs associated with proposed rule 22e-3 would be minimal, however, because the proposed rule would provide a limited exemption that is only triggered in the event of a fund breaking the buck and liquidating. We request comment on this analysis, and on any other potential costs and benefits of proposed rule 22e-3.

D. Rule 30b1-6 and Form N-MFP: Monthly Reporting of Portfolio Holdings

Proposed rule 30b1-6 and Form N-MFP would require money market funds to file with the Commission interactive data-formatted portfolio holdings information on a monthly basis. We expect that the proposed rule would improve the efficiency and effectiveness of the Commission's oversight of money market funds by enabling Commission staff to manage and analyze money market fund portfolio information more quickly and at a lower cost than is currently possible. The interactive data would also facilitate the flow of information between money market funds and other users of this information, such as information services, academics, and investors. As the development of software products to analyze the data continues to grow, we expect these benefits would increase.

395 This estimate is based on the following calculation: $305/hour x 1 ÷ 6 hour = $51.

Money market funds may also realize cost savings from the proposed rule. Currently, money market funds provide portfolio holdings information in a variety of formats to different third-parties, such as information services and NRSROs. The proposed rule may encourage the industry to adopt a standardized format, thereby reducing the burdens on money market funds of having to produce this information in multiple formats. In addition, money market funds may also benefit from cost savings to the extent that we exempt them from filing certain information required to be disclosed in existing quarterly portfolio holdings reports.

The proposed reporting requirement would also impose certain costs. We estimate that, for the purposes of the PRA, these filing requirements (including collecting, tagging, and electronically filing the report) would impose 128 burden hours at a cost of $35,968[396] per money market fund for the first year, and 96 burden hours at a cost of $26,976[397] per money market fund in subsequent years.[398]

For the reasons outlined in the discussion on the monthly website posting requirement, we estimate that there would be minimal additional costs incurred in connection with the proposed reporting requirement. We request comment on our estimates, including whether our assumptions about the costs and benefits are correct. We also request comment on other potential costs and benefits of the proposed reporting requirement.

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396 This estimate is based on the following calculation: $281/hour x 128 hours (senior database administrator) = $35,968.

397 This estimate is based on the following calculation: $281/hour x 96 hours (senior database administrator) = $26,976.

398 We understand that some money market funds may outsource all or a portion of these responsibilities to a filing agent, software consultant, or other third-party service provider. We believe, however, that a fund would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs of compiling, tagging, and filing the Form N-MFP.

E. Request for Comments

The Commission requests comment on the potential costs and benefits of the proposed rules and rule amendments. We also request comment on the potential costs and benefits of any alternatives suggested by commenters. We encourage commenters to identify, discuss, analyze, and supply relevant data regarding any additional costs and benefits. For purposes of the Small Business Regulatory Enforcement Act of 1996,[399] the Commission also requests information regarding the potential annual effect of the proposals on the U.S. economy. Commenters are requested to provide empirical data to support their views.

VI. COMPETITION, EFFICIENCY AND CAPITAL FORMATION

Section 2(c) of the Investment Company Act requires the Commission, when engaging in rulemaking that requires it to consider or determine whether an action is consistent with the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.[400]

A. Rule 2a-7

1. Second Tier Securities, Portfolio Maturity, and Liquidity Limits

We are proposing several amendments to rule 2a-7 to tighten the risk-limiting conditions of the rule. We are proposing to limit money market fund investments to only first tier securities, *i.e.*, securities receiving the highest short-term ratings from the requisite NRSROs or unrated securities that the fund's board of directors or its delegate determines are of comparable quality.[401] We also are proposing to limit money market funds to acquiring long-term securities

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[399] Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

[400] 15 U.S.C. 80a-2(c).

[401] *See* proposed rule 2a-7(a)(11)(iii); proposed rule 2a-7(a)(11)(iv).

that have received long-term ratings in the highest two ratings categories.[402]

The proposed amendments would reduce the maximum weighted average maturity of a money market fund permitted by rule 2a-7 from 90 days to 60 days.[403] They also would impose a new maturity limitation based on the weighted average "life" of fund securities that would limit the portion of a fund's portfolio that could be held in longer term floating- or variable-rate securities.[404] We are proposing to delete a provision in rule 2a-7 that permits money market funds not relying on the amortized cost method of valuation to acquire Government securities with a remaining maturity of up to 762 calendar days.

Finally, we are proposing new liquidity requirements on money market funds. Under the proposed amendments, money market funds would be prohibited from acquiring illiquid securities[405] and money market funds would be required to comply with certain minimum daily and weekly liquidity requirements.[406] The amended rule also would require that a money market fund at all times hold highly liquid securities sufficient to meet reasonably foreseeable redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders.[407]

We believe that these changes would reduce money market funds' sensitivity to interest rate, credit, and liquidity risks. These changes also would limit the credit spread risk and interest rate spread risk produced by longer term securities. A reduction of these risks would better enable money market funds to weather market turbulence and maintain a stable net asset value

402 *See* proposed rule 2a-7(a)(11)(iv)(A).

403 *See* proposed rule 2a-7(c)(2)(ii).

404 *See* proposed rule 2a-7(c)(2)(iii).

405 *See* proposed rule 2a-7(c)(5)(i).

406 *See* proposed rule 2a-7(c)(5).

407 *See* proposed rule 2a-7(c)(5)(ii).

per share. We believe that the changes would reduce the risk that a money market fund will break the buck and therefore prevent losses to fund investors. To the extent that money market funds are more stable, the changes also would reduce systemic risk to the capital markets and ensure a stable source of financing for issuers of short-term credit instruments. We believe that these effects would encourage capital formation by encouraging investment in money market funds, thereby allowing them to expand as a source of short-term financing in the capital markets.

These changes also may reduce maturities of short-term credit securities that issuers offer, which may increase financing costs for these issuers who might have to go back more frequently to the market for financing. To the extent that some issuers are unwilling or unable to issue securities that match money market fund demand given these proposed restrictions, the amendments could have a negative impact on capital formation.

If the proposed amendments reduce yields that money market funds are able to offer, some investors may move their money to, among other places, offshore unregulated money market funds that do not follow rule 2a-7's strictures and thus are able to offer a higher yield. Beyond the competitive impact, such a change could increase systemic risks to short-term credit markets and capital formation by increasing investment in less stable short-term instruments.

Precluding ownership of second tier securities also may have anticompetitive effects on some relatively small money market funds that may compete with larger funds on the basis of yield. The proposed elimination of the ability of money market funds to invest in second tier securities may affect the capital raising ability and strategies of the issuers of second tier securities or otherwise affect their financing arrangements, and may affect the flexibility of investing options for funds. As noted above, however, second tier securities represent only a very small percentage of money market fund portfolios today, which suggests that our proposed amendments would not have a material effect on capital formation. We solicit specific comment on whether the proposed amendments regarding second tier securities would promote efficiency, competition and capital formation.

2. *Stress Testing*

We are proposing to amend rule 2a-7 to require the board of directors of each money market fund to adopt procedures providing for periodic stress testing of the money market fund's portfolio, reporting the results of the testing to fund boards, and providing an assessment to the board.[408] We believe that stress testing could increase the efficiency of money market funds by enhancing their risk management and thus making it more likely that the fund will be better prepared for potential stress on the fund due to market events or shareholder behavior. Money market funds may become more stable as a result of the risk management benefits provided by stress testing, allowing them to expand and attract further investment. If so, this result will promote capital formation. We do not believe that stress testing would have an adverse impact on competition or capital formation. What effect would the proposed requirement have on competition, efficiency and capital formation?

3. *Repurchase Agreements*

We are proposing to allow money market funds to treat the acquisition of a repurchase agreement to be an acquisition of the collateral for purposes of rule 2a-7's diversification requirement only if the repurchase agreement is collateralized by cash items or Government securities[409] and after the board of directors or its delegate has evaluated the creditworthiness of

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408 Proposed rule 2a-7(c)(8)(ii)(D).

409 Proposed rule 2a-7(a)(5).

the counterparty.[410]

We believe that these changes would limit money market funds' exposure to credit risk. The reduction of credit risk would increase money market funds' ability to maintain a stable net asset value per share, thereby preventing losses to fund investors, reducing systemic risk to the capital markets and ensuring a stable source of financing for issuers of short-term credit instruments. More stable money market funds may attract greater investments, thus promoting capital formation and providing a greater source of short-term financing in the capital markets.

The limitation on money market funds' ability to invest in repurchase agreements collateralized with securities other than cash items and Government securities may result in an increase in the short-term financing costs of the counterparties in such agreements, thereby reducing their willingness to invest in those securities. As a result, issuers of such securities could also be indirectly affected by our proposed change, which therefore could have a negative impact on capital formation. We request comment on what effect the proposed amendments would have on competition, efficiency, and capital formation.

4. *Public Website Disclosure*

We are proposing to require money market funds to disclose certain portfolio holdings information on their websites on a monthly basis.[411] The proposed rule amendment would provide greater transparency of the fund's investments for current and prospective shareholders, and may thus promote more efficient allocation of investments by investors. We believe the proposed rule amendment may also improve competition, as better-informed investors may prompt funds managers to provide better services and products. We do not anticipate that funds would be disadvantaged, with respect to competition, because so many already have chosen to

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410 Proposed rule 2a-7(c)(4)(ii)(A).

411 *See supra* Section II.F.1.

provide the information more frequently than monthly. In addition, the investments selected by money market funds are less likely than, for example, equity funds, to be investments from which competing funds would obtain benefit by scrutinizing on a monthly basis. The proposed rule may also promote capital formation by making portfolio holdings information readily accessible to investors, who may thus be more inclined to allocate their investments in a particular fund or in money market funds instead of an alternative product. Alternatively, the proposed rule could have the reverse effect if the portfolio holdings information makes investors less confident regarding the risks associated with money market funds, including the risk that market participants may use the information obtained through the disclosures to the detriment of the fund and its investors, such as by trading along with the fund or ahead of the fund by anticipating future transactions based on past transactions. We request comment on what effect this proposed rule would have on competition, efficiency, and capital formation.

5. *Processing of Transactions*

We are proposing to require that each money market fund's board determine, at least once each calendar year, that the fund has the capability to redeem and sell its securities at prices other than the fund's stable net asset value per share.[412] This amendment would require money funds to have the operational capacity if they break the buck to continue to process investor transactions in an orderly manner. This amendment would increase efficiency at money market funds that break the buck by increasing the speed and minimizing the operational difficulties in satisfying shareholder redemption requests in such circumstances. It may also reduce investors' concerns that redemption would be unduly delayed if a money market fund were to break the buck. We do not believe that this amendment would have a material impact on competition or

[412] Proposed rule 2a-7(c)(1).

capital formation. We request comment on what effect this proposed amendment would have on competition, efficiency, and capital formation.

B. Rule 17a-9

The Commission is proposing to amend rule 17a-9 to expand the circumstances under which affiliated persons can purchase money market fund securities. Under the proposed amendments, a money market fund could sell a portfolio security that has defaulted (other than an immaterial default unrelated to the financial condition of the issuer) to an affiliated person for the greater of the security's amortized cost value or market value (plus accrued and unpaid interest), even though the security continued to be an eligible security.[413] In addition, the proposed amendment would permit affiliated persons, for any reason, to purchase other portfolio securities from an affiliated money market fund on the same terms provided that such person is required to promptly remit to the fund any profit it realizes from the later sale of the security.[414] These amendments would increase the efficiency of both the Commission and money market funds by allowing affiliated persons to purchase portfolio securities from money market funds under distress without having to seek no-action assurances from Commission staff. We do not believe that the proposed amendments will have any material impact on competition or capital formation. We request comment on our analysis. What effect would the proposed amendment to rule 17a-9 have on efficiency, competition and capital formation?

C. Rule 22e-3

Proposed rule 22e-3 would permit money market funds that break the buck to suspend redemptions and postpone the payment of proceeds pending board-approved liquidation proceedings. We anticipate that the rule would promote efficiency in the financial markets by

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[413] *See* proposed rule 17a-9(a).

[414] *See* proposed rule 17a-9(b).

facilitating orderly disposal of assets during liquidation. To the extent that investors choose money market funds over alternative investments because the proposed rule would provide reassurance as to the protection of their assets in the event the fund breaks the buck and minimize disruption in the financial markets, the rule also may promote capital formation. If, however, the possibility that redemptions can be suspended during a liquidation makes money market funds less appealing to investors, the rule may have a negative effect on capital formation. The proposed rule also could help make investors more confident that they would be able to receive the proceeds from their investment in the event of a liquidation of the fund. We do not believe that the proposed rule would have an adverse effect on competition. We request comment on what effect the proposed rule would have on competition, efficiency, and capital formation.

D. Rule 30b1-6 and Form N-MFP: Monthly Reporting of Portfolio Holdings

Proposed new rule 30b1-6 and Form N-MFP would mandate the monthly electronic filing of each money market fund's portfolio holdings information in XML-tagged format. As discussed above, we believe the new reporting requirement would improve the efficiency and effectiveness of the Commission's oversight of money market funds. The availability, and usability, of this data would also promote efficiency for other third-parties that may be interested in collecting and analyzing money market funds' portfolio holdings information. Money market funds currently are often required to provide this information to various third parties in different formats. To the extent that the proposal may encourage a standardized format for disclosure or transmission of portfolio holdings information, the proposal may promote efficiency for money market funds. We do not believe that the proposed rule would have an adverse effect on competition or capital formation. We request comment on what effect the proposed rule would have on competition, efficiency, and capital formation.

