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 **August 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

MINUTE COPY

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

June 5, 2009

IN THE MATTER OF	:	
Sunrise Solar Corporation	:	**ORDER OF SUSPENSION OF TRADING**
File No. 500-1	:	

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Sunrise Solar Corporation ("Sunrise") because of questions regarding the accuracy of statements by Sunrise Solar Corporation in press releases to investors concerning, among other things, the company's business prospects and agreements.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of Sunrise Solar Corporation.

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 5, 2009 through 11:59 p.m. EDT, on June 18, 2009.

By the Commission.

Elizabeth M. Murphy
Secretary

J. Lynn Taylor

By: J. Lynn Taylor
Assistant Secretary

Service List

The attached Order of Suspension of Trading issued pursuant to Section 12(k) of the Securities Exchange Act of 1934 has been sent via U.S. Mail to the following persons and entities the 5th day of June, 2009:

Sunrise Solar Corporation
4703 Shavano Oak
Suite 104
San Antonio, TX 78249

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT COMPANY ACT OF 1940
Release No. 28841 / August 3, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13568

In the Matter of **RYAN DOUGLAS SMITH,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTIONS 9(b) AND 9(f) OF THE INVESTMENT COMPANY ACT OF 1940**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act") against Ryan Douglas Smith ("Smith" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Order"), as set forth below.

III.

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

Respondent

1. Smith, 34 years old, is a resident of Kansas City, Missouri. Smith served as president of Bellwether Capital Fund I, Inc. from December 31, 2004 through May 11, 2007. From February 1999 through September 2004, Smith was associated as a registered representative with multiple registered broker-dealers and held Series 7 and 55 licenses.

Other Relevant Entity

2. Bellwether Capital Fund I, Inc. ("Bellwether")[2] is a Maryland corporation located in Irvine, California. Bellwether was originally incorporated as Landmark Microcap Fund, Inc., changed its name to Rhino Microcap Fund, Inc. in November 2002, changed its name to Tiger Fund, Inc. in January 2003, and then changed its name to Bellwether in March 2005. Bellwether operated as a closed-end investment company from at least February 2003 through September 2005. It has never been registered with the Commission as an investment company.

Facts

3. On November 11, 2002, Bellwether filed a Form N-6F with the Commission, indicating its intent to operate as a business development company ("BDC") and be subject to Sections 55 through 65 of the Investment Company Act ("BDC provisions"). Bellwether, however, neither had a class of equity securities registered under Section 12 of the Securities Exchange Act of 1934 ("Exchange Act") nor had it filed a registration statement pursuant to Section 12 of the Exchange Act for a class of its equity securities. As such, Bellwether could not comply with the requirements of Section 54(a) of the Investment Company Act and was ineligible to elect BDC status. In addition, Bellwether never made the appropriate filing on Form N-54A to elect BDC status. As a result of the above, Bellwether never became a BDC.

4. In addition, Bellwether never registered as an investment company under Section 8 of the Investment Company Act. Nevertheless, Bellwether held itself out to the public, and operated, as an investment company. In offering documents filed with the Commission, Bellwether described itself as a "recently organized, externally managed, non-diversified closed end management investment company."

5. In August 2004, Bellwether filed a Form 1-E with the Commission as part of its efforts to raise capital in a public offering of its securities. Form 1-E is required by Regulation E, which provides that a closed-end investment company that has elected, or intends to elect, to be

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

[2] On July 31, 2009, the Commission filed a civil action against Bellwether related to the conduct described herein, entitled SEC v. Omar Ali Rizvi, Bellwether Venture Capital Fund I, Inc., and Strategy Partners, LLC, Civil Action No. 4:09-CV-371 (N.D. Tx.).

regulated as a BDC may issue, in a one-year period, up to $5 million of its securities in an offering exempt from registration under the Securities Act of 1933.

6. From August 2004 through September 2005, Bellwether raised approximately $1.9 million through the offer and sale of its securities to at least 173 investors located throughout the United States. Bellwether used approximately $673,000 of those funds to purchase controlling interests in two publicly traded companies.

7. In December 2004, during the time Bellwether was conducting an offering of its securities, Smith was hired to serve as Bellwether's president. Prior to that time, Smith had never operated, managed, or worked for a BDC. However, Smith did not manage the day-to-day operations of Bellwether, but instead spent the majority of his time managing the daily operations of one of Bellwether's portfolio companies.

8. Smith reviewed Bellwether's website, assisted in preparing and signed a new Form 1-E in or around August 2005, which included an offering circular with a "Risk Factors" section that stated Bellwether had not yet elected to be regulated as a BDC. In addition, Commission staff sent Smith a letter in September 2005 stating that Bellwether had not elected BDC status, a fact that indicated that Bellwether was likely operating as an unregistered investment company. Yet, in May 2007, when Smith resigned as president, Bellwether had not elected BDC status or registered with the Commission as an investment company.

9. During the period when Smith was Bellwether's president and knew that Bellwether was offering its securities to the public, Bellwether was an investment company within the meaning of Section 3(a)(1) of the Investment Company Act. Section 3(a)(1) defines "investment company" to mean, among other things, any issuer that "is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities" or "is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 per centum of the value of such issuer's total assets . . . on an unconsolidated basis." Bellwether did not meet any statutory exclusion from the definition of an "investment company," and was not exempted from complying with any provisions of that act or the rules thereunder.

Violations

10. As a result of the conduct described above, Bellwether violated Section 7(a) of the Investment Company Act, which prohibits an investment company not registered with the Commission from engaging in any business in interstate commerce, including offering, selling, purchasing, or redeeming interests in the investment company.

11. As a result of the conduct described above, Smith willfully aided and abetted and caused Bellwether's violation of Section 7(a) of the Investment Company Act.

IV.

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

Accordingly, pursuant Sections 9(b) and 9(f) of the Investment Company Act, it is hereby ORDERED that:

A. Respondent Smith cease and desist from causing any violations and any future violations of Section 7(a) of the Investment Company Act.