VII. Regulatory Flexibility Act Certification

Section 3(a) of the Regulatory Flexibility Act of 1980[415] ("RFA") requires the Commission to undertake an initial regulatory flexibility analysis ("IRFA") of the proposed rule amendments on small entities unless the Commission certifies that the rule, if adopted, would not have a significant economic impact on a substantial number of small entities.[416] Pursuant to 5 U.S.C. section 605(b), the Commission hereby certifies that the proposed amendments to rules 2a-7, 17a-9, and 30b1-5, and proposed rules 30b1-6 and 22e-3 under the Investment Company Act, would not, if adopted, have a significant economic impact on a substantial number of small entities.

The proposal would amend rule 2a-7 under the Investment Company Act to:

(i) Limit money market fund investments to first tier securities (*i.e.*, securities that received the highest short-term ratings categories from the requisite NRSROs or unrated securities that the board of directors (or its delegate) determines are of comparable quality);

(ii) Limit money market funds to acquiring long-term securities that have received long-term ratings in the highest two ratings categories from the requisite NRSROs;

(iii) Reduce the maximum weighted average maturity of money market funds' portfolio securities from 90 to 60 days;

(iv) Require money market funds to maintain a maximum weighted average life to maturity of portfolio securities of no more than 120 days;

(v) Eliminate a provision of the rule that permits a fund that relies exclusively on the penny-rounding method of pricing to acquire Government securities with remaining maturities of up to 762 days, rather than the 397-day limit otherwise provided by the rule;

(vi) Prohibit money market funds from acquiring securities unless, at the time acquired, they are liquid, *i.e.*, can be sold or disposed of in the ordinary course of

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[415] 5 U.S.C. 603(a).

[416] 5 U.S.C. 605(b).

business within seven days at approximately the value ascribed to it by the money market fund;

(vii) Require that immediately after the acquisition of a security, a taxable "retail fund" hold no less than 5 percent of its total assets in cash, U.S. Treasury securities, or other securities (including repurchase agreements) that mature, or are subject to a demand feature exercisable in one business day, and (ii) an "institutional fund" hold no less than 10 percent of those instruments;

(viii) Require that immediately after the acquisition of a security (i) a "retail fund" holds no less than 15 percent of its total assets in cash, U.S. Treasury securities, or other securities (including repurchase agreements) that are convertible to cash within five business days, and (ii) an "institutional fund" holds no less than 30 percent of those instruments;

(ix) Require that a money market fund at all times hold cash, U.S. Treasury securities, or securities readily convertible to cash on a daily or weekly basis sufficient to meet reasonably foreseeable redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders;

(x) Require the board of directors of each money market fund to adopt procedures providing for periodic stress testing of the money market fund's ability to maintain a stable net asset value per share based on certain hypothetical events, a report of the testing results to the board, and an assessment by the fund's adviser of the fund's ability to withstand the events that are reasonably likely to occur within the following year;

(xi) Limit money market funds to investing in repurchase agreements collateralized by cash items or Government securities in order to obtain special treatment under the diversification provisions of rule 2a-7;

(xii) Require that the money market fund's board of directors or its delegate evaluate the creditworthiness of the counterparty, regardless of whether the repurchase agreement is collateralized fully;

(xiii) Require money market funds to post monthly portfolio information on their websites; and

(xiv) Require that a money market fund's board determine, on an annual basis, that the fund (or its transfer agent) has the capacity to redeem and sell securities at prices that do not correspond to the fund's stable net asset value.

We also are proposing to amend rule 17a-9 to permit a money market fund to sell a portfolio security that has defaulted (other than an immaterial default unrelated to the financial condition of the issuer) to an affiliated person for the greater of the security's amortized cost value or market value (plus accrued and unpaid interest), even though the security continues to be an eligible security. In addition, we are proposing to permit an affiliated person, for any reason, to purchase any other portfolio security (*e.g.*, an eligible security that has not defaulted) from an affiliated money market fund for cash at the greater of the security's amortized cost value or market value, provided that such person promptly remits to the fund any profit it realizes from the later sale of the security. Under the proposal, a money market fund whose portfolio securities are purchased in reliance on rule 17a-9 would be required to provide notice of the transaction to the Commission by e-mail.

We are also proposing to amend rule 30b1-5 to exempt money market funds from the requirement to file their schedules of investments pursuant to Item 1 of Form N-Q, a quarterly schedule of portfolio holdings of management investment companies. The proposed amendment is intended to avoid unnecessarily duplicative disclosure obligations.

Finally, we are proposing two new rules. Proposed rule 22e-3 would exempt money market funds from section 22(e) to permit them to suspend redemptions in order to facilitate an orderly liquidation of fund assets. Rule 30b1-6 would mandate the monthly electronic filing in XML-tagged format of valuation and other information about the risk characteristics of the money market fund and each security in its portfolio.

Based on information in filings submitted to the Commission, we believe that there are no money market funds that are small entities.[417] For this reason, the Commission believes the proposed amendments to rules 2a-7, 17a-9, and 30b1-5, and proposed rules 22e-3 and 30b1-6 under the Investment Company Act would not, if adopted, have a significant economic impact on

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[417] Under rule 0-10 under the Investment Company Act, an investment company is considered a small entity if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.

a substantial number of small entities.

We encourage written comments regarding this certification. The Commission solicits comment as to whether the proposed amendments to rules 2a-7, 17a-9, and 30b1-5, and proposed rules 22e-3 and 30b1-6 could have an effect on small entities that has not been considered. We request that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of such impact.

VIII. STATUTORY AUTHORITY

The Commission is proposing amendments to rule 2a-7 under the exemptive and rulemaking authority set forth in sections 6(c), 8(b), 22(c), and 38(a) of the Investment Company Act of 1940 [15 U.S.C. 80a-6(c), 80a-8(b), 80a-22(c), 80a-37(a)]. The Commission is proposing amendments to rule 17a-9 pursuant to the authority set forth in sections 6(c) and 38(a) of the Investment Company Act [15 U.S.C. 80a-6(c), 80a-37(a)]. The Commission is proposing rule 22e-3 pursuant to the authority set forth in sections 6(c), 22(e) and 38(a) of the Investment Company Act [15 U.S.C. 80a-6(c), 80a-22(e), and 80a-37(a)]. The Commission is proposing amendments to rule 30b1-5 and new rule 30b1-6 and Form N-MFP pursuant to authority set forth in Sections 8(b), 30(b), 31(a), and 38(a) of the Investment Company Act [15 U.S.C. 80a-8(b), 80a-29(b), 80a-30(a), and 80a-37(a)].

List of Subjects

17 CFR Parts 270 and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

TEXT OF PROPOSED RULES AND FORM

For reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 270 – RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF

1940

1. The authority citation for Part 270 continues to read, in part, as follows:

Authority: 15 U.S.C. 80a-1 *et seq.*, 80a-34(d), 80a-37, and 80a-39, unless otherwise noted.

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2. Section 270.2a-7 is revised to read as follows:

§ 270.2a-7 Money market funds.

(a) *Definitions.*

(1) *Acquisition (or Acquire)* means any purchase or subsequent rollover (but does not include the failure to exercise a Demand Feature).

(2) *Amortized Cost Method* of valuation means the method of calculating an investment company's net asset value whereby portfolio securities are valued at the fund's Acquisition cost as adjusted for amortization of premium or accretion of discount rather than at their value based on current market factors.

(3) *Asset Backed Security* means a fixed income security (other than a Government security) issued by a Special Purpose Entity (as defined in this paragraph), substantially all of the assets which consist of Qualifying Assets (as defined in this paragraph). *Special Purpose Entity* means a trust, corporation, partnership or other entity organized for the sole purpose of issuing securities that entitle their holders to receive payments that depend primarily on the cash flow from Qualifying Assets, but does not include a registered investment company. *Qualifying Assets* means financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to security holders.

(4) *Business Day* means any day, other than Saturday, Sunday, or any customary business holiday.

(5) *Collateralized Fully* means "Collateralized Fully" as defined in § 270.5b-3(c)(1) except that § 270.5b-3(c)(1)(iv)(C) and (D) shall not apply.

(6) *Conditional Demand Feature* means a Demand Feature that is not an Unconditional Demand Feature. A Conditional Demand Feature is not a Guarantee.

(7) *Conduit Security* means a security issued by a Municipal Issuer (as defined in this paragraph) involving an arrangement or agreement entered into, directly or indirectly, with a person other than a Municipal Issuer, which arrangement or agreement provides for or secures repayment of the security. *Municipal Issuer* means a state or territory of the United States (including the District of Columbia), or any political subdivision or public instrumentality of a state or territory of the United States. A Conduit Security does not include a security that is:

(i) Fully and unconditionally guaranteed by a Municipal Issuer;

(ii) Payable from the general revenues of the Municipal Issuer or other Municipal Issuers (other than those revenues derived from an agreement or arrangement with a person who is not a Municipal Issuer that provides for or secures repayment of the security issued by the Municipal Issuer);

(iii) Related to a project owned and operated by a Municipal Issuer; or

(iv) Related to a facility leased to and under the control of an industrial or commercial enterprise that is part of a public project which, as a whole, is owned and under the control of a Municipal Issuer.

(8) *Daily Liquid Assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government; or

(iii) Securities that will mature or are subject to a Demand Feature that is exercisable and payable within one Business Day.

(9) *Demand Feature* means:

(i) A feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise. A Demand Feature must be exercisable either:

(A) At any time on no more than 30 calendar days' notice;

(B) At specified intervals not exceeding 397 calendar days and upon no more than 30 calendar days' notice; or

(ii) A feature permitting the holder of an Asset Backed Security unconditionally to receive principal and interest within 397 calendar days of making demand.

(10) *Demand Feature Issued By A Non-Controlled Person* means a Demand Feature issued by:

(i) A person that, directly or indirectly, does not control, and is not controlled by or under common control with the issuer of the security subject to the Demand Feature (*control* means "control" as defined in section 2(a)(9) of the Act (15 U.S.C. 80a-2(a)(9)); or

(ii) A sponsor of a Special Purpose Entity with respect to an Asset Backed Security.

(11) *Eligible Security* means:

(i) A security issued by a registered investment company that is a money market fund;

(ii) A Government Security;

(iii) A Rated Security with a remaining maturity of 397 calendar days or less that has received a rating from the Requisite NRSROs in the highest short-term rating category (within which there may be sub-categories or gradations indicating relative standing); or

(iv) An Unrated Security that is of comparable quality to a security meeting the requirements for a Rated Security in paragraph (a)(11)(iii) of this section, as determined by the money market fund's board of directors; provided, however, that:

(A) A security that at the time of issuance had a remaining maturity of more than 397 calendar days but that has a remaining maturity of 397 calendar days or less and that is an Unrated Security is not an Eligible Security if the security has received a long-term rating from any NRSRO that is not within the NRSRO's two highest long-term ratings categories (within which there may be sub-categories or gradations indicating relative standing), unless the security has received a long-term rating from the Requisite NRSROs in one of the two highest rating categories;

(B) An Asset Backed Security (other than an Asset Backed Security substantially all of whose Qualifying Assets consist of obligations of one or more Municipal Issuers, as that term is defined in paragraph (a)(7) of this section) shall not be an Eligible Security unless it has received a rating from an NRSRO.

(v) In addition, in the case of a security that is subject to a Demand Feature or Guarantee:

(A) The Guarantee has received a rating from an NRSRO or the Guarantee is issued by a guarantor that has received a rating from an NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security to the Guarantee, unless:

(1) The Guarantee is issued by a person that, directly or indirectly, controls, is

controlled by or is under common control with the issuer of the security subject to the Guarantee (other than a sponsor of a Special Purpose Entity with respect to an Asset Backed Security);

(*2*) The security subject to the Guarantee is a repurchase agreement that is Collateralized Fully; or

(*3*) The Guarantee is itself a Government Security; and

(B) The issuer of the Demand Feature or Guarantee, or another institution, has undertaken promptly to notify the holder of the security in the event the Demand Feature or Guarantee is substituted with another Demand Feature or Guarantee (if such substitution is permissible under the terms of the Demand Feature or Guarantee).

(12) *Event of Insolvency* means "Event of Insolvency" as defined in § 270.5b-3(c)(2).

(13) *Floating Rate Security* means a security the terms of which provide for the adjustment of its interest rate whenever a specified interest rate changes and that, at any time until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(14) *Government Security* means any "Government security" as defined in section 2(a)(16) of the Act (15 U.S.C. 80a-2(a)(16)).

(15) *Guarantee* means an unconditional obligation of a person other than the issuer of the security to undertake to pay, upon presentment by the holder of the Guarantee (if required), the principal amount of the underlying security plus accrued interest when due or upon default, or, in the case of an Unconditional Demand Feature, an obligation that entitles the holder to receive upon exercise the approximate amortized cost of the underlying security or securities, plus accrued interest, if any. A Guarantee includes a letter of credit, financial guaranty (bond)

insurance, and an Unconditional Demand Feature (other than an Unconditional Demand Feature provided by the issuer of the security).

(16) *Guarantee Issued By A Non-Controlled Person* means a Guarantee issued by:

(i) A person that, directly or indirectly, does not control, and is not controlled by or under common control with the issuer of the security subject to the Guarantee (control means "control" as defined in section 2(a)(9) of the Act (15 U.S.C. 80a-2(a)(9)); or

(ii) A sponsor of a Special Purpose Entity with respect to an Asset Backed Security.

(17) *Institutional Fund* means a money market fund whose board of directors determines, no less frequently than once each calendar year, is intended to be offered primarily to institutional investors or has the characteristics of such a fund, based on the:

(i) Nature of the record owners of the fund's shares;

(ii) Minimum initial investment requirements; and

(iii) Historical cash flows that have resulted or expected cash flows that would result from purchases and redemptions.

(18) *Liquid Security* means a security that can be sold or disposed of in the ordinary course of business within seven calendar days at approximately its amortized cost.

(19) *NRSRO* means any nationally recognized statistical rating organization, as that term is defined in section 3(a)(62) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(62)), that is not an "affiliated person," as defined in section 2(a)(3)(C) of the Act (15 U.S.C. 80a-2(a)(3)(C)), of the issuer of, or any insurer or provider of credit support for, the security.