B. Respondent Smith be, and hereby is prohibited from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter, with the right to reapply for association after five (5) years to the appropriate self-regulatory organization, or if there is none, to the Commission;

C. Any reapplication for association by Respondent Smith 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 Smith, 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

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 275

[Release No. IA-2910; File No. S7-18-09]

RIN 3235-AK39

Political Contributions by Certain Investment Advisers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission is proposing for comment a new rule under the Investment Advisers Act of 1940 that would prohibit an investment adviser from providing advisory services for compensation to a government client for two years after the adviser or certain of its executives or employees make a contribution to certain elected officials or candidates. The new rule would also prohibit an adviser from providing or agreeing to provide, directly or indirectly, payment to any third party for a solicitation of advisory business from any government entity on behalf of such adviser. Additionally, the new rule would prevent an adviser from soliciting from others, or coordinating, contributions to certain elected officials or candidates or payments to political parties where the adviser is providing or seeking government business. The Commission also is proposing rule amendments that would require a registered adviser to maintain certain records of the political contributions made by the adviser or certain of its executives or employees. The new rule and rule amendments would address "pay to play" practices by investment advisers.

DATES: Comments should be received on or before [insert date 60 days after publication in Federal Register], 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 S7-18-09 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 S7-18-09. 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/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 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: Melissa A. Roverts, Attorney-Adviser, Matthew N. Goldin, Senior Counsel, Daniel S. Kahl, Branch Chief, or Sarah A. Bessin, Assistant Director, at (202) 551-6787 or <IArules@sec.gov>, Office of Investment Adviser Regulation, Division of Investment Management, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-8549.

SUPPLEMENTARY INFORMATION: The Commission is requesting public comment on proposed rule 206(4)-5 [17 CFR 275.206(4)-5] and proposed amendments to rules 204-2 [17 CFR 275.204-2] and 206(4)-3 [17 CFR 275.206(4)-3] under the Investment Advisers Act of 1940 [15 U.S.C. 80b] ("Advisers Act" or "Act").

I. BACKGROUND AND INTRODUCTION

II. DISCUSSION

A. RULE 206(4)-5: "PAY TO PLAY" RESTRICTIONS
  1. Advisers Subject to the Rule
  2. Relationship with MSRB Rules; Alternative Approaches
  3. Pay to Play Restrictions
    (a) Two-Year "Time Out" for Contributors
      (1) Prohibition on Compensation
      (2) Officials of a Government Entity
      (3) Contributions
      (4) Covered Associates
      (5) "Look Back"
      (6) Exception for De Minimis Contributions
      (7) Exception for Certain Returned Contributions
    (b) Ban on Using Third Parties To Solicit Government Business
    (c) Restrictions on Soliciting and Coordinating Contributions and Payments
    (d) Direct and Indirect Contributions or Solicitations
    (e) Investment Pools
      (1) Application of the Rule to Pooled Investment Vehicles
      (2) Covered Investment Pools
      (3) Applying the Compensation Limit to Covered Investment Pools
    (f) Exemptions

B. RECORDKEEPING

C. AMENDMENT TO CASH SOLICITATION RULE

D. TRANSITION PERIOD

E. GENERAL REQUEST FOR COMMENT

III. COST/BENEFIT ANALYSIS

A. BENEFITS

B. COSTS

C. REQUEST FOR COMMENT

IV. PAPERWORK REDUCTION ACT

A. RULE 204-2
B. RULE 206(4)-3
C. REQUEST FOR COMMENT

V. INITIAL REGULATORY FLEXIBILITY ANALYSIS

A. REASONS FOR PROPOSED ACTION
B. OBJECTIVES AND LEGAL BASIS
C. SMALL ENTITIES SUBJECT TO RULE
D. REPORTING, RECORDKEEPING, AND OTHER COMPLIANCE REQUIREMENTS
E. DUPLICATIVE, OVERLAPPING, OR CONFLICTING FEDERAL RULES
F. SIGNIFICANT ALTERNATIVES
G. SOLICITATION OF COMMENTS

VI. EFFECTS ON COMPETITION, EFFICIENCY AND CAPITAL FORMATION

VII. CONSIDERATION OF IMPACT ON THE ECONOMY

VIII. STATUTORY AUTHORITY

I. BACKGROUND AND INTRODUCTION

Investment advisers provide a wide variety of advisory services to state and local governments.[1] Advisers manage public monies that fund pension plans and a number of other important public programs, including transportation, children's programs, arts programs, environmental reclamation, and financial aid for education. In addition, advisers provide risk management,[2] asset allocation,[3] financial planning[4] and cash management services;[5] assist in

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1 See Sofia Anastopoulos, AN INTRODUCTION TO INVESTMENT ADVISERS FOR STATE AND LOCAL GOVERNMENTS (2d ed. 2007); Werner Paul Zorn, Public Employee Retirement Systems and Benefits, in LOCAL GOVERNMENT FINANCE, CONCEPTS AND PRACTICES 376 (John E. Peterson and Dennis R. Strachota, eds., 1st ed. 1991) (discussing the services investment advisers provide for public funds).

2 See ROBERT A. FIPPINGER, THE SECURITIES LAW OF PUBLIC FINANCE 669 (2d ed. 2004).

3 See, e.g., John H. Ilkiw, Investment Policies, Processes and Problems in U.S. Public Sector Pension Plans: Some Observations and Solutions from a Practitioner, in PUBLIC PENSION FUND MANAGEMENT: GOVERNANCE, ACCOUNTABILITY AND INVESTMENT POLICIES (Alberto R.

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investing proceeds from bond offerings;[6] help state and local governments find and evaluate other advisers that manage public funds ("pension consultants");[7] and provide other types of services.[8]

Most of the public funds managed by investment advisers fund state and municipal pension plans.[9] These pension plans have over $2.2 trillion of assets and represent one-third of

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Musalem and Robert J. Palacios, eds. 2004). See also Barry B. Burr, The New $100 Billion Club, PENS. & INV. (May 4, 1998), at 1.

4 See CAL. ED. CODE § 22303.5 (2008) (requiring teachers' retirement system to offer retirement planning services to beneficiaries); CalSTRS Counseling and Workshops, available at http://www.calstrs.com/Counseling%20and%20Workshops/index.aspx. Other funds also offer financial planning services to their beneficiaries. See, e.g., CalPERS Launches Online Education Classes, US STATES NEWS (Mar. 3, 2008).

5 See GOVERNMENT FINANCE OFFICERS ASSOCIATION, AN INTRODUCTION TO EXTERNAL MONEY MANAGEMENT FOR PUBLIC CASH MANAGERS 5 (1991).

6 See In the Matter of O'Brien Partners, Inc., Investment Advisers Act Release No. 1772 (Oct. 27, 1998) (settled enforcement action in which financial advisor was deemed subject to the Advisers Act for rendering advice to municipal securities issuers "concerning their investment of bond proceeds in securities, including [non-government securities], and was compensated for that advice").

7 In addition to assisting public funds in selecting investment advisers, pension consultants may also provide advice to state and local governments on such things as designing investment objectives, or recommending specific securities or investments for the fund. Pension consultants may be investment advisers subject to the Advisers Act. See Applicability of the Investment Advisers Act of 1940 to Financial Planners, Pension Consultants, and Other Persons Who Provide Others with Investment Advice as a Component of Other Financial Services, Investment Advisers Act Release No. 1092 (Oct. 8, 1987) [52 FR 38400 (Oct. 16, 1987)] ("Release 1092").

8 For example, public funds may retain advisers to perform custodial services. See, e.g., Public Employee Retirement Systems, supra note 1, at 376-77.

9 For this reason, in this Release, we use the term "public pension plan" interchangeably with "government client" and "government entity"; however, our proposed rule would apply broadly to investment advisory activities for government clients, such as those mentioned here in this Background and Introduction, regardless of whether they are retirement funds. For a discussion of how the proposed rule would apply with respect to investment programs or plans sponsored or established by government entities, such as "qualified tuition plans" authorized by Section 529 of the Internal Revenue Code [26 U.S.C. 529] and retirement plans authorized by Section 403(b) or

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all U.S. pension assets.[10] They are among the largest and most active institutional investors in the United States.[11] The management of these funds significantly affects publicly held companies[12] and the securities markets.[13] But most significantly, their management affects taxpayers and the beneficiaries of these funds, including the millions of present and future state and municipal retirees[14] who rely on the funds for their pensions and other benefits.[15]

Public pension plan assets are held, administered and managed by elected officials who often are responsible for selecting investment advisers to manage the funds they oversee. Pay to

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457 of the Internal Revenue Code [26 U.S.C. 403(b) or 457], see infra section II.A.3(e) of this Release.

10 Board of Governors of the Federal Reserve System, Flow of Funds Accounts of the United States, Flows and Outstandings, First Quarter 2009 (June 11, 2009) (at table L.119). Since 2002, total financial assets of public pension funds have grown by 13% Id.

11 According to a recent survey, seven of the ten largest pension funds were sponsored by state and municipal governments. The Top 200 Pension Funds/Sponsors, PENS. & INV. (Sept. 30, 2008), available at http://www.pionline.com/article/20090126/CHART/901209995.

12 See Stephen J. Choi & Jill E. Fisch, On Beyond CalPERS: Survey Evidence on the Developing Role of Public Pension Funds in Corporate Governance, 61 VANDERBILT L.REV. 315 (Mar. 2008) (noting, "Collectively, public pension funds have the potential to be a powerful shareholder force, and the example of CalPERS and its activities have spurred many to advocate greater institutional activism.").

13 Federal Reserve reports indicate that, of the $2.2 trillion in non-federal government plans, $1.1 trillion are invested in corporate equities. Flow of Funds Accounts of the United States, supra note 10 (at table L.119).

14 See PAUL ZORN, 1997 SURVEY OF STATE AND LOCAL GOVERNMENT EMPLOYEE RETIREMENT SYSTEMS 61 (1997) ("[t]he investment of plan assets is an issue of immense consequence to plan participants, taxpayers, and to the economy as a whole" as a low rate of return will require additional funding from the sponsoring government, which "can place an additional strain on the sponsoring government and may require tax increases").

15 The most current census data reports that public pension funds have 18.6 million beneficiaries. 2007 CENSUS OF GOVERNMENTS, U.S. BUREAU OF CENSUS, Number and Membership of State and Local Government Employee-Retirement Systems by State: 2006-2007 (2007) (at Table 5), available at http://www.census.gov/govs/retire/2007ret05.html.

play practices undermine the fairness of the selection process when advisers seeking to do business with the governments of states and municipalities make political contributions to elected officials or candidates, hoping to influence the selection process. In other cases, political contributions may be solicited from advisers, or it is simply understood that only contributors will be considered for selection. Contributions, in this circumstance, may not always guarantee an award of business to the contributor, but the failure to contribute will guarantee that another is selected. Hence the term "pay to play."

Elected officials who allow political contributions to play a role in the management of these assets violate the public trust by rewarding those who make political contributions. Similarly, investment advisers that seek to influence the award of advisory contracts by public entities, by making or soliciting political contributions to those officials who are in a position to influence the awards, compromise their fiduciary obligations. Pay to play practices can distort the process by which investment advisers are selected and can harm advisers' public pension plan clients, and the pension plan beneficiaries, which may receive inferior advisory services and pay higher fees because, for instance, advisers must recoup contributions, or because contract negotiations are not handled on an arm's-length basis. Pay to play practices also may manipulate the market for advisory services by creating an uneven playing field among investment advisers. These practices also may hurt smaller advisers that cannot afford the required contributions. We believe that advisers' participation in pay to play practices is inconsistent with the high standards of ethical conduct required of them under the Advisers Act.

Pay to play practices are rarely explicit: participants do not typically let it be publicly known that contributions or payments are made or accepted for the purpose of influencing the selection of an adviser. As one court noted, in its decision upholding one of the rules on which the proposed rule is modeled, "[w]hile the risk of corruption is obvious and substantial, actors in this field are presumably shrewd enough to structure their relations rather indirectly."[16] Pay to play practices may take a variety of forms, including an adviser's direct contributions to government officials, an adviser's solicitation of third parties to make contributions or payments to government officials or political parties in the state or locality where the adviser seeks to provide services, or an adviser's payments to third parties to solicit (or as a condition of obtaining) government business. As a result, the full extent of pay to play practice remains hidden and is often hard to prove.

The rule we are proposing today is modeled on rules G-37 and G-38 of the Municipal Securities Rulemaking Board ("MSRB"),[17] which address pay to play practices in the municipal securities markets.[18] The Commission approved rule G-37 in 1994, after concluding that pay to play practices harm municipal securities markets.[19] MSRB rule G-37 prohibits a broker-dealer

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16 Blount v. SEC, 61 F.3d 938, 945 (DC Cir. 1995), cert. denied, 517 U.S. 1119 (1996).

17 In 1999 the Commission proposed a similar rule, which also would have been codified as rule 206(4)-5 under the Advisers Act, had it been adopted. See Political Contributions by Certain Investment Advisers, Investment Advisers Act Release No. 1812 (Aug. 4, 1999) [64 FR 43556 (Aug. 10, 1999)] ("1999 Proposing Release"). The Commission also proposed amendments in 1999 to rule 204-2 [17 CFR 275.204-2] under the Advisers Act, which would have required advisers with government clients to keep certain records relating to the 1999 proposed rule. See id., at section II.B. We are not re-proposing that rule or those rule amendments today; we are withdrawing our 1999 proposal and proposing a new rule 206(4)-5 as well as new amendments to rule 204-2.