(20) *Penny-Rounding Method* of pricing means the method of computing an investment company's price per share for purposes of distribution, redemption and repurchase

whereby the current net asset value per share is rounded to the nearest one percent.

(21) *Rated Security* means a security that meets the requirements of paragraphs (a)(21)(i) or (ii) of this section, in each case subject to paragraph (a)(21)(iii) of this section:

(i) The security has received a short-term rating from an NRSRO, or has been issued by an issuer that has received a short-term rating from an NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the security; or

(ii) The security is subject to a Guarantee that has received a short-term rating from an NRSRO, or a Guarantee issued by a guarantor that has received a short-term rating from an NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the Guarantee; but

(iii) A security is not a Rated Security if it is subject to an external credit support agreement (including an arrangement by which the security has become a Refunded Security) that was not in effect when the security was assigned its rating, unless the security has received a short-term rating reflecting the existence of the credit support agreement as provided in paragraph (a)(21)(i) of this section, or the credit support agreement with respect to the security has received a short-term rating as provided in paragraph (a)(21)(ii) of this section.

(22) *Refunded Security* means "Refunded Security" as defined in § 270.5b-3(c)(4).

(23) *Requisite NRSROs* means:

(i) Any two NRSROs that have issued a rating with respect to a security or class of debt obligations of an issuer; or

(ii) If only one NRSRO has issued a rating with respect to such security or class of debt obligations of an issuer at the time the fund acquires the security, that NRSRO.

(24) *Retail Fund* means any money market fund that the board of directors has not determined within the calendar year is an Institutional Fund under paragraph (c)(5)(v) of this section.

(25) *Single State Fund* means a Tax Exempt Fund that holds itself out as seeking to maximize the amount of its distributed income that is exempt from the income taxes or other taxes on investments of a particular state and, where applicable, subdivisions thereof.

(26) *Tax Exempt Fund* means any money market fund that holds itself out as distributing income exempt from regular federal income tax.

(27) *Total Assets* means, with respect to a money market fund using the Amortized Cost Method, the total amortized cost of its assets and, with respect to any other money market fund, the total market-based value of its assets.

(28) *Unconditional Demand Feature* means a Demand Feature that by its terms would be readily exercisable in the event of a default in payment of principal or interest on the underlying security or securities.

(29) *United States Dollar-Denominated* means, with reference to a security, that all principal and interest payments on such security are payable to security holders in United States dollars under all circumstances and that the interest rate of, the principal amount to be repaid, and the timing of payments related to such security do not vary or float with the value of a foreign currency, the rate of interest payable on foreign currency borrowings, or with any other interest rate or index expressed in a currency other than United States dollars.

(30) *Unrated Security* means a security that is not a Rated Security.

(31) *Variable Rate Security* means a security the terms of which provide for the adjustment of its interest rate on set dates (such as the last day of a month or calendar quarter)

and that, upon each adjustment until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(32) *Weekly Liquid Assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government; or

(iii) Securities that will mature or are subject to a Demand Feature that is exercisable and payable within five Business Days.

(b) *Holding Out and Use of Names and Titles.*

(1) It shall be an untrue statement of material fact within the meaning of section 34(b) of the Act (15 U.S.C. 80a-33(b)) for a registered investment company, in any registration statement, application, report, account, record, or other document filed or transmitted pursuant to the Act, including any advertisement, pamphlet, circular, form letter, or other sales literature addressed to or intended for distribution to prospective investors that is required to be filed with the Commission by section 24(b) of the Act (15 U.S.C. 80a-24(b)), to hold itself out to investors as a money market fund or the equivalent of a money market fund, unless such registered investment company meets the conditions of paragraphs (c)(2), (c)(3), (c)(4) and (c)(5) of this section.

(2) It shall constitute the use of a materially deceptive or misleading name or title within the meaning of section 35(d) of the Act (15 U.S.C. 80a-34(d)) for a registered investment company to adopt the term "money market" as part of its name or title or the name or title of any redeemable securities of which it is the issuer, or to adopt a name that suggests that it is a money market fund or the equivalent of a money market fund, unless such registered investment

company meets the conditions of paragraphs (c)(2), (c)(3), (c)(4), and (c)(5) of this section.

(3) For purposes of this paragraph, a name that suggests that a registered investment company is a money market fund or the equivalent thereof shall include one that uses such terms as "cash," "liquid," "money," "ready assets" or similar terms.

(c) *Share Price Calculations.*

The current price per share, for purposes of distribution, redemption and repurchase, of any redeemable security issued by any registered investment company ("money market fund" or "fund"), notwithstanding the requirements of section 2(a)(41) of the Act (15 U.S.C. 80a-2(a)(41)) and of §§ 270.2a-4 and 270.22c-1 thereunder, may be computed by use of the Amortized Cost Method or the Penny-Rounding Method; provided, however, that:

(1) *Board Findings*. The board of directors of the money market fund shall determine, in good faith, that it is in the best interests of the fund and its shareholders to maintain a stable net asset value per share or stable price per share, by virtue of either the Amortized Cost Method or the Penny-Rounding Method, and that the money market fund will continue to use such method only so long as the board of directors believes that it fairly reflects the market-based net asset value per share. The board shall annually determine in good faith that the fund (or its transfer agent) has the capacity to redeem and sell securities issued by the fund at a price based on the current net asset value per share pursuant to § 270.22c-1. Such capacity shall include the ability to redeem and sell securities at prices that do not correspond to a stable net asset value or price per share.

(2) *Portfolio Maturity.* The money market fund shall maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable net asset value per share or price per share; provided, however, that the money market fund will not:

(i) Acquire any instrument with a remaining maturity of greater than 397 calendar days;

(ii) Maintain a dollar-weighted average portfolio maturity that exceeds 60 calendar days; or

(iii) Maintain a dollar-weighted average portfolio maturity that exceeds 120 calendar days, determined without reference to the exceptions in paragraph (d) of this section regarding interest rate readjustments.

(3) *Portfolio Quality.*

(i) *General.* The money market fund shall limit its portfolio investments to those United States Dollar-Denominated securities that the fund's board of directors determines present minimal credit risks (which determination must be based on factors pertaining to credit quality in addition to any rating assigned to such securities by an NRSRO) and that are at the time of Acquisition Eligible Securities.

(ii) *Securities Subject to Guarantees.* A security that is subject to a Guarantee may be determined to be an Eligible Security based solely on whether the Guarantee is an Eligible Security.

(iii) *Securities Subject to Conditional Demand Features.* A security that is subject to a Conditional Demand Feature ("Underlying Security") may be determined to be an Eligible Security only if:

(A) The Conditional Demand Feature is an Eligible Security;

(B) At the time of the Acquisition of the Underlying Security, the money market fund's board of directors has determined that there is minimal risk that the circumstances that would result in the Conditional Demand Feature not being exercisable will occur; and

(*1*) The conditions limiting exercise either can be monitored readily by the fund, or relate to the taxability, under federal, state or local law, of the interest payments on the security; or

(*2*) The terms of the Conditional Demand Feature require that the fund will receive notice of the occurrence of the condition and the opportunity to exercise the Demand Feature in accordance with its terms; and

(C) The Underlying Security or any Guarantee of such security (or the debt securities of the issuer of the Underlying Security or Guarantee that are comparable in priority and security with the Underlying Security or Guarantee) has received either a short-term rating or a long-term rating, as the case may be, from the Requisite NRSROs within the NRSROs' highest short-term or long-term rating categories (within which there may be sub-categories or gradations indicating relative standing) or, if unrated, is determined to be of comparable quality by the money market fund's board of directors to a security that has received a rating from the Requisite NRSROs within the NRSROs' highest short-term or long-term rating categories, as the case may be.

(4) *Portfolio Diversification.*

(i) *Issuer Diversification.* The money market fund shall be diversified with respect to issuers of securities Acquired by the fund as provided in paragraphs (c)(4)(i) and (c)(4)(ii) of this section, other than with respect to Government Securities and securities subject to a Guarantee Issued By A Non-Controlled Person.

(A) *Taxable and National Funds.* Immediately after the Acquisition of any security, a money market fund other than a Single State Fund shall not have invested more than five percent of its Total Assets in securities issued by the issuer of the security; provided, however, that such a fund may invest up to twenty-five percent of its Total Assets in the securities of a single issuer for a period of up to three Business Days after the Acquisition thereof; Provided, further, that the fund may not invest in the securities of more than one issuer in accordance with the foregoing proviso in this paragraph at any time.

(B) *Single State Funds.* With respect to seventy-five percent of its Total Assets, immediately after the Acquisition of any security, a Single State Fund shall not have invested more than five percent of its Total Assets in securities issued by the issuer of the security.

(ii) *Issuer Diversification Calculations.* For purposes of making calculations under paragraph (c)(4)(i) of this section:

(A) *Repurchase Agreements.* The Acquisition of a repurchase agreement may be deemed to be an Acquisition of the underlying securities, provided the obligation of the seller to repurchase the securities from the money market fund is Collateralized Fully and the fund's board of directors has evaluated the seller's creditworthiness.

(B) *Refunded Securities.* The Acquisition of a Refunded Security shall be deemed to be an Acquisition of the escrowed Government Securities.

(C) *Conduit Securities.* A Conduit Security shall be deemed to be issued by the person (other than the Municipal Issuer) ultimately responsible for payments of interest and principal on the security.

(D) *Asset Backed Securities.*

(*1*) *General.* An Asset Backed Security Acquired by a fund ("Primary ABS") shall be deemed to be issued by the Special Purpose Entity that issued the Asset Backed Security; provided, however:

(*i*) Holdings of Primary ABS. Any person whose obligations constitute ten percent or more of the principal amount of the Qualifying Assets of the Primary ABS ("Ten Percent

Obligor") shall be deemed to be an issuer of the portion of the Primary ABS such obligations represent; and

(*ii*) Holdings of Secondary ABS. If a Ten Percent Obligor of a Primary ABS is itself a Special Purpose Entity issuing Asset Backed Securities ("Secondary ABS'), any Ten Percent Obligor of such Secondary ABS also shall be deemed to be an issuer of the portion of the Primary ABS that such Ten Percent Obligor represents.

(*2*) *Restricted Special Purpose Entities*. A Ten Percent Obligor with respect to a Primary or Secondary ABS shall not be deemed to have issued any portion of the assets of a Primary ABS as provided in paragraph (c)(4)(ii)(D)(1) of this section if that Ten Percent Obligor is itself a Special Purpose Entity issuing Asset Backed Securities ("Restricted Special Purpose Entity"), and the securities that it issues (other than securities issued to a company that controls, or is controlled by or under common control with, the Restricted Special Purpose Entity and which is not itself a Special Purpose Entity issuing Asset Backed Securities) are held by only one other Special Purpose Entity.

(*3*) *Demand Features and Guarantees*. In the case of a Ten Percent Obligor deemed to be an issuer, the fund shall satisfy the diversification requirements of paragraph (c)(4)(iii) of this section with respect to any Demand Feature or Guarantee to which the Ten Percent Obligor's obligations are subject.

(E) *Shares of Other Money Market Funds*. A money market fund that Acquires shares issued by another money market fund in an amount that would otherwise be prohibited by paragraph (c)(4)(i) of this section shall nonetheless be deemed in compliance with this section if the board of directors of the Acquiring money market fund reasonably believes that the fund in which it has invested is in compliance with this section.

(iii) *Diversification Rules for Demand Features and Guarantees*. The money market fund shall be diversified with respect to Demand Features and Guarantees Acquired by the fund as provided in paragraphs (c)(4)(iii) and (c)(4)(iv) of this section, other than with respect to a Demand Feature issued by the same institution that issued the underlying security, or with respect to a Guarantee or Demand Feature that is itself a Government Security.

(A) *General*. Immediately after the Acquisition of any Demand Feature or Guarantee or security subject to a Demand Feature or Guarantee, a money market fund, with respect to seventy-five percent of its Total Assets, shall not have invested more than ten percent of its Total Assets in securities issued by or subject to Demand Features or Guarantees from the institution that issued the Demand Feature or Guarantee, subject to paragraph (c)(4)(iii) (B) of this section.

(B) *Demand Features or Guarantees Issued by Non-Controlled Persons*. Immediately after the Acquisition of any security subject to a Demand Feature or Guarantee, a money market fund shall not have invested more than ten percent of its Total Assets in securities issued by, or subject to Demand Features or Guarantees from the institution that issued the Demand Feature or Guarantee, unless, with respect to any security subject to Demand Features or Guarantees from that institution (other than securities issued by such institution), the Demand Feature or Guarantee is a Demand Feature or Guarantee Issued By A Non-Controlled Person.

(iv) *Demand Feature and Guarantee Diversification Calculations*.

(A) *Fractional Demand Features or Guarantees*. In the case of a security subject to a Demand Feature or Guarantee from an institution by which the institution guarantees a specified portion of the value of the security, the institution shall be deemed to guarantee the specified portion thereof.

(B) *Layered Demand Features or Guarantees*. In the case of a security subject to

Demand Features or Guarantees from multiple institutions that have not limited the extent of their obligations as described in paragraph (c)(4)(iv)(A) of this section, each institution shall be deemed to have provided the Demand Feature or Guarantee with respect to the entire principal amount of the security.

(v) *Diversification Safe Harbor.* A money market fund that satisfies the applicable diversification requirements of paragraphs (c)(4) and (c)(6) of this section shall be deemed to have satisfied the diversification requirements of section 5(b)(1) of the Act (15 U.S.C. 80a-5(b)(1)) and the rules adopted thereunder.

(5) *Portfolio Liquidity.*

(i) *Liquid Securities.* The money market fund shall limit its portfolio investments to cash and securities that at the time of Acquisition are Liquid Securities.