18 MSRB rule G-37 and G-38 are available on the MSRB's Web site at http://www.msrb.org/msrb1/rules/ruleg37.htm and http://www.msrb.org/msrb1/rules/ruleg38.htm, respectively.

19 See In the Matter of Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Political Contributions and Prohibitions on Municipal Securities Business and Notice of Filing and Order Approving on an Accelerated Basis Amendment No. 1 Relating to the Effective Date and Contribution Date of the Proposed Rule, Exchange Act Release No. 33868 (Apr. 7, 1994) [59 FR 17621 (Apr. 13, 1994)] ("MSRB Rule G-37 Approval Order"), at sections V.A.1 and 2. In approving MSRB rule G-37, we

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from engaging in municipal securities business with a municipal issuer for two years after making a political contribution to an elected official of the issuer who can influence the selection of the broker-dealer.[20] The rule also prohibits a broker-dealer from providing or seeking to provide underwriting services to a government if the firm or any of its "municipal finance professionals" solicit contributions for a candidate or an elected official of that government, or if they solicit payments to political parties where the firm is providing or seeking to provide services to a government client.[21] MSRB rule G-38 prohibits municipal securities dealers from making payments to consultants for soliciting municipal securities business.[22] We believe that MSRB rules G-37 and G-38 have been successful in addressing pay to play practices in the municipal securities market.[23]

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concluded that pay to play practices may harm the municipal markets by fostering a selection process that excludes those firms that do not make contributions, causes less qualified underwriters to be retained, and undermines equitable practices in the municipal securities industry. Id. at section V.

20 MSRB rule G-37(b). Shortly after MSRB rule G-37 became effective, a municipal securities dealer challenged it as an infringement on the constitutional rights of municipal securities professionals. A federal appeals court upheld the constitutionality of MSRB rule G-37, finding that the rule is narrowly tailored to serve a compelling government interest. See Blount, supra note 16.

21 MSRB rule G-37(c). A "municipal finance professional" is an associated person of a broker-dealer who is "primarily engaged" in municipal securities activities, who solicits municipal securities business on behalf of a broker-dealer, who supervises associated persons primarily engaged in municipal securities activities "up through and including" the chief executive officer of the firm (or person performing similar functions), or who is a member of the firm's executive or management committee (or person performing similar functions). MSRB rule G-37(g)(iv).

22 MSRB rule G-38(a).

23 Others, including the MSRB, agree. See, e.g., MSRB Notice 2009-35, Request for Comment: Rule G-37 on Political Contributions and Prohibitions on Municipal Securities Business – Bond Ballot Campaign Committee Contributions (June 22, 2009) ("The MSRB believes the rule has provided substantial benefits to the industry and the investing public by greatly reducing the

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Following the adoption of MSRB rule G-37, we were increasingly concerned that the very success of the rule may have caused pay to play practices to migrate to an area not covered by the MSRB rules – the management of public pension plans.[24] Public pension plans are particularly vulnerable to pay to play practices. Management decisions over these investment pools, some of which are quite large, are typically made by one or more trustees who are (or are appointed by) elected officials. And the elected officials that govern the funds are also often involved, directly or indirectly, in selecting advisers to manage the public pension funds' assets.

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direct connection between political contributions given to issuer officials and the awarding of municipal securities business to dealers, thereby effectively eliminating pay-to-play practices in the new issue municipal securities market." [footnote omitted]); MSRB Notice 2003-32, Notice Concerning Indirect Rule Violations: Rules G-37 and G-38 (Aug. 6, 2003) ("The impact of Rules G-37 and G-38 has been very positive. The rules have altered the political contribution practices of municipal securities dealers and opened discussion about the political contribution practices of the entire municipal industry."); Letter from Darrick L. Hills and Linda L. Rittenhouse of the CFA Institute to Jill C. Finder, Asst. Gen. Counsel of the MSRB, dated Oct. 19, 2001, available at http://www.cfainstitute.org/centre/topics/comment/2001/01msrb_ruleg37.html (stating, "We generally believe that the existing [MSRB] pay-to-play prohibitions have been effective in stemming practices that compromise the integrity of the [municipal securities] market by using political contributions to curry favor with politicians in positions of influence."); Cmte. on Cap. Mkts. Reg., Interim Report of the Cmte. on Cap. Mkts. Reg. (Nov. 30, 2006), available at http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf (stating, upon describing MSRB Rule G-37 and the 2005 amendments to MSRB Rule G-38, "Taken together, the MSRB's rules have largely put an end to the old "pay to play" practices in municipal underwriting.").

24 1999 Proposing Release, supra note 17, at section I ("We have become particularly concerned about the possibility that the adoption of rule G-37 has resulted in a shift of pay to play practices to [the management of public pension funds] as political contributions by broker-dealers are curtailed."). See also Bill Krueger, Money Managers Giving to Boyles, NEWS & OBSERVER (May 2, 1996), at A1 (noting that rule G-37 "dried up" a contribution source for a state treasurer, "so now he is getting campaign contributions from a group [investment advisers] that is not subject to [rule G-37]"); Gerri Willis, Filling Carl's War Chest: Comptroller Getting Thousands From State's Money Managers, CRAIN'S N.Y. BUS. (Sept. 16, 1996), at 1 (noting the observation of a securities executive that "[b]ecause of the SEC's crackdown on the pay to play nature of the muni bond business, the game has shifted to asset management and brokerage").

These officials may have the sole authority to select advisers,[25] may be members of a governing board that selects advisers,[26] or may appoint some or all of the board members who make the selection.[27]

In response to these concerns, in 1999 we proposed a rule under the Advisers Act, modeled substantially on MSRB rule G-37, that was designed to prevent advisers from participating in pay to play practices affecting the management of public pension plans.[28] In particular, the 1999 rule proposal would have prohibited an adviser from receiving compensation for the provision of advisory services for two years after the advisory firm or any of its partners, executive officers or solicitors, directly or indirectly, made a contribution to an elected official who (or a candidate for an elected office that) has the ability to influence the selection of the adviser.[29] Comments on the proposal were mixed, and some commenters that objected asserted that pay to play was not a problem in the management of public funds.[30]

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25 See, e.g., 2 NYCRR § 320.2 (placement of state and local government retirement systems assets (valued at $109 billion as of Mar. 2009) is under the sole custodianship of the New York State Comptroller).