(ii) *General Liquidity Requirement.* The money market fund shall hold Daily Liquid Assets and Weekly Liquid Assets sufficient to meet reasonably foreseeable shareholder redemptions in light of the fund's obligations under section 22(e) of the Act (15 U.S.C. 80a-22(e)) and any commitments the fund has made to shareholders.

(iii) *Minimum Daily Liquidity Requirement.* A money market fund shall not Acquire any security other than a Daily Liquid Asset if, immediately after the Acquisition, a Retail Fund would have invested less than five percent of its Total Assets, and an Institutional Fund would have invested less than ten percent of its Total Assets, in Daily Liquid Assets. This provision shall not apply to Tax Exempt Funds.

(iv) *Minimum Weekly Liquidity Requirement.* A money market fund shall not Acquire any security if, immediately after the Acquisition, a Retail Fund would have invested less than fifteen percent of its Total Assets, and an Institutional Fund would have invested less than thirty percent of its Total Assets, in Weekly Liquid Assets.

(v) *Annual Board Determination.* The board of directors of each money market fund shall determine no less than once each calendar year whether the fund is an Institutional Fund for purposes of meeting the minimum liquidity requirements set forth in paragraphs (c)(5)(iii) and (iv) of this section.

(6) *Demand Features and Guarantees Not Relied Upon.* If the fund's board of directors has determined that the fund is not relying on a Demand Feature or Guarantee to determine the quality (pursuant to paragraph (c)(3) of this section), or maturity (pursuant to paragraph (d) of this section), or liquidity of a portfolio security, and maintains a record of this determination (pursuant to paragraphs (c)(10)(ii) and (c)(11)(vi) of this section), then the fund may disregard such Demand Feature or Guarantee for all purposes of this section.

(7) *Downgrades, Defaults and Other Events.*

(i) *Downgrades.*

(A) *General.* In the event that the money market fund's investment adviser (or any person to whom the fund's board of directors has delegated portfolio management responsibilities) becomes aware that any Unrated Security held by the money market fund has, since the security was Acquired by the fund, been given a rating by any NRSRO below the NRSRO's highest short-term rating category, the board of directors of the money market fund shall reassess promptly whether such security continues to present minimal credit risks and shall cause the fund to take such action as the board of directors determines is in the best interests of the money market fund and its shareholders.

(B) The reassessment required by paragraph (c)(7)(i)(A) of this section shall not be required if the fund disposes of the security (or it matures) within five Business Days.

(ii) *Defaults and Other Events*. Upon the occurrence of any of the events specified in paragraphs (c)(7)(ii)(A) through (D) of this section with respect to a portfolio security, the money market fund shall dispose of such security as soon as practicable consistent with achieving an orderly disposition of the security, by sale, exercise of any Demand Feature or otherwise, absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund (which determination may take into account, among other factors, market conditions that could affect the orderly disposition of the portfolio security):

(A) The default with respect to a portfolio security (other than an immaterial default unrelated to the financial condition of the issuer);

(B) A portfolio security ceases to be an Eligible Security;

(C) A portfolio security has been determined to no longer present minimal credit risks; or

(D) An Event of Insolvency occurs with respect to the issuer of a portfolio security or the provider of any Demand Feature or Guarantee.

(iii) *Notice to the Commission.* The money market fund shall promptly notify the Commission by electronic mail directed to the Director of Investment Management or the Director's designee, of any:

(A) Default with respect to one or more portfolio securities (other than an immaterial default unrelated to the financial condition of the issuer) or an Event of Insolvency with respect to the issuer of the security or any Demand Feature or Guarantee to which it is subject, where immediately before default the securities (or the securities subject to the Demand Feature or Guarantee) accounted for 1/2 of 1 percent or more of a money market fund's Total Assets, the money market fund shall promptly notify the Commission of such fact and the actions the money market fund intends to take in response to such situation; or

(B) Purchase of a security from the fund by an affiliated person in reliance on § 270.17a-9 of this section, and the reasons for such purchase.

(iv) *Defaults for Purposes of Paragraphs (c)(7)(ii) and (iii).* For purposes of paragraphs (c)(7)(ii) and (iii) of this section, an instrument subject to a Demand Feature or Guarantee shall not be deemed to be in default (and an Event of Insolvency with respect to the security shall not be deemed to have occurred) if:

(A) In the case of an instrument subject to a Demand Feature, the Demand Feature has been exercised and the fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest; or

(B) The provider of the Guarantee is continuing, without protest, to make payments as due on the instrument.

(8) *Required Procedures: Amortized Cost Method.* In the case of a money market fund using the Amortized Cost Method:

(i) *General.* In supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market fund's investment adviser, the money market fund's board of directors, as a particular responsibility within the overall duty of care owed to its shareholders, shall establish written procedures reasonably designed, taking into account current market conditions and the money market fund's investment objectives, to stabilize the money market fund's net asset value per share, as computed for the purpose of distribution, redemption and repurchase, at a single value.

(ii) *Specific Procedures.* Included within the procedures adopted by the board of directors shall be the following:

(A) *Shadow Pricing*. Written procedures shall provide:

(*1*) That the extent of deviation, if any, of the current net asset value per share calculated using available market quotations (or an appropriate substitute that reflects current market conditions) from the money market fund's amortized cost price per share, shall be calculated at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions;

(*2*) For the periodic review by the board of directors of the amount of the deviation as well as the methods used to calculate the deviation; and

(*3*) For the maintenance of records of the determination of deviation and the board's review thereof.

(B) *Prompt Consideration of Deviation*. In the event such deviation from the money market fund's amortized cost price per share exceeds 1/2 of 1 percent, the board of directors shall promptly consider what action, if any, should be initiated by the board of directors.

(C) *Material Dilution or Unfair Results*. Where the board of directors believes the extent of any deviation from the money market fund's amortized cost price per share may result in material dilution or other unfair results to investors or existing shareholders, it shall cause the fund to take such action as it deems appropriate to eliminate or reduce to the extent reasonably practicable such dilution or unfair results.

(D) *Stress Testing*. Written procedures shall provide for:

(*1*) The periodic testing, at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions, of the money market fund's ability to maintain a stable net asset value per share based upon specified hypothetical events, that include, but are not limited to, a change in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on portfolio securities, and the widening or narrowing of spreads between yields on an appropriate benchmark the fund has selected for overnight interest rates and commercial paper and other types of securities held by the fund;

(*2*) A report on the results of such testing to be provided to the board of directors at its next regularly scheduled meeting, which report shall include the date(s) on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value calculated using available market quotations (or appropriate substitutes which reflect current market conditions) from its net asset value per share calculated using amortized cost to exceed ½ of 1 percent; and

(*3*) An assessment by the fund's adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably likely to occur within the following year.

(9) *Required Procedures: Penny-Rounding Method.* In the case of a money market fund using the Penny-Rounding Method, in supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market fund's investment adviser, the money market fund's board of directors undertakes, as a particular responsibility within the overall duty of care owed to its shareholders, to assure to the extent reasonably practicable, taking into account current market conditions affecting the money market fund's investment objectives, that the money market fund's price per share as computed for the purpose of distribution, redemption and repurchase, rounded to the nearest one percent, will not deviate from the single price established by the board of directors.

(10) *Specific Procedures: Amortized Cost and Penny-Rounding Methods.* Included

within the procedures adopted by the board of directors for money market funds using either the Amortized Cost or Penny-Rounding Methods shall be the following:

(i) *Securities for Which Maturity is Determined by Reference to Demand Features.* In the case of a security for which maturity is determined by reference to a Demand Feature, written procedures shall require ongoing review of the security's continued minimal credit risks, and that review must be based on, among other things, financial data for the most recent fiscal year of the issuer of the Demand Feature and, in the case of a security subject to a Conditional Demand Feature, the issuer of the security whose financial condition must be monitored under paragraph (c)(3)(iv) of this section, whether such data is publicly available or provided under the terms of the security's governing documentation.

(ii) *Securities Subject to Demand Features or Guarantees.* In the case of a security subject to one or more Demand Features or Guarantees that the fund's board of directors has determined that the fund is not relying on to determine the quality (pursuant to paragraph (c)(3) of this section), maturity (pursuant to paragraph (d) of this section) or liquidity of the security subject to the Demand Feature or Guarantee, written procedures shall require periodic evaluation of such determination.

(iii) *Adjustable Rate Securities Without Demand Features.* In the case of a Variable Rate or Floating Rate Security that is not subject to a Demand Feature and for which maturity is determined pursuant to paragraphs (d)(1), (d)(2) or (d)(4) of this section, written procedures shall require periodic review of whether the interest rate formula, upon readjustment of its interest rate, can reasonably be expected to cause the security to have a market value that approximates its amortized cost value.

(iv) *Asset Backed Securities.* In the case of an Asset Backed Security, written procedures shall require the fund to periodically determine the number of Ten Percent Obligors (as that term is used in paragraph (c)(4)(ii)(D) of this section) deemed to be the issuers of all or a portion of the Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section; Provided, however, written procedures need not require periodic determinations with respect to any Asset Backed Security that a fund's board of directors has determined, at the time of Acquisition, will not have, or is unlikely to have, Ten Percent Obligors that are deemed to be issuers of all or a portion of that Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section, and maintains a record of this determination.

(11) *Record Keeping and Reporting.*

(i) *Written Procedures.* For a period of not less than six years following the replacement of such procedures with new procedures (the first two years in an easily accessible place), a written copy of the procedures (and any modifications thereto) described in paragraphs (c)(7) through (c)(10) and (e) of this section shall be maintained and preserved.

(ii) *Board Considerations and Actions.* For a period of not less than six years (the first two years in an easily accessible place) a written record shall be maintained and preserved of the board of directors' considerations and actions taken in connection with the discharge of its responsibilities, as set forth in this section, to be included in the minutes of the board of directors' meetings.

(iii) *Credit Risk Analysis.* For a period of not less than three years from the date that the credit risks of a portfolio security were most recently reviewed, a written record of the determination that a portfolio security presents minimal credit risks and the NRSRO ratings (if any) used to determine the status of the security as an Eligible Security shall be maintained and preserved in an easily accessible place.

(iv) *Determinations With Respect to Adjustable Rate Securities.* For a period of not less than three years from the date when the determination was most recently made, a written record shall be preserved and maintained, in an easily accessible place, of the determination required by paragraph (c)(10)(iii) of this section (that a Variable Rate or Floating Rate Security that is not subject to a Demand Feature and for which maturity is determined pursuant to paragraphs (d)(1), (d)(2) or (d)(4) of this section can reasonably be expected, upon readjustment of its interest rate at all times during the life of the instrument, to have a market value that approximates its amortized cost).

(v) *Determinations with Respect to Asset Backed Securities.* For a period of not less than three years from the date when the determination was most recently made, a written record shall be preserved and maintained, in an easily accessible place, of the determinations required by paragraph (c)(10)(iv) of this section (the number of Ten Percent Obligors (as that term is used in paragraph (c)(4)(ii)(D) of this section) deemed to be the issuers of all or a portion of the Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section). The written record shall include:

(A) The identities of the Ten Percent Obligors (as that term is used in paragraph (c)(4)(ii)(D) of this section), the percentage of the Qualifying Assets constituted by the securities of each Ten Percent Obligor and the percentage of the fund's Total Assets that are invested in securities of each Ten Percent Obligor; and

(B) Any determination that an Asset Backed Security will not have, or is unlikely to have, Ten Percent Obligors deemed to be issuers of all or a portion of that Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section.

(vi) *Evaluations with Respect to Securities Subject to Demand Features or*

Guarantees. For a period of not less than three years from the date when the evaluation was most recently made, a written record shall be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (c)(10)(ii) (regarding securities subject to one or more Demand Features or Guarantees) of this section.

(vii) *Reports and Assessments with Respect to Stress Testing*. For a period of not less than six years (the first two years in an easily accessible place), a written copy of the report required under paragraph (c)(8)(ii)(D)(2) of this section and a written record of the assessment required under paragraph (c)(8)(ii)(D)(3) of this section shall be maintained and preserved.

(viii) *Inspection of Records*. The documents preserved pursuant to this paragraph (c)(11) shall be subject to inspection by the Commission in accordance with section 31(b) of the Act (15 U.S.C. 80a-30(b)) as if such documents were records required to be maintained pursuant to rules adopted under section 31(a) of the Act (15 U.S.C. 80a-30(a)). If any action was taken under paragraphs (c)(7)(ii) (with respect to defaulted securities and events of insolvency) or (c)(8)(ii) (with respect to a deviation from the fund's share price of more than 1/2 of 1 percent) of this section, the money market fund will file an exhibit to the Form N-SAR (17 CFR 274.101) filed for the period in which the action was taken describing with specificity the nature and circumstances of such action. The money market fund will report in an exhibit to such Form any securities it holds on the final day of the reporting period that are not Eligible Securities.

(12) *Public Disclosure of Valuations.* The money market fund shall post on its website, for a period of not less than twelve months, beginning no later than the second business day of the month, the fund's schedule of investments, as prescribed by rules 12-12 – 12-14 of Regulation S-X [17 CFR 210.12.-12 – 12-14], as of the last business day of the prior month.

(d) *Maturity of Portfolio Securities.*

For purposes of this section, the maturity of a portfolio security shall be deemed to be the period remaining (calculated from the trade date or such other date on which the fund's interest in the security is subject to market action) until the date on which, in accordance with the terms of the security, the principal amount must unconditionally be paid, or in the case of a security called for redemption, the date on which the redemption payment must be made, except as provided in paragraphs (d)(1) through (d)(8) of this section:

(1) *Adjustable Rate Government Securities*. A Government Security that is a Variable Rate Security where the variable rate of interest is readjusted no less frequently than every 397 calendar days shall be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate. A Government Security that is a Floating Rate Security shall be deemed to have a remaining maturity of one day.