26 See, e.g., S.C. CODE ANN. §§ 9-1-20, 1-11-10 (2008) (board consists of all elected officials); CAL. GOV'T CODE § 20090 (Deering 2008) (board consists of some elected officials, some appointed members, and some representatives of interest groups chosen by the members of those groups); MD. CODE ANN., STATE PERS. & PENS. § 21-104 (2008) (pension board consists of some elected officials, some appointed members, and some representatives of interest groups chosen by the members of those groups).

27 See, e.g., ARIZ. REV. STAT. ANN. § 38-713 (2008) (governor appoints all nine members); HAWAII REV. STAT. § 88-24 (2008) (governor appoints three of eight members); IDAHO CODE § 59-1304 (2008) (governor appoints all five members).

28 See 1999 Proposing Release, supra note 17.

29 See id., at section II.A.1.

30 We received 59 comment letters on our 1999 proposal. Commenters representing beneficiaries and public pension plans expressed concern about pay to play practices and generally favored our proposed rule. State government officials and investment advisers generally opposed the rule. State government officials generally argued that there was no demonstrated need for the

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Since then, it has become increasingly clear that pay to play is a significant problem in the management of public funds by investment advisers. In recent years, we and criminal authorities have brought a number of actions charging investment advisers with participating in pay to play schemes. We recently brought a civil action in federal court charging former New York State officials, as well as a "placement agent," with engaging in a fraudulent scheme to extract kickbacks from investment advisers seeking to manage assets of the New York State Common Retirement Fund.[31] Investment advisers allegedly paid sham "placement agent" fees, portions of which were funneled to public officials, as a means of obtaining public pension fund investments in the funds those advisers managed.[32] Another settled administrative action involved an investment adviser who allegedly paid kickbacks in return for investment advisory business awarded by the New Mexico state treasurer's office.[33] In addition, we brought two separate cases against the former treasurer of the State of Connecticut and various other parties in which we alleged that the former treasurer awarded state pension fund investments to private equity fund

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proposed rule and that state laws are adequate to address any concerns. Most advisers submitting comments opposed the rule's breadth and complained that the consequences of violating the rule were too harsh; some denied the existence of the problem we sought to address. Comment letters on our 1999 proposal and a summary of comments prepared by our staff are available in our Public Reference Room in File No. S7-19-99. Comment letters we received electronically are also available at http://www.sec.gov/rules/proposed/s71999.shtml.

31 See SEC v. Henry Morris, et al, Litigation Release No. 21036 (May 12, 2009).

32 See id.

33 See In the Matter of Kent D. Nelson, Investment Advisers Act Release No. 2765 (Aug. 1, 2008); Initial Decision Release No. 371 (Feb. 24, 2009); Investment Advisers Act Release No. 2868 (Apr. 17, 2009) (in which investment adviser was barred from association with any broker, dealer or investment adviser).

managers in exchange for fees paid to the former treasurer's friends and political associates.[34] Criminal authorities have in recent years also brought cases in New York,[35] New Mexico,[36] Illinois,[37] Ohio,[38] Connecticut,[39] and Florida,[40] charging defendants with the same or similar

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34 See SEC v. Paul J. Silvester et al., Litigation Release No. 16759 (Oct. 10, 2000); Litigation Release No. 20027 (Mar. 2, 2007); Litigation Release No. 19583 (Mar. 1, 2006); Litigation Release No. 18461 (Nov. 17, 2003); Litigation Release No. 16834 (Dec. 19, 2000); SEC v. William A. DiBella et al., Litigation Release No. 20498 (Mar. 14; 2008). See also U.S.. v. Ben F. Andrews, Litigation Release No. 19566 (Feb. 15, 2006); In the Matter of Thayer Capital Partners, TC Equity Partners IV, L.L.C., TC Management Partners IV, L.L.C., and Frederick V. Malek, Investment Advisers Act Release No. 2276 (Aug. 12, 2004); In the Matter of Frederick W. McCarthy, Investment Advisers Act Release No. 2218 (Mar. 5, 2004); In the Matter of Lisa A. Thiesfield, Investment Advisers Act Release No. 2186 (Oct. 29, 2003).

35 See New York v. Henry "Hank" Morris and David Loglisci, Indictment No. 25/2009 (NY Mar. 19, 2009) (alleging that the deputy comptroller and a "placement agent" engaged in enterprise corruption and state securities fraud for selling access to management of public funds in return for kickbacks and other payments for personal and political gain).

36 See U.S. v. Montoya, Criminal No. 05-2050 JP (D.N.M. Nov. 8, 2005) (the former treasurer of New Mexico pleaded guilty); U.S. v. Kent Nelson, Criminal Information No. 05-2021 JP, (D.N.M. 2007) (defendant pleaded guilty to one count of mail fraud); U.S. v. Vigil, 523 F. 3d 1258 (10th Cir. 2008) (affirming the conviction for attempted extortion of the former treasurer of New Mexico's successor for requiring that a friend be hired by an investment manager at a high salary in return for the former treasurer's willingness to accept a proposal from the manager for government business).

37 See Jeff Coen et al., State's Ultimate Insider Indicted, CHICAGO TRIBUNE (Oct. 31, 2008) (describing the thirteenth indictment in an Illinois pay to play probe).

38 See Reginald Fields, Four More Convicted in Pension Case: Ex-Board Members Took Gifts from Firm, CLEVELAND PLAIN DEALER (Sept. 20, 2006) (addressing pay to play activities of members of the Ohio Teachers Retirement System).

39 See U.S. v. Joseph P. Ganim, 2007 U.S. App. LEXIS 29367 (2d Cir. 2007) (affirming the district court's decision to uphold an indictment of the former mayor of Bridgeport, Connecticut, in connection with his conviction for, among other things, requiring payment from an investment adviser in return for city business); U.S. v. Triumph Capital Group, et al, No. 300CR217 JBA (D. Conn. filed Oct. 10, 2000) (the former treasurer, along with certain others, pleaded guilty – while others were ultimately convicted).

40 See United States v. Poirier, 321 F.3d 1024 (11th Cir.), cert. denied sub nom., deVegter v. United States, 540 U.S. 874 (2003) (partner at Lazard Freres & Co., a municipal services firm, was found liable for conspiracy and wire fraud for fraudulently paying $40,000 through an intermediary to Fulton County's independent financial adviser to secure an assurance that Lazard would be selected for the Fulton County underwriting contract).

conduct. In addition, there are a growing number of reports about pay to play activities involving investment advisers in other jurisdictions.[41] These cases involving investment advisers, as well as others involving broker-dealers, may reflect more widespread involvement by securities professionals in pay to play activities.[42]

Recognizing the harm pay to play practices cause in the management of public funds, several states, counties, localities, and even individual public pension funds, have undertaken to

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41 See, e.g., David Zahniser, California; Private Finances, Public Role Intersect; Former Pension Board Member Had Consulted for a Firm that Sought Work with the Panel on Which He Served, LOS ANGELES TIMES (May 9, 2009) (discussing alleged pay to play activities relating to a former member of the Los Angeles Fire and Police Pensions Board); Rick Rothacker & David Ingram, Moore Defends Pension System, CHARLOTTE OBSERVER (Feb. 25, 2007) (discussing alleged pay to play activities involving North Carolina's state treasurer); Len Boselovic, Pensions, Politics and Consultants Make for Unsavory Bedfellows, PITTSBURGH POST-GAZETTE (Aug. 13, 2006) and Jeffrey Cohan, Fund Managers 'Pay to Play': Six Firms Managing County's Pension Investments Gave to Board Members' Campaigns, PITTSBURGH POST-GAZETTE (Feb. 22, 2001) (discussing alleged pay to play activities relating to the Allegheny County Retirement Board); Mary Williams Walsh, Political Money Said to Sway Pension Investments, N.Y. TIMES (Feb. 10, 2004) (regarding a 2002 audit by then-new controller of Luzerne County, Pennsylvania alleging pay to play activities among various parties involved with county pension funds).

42 For example, we recently brought a case against the mayor of Birmingham, Alabama, and other defendants, alleging that while the mayor served as president of the County Commission of Jefferson County, Alabama, he accepted undisclosed cash and benefits through a lobbyist as a conduit from the chairman of a Montgomery, Alabama-based broker-dealer, in return for awarding municipal bond business and swap transactions to the broker-dealer. See SEC v. Larry P. Langford et al., Litigation Release No. 20545 (Apr. 30, 2008). Several years earlier, we brought an enforcement action against the former treasurer of the City of Chicago, to whom two registered representatives were alleged to have made secret cash payments to obtain a share of the city's lucrative securities investments. See SEC v. Miriam Santos et al., Litigation Release No. 17839 (Nov. 14, 2002); Litigation Release No. 19269 (June 14, 2005). We also brought enforcement actions against the registered representatives allegedly involved in the scheme. See SEC v. Miriam Santos, Peter J. Burns, and Michael F. Hollendoner, Litigation Release Nos. 19270 and 19271 (June 14, 2005). In addition, we brought a case against a broker-dealer, two of its officers and a city official for participating in a scheme to defraud the City of Atlanta in connection with the purchase and sale of certain securities while providing substantial, undisclosed monetary benefits to the city's investment officer who was authorized to select a broker-dealer for the transactions. See In the Matter of Pryor, McClendon, Counts & Co., Inc. et al., Securities Act Release No. 7673 (Apr. 29, 1999); Securities Act Release No. 8062 (Feb. 6, 2002); Exchange Act Release No. 48095 (June 26, 2003); Securities Act Release No. 8245 (June 26, 2003); Securities Act Release No. 8246 (June 26, 2003).

prohibit or regulate these practices in recent years.[43] And, most recently, in response to pay to play scandals that have emerged in their jurisdictions, public officials with oversight of public pension funds have written to us expressing support for a Commission rule to prohibit investment advisers from participating in pay to play practices, including prohibiting the use by advisers of placement agents (or other types of consultants) to help secure government business.[44]

These developments indicate that investment advisers may be playing an increasing role in pay to play activities. We therefore believe it is time for us to act with respect to investment advisers who may engage in such activities.[45]

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43 For an example of a state statutory restriction on pay to play activities, see Ill. Pub. Act 095-0971 (2008). For an example of a restriction pursuant to a state constitutional amendment, see COLO. CONST. amend. LIV (2008). For an example of a county restriction, see Resolution No. 08-397 (May 8, 2008) Special Pay to Play Restrictions for Professional Service Contracts and Extraordinary Unspecifiable Service Contracts, Monmouth County, NJ. For an example of a city restriction, see Ordinance 3663 (July 2, 2007), Prohibition of Redevelopment with Certain Contributors, Township of Franklin, NJ. For an example of a particular local government agency restriction, see CAL. PUB. UTIL. CODE § 130051.20 (2008), Contributions to Authority Members, Los Angeles County Metropolitan Transportation Authority. For an example of a particular public pension fund restriction, see Prohibitions on Campaign Contributions, California State Teachers' Retirement System, 5 CCR § 24010 (2009).

44 See, e.g., Letter from New York City Comptroller William C. Thompson, Jr., to Securities and Exchange Commission Chairman Mary L. Schapiro, dated May 12, 2009, available at http://www.comptroller.nyc.gov/press/pdfs/05-13-09_SEC-letter.pdf, at 2; Letter from New York State Comptroller Thomas P. DiNapoli to Securities and Exchange Commission Chairman Mary L. Schapiro, dated May 7, 2009, available at http://www.osc.state.ny.us/press/releases/may09/sec050709.pdf, at 1-2.

45 Another reason we believe it is important for us to act is because pay to play practices are characterized by what the Blount court called a "collective action problem [that tends] to make the misallocation of resources persist." Blount, supra note 16 at 945-46. Elected officials that accept contributions from state contractors may believe they have an advantage over their opponents that forswear the contributions, and firms that do not "pay" may fear they will lose government business to those that do. See id. See generally MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION; PUBLIC GOODS AND THE THEORY OF GROUPS 44 (17th ed. 1998) (group members that seek to maximize their individual personal welfare will not act to advance common objectives absent coercion or other incentive). See also Paul Jacobs, Donations to Pension

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Section 206(1) of the Advisers Act prohibits an investment adviser from "employ[ing] any device, scheme, or artifice to defraud any client or prospective client."[46] Section 206(2) prohibits advisers from engaging in "any transaction, practice or course of business which operates as a fraud or deceit on any client or prospective client."[47] The Supreme Court has construed section 206 as establishing a federal fiduciary standard governing the conduct of advisers.[48]

Investment advisers that seek to influence the award of advisory contracts by public pension plans, by making political contributions to or soliciting them for those officials who are in a position to influence the awards, compromise their fiduciary obligations to the public pension plans.[49] In making such contributions, the adviser hopes to benefit from officials that

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Officials Scrutinized; Politics: Connell, Fong Say They Are not Influenced by Contributions from Firms Doing Business with State Systems, L.A. TIMES, Aug. 21, 1997, at A41 (fund contractor quoted as saying, "[i]f you don't contribute, you're subject to the concern that others might make contributions").