(2) *Short-Term Variable Rate Securities*. A Variable Rate Security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in 397 calendar days or less shall be deemed to have a maturity equal to the earlier of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(3) *Long-Term Variable Rate Securities*. A Variable Rate Security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a Demand Feature, shall be deemed to have a maturity equal to the longer of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(4) *Short-Term Floating Rate Securities*. A Floating Rate Security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in

397 calendar days or less shall be deemed to have a maturity of one day.

(5) *Long-Term Floating Rate Securities.* A Floating Rate Security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a Demand Feature, shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

(6) *Repurchase Agreements.* A repurchase agreement shall be deemed to have a maturity equal to the period remaining until the date on which the repurchase of the underlying securities is scheduled to occur, or, where the agreement is subject to demand, the notice period applicable to a demand for the repurchase of the securities.

(7) *Portfolio Lending Agreements.* A portfolio lending agreement shall be treated as having a maturity equal to the period remaining until the date on which the loaned securities are scheduled to be returned, or where the agreement is subject to demand, the notice period applicable to a demand for the return of the loaned securities.

(8) *Money Market Fund Securities.* An investment in a money market fund shall be treated as having a maturity equal to the period of time within which the Acquired money market fund is required to make payment upon redemption, unless the Acquired money market fund has agreed in writing to provide redemption proceeds to the investing money market fund within a shorter time period, in which case the maturity of such investment shall be deemed to be the shorter period.

(e) *Delegation.*

The money market fund's board of directors may delegate to the fund's investment adviser or officers the responsibility to make any determination required to be made by the board of directors under this section (other than the determinations required by paragraphs (c)(1) (board findings); (c)(7)(ii) (defaults and other events); (c)(8)(i) (general required procedures: Amortized Cost Method); (c)(8)(ii)(A) (shadow pricing), (B) (prompt consideration of deviation), and (C) (material dilution or unfair results); and (c)(9) (required procedures: Penny-Rounding Method) of this section) provided:

(1) *Written Guidelines*. The Board shall establish and periodically review written guidelines (including guidelines for determining whether securities present minimal credit risks as required in paragraph (c)(3) of this section) and procedures under which the delegate makes such determinations:

(2) *Oversight*. The Board shall take any measures reasonably necessary (through periodic reviews of fund investments and the delegate's procedures in connection with investment decisions and prompt review of the adviser's actions in the event of the default of a security or Event of Insolvency with respect to the issuer of the security or any Guarantee to which it is subject that requires notification of the Commission under paragraph (c)(7)(iii) of this section) to assure that the guidelines and procedures are being followed.

3. Section 270.17a-9 is revised to read as follows:

§ 270.17a-9 Purchase of certain securities from a money market fund by an affiliate, or an affiliate of an affiliate.

The purchase of a security from the portfolio of an open-end investment company holding itself out as a money market fund by any affiliated person or promoter of or principal underwriter for the money market fund or any affiliated person of such person shall be exempt from Section 17(a) of the Act (15 U.S.C. 80a-17(a)); provided that:

(a) In the case of a portfolio security that has ceased to be an Eligible Security (as defined in § 270.2a-7 (a)(11), or has defaulted (other than an immaterial default unrelated to the financial condition of the issuer):

(1) The purchase price is paid in cash; and

(2) The purchase price is equal to the greater of the amortized cost of the security or its market price (in each case, including accrued interest).

(b) In the case of any other portfolio security:

(1) The purchase price meets the requirements of paragraph (a)(1) and (2) of this section; and

(2) In the event that the purchaser thereafter sells the security for a higher price than the purchase price paid to the money market fund, the purchaser shall promptly pay to the fund the amount by which the subsequent sale price exceeds the purchase price paid to the fund.

4. Section 270.22e-3 is added to read as follows:

§ 270.22e-3 Exemption for liquidation of money market funds.

(a) A registered open-end management investment company or series thereof ("fund") that is regulated as a money market fund under § 270.2a-7 is exempt from the requirements of section 22(e) of the Act (15 U.S.C. 80a-22(e)) if:

(1) The fund's current price per share calculated pursuant to § 270.2a-7(c) is less than the fund's stable net asset value or price per share;

(2) The fund's board of directors, including a majority of directors who are not interested persons of the fund, has approved the liquidation of the fund; and

(3) The fund, prior to suspending redemptions, notifies the Commission of its decision to liquidate and suspend redemptions, by electronic mail directed to the attention of the Director of the Division of Investment Management or his designee.

(b) Any fund that owns, pursuant to section 12(d)(1)(E) of the Act (15 U.S.C. 80a-12(d)(1)(E)), shares of a money market fund that has suspended redemptions of shares pursuant to paragraph (a) of this section also is exempt from the requirements of section 22(e) of the Act. A fund relying on the exemption provided in this paragraph must promptly notify the Commission that it has suspended redemptions in reliance on this section. Notification under this paragraph shall be made by electronic mail directed to the attention of the Director of the Division of Investment Management or his designee.

(c) For the protection of fund shareholders, the Commission may issue an order to rescind or modify the exemption provided by this section as to that fund, after appropriate notice and opportunity for hearing in accordance with section 40 of the Act (15 U.S.C. 80a-39).

5. Section 270.30b1-5 is revised to read as follows:

§ 270.30b1-5 Quarterly report.

Every registered management investment company, other than a small business investment company registered on Form N-5 (§§ 239.24 and 274.5 of this chapter), shall file a quarterly report on Form N-Q (§§ 249.332 and 274.130 of this chapter) not more than 60 days after the close of the first and third quarters of each fiscal year. A registered management investment company that has filed a registration statement with the Commission registering its securities for the first time under the Securities Act of 1933 is relieved of this reporting obligation with respect to any reporting period or portion thereof prior to the date on which that registration statement becomes effective or is withdrawn. A registered management investment company regulated as a money market fund under § 270.2a-7 is relieved of the reporting obligation required pursuant to Item 1 of Form N-Q.

6. Section 270.30b1-6 is added to read as follows:

§ 270.30b1-6 Monthly report for money market funds.

Every registered open-end management investment company, or series thereof, that is regulated as a money market fund under § 270.2a-7 must file with the Commission a monthly report of portfolio holdings on Form N-MFP no later than the second business day of each month.

PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

7. The authority citation for Part 274 continues to read in part as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78*l*, 78m, 78n, 78o(d), 80a-8, 80a-24, 80a-26, and 80a-29, unless otherwise noted.

8. Section 274.201 and Form N-MFP are added to read as follows:

§ 274.201 Form N-MFP, Portfolio Holdings of Money Market Funds

This form shall be used by registered management investment companies that are regulated as money market funds under § 270.2a-7 of this chapter to file reports pursuant to § 270.30b1-6 of this chapter not later than two business days after the end of each month.

Note: The text of Form N-MFP will not appear in the Code of Federal Regulations.

FORM N-MFP

MONTHLY SCHEDULE OF PORTFOLIO HOLDINGS

OF MONEY MARKET FUNDS

Form N-MFP is to be used by open-end management investment companies, or series thereof, that are regulated as money market funds under § 270.2a-7 ("money market funds"), to file reports with the Commission, not later than the second business day of each month, pursuant to rule 30b1-6 under the Investment Company Act of 1940 (17 CFR 270.30b1-6). The Commission may use the information provided on Form N-MFP in its regulatory, disclosure review, inspection, and policymaking roles.

GENERAL INSTRUCTIONS

A. Rule as to Use of Form N-MFP

Form N-MFP is the public reporting form that is to be used for monthly reports of money market funds under section 30(b) of the Investment Company Act of 1940 (the "Act") and rule 30b1-6 of the Act (17 CFR 270.30b1-6). Form N-MFP must be filed no later than the second business day of each month, and will contain certain information about the money market fund and its portfolio holdings as of the last business day of the preceding month.

B. Application of General Rules and Regulations

The General Rules and Regulations under the Act contain certain general requirements that are applicable to reporting on any form under the Act. These general requirements should be carefully read and observed in the preparation and filing of reports on this form, except that any provision in the form or in these instruction shall be controlling.

C. Filing of Form N-MFP

A money market fund must file Form N-MFP no later than the second business day of each month, in accordance with rule 232.13 of Regulation S-T. Form N-MFP must be filed electronically using the Commission's EDGAR system.

D. Paperwork Reduction Act Information

A registrant is not required to respond to the collection of information contained in Form N-MFP unless the Form displays a currently valid Office of Management and Budget ("OMB") control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to the Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. 3507.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM N-MFP
MONTHLY SCHEDULE OF PORTFOLIO HOLDINGS
OF MONEY MARKET FUNDS

Date of Filing:

Report for [Month, Day, Year]

Name and Address of Fund or Portfolio Filing This Report:

CIK Number:

SEC File Number:

EDGAR Series Identifier:

Number of share classes offered:

Check here if Amendment [ ]

Amendment Number:

Is this an Initial Filing? [Y/N]

Is this a Final Filing? [Y/N]

Is the fund liquidating? [Y/N]

Is the fund merging with another fund? [Y/N]

If so, please identify the other fund by name, SEC File Number, and EDGAR Series Identifier.

Is the fund being acquired by another fund? [Y/N]

If so, please identify the acquiring fund by name, SEC File Number, and EDGAR Series Identifier.

Part I: Information about the Fund

Item 1. Name of Investment Adviser.

a. SEC file number of Investment Adviser.

Item 2. Name of Sub-Adviser. If a fund has multiple sub-advisers, disclose the name of all sub-advisers to the fund.

a. SEC file number of Sub-Adviser. Disclose the SEC file number of each sub-adviser to the fund.

Item 3. Independent Auditor.

Item 4. Administrator.

Item 5. Transfer Agent.

a. SEC file number of Transfer Agent.

Item 6. Minimum initial investment.

Item 7. Is this a feeder fund? [Y/N]

a. If this is a feeder fund, identify the master fund.

b. SEC File Number of the master fund.

Item 8. Is this a master fund? [Y/N]

a. If this is a master fund, identify all feeder funds.

b. SEC File Number of each feeder fund.

Item 9. Is this portfolio primarily used to invest cash collateral? [Y/N]

Item 10. Is this portfolio primarily used to fund variable accounts? [Y/N]

Item 11. Category. Indicate whether the money market fund is a Treasury, Government/Agency, Prime, Tax-Free National, or Tax-Free State Fund.

Item 12. Total value of the portfolio at cost, to the nearest hundredth of a cent.

Item 13. Net value of other assets and liabilities, to the nearest hundredth of a cent.

Item 14. Net asset value per share for purposes of distributions, redemptions, and repurchase, to the nearest hundredth of a cent.

Item 15. Net shareholder flow activity for the month ended (subscriptions less redemptions).

Item 16. Dollar weighted average maturity. Calculate the dollar weighted average maturity of portfolio securities, based on the time remaining until the next interest rate re-set.

Item 17. Dollar weighted average life maturity. Calculate the dollar weighted average maturity of portfolio securities based on final legal maturity or demand feature.

Item 18. 7-day gross yield. Based on the 7 days ended on the last day of the prior month, calculate the Fund's yield by determining the net change, exclusive of capital changes and income other than investment income, in the value of a hypothetical pre-existing account having a balance of one share at the beginning of the period and dividing the difference by the value of the account at the beginning of the base period to obtain the base period return, and then multiplying the base period return by (365/7) with the resulting yield figure carried to at least the nearest hundredth of one percent. The 7-day gross yield should not reflect a deduction of shareholders fees and fund operating expenses.

Part 2: Schedule of Portfolio Securities. For each security held by the money market fund, please disclose the following:

Item 19. The name of the issuer.

Item 20. CIK number of the issuer.

Item 21. The title of the issue.

Item 22. The CUSIP.

Item 23. Other unique identifier (if the instrument does not have a CUSIP).

Item 24. The category of investment. Please indicate the category that most closely identifies the instrument from among the following: Treasury Debt; Government Agency Debt; Variable Rate Demand Notes; Other Municipal Debt; Financial Company Commercial Paper; Asset Backed Commercial Paper; Certificate of Deposit; Structured Investment Vehicle Notes; Other Notes; Treasury Repurchase Agreements; Government Agency Repurchase Agreements; Other Repurchase Agreements; Insurance Company Funding Agreements; Investment Company; Other Instrument.

Item 25. Rating. Please indicate whether the security is a 1st tier security, unrated, or no longer eligible.

Item 26. Requisite NRSROs.

a. Identify each Requisite NRSRO.

b. For each Requisite NRSRO, disclose the credit rating given by the Requisite NRSRO.

Item 27. The maturity date as determined under rule 2a-7. Disclose the maturity date, taking into account the maturity shortening provisions of rule 2a-7.

Item 28. The final legal maturity date.

Item 29. Is the maturity date extendable? [Y/N]

Item 30. Does the security have a credit enhancement? [Y/N]

Item 31. For each credit enhancement, disclose:

a. The type of credit enhancement.

b. The identity of the credit enhancement provider.

c. The credit rating of the credit enhancement provider.

Item 32. Does the security have an insurance guarantee? [Y/N]

Item 33. For each insurance guarantee provider, disclose:

a. The identity of the insurance guarantee provider.

b. The credit rating of the insurance guarantee provider.

Item 34. Does the security have a liquidity provider? [Y/N]

Item 35. For each liquidity provider, disclose:

a. The identity of the liquidity provider.

b. The credit rating of the liquidity provider.

Item 36. The principal amount of the security.

Item 37. The current amortized cost, to the nearest hundredth of a cent.

Item 38. Is this a Level 1, Level 2, or Level 3 security, or Other? Please explain how the security was valued. Level 1 securities are valued based on quoted prices in active markets for identical securities. Level 2 securities are valued based on other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, credit risks, etc.). Level 3 securities are valued based on significant unobservable inputs (including the fund's own assumptions in determining the fair value of investments). *See* Statement of Financial Accounting Standards Board No. 157, "Fair Value Measurement."

Item 39. The percentage of the money market fund's gross assets invested in the security, to the nearest hundredth of one percent.

Item 40. Explanatory notes. Please disclose any other information that may be material to other disclosure in the Form.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Dated: June 30, 2009

Commissioner Aguilar and
Commissioner Paredes
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
June 30, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13532

In the Matter of

Prime Capital Services, Inc.,
Gilman Ciocia, Inc.,
Michael P. Ryan,
Rose M. Rudden,
Christie A. Andersen,
Eric J. Brown,
Matthew J. Collins,
Kevin J. Walsh,
Mark W. Wells,

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 203(f) 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 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 203(f) of the Investment Advisers Act of 1940 ("Advisers Act"), against Prime Capital Services, Inc. ("PCS"), Gilman Ciocia, Inc. ("G&C"), Michael P. Ryan ("Ryan"), Rose M. Rudden ("Rudden"), Christie A. Andersen ("Andersen"), Eric J. Brown ("Brown"), Matthew J. Collins ("Collins"), Kevin J. Walsh ("Walsh") and Mark W. Wells ("Wells").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Gilman Ciocia, Inc. ("G&C"), is an income tax preparation business headquartered in Poughkeepsie, New York. It also offers financial services in New York, New Jersey, Pennsylvania and Florida through its wholly-owned subsidiaries, Prime Capital Services, Inc. ("PCS"), a broker-dealer registered with the Commission, and Asset & Financial Planning, Ltd. ("AFP"), an investment adviser registered with the Commission. All the individual respondents were employees of G&C during the time of the conduct at issue in these proceedings. In fiscal year 2007, approximately ninety percent of G&C's revenue was derived from commissions and fees from financial services, including commissions from sales of variable annuities, and the remaining approximately ten percent of revenue was derived from tax preparation and accounting services. G&C was registered with the Commission as an investment adviser from 2000 through 2006. G&C's common stock is quoted on the OTC Bulletin Board under the symbol "GTAX."

2. Prime Capital Services, Inc. ("PCS") is a wholly-owned subsidiary of G&C that provides securities brokerage services. It is registered with the Commission as a broker-dealer and is a member of the Financial Industry Regulatory Authority ("FINRA"). All the individual respondents were associated with PCS during the time of the conduct at issue in these proceedings. A significant percentage of the revenue generated by PCS from 1999 through February 2007 came from sales of variable annuities. PCS operates under a management agreement with G&C under which PCS remits revenues to G&C, and G&C pays various expenses for PCS including personnel compensation, training, and marketing costs associated with free-lunch seminars that are provided by PCS's registered representatives and are used to recruit new customers. Prior to November 2003, marketing for the seminars was provided by G&C's in-house telemarketing department; since November 2003, G&C has paid for marketing and PCS has reimbursed G&C pursuant to the management agreement. PCS and G&C consolidate their financial statements and are under common control.

3. Michael P. Ryan ("Ryan"), 51, of Poughkeepsie, New York, has been the president of PCS and AFP since at least 2000, and the president and chief executive officer of G&C since 2002. Since 2000, Ryan has worked with the successive chief compliance officers of PCS, who have reported to him. Ryan also was directly involved with state licensing issues of certain registered representatives. Ryan is licensed to sell securities and as a general securities principal.

4. Rose M. Rudden ("Rudden"), 57, of Hyde Park, New York, started work in PCS's compliance department in 2001 and has been serving as the most senior compliance officer since 2004, although she did not officially take the title of chief compliance officer until April 2005. She supervises compliance department employees in Poughkeepsie, and supervisors and registered representatives in offices around the country, including Florida. Rudden is licensed to sell securities and as a securities principal. She is an employee of G&C and also serves as AFP's chief compliance officer.

5. Christie A. Andersen ("Andersen"), 39, of Green Acres, Florida, joined PCS's Boca Raton branch office in 2002 as a compliance officer and became the supervisor of the office in 2004. As a supervisor, she reviewed and approved variable annuity transactions for Respondent Mark W. Wells and others until she left PCS in October 2006. While at PCS, Andersen was an employee of G&C and was licensed to sell securities and as a securities principal. In addition, since leaving PCS, Andersen has been a representative of an investment adviser and its chief compliance officer.

6. Eric J. Brown ("Brown"), 40, of Highland Beach, Florida was a registered representative associated with PCS in its Delray Beach and Boynton Beach offices from 1998 until March 2006. Brown was an employee of G&C during his tenure at PCS. While associated with PCS, Brown was the subject of a multi-phase regulatory action by the State of Florida Department of Financial Services, including revocation of his insurance license in December 2003, reinstatement of his insurance license in April 2004 with restrictions prohibiting sales of variable annuities to new customers over the age of 65, and permanent revocation of his license to sell insurance in January 2006. FINRA barred Brown from association with a broker-dealer as of October 5, 2007.

7. Matthew J. Collins ("Collins"), 37, of Boynton Beach, Florida has been a registered representative associated with PCS in its Delray Beach and Boynton Beach offices since 2001 and was Respondent Brown's supervisor from September 2002 until early 2005. Collins is an employee of G&C and a licensed representative of AFP. He also is licensed to sell securities and as a securities principal, in addition to having state insurance licenses. The State of Florida Department of Financial Services placed Collins on probation for one year starting in December 2006 and fined him $5,000 after a settled proceeding in which it alleged Collins made misrepresentations on insurance applications, specifically, that he represented that he was the sales agent on variable annuity transactions that Respondent Brown actually had solicited.

8. Kevin J. Walsh ("Walsh"), 42, of Viera, Florida was a registered representative associated with PCS in its Melbourne, Florida office from 1998 to 2007. He was an employee of G&C during his association with PCS, and also a representative of AFP. Walsh is licensed to sell securities.

9. Mark W. Wells ("Wells"), 42, of Boca Raton, Florida has been a registered representative associated with PCS in the Boca Raton office since May 2001. Wells, an employee of G&C and representative of AFP, is licensed to sell securities.

B. FRAUDULENT SALES OF VARIABLE ANNUITIES TO SENIORS AND FAILURE TO SUPERVISE VARIABLE ANNUITY TRANSACTIONS

Overview of Fraudulent Sales Practices

1. From approximately November 1999 through February 2007 (the "relevant period"), representatives associated with Respondent PCS offered and sold variable annuities to senior citizen customers in south Florida. At various times during the relevant period, Respondents

Brown, Collins, Walsh and Wells, while associated with PCS and employed by Respondent G&C, were among those offering and selling variable annuities to senior citizens. Most of their customers had attended G&C's free-lunch seminars in south Florida communities, during which the four representatives touted PCS's financial services in general and, during most of the relevant period, variable annuities in particular. The seminar script, which the representatives used during their presentations, had been provided to them by PCS.

2. Variable annuities are long-term investments with an insurance component. The insurance component provides a death benefit for the owner's beneficiaries, guaranteeing that they will receive at least the amount of principal the owner invested (excluding any withdrawals or outstanding loans), regardless of the variable annuity's investment value at the time of the insured person's death. As with other life insurance products, earnings accumulate on a tax deferred basis and are taxed as ordinary income upon withdrawal. Each variable annuity contract includes subaccounts which have investment strategies similar to retail mutual funds, such as growth, speculation or money market. Variable annuity issuers charge fees that include annual mortality, expense and administrative fees, as well as fees for the management of the subaccounts by investment advisers. The variable annuities Respondents Brown, Walsh and Wells sold were also structured so that a sales charge was not incurred upon purchase but was instead charged if, during the first six to eight years, the owner surrendered the contract for cash, withdrew funds above a certain amount from the account, or exchanged the variable annuity for another annuity. Those charges, called surrender charges, were highest during the initial years of the variable annuity, typically starting at approximately six to eight percent of the amount the customer invested. The charges decreased over the surrender period. The owner of a variable annuity contract can reallocate his or her investment among the available subaccounts offered through the variable annuity without incurring surrender charges.

3. During some or all of the relevant period, Respondents Brown, Walsh and Wells induced customers into purchasing variable annuities by means of material misrepresentations and omissions. For example: these representatives sometimes told customers that the principal invested in the variable annuity was guaranteed not to lose money, without disclosing that the guarantee was triggered by the death of an annuitant, and without disclosing that until the annuitant's death the value could fluctuate and decline; they sometimes promised customers that the customers would receive a guaranteed return on their investment without disclosing that such return would be paid only over the course of the annuitization period if, in the future, the customers elected to annuitize; they sometimes told customers they would have access to their invested money whenever they needed it, omitting to tell them about charges for early withdrawals above a certain amount; they often failed to disclose to customers the ownership costs of variable annuities, which in some cases were more than three percent annually of the invested amount. Certain written disclosures provided to customers, and other records in customers' files, were incomplete and/or inaccurate, and in some cases were altered after the customer signed to make it appear that disclosures had been provided and that the sales were suitable when, in fact, they were not.

4. Many of the variable annuities sold by Respondents Brown, Walsh and Wells were unsuitable investments based on the customers' ages, incomes, liquid assets and

investment objectives. For example, because of their advanced age, some customers who wanted full access to their money were unlikely to outlive the period during which they would pay surrender fees on their variable annuities, and other customers were induced to invest more than seventy-five percent of their liquid assets in variable annuities with limitations and/or fees on withdrawals. In addition, variable annuities limited access to the invested principal that was expressly contrary to some customers' objectives for their money.

5. During times when Florida authorities had revoked or restricted Respondent Brown's license to sell insurance, Respondent Collins signed as the associated person on the account for variable annuities Brown solicited. Thus, on paperwork for the customer and the variable annuity issuing company, Collins misrepresented who sold the variable annuity.

6. Compared to other investment products, which generally paid less than three percent in sales commissions, the variable annuities sold by Respondents Brown, Collins, Walsh and Wells generally paid approximately a six percent gross sales commission to Respondent PCS. As compensation, PCS typically paid out approximately half of the sales commission to Brown, Collins and Walsh, and as much as seventy percent of the sales commission to Wells. During the relevant period, PCS, Brown, Walsh and Wells each earned millions of dollars in sales commissions from variable annuity transactions, and Collins earned hundreds of thousands of dollars.

7. During the relevant period, based on the recommendations of Respondents Brown, Walsh and Wells, at least twenty-three customers were induced to buy at least thirty-five variable annuities, investing an aggregate of nearly $5 million.

8. Most of twenty-three customers who bought variable annuities from Respondents Brown, Walsh and Wells met these registered representatives at free-lunch seminars that Respondent G&C marketed and arranged. At the free-lunch seminars, Brown, Walsh and Wells discussed tax and financial planning, including during most of the relevant period, variable annuities. After the seminars, the customers were invited to schedule private appointments with Brown, Walsh and Wells. The variable annuities were sold in one-on-one sales meetings at Respondent PCS's offices in Delray Beach, Boynton Beach, Melbourne and/or Boca Raton, Florida.

9. Respondent G&C's free-lunch seminars were instrumental in providing a steady stream of variable annuity customers to Respondents PCS, Brown, Walsh and Wells. G&C arranged and marketed the seminars, including identifying prospective customers, sending them invitations, otherwise advertising the seminars, preparing presentation materials, and training PCS representatives to make seminar presentations. Many members of the public who attended seminars ultimately purchased variable annuities through PCS representatives, including Brown, Walsh and Wells, and those representatives recruited almost all their customers at G&C's free-lunch seminars.

Overview of Failure to Supervise Variable Annuity Transactions

10 From at least 1999 through 2007, Respondent Ryan was the president of Respondent PCS. From at least 2004 through 2007, Respondent Rudden was the highest ranking compliance officer, who also participated in branch examinations and reviews of variable annuity transactions. Ryan and Rudden had supervisory authority over the other individual respondents because they had the ability to control the other individual respondents' conduct by, among other things, terminating their employment, withholding their compensation, levying fines, requiring heightened supervision if they determined there was a need of closer oversight, or any combination of those and other measures.

11. Respondent PCS had written supervisory procedures, including procedures specifically pertaining to the sale and supervisory review of variable annuity transactions. Respondent Ryan, as PCS's president, was responsible for implementing PCS's written supervisory procedures. However, neither Ryan nor PCS put systems in place to implement many of the written supervisory procedures. Therefore, PCS's and Ryan's supervision of Brown, Collins, Walsh and Wells could not reasonably be expected to detect or prevent their violations of the federal securities statutes, rules and regulations.

12. At times during the relevant period, Respondent Andersen was the direct supervisor for Respondent Wells and Respondent Collins was the direct supervisor for Respondent Brown. As supervisors, Andersen and Collins were responsible for reviewing variable annuity transactions for suitability and approving them if they were suitable or rejecting them if they were not. Andersen approved certain variable annuity transactions of Wells' and failed to review others. Collins failed to review Brown's variable annuity transactions.

13. During all or part of the relevant period, Respondents Ryan, Rudden, Andersen and Collins failed to respond reasonably to red flags of wrongdoing in the variable annuity sales practices of Respondents Brown, Walsh and/or Wells, and thereby failed to detect or prevent Brown's, Walsh's and/or Wells' violations of the federal securities statutes, rules and regulations.

Variable Annuity Sales at PCS's Delray Beach and Boynton Beach Branch Offices

14. Respondent Brown's misrepresentations to variable annuity customers included misleading statements and material omissions about access to invested money, guaranteed minimum returns and/or guarantees against losses. Some of Brown's customer files included inaccurate information about customers' net worth, liquid assets and/or income.