46 15 U.S.C. 80b-6(1).

47 15 U.S.C. 80b-6(2).

48 Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, 17 (1979); SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-192 (1963).

49 See 1999 Proposing Release, supra note 17, at 3. As a fiduciary, an adviser has a duty to deal fairly with clients and prospective clients, and must make full disclosure of any material conflict or potential conflict. See, e.g., Capital Gains Research Bureau, 375 U.S. at 189, 191-192; Release 1092, supra note 7. Most public pension plans establish procedures for hiring investment advisers, the purpose of which is to obtain the best possible management services. When an adviser makes political contributions for the purpose of influencing the selection of the adviser to advise a public pension plan, the adviser seeks to interfere with the merit-based selection process established by its prospective clients – the public pension plan. The contribution creates a conflict of interest between the adviser (whose interest is in being selected) and its prospective client (whose interest is in obtaining the best possible management services). Even if the conflict was acknowledged and disclosed by the adviser, disclosure may not be effective in protecting the plan from harm. Disclosure to the trustee or board of trustees may be

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"award the contracts on the basis of benefit to their campaign chests rather than to the governmental entity."[50] If pay to play is a factor in the selection process, the public pension plan can be harmed in several ways. The most qualified adviser may not be selected, potentially leading to inferior management, diminished returns or greater losses. The pension plan may pay higher fees because advisers must recoup the contributions, or because contract negotiations may not occur on an arm's-length basis. The absence of arm's-length negotiations may enable advisers to obtain greater ancillary benefits, such as "soft dollars," from the advisory relationship, which may be directed for the benefit of the adviser, potentially at the expense of the pension plan, thereby using a pension plan asset for the adviser's own purposes.[51]

We believe that play to play is inconsistent with the high standards of ethical conduct required of fiduciaries under the Advisers Act. We have authority under section 206(4) of the Act to adopt rules "reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive or manipulative."[52] Congress gave us this authority to prohibit "specific evils" that the broad anti-fraud provisions may be incapable of covering.[53] The

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futile in protecting the plan since the trustees may be similarly conflicted, having accepted the contribution. Disclosure to beneficiaries may also be inadequate as they may be unable to act on the disclosure – beneficiaries generally cannot fire the adviser or find another pension plan.

50 See Blount, supra note 16, at 944-45.

51 Cf. In re Performance Analytics, et al., Investment Advisers Act Release No. 2036 (June 17, 2002) (settled enforcement action in which an investment consultant for a union pension fund entered into a $100,000 brokerage arrangement with a soft dollar component in which the investment consultant would continue to recommend the investment adviser to the pension fund as long as the investment adviser sent its trades to one particular broker-dealer).

52 15 U.S.C. 80b-6(4).

53 S. REP. NO. 1760, 86th Cong., 2d Sess. 4, 8 (1960). The Commission has used this authority to adopt seven rules addressing abusive advertising practices, custodial arrangements, the use of

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provision thus permits the Commission to adopt prophylactic rules that may prohibit acts that are not themselves fraudulent.[54] As noted above, pay to play practices are rarely explicit and often hard to prove, which makes a prophylactic rule particularly appropriate.[55] We are today proposing new rule 206(4)-5 under the Advisers Act designed to eliminate adviser participation in pay to play practices.

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solicitors, required disclosures regarding the adviser's financial condition and disciplinary history, proxy voting, compliance procedures and practices, and deterring fraud with respect to pooled investment vehicles. 17 CFR 275.206(4)-1; 275.206(4)-2; 275.206(4)-3; 275.206(4)-4; 275.206(4)-6; 275.206(4)-7; and 275.206(4)-8.

54 Section 206(4) was added to the Advisers Act in Pub. L. No. 86-750, 74 Stat. 885 (1960) at sec. 9. See H.R. Rep. No. 2197, 86th Cong., 2d Sess. (1960) at 7-8 ("Because of the general language of section 206 and the absence of express rulemaking power in that section, there has always been a question as to the scope of the fraudulent and deceptive activities which are prohibited and the extent to which the Commission is limited in this area by common law concepts of fraud and deceit . . . [Section 206(4)] would empower the Commission, by rules and regulations to define, and prescribe means reasonably designed to prevent, acts, practices, and courses of business which are fraudulent, deceptive, or manipulative. This is comparable to Section 15(c)(2) of the Securities Exchange Act [15 U.S.C. 78o(c)(2)] which applies to brokers and dealers."). See also S. REP. NO. 1760, 86th Cong., 2d Sess. (1960) at 8 ("This [section 206(4) language] is almost the identical wording of section 15(c)(2) of the Securities Exchange Act of 1934 in regard to brokers and dealers."). The Supreme Court, in United States v. O'Hagan, interpreted nearly identical language in section 14(e) of the Securities Exchange Act [15 U.S.C. 78n(e)] as providing the Commission with authority to adopt rules that are "definitional and prophylactic" and that may prohibit acts that are "not themselves fraudulent ... if the prohibition is 'reasonably designed to prevent ... acts and practices [that] are fraudulent.'" United States v. O'Hagan, 521 U.S. 642, at 667, 673 (1997). The wording of the rulemaking authority in section 206(4) remains substantially similar to that of section 14(e) and section 15(c)(2) of the Securities Exchange Act. See also Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles, Investment Advisers Act Release No. 2628 (Aug. 3, 2007) [72 FR 44756 (Aug. 9, 2007)] (stating, in connection with the suggestion by commenters that section 206(4) provides us authority only to adopt prophylactic rules that explicitly identify conduct that would be fraudulent under a particular rule, "We believe our authority is broader. We do not believe that the commenters' suggested approach would be consistent with the purposes of the Advisers Act or the protection of investors.").

55 Cf. Blount, supra note 16 at 945 ("no smoking gun is needed where, as here, the conflict of interest is apparent, the likelihood of stealth great, and the legislative purpose prophylactic").