15. Respondent Brown made material misrepresentations and omissions, and/or sold unsuitable variable annuities to senior citizen customers, including in the following instances:

a. In 2000 and 2001, Respondent Brown induced an elderly couple into buying at least ten variable annuities, including several that were purchased by partially surrendering the variable annuity contracts Brown sold them a year earlier. The purchases and redemptions generated more than $50,000 in sales commissions for PCS, of which more than $20,000 was paid out to Respondent Brown. As a result of the transactions, more than three-quarters of the couple's liquid assets was invested in illiquid variable annuities. No supervisor reviewed or approved the transactions.

b. In 1999 and 2000, Respondent Brown induced a 76-year-old widow to rearrange her diversified portfolio of stocks and bonds so that eighty percent of her assets was invested in variable annuities with surrender periods during which time access to her money would be limited. The concentration in variable annuities was unsuitable and contrary to the customer's investment objectives. The sales generated approximately $16,000 in commissions for Brown and approximately the same amount in net commissions to Respondent PCS. Among the transactions Brown orchestrated was the purchase of a variable annuity and its subsequent liquidation for reinvestment in another variable annuity at a cost of $20,000 in surrender charges for the early withdrawal. No supervisor reviewed or approved the transactions.

c. In 2000, Respondent Brown induced a 68-year-old widow to use money from a maturing bank certificate of deposit to buy a variable annuity in her retirement account. Documents surrounding the variable annuity investment included a forged customer signature with the customer's name misspelled. Respondents Ryan and Rudden later confirmed with a handwriting expert that the customer's signature was not genuine. Brown earned approximately $3,000 in sales commissions and Respondent PCS earned slightly more. No supervisor reviewed or approved the transaction.

d. In 2001, Respondent Brown induced a 79-year-old customer to partially redeem a variable annuity to fund a new variable annuity purchase. The exchange caused the customer to lose approximately $20,000 worth of the death benefit in the original variable annuity. When the customer noticed it, he was within the time period to reverse the transaction at no cost and instructed Brown to do so. Brown delayed. The customer died. The customer's widow lost approximately $20,000 in death benefit due to Brown's misconduct. No supervisor reviewed or approved the exchange that caused the customer to lose approximately $20,000 worth of death benefits.

16. Respondent Collins, who was Respondent Brown's supervisor from 2002 to 2005, failed to review or approve variable annuity business Brown wrote. Respondent Rudden was advised of this in an October 2003 branch exam that noted Collins' failure to supervise Brown.

17. In December 2003, the State of Florida Department of Financial Services revoked Respondent Brown's license to sell insurance. In April 2004, Brown consented to reinstatement of his insurance license with a restriction that prohibited him from marketing variable annuities to new customers over the age of 65. During the period when his license was revoked or restricted, Brown continued to solicit variable annuity business including to customers over the age of 65. Respondent Collins, who was Brown's supervisor at those times, knew of the revocation and subsequent restriction and took no action to curtail Brown's activities. In fact, for new variable annuity customers over the age of 65 whom Brown solicited in violation of his licensing restriction, Collins signed the paperwork and misrepresented himself as the associated

person on the account. In addition, Respondents Ryan and Rudden knew of Brown's solicitations during the period when his license was revoked and/or restricted but did not take action to stop his marketing activities. It was not until February 2005 that they placed him on "heightened supervision," requiring that Brown's variable annuity sales be reviewed before being submitted to the variable annuity issuing companies.

18. Monthly reports in 2004 and annual branch exams from the Delray Beach and Boynton Beach offices from 2003 through 2006, which Respondent Rudden reviewed, included descriptions of disclosure and documentation deficiencies and details of Respondent Brown's unsuitable variable annuity sales to senior citizen investors. For example, branch exams revealed that for Brown's variable annuity transactions, disclosure forms were missing or missing key information, that elderly customers had invested high percentages of their liquid assets in illiquid variable annuities, and that no supervisor had reviewed certain transactions. The monthly reports Collins submitted to Rudden's compliance department in 2004, and an evaluation of Brown's free-lunch seminar that Rudden reviewed, also indicated that during times when Brown's insurance license was revoked or restricted, he continued to market variable annuities at G&C's free-lunch seminars without regard to specific, state-imposed limitations on his marketing activities.

19. Brown and Collins made material misrepresentations and omissions, and/or sold unsuitable variable annuities to senior citizen customers, including in the following instances:

a. In 2005, Respondent Brown recommended to a disabled customer's father the he invest all of his son's liquid assets in a variable annuity with an eight-year surrender period. The disabled customer had an annual income of approximately $13,000, and was neither consulted on the investment nor signed any of the forms authorizing it. Brown knew the customer's father had signed his son's name on the forms. Respondent Collins purported to guarantee the customer's signature, although neither he nor Brown had ever met the customer, or had seen any documentation verifying the customer's signature. A supervisor approved the transaction.

b. In 2004 and 2005, Respondent Brown induced an octogenarian couple to exchange six variable annuities that they owned for six others that Brown recommended, costing them more than $61,000 in surrender fees. At the time, Brown was prohibited by state orders from marketing variable annuities to new customers over the age of 65, and Respondent Collins signed as the associated person on the account for the transactions. A supervisor approved the transactions after discussing them with Respondent Rudden.

c. In 2004, Respondent Brown induced a septuagenarian couple to buy two variable annuities at a time when Brown's insurance license was revoked. Brown's name and representative information is crossed out on the paperwork for the transactions, and Respondent Collins, who was Brown's supervisor at the time, signed as the associated person on the account. Brown initially was credited with the sales commission of more than $5,000. No other supervisor reviewed or approved the transactions.

d. In 2004, Respondent Brown induced a 72-year-old customer to buy a variable annuity at a time when Brown was prohibited from marketing variable annuities to new customers over the age of 65. Respondent Collins' name, information and signature appear on the paperwork for the customer's transaction as the associated person on the account in places where Brown's information is crossed out, and Collins earned a sales commission of more than $1,000. Collins was Brown's supervisor at the time of the transaction, but no other supervisor reviewed or approved the transaction.

Variable Annuity Sales at PCS's Melbourne, Florida Branch Office

20. During the time period from late 2003 through 2004, Respondent Walsh refused to submit most of his variable annuity business to his supervisor for review, which violated Respondent PCS's written supervisory procedures. Walsh's supervisor complained numerous times about Walsh's misconduct to Respondent Rudden, who acknowledged the problem and involved Respondent Ryan in addressing the behavior. During the time period when Walsh refused to submit his variable annuity business for supervisory review, Respondents Rudden did not curtail Walsh's sales activities; Walsh continued to sell hundreds of variable annuities during that time. Rudden took no remedial action against Walsh for his misconduct. Walsh earned approximately $385,000 in sales commissions from his variable annuities business in 2004, and PCS retained approximately the same amount from those transactions.

21. Respondent Walsh's misrepresentations to variable annuity customers included misleading statements and material omissions about access to invested money, guaranteed minimum returns and/or guarantees against losses. In some cases, Walsh selected subaccount allocations for the variable annuity investments that were inconsistent with customers' investment objectives. Some of Walsh's customer files included inaccurate information about customers' net worth, liquid assets and/or income.

22. Branch exams from the Melbourne office from 2003 through 2006, which Respondent Rudden reviewed, included details of unsuitable variable annuity sales to senior citizen investors. For example, branch exams reflected that Walsh's business was almost exclusively selling variable annuities to senior citizens, and investing high percentages of those elderly customers' liquid assets in illiquid variable annuities. The branch exams also reflected missing explanations of investments, missing disclosures – including costs associated with variable annuities – and purported disclosures that customers had not acknowledged receiving.

23. Walsh made material misrepresentations and omissions, and/or sold unsuitable variable annuities to senior citizen customers, including in the following instances:

a. In 2005, Respondent Walsh induced a 69-year-old customer to convert her two retirement portfolios into two variable annuities with seven-year surrender periods during which access to her money was limited. Although the customer wanted to participate in market returns, Walsh invested her entirely in money market subaccounts within her two variable annuities. The customer's paperwork contains multiple inaccuracies, including the purported issuance of a prospectus dated several months after the transaction, and a length of investment experience that would have required the customer to have started investing at age eleven. Walsh earned nearly $6,000 in sales commissions. More than a month after the transaction, a supervisor retroactively approved one of the two variable annuities the customer bought. His approval was based on the tax benefits of the investment, even though the assets had previously been in a tax-advantaged retirement account. No supervisor reviewed or approved the other variable annuity.

b. In 2004, Respondent Walsh induced an octogenarian customer to invest $100,000 – or about seventy-five percent of her liquid assets – in a variable annuity, earning Walsh more than $2,000 in sales commissions. A supervisor retroactively approved the transaction months after the sale on grounds that did not apply to the customer's circumstances, including that the customer, who was already in the lowest tax bracket, would benefit from tax deferral available for a variable annuity.

c. In 2004 and 2005, Respondent Walsh induced a 77-year-old customer to invest in two variable annuities, earning Walsh and PCS nearly $8,000 each in sales commissions. After the customer learned of an annual administrative charge that he said Walsh did not disclose at the time of sale, the customer terminated his investments and paid $12,000 in early withdrawal charges. Disclosure forms in the customer's file indicate that after the customer signed them, Walsh added information about fees and other terms of the investment. The transactions were retroactively approved by a supervisor months after the sales.

d. In 2001, Respondent Walsh induced an 80-year-old customer to invest more than three quarters of his liquid assets in variable annuities. Walsh earned more than $6,000 in sales commissions in transactions that were unreviewed by a supervisor, and limited the customer's access to his money for eight years.

Variable Annuity Sales at PCS's Boca Raton, Florida Office

24. Respondent Wells' misrepresentations to variable annuity customers included misleading statements and material omissions about access to invested money, guaranteed minimum returns and/or guarantees against losses. Some of Wells' customer files included inaccurate information about customers' net worth, liquid assets and/or income.

25. Annual branch exams from the Boca Raton office from 2004 through 2006, which Respondent Rudden reviewed, included details of unsuitable variable annuity sales to senior citizen investors, including high percentages of elderly customers' liquid assets invested in illiquid variable annuities, and ongoing deficiencies in disclosure forms provided to customers to explain the terms of their variable annuity investments. In addition, net worth figures frequently matched figures for liquid assets, even where customers already owned variable annuities.

26. Respondent Andersen, who reviewed the 2004 and 2005 Boca Raton branch exams, advised Respondent Rudden in 2004 that she was having difficulty managing her duties as supervisor for Respondent Wells and others, and sought assistance reviewing variable annuity transactions for suitability. Rudden took no action in response to Andersen's concerns, which left Wells and others with supervision Andersen indicated was inadequate.

27. Paperwork for Respondent Wells' variable annuity customers contain patterns that indicate the sales were unsuitable for individual customers' needs and circumstances. As one example, Wells' customer disclosure forms acknowledging understanding of the terms of the investment were initialed by Wells' assistant, not the customers. This is evident from the handwriting of the initials, which belonged to Wells' sales assistant and bears no resemblance to the customers' authentic signatures. As another example, explanations of the reason for investing in variable annuities are not initialed by customers, as required by the firm's form. Respondent Andersen did not follow up on these patterns, make inquiries or take any remedial action.

28. Wells made material misrepresentations and omissions, and/or sold unsuitable variable annuities to senior citizen customers, including in the following instances:

a. In 2004 and 2005, Respondent Wells induced a 71-year-old woman to liquidate her retirement account and invest all of her retirement savings – which was more than half her net worth – in variable annuities. Wells earned more than $5,000 in sales commissions. Andersen approved some of the transactions, but others were unreviewed by a supervisor.

b. In 2004 and 2005, Respondent Wells induced a 65-year-old retiree into buying six variable annuities in his trading and retirement accounts, thereby subjecting the customer to limitations for eight years on about two-thirds of his liquid assets. Wells earned more than $16,000 in sales commissions. Andersen approved some of the transactions, but others were unreviewed by a supervisor.

c. In 2006, Respondent Wells induced an 80-year-old widow to exchange a variable annuity that was out of its surrender period for a new one that limited her access to half her net worth for six years. Wells earned more than $6,000 in sales commissions. Despite a comparison that showed the customer's new annuity would cost more in fees and be worth less in the future than her old one, and despite the customer's age and concentration of her net worth in the variable annuity, Andersen approved the transaction as suitable.

d. In 2003 and 2004, Respondent Wells induced a 67-year-old widow to invest nearly eighty percent of her liquid assets in variable annuities with surrender periods as long as eight years, earning nearly $15,000 in sales commissions. Wells' assistant discouraged the customer from seeking a comparison form that Florida requires be offered to variable annuity customers by instructing her to initial a box declining the comparison; neither Wells nor Respondent Andersen questioned the sales assistant's written indication that the customer should decline the comparative information form. Paperwork in the customer's file indicates signed documents were copied and altered. Andersen approved some of the transactions, but others were unreviewed by a supervisor.

e. In 2007, Respondent Wells induced a septuagenarian couple to invest $100,000 of their approximately $148,000 in liquid assets in a variable annuity with a seven-year surrender period, earning him more than $3,000 in sales commissions. The transaction was approved by a supervisor.

f. In 2006, Respondent Wells induced a retired couple to buy matching variable annuities, generating for himself more than $4,000 in sales commissions. The customers did not understand the fee structure of their investments, and were misled regarding the returns they could expect. The transactions were approved by a supervisor after the application was submitted to the variable annuity issuing company.

Supervisory Failures of Respondents PCS, Ryan, Rudden, Andersen and Collins

29. Respondent PCS had written supervisory procedures, including some specifically pertaining to the sale and supervisory review of variable annuity transactions. Respondent Ryan, as PCS's president, was responsible for implementing PCS's written supervisory procedures. However, neither Ryan nor PCS had a system in place to implement the written supervisory procedures. Therefore, Ryan's and the firm's supervision of Brown, Collins, Walsh and Wells could not reasonably be expected to detect or prevent their violations of the federal securities statutes, rules and regulations. For example, PCS and Ryan failed to implement the firm's written supervisory procedures in the following ways:

a. Respondents PCS and Ryan failed to implement a system for review and follow-up of branch exams that reasonably could have been expected to detect and prevent violations of the federal securities laws by Respondents Brown, Collins, Walsh and Wells. Respondents Rudden and Andersen reviewed branch exams from Delray Beach, Boynton Beach, Melbourne and/or Boca Raton that included repeated indications of fraudulent and/or unsuitable variable annuity sales by Brown, Collins, Walsh and/or Wells, such as missing or deficient disclosure documents, patterns of similar customer profiles for which variable annuities were not suitable, and repeated instances of elderly customers investing large percentages of their assets in variable annuities.

b. Respondents PCS and Ryan failed to implement a system for supervisory review and approval of variable annuity transactions that reasonably could have been expected to detect and prevent violations of the federal securities laws by Respondents Brown, Collins, Walsh and Wells. Brown, Collins, Walsh and Wells sold many variable annuities that were never reviewed by a supervisor, or were not reviewed by a supervisor until long after the transaction. Certain variable annuity transactions of Brown, Walsh and Wells were unsuitable based on information in the customers' files.

c. Respondents PCS and Ryan failed to implement a system for responding to customer complaints that reasonably could have been expected to detect and prevent violations of the federal securities laws by Respondents Brown, Collins and Walsh. Variable annuity customers of Brown and Walsh sent numerous complaints to the firm, regarding, among other things, the unsuitability of their investments, misrepresentations and omissions during sales meetings, and in one instance, forgery. Respondent Rudden, who drafted many of the replies to customers, inadequately investigated the complaints and instead relied on the statements of Brown, Collins and Walsh, who had no oversight in responding to customers' complaints of their variable annuity sales practices. While PCS documented the complaints and replies, there was no action by the firm in response to complaints that reasonably would have led to detection and prevention of securities law violations by Brown, Collins and Walsh.

d. Respondents PCS and Ryan failed to implement a system to comply with state regulatory orders, such as the revocation and restriction of Respondent Brown's insurance license. Had PCS and Ryan implemented a system to enforce the restriction on Brown's sales of variable annuities, it is likely that Brown's fraudulent sales of variable annuities would have been prevented and detected.

e. Respondents PCS and Ryan also failed to implement a reasonable system for supervision of Respondent Brown, including failure to devote adequate resources to his supervision. In particular, Ryan unreasonably delegated Brown's supervision from 1999 to 2001 to a former chief compliance officer at PCS. The former chief compliance officer complained to Ryan that she was having difficulty managing her dual responsibilities as chief compliance officer and Brown's supervisor, and told Ryan that she needed help supervising Brown effectively. Ryan's delegation to her while she was burdened with compliance responsibilities was unreasonable because she told him she was overwhelmed by her duties, and he failed to follow up to determine whether the delegated responsibilities were being exercised diligently.

30. Respondent Ryan, from 2000 through 2006, failed to respond reasonably to red flags of wrongdoing in the variable annuity sales practices of Respondent Brown, and thereby failed to detect and prevent Brown's violations of the federal securities statutes, rules and regulations. For example, Ryan knew that:

a. in contravention of State orders, Respondent Brown was marketing variable annuities during times when his insurance license was revoked or restricted.

b. numerous customers submitted complaints against Respondent Brown, including a credible accusation that Brown forged a customer's signature to sell an unsuitable variable annuity, and credible assertions that Respondent Collins was misrepresenting himself as the associated person on the account for variable annuities that Brown solicited.

31. Respondent Rudden from 2004 through 2007 failed to respond reasonably to red flags of wrongdoing in the variable annuity sales practices of Respondents Brown, Collins, Walsh and Wells, and thereby failed to detect and prevent their violations of the federal securities statutes, rules and regulations. For example, Rudden knew that:

a. branch exams from 2003 to 2006 in Delray Beach, Melbourne and Boca Raton that she received -- including one that she personally participated in -- reflected Respondents Brown's, Collins', Walsh's and Wells' noncompliance with firm procedures and their fraudulent and/or unsuitable sales of variable annuities. In particular, the branch exams that Rudden participated in and/or reviewed noted inadequate explanations of variable annuity sales, incomplete disclosure forms, uniform investment objectives and/or time horizons of all reviewed files, patterns of seniors investing high percentages of their assets in variable annuities, and lack of supervisory review and approval of certain variable annuity transactions.

b. customers had complained that Respondents Brown and Walsh had misled them in connection with their variable annuity purchases, and/or over-concentrated their investment portfolios in variable annuities.

c. Respondent Collins' supervisor was concerned about the suitability of variable annuity sales to two elderly investors. Respondent Rudden inquired into one of them and instructed the supervisor to approve it. She made no inquiry into the other, but based on Rudden's instruction to approve the first transaction, Collins' supervisor approved that one, as well.

d. numerous customers submitted complaints against Respondent Brown, including a credible accusation that Brown forged a customer's signature to sell an unsuitable variable annuity, and credible assertions that Respondent Collins was misrepresenting himself as the associated person on the account for variable annuities that Brown solicited.

e. monthly reports from Respondent Collins indicated that Respondent Brown continued to give seminars at which he discussed variable annuities at a time when Brown's state license to sell insurance had been revoked and/or was restricted insofar as it prohibited marketing variable annuities to new customers over the age of 65.

f. Respondent Brown's variable annuity business was devoid of supervision during Respondent Collins' tenure as Brown's supervisor.

g. Respondent Walsh for more than a year refused to submit variable annuity business he wrote for supervisory review.

h. Respondent Andersen was unable to provide adequate suitability reviews for variable annuities sold from the Boca Raton office, including those sold by Respondent Wells. In 2004, Andersen appealed to Rudden for assistance in conducting suitability reviews, indicating that she recognized her own inability to detect compliance problems.

32. Respondent Andersen failed to respond reasonably to red flags of wrongdoing in the variable annuity sales practices of Respondent Wells, and thereby failed to detect and prevent Wells' violations of the federal securities statutes, rules and regulations. For example, Andersen knew that:

a. successive annual branch exams in 2003 through 2005 indicated deficiencies in the disclosures Respondent Wells provided to his variable annuity customers.

b. successive annual branch exams in 2003 through 2005 indicated that almost all randomly selected files were variable annuities sold to senior citizens involving high concentrations of customers' liquid assets, and that customers had uniform investment objectives and/or time horizons.

c. Respondent Wells' assistant continued to initial customer disclosure forms that should have been initialed by the customers themselves as an acknowledgment of having received disclosures in 2004 and 2005, even after Andersen instructed her to stop that practice.

d. documentation in certain of Respondent Wells' customer files in 2003 through 2005 indicated that variable annuities were unsuitable for those customers.

33. Respondent Collins failed to follow Respondent PCS's procedures requiring review of variable annuity transactions. Collins failed to review Respondent Brown's variable annuity sales.

34. Respondent Collins failed to respond reasonably to red flags of wrongdoing in the variable annuity sales practices of Respondent Brown, and thereby failed to detect and prevent Brown's violations of the federal securities statutes, rules and regulations. For example, Collins knew that:

a. Respondent Brown sold variable annuities in 2003 and 2004 when the state had revoked Brown's license to sell insurance.

b. Respondent Brown marketed variable annuities in 2004 and 2005 to new customers over age 65 after a State order prohibited such activity.

C. VIOLATIONS

1. As a result of the conduct described above, Respondent PCS 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 or sale of securities; Section 15(c) of the Exchange Act, which prohibits a broker or dealer from engaging in fraudulent conduct in connection with the purchase or sale of securities; and Section 17(a) of the Exchange Act and Rule 17a-3 thereunder, which require brokers and dealers to make and keep current certain books records relating to its business for prescribed periods of time and furnish them to the Commission as necessary and appropriate for the public interest; and failed reasonably to supervise pursuant to Section 15(b)(4)(E) of the Exchange Act with a view to prevent and detect violations of the federal securities statutes, rules and regulations by Respondents Brown, Collins, Walsh and Wells.

2. As a result of the conduct described above, Respondent G&C aided, abetted and caused Respondent PCS's violations of: 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 or sale of securities; and Section 15(c) of the Exchange Act, which prohibits a broker or dealer from engaging in fraudulent conduct in connection with the purchase or sale of securities.

3. As a result of the conduct described above, Respondents Ryan, Rudden, Andersen and Collins failed reasonably to supervise pursuant to Section 15(b)(6) of the Exchange Act, which incorporates by reference Section 15(b)(4)(E), with a view to preventing and detecting violations of the federal securities statutes, rules and regulations by Respondents Brown, Collins, Walsh and Wells.

4. As a result of the conduct described above, Respondents Brown, Collins, Walsh and Wells willfully violated Section 17(a) of the Securities Act and 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 or sale of securities; and aided, abetted and caused Respondent PCS's violation of Section 17(a) of the Exchange Act and Rule 17a-3 thereunder, which require brokers and dealers to make and keep current certain books and records relating to its business for prescribed periods of time and furnish them to the Commission as necessary and appropriate for the public interest.

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 Respondents pursuant to Section 15(b) of the Exchange Act including, but not limited to, disgorgement and civil penalties pursuant to Section 21B of the Exchange Act;

C. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Section 203(f) of the Advisers Act including, but not limited to, civil penalties pursuant to Section 203(i) of the Advisers Act and disgorgement pursuant to Section 203(j) of the Advisers Act;

D. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondent PCS 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, Sections 10(b), 15(b)(4)(E), 15(c) and 17(a) of the Exchange Act and Rules 10b-5 and 17a-3 thereunder, and whether Respondent PCS should be ordered to pay disgorgement pursuant to Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act.

E. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondent G&C 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 and Sections 10(b) and 15(c) of the Exchange Act and Rules 10b-5 thereunder, and whether Respondent G&C should be ordered to pay disgorgement pursuant to Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act.

F. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondents Ryan, Rudden, Andersen and Collins should be ordered to cease and desist from committing or causing violations of and any future violations of Section 15(b)(4)(E) of the Exchange Act.

G. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondents Brown, Collins, Walsh and Wells 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, Sections 10(b) and 17(a) of the Exchange Act and Rules 10b-5 and 17a-3 thereunder; and whether Respondents should be ordered to pay disgorgement 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 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 any 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 or her 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.

Elizabeth M. Murphy
Secretary

By: J. Lynn Taylor
Assistant Secretary

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION

Securities Exchange Act of 1934
Release No. 60203 / June 30, 2009

In the Matter of: The NASDAQ Stock Market LLC File No. SR-NASDAQ-2009-053	ORDER OF SUMMARY ABROGATION

Notice is hereby given that the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(3)(C) of the Securities Exchange Act of 1934 ("Act"),[1] is summarily abrogating a certain proposed rule change of The NASDAQ Stock Market LLC ("NASDAQ" or "Exchange").

On June 24, 2009, NASDAQ filed SR-NASDAQ-2009-053. The proposed rule change establishes a four-month pilot program that would reduce transaction fees for members that trade equities on NASDAQ provided that they also make markets in options on the NASDAQ OMX PHLX, Inc. ("Phlx") options exchange. The proposed rule change was immediately effective upon filing with the Commission pursuant to Section 19(b)(3)(A) of the Act.[2]

1 15 U.S.C. 78s(b)(3)(C).

2 15 U.S.C. 78s(b)(3)(A).

Pursuant to Section 19(b)(3)(C) of the Act,[3] at any time within 60 days of the date of filing a proposed rule change pursuant to Section 19(b)(1) of the Act,[4] the Commission may summarily abrogate the change in the rules of the self-regulatory organization and require that the proposed rule change be re-filed in accordance with the provisions of Section 19(b)(1) of the Act[5] and reviewed in accordance with Section 19(b)(2) of the Act,[6] if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

NASDAQ proposes to offer a reduced transaction fee for securities listed on NASDAQ and the New York Stock Exchange LLC ("NYSE") only to member firms that: (1) make markets in 400 or more options classes as a Specialist, Streaming Quote Trader, or Remote Streaming Quote Trader on Phlx; and (2) add average daily volume of 35 million shares of liquidity on NASDAQ. Member firms meeting these criteria would pay a reduced transaction fee of $0.0027 per share executed on NASDAQ for securities listed on NASDAQ or NYSE. The Commission is concerned about whether the proposal is consistent with the statutory requirements applicable to a national securities exchange under the Act, including, among other provisions, Section 6(b)(4) of the Act,[7] which requires that the rules of a national securities exchange provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and

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3 15 U.S.C. 78s(b)(3)(C).

4 15 U.S.C. 78s(b)(1).

5 Id.

6 15 U.S.C. 78s(b)(2).

7 15 U.S.C. 78f(b)(4).

other parties using its facilities; Section 6(b)(5) of the Act,[8] which requires, among other things, that the rules of a national securities exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers; and Section 6(b)(8) of the Act,[9] which requires that the rules of a national securities exchange do not impose any burden on competition not necessary or appropriate in furtherance of the Act.

Accordingly, the Commission believes that the procedures provided by Section 19(b)(2) of the Act[10] will provide a more appropriate mechanism for determining whether the proposed rule change is consistent with the Act. Therefore, the Commission finds that it is appropriate in the public interest, for the protection of investors, and otherwise in furtherance of the purposes of the Act, to abrogate the proposed rule change.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(3)(C) of the Act,[11] that File No. SR-NASDAQ-2009-053, be and hereby is, summarily abrogated. If NASDAQ chooses to re-file the proposed rule change, it must do so pursuant to Sections 19(b)(1)[12] and 19(b)(2) of the Act.[13]

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

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8 15 U.S.C. 78f(b)(5).

9 15 U.S.C. 78f(b)(8).

10 Id.

11 15 U.S.C. 78s(b)(3)(C).

12 15 U.S.C. 78s(b)(1).

13 15 U.S.C. 78s(b)(2).