II. DISCUSSION

A. Rule 206(4)-5: "Pay to Play" Restrictions

The rule we are proposing today is designed to protect public pension plans from the consequences of pay to play practices by preventing advisers' participation in such practices. As a result, advisers and government officials may attempt to structure their transactions in a manner intended to hide the true purpose of a contribution or a payment. For that reason, our proposed pay to play restrictions would capture not only direct political contributions by advisers, but also other ways that advisers may engage in pay to play arrangements. Rule 206(4)-5 would accomplish this through three measures. First, the rule would make it unlawful for an adviser to receive compensation for providing advisory services to a government entity for a two-year period after the adviser or any of its covered associates makes a political contribution to a public official of a government entity that is in a position to influence the award of advisory business.[56] Proposed rule 206(4)-5 would not, therefore, ban or limit the amount of political contributions an adviser or its covered associates could make; rather, it would impose a two-year "time out" on conducting compensated advisory business with a government client after a contribution is made. This aspect of the proposed rule is modeled on MSRB rule G-37 and is consistent with our 1999 proposal.

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[56] Proposed rule 206(4)-5(a)(1) states: "As a means reasonably designed to prevent fraudulent, deceptive or manipulative acts, practices, or courses of business within the meaning of section 206(4) of the Act [15 U.S.C. 80b-6(4)], it shall be unlawful: (1) for any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act [15 U.S.C. 80b-3(b)(3)], to provide investment advisory services for compensation to a government entity within two years after a contribution to an official of the government entity is made by the investment adviser or any covered associate of the investment adviser (including a person who becomes a covered associate within two years after the contribution is made)."

Second, the rule would prohibit advisers from paying third parties to solicit government entities for advisory business.[57] That is, an adviser would be prohibited from providing or agreeing to provide, directly or indirectly, payment to any person who is not a related person of the adviser for solicitation of government advisory business on behalf of such adviser. This aspect of our proposed rule is modeled on MSRB rule G-38.[58] Third, the rule would also make it unlawful for an adviser itself or through any of its covered associates to solicit or to coordinate contributions for an official of a government entity to which the investment adviser is seeking to provide investment advisory services, or payments to a political party of a state or locality where the investment adviser is providing or seeking to provide investment advisory services to a government entity. MSRB rule G-37 contains a similar prohibition, as did our 1999 proposal.[59]

We recognize that we cannot anticipate all of the ways advisers and government officials may structure pay to play arrangements to attempt to evade the prohibitions of our proposed rule. For that reason, we are also proposing to include a provision that would make it unlawful for an adviser or any of its covered associates to do anything indirectly which, if done directly, would result in a violation of the proposed rule. Finally, for purposes of the proposed rule, an investment adviser to certain pooled investment vehicles in which a government entity invests or

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57 Proposed rule 206(4)-5(a)(2)(i).

58 MSRB rule G-38 was amended in 2005 to prohibit municipal securities dealers from paying third-party solicitors to solicit municipal securities business. In the Matter of Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 to the Proposed Rule Change Relating to Solicitation of Municipal Securities Business under MSRB Rule G-38, Exchange Act Release No. 52278 (Aug. 17, 2005) [70 FR 49342 (Aug. 23, 2005)]. Our 1999 proposal did not include an analogous prohibition.

59 See MSRB rule G-37(c); 1999 Proposing Release, supra note 17, at section II.A.2.

is solicited to invest would be treated as though the adviser were providing or seeking to provide investment advisory services directly to the government entity.

Although today's proposal is similar to the one we made in 1999, we are proposing a few critical changes in response to intervening developments that we highlight in the discussion below. We have made these changes to conform our proposal to measures undertaken in recent years to curtail pay to play activities by the MSRB and various state and local authorities and to deter circumvention of the restrictions through the use of third-party placement agents or through an adviser obtaining government clients indirectly by soliciting investment in funds it manages.

1. Advisers Subject to the Rule

Proposed rule 206(4)-5 would apply to any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act [15 U.S.C. 80b-3(b)(3)].[60] We are including this category of exempt advisers within the scope of the rule in order to make the rule applicable to the many advisers to private investment companies that are not registered under the Advisers Act.[61] The rule would not apply, however, to most small advisers that are registered with the state securities authorities,[62] and certain other advisers that are exempt from registration with us.[63] We believe

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60 Proposed rule 206(4)-5(a)(1) and (2). Section 203(b)(3) [15 U.S.C. 80b-3(b)(3)] exempts from registration any investment adviser that is not holding itself out to the public as an investment adviser and had fewer than 15 clients during the last 12 months.

61 See discussion infra section II.A.3(e).

62 Section 203A of the Advisers Act [15 U.S.C. 80b-3A] prohibits investment advisers with less than $25 million in assets under management from registering with the Commission; although we do not propose to include them within the coverage of this rule, they remain subject to the Act's general anti-fraud authority. See, e.g., Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 1633, n.154 and accompanying text (May 15, 1997) [62 FR 28112 (May 22, 1997)] ("Both the Commission and the states will be

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that the rule would apply to most advisers to public pension plans.[64] We request comment on the scope of the proposed rule. Should we apply the rule to state-registered advisers? Should we limit the rule only to advisers registered (or required to be registered) with us? Should we apply the rule to advisers that are exempt from registration in reliance on Advisers Act section 203(b)(3)? We request comment on whether we should extend the scope of the rule to apply to advisers exempt from registering with us pursuant to any or all of the other categories under Advisers Act section 203(b). For example, should we include advisers exempt from registration pursuant to any or all of Advisers Act sections 203(b)(1) (intrastate advisers), 203(b)(2) (advisers with only insurance company clients), 203(b)(4) (investments advisers that are charitable organizations), 203(b)(5) (advisers that are plans described in section 414(e) of the Internal Revenue Code of 1986 or certain persons associated with such plans), or 203(b)(6) (certain

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able to continue bringing antifraud actions against investment advisers regardless of whether the investment adviser is registered with the state or the SEC."). See also S. REP. NO. 293, 104th Cong., 2d Sess. 3-4 (1996) ("1996 Senate Report") at 4.

63 See, e.g, exemption for intrastate investment advisers under section 203(b)(1) [15 U.S.C. 80b-3(b)(1)].

64 With the exception of the exemption from registration provided for by section 203(b)(3) [15 U.S.C. 80b-3(b)(3)], advisers that are exempt from SEC registration are unlikely to have state or municipal government clients as providing advisory services to them would result in the adviser no longer being eligible for the exemption, e.g., section 203(b)(2) [15 U.S.C. 80b-3(b)(2)] and section 203(b)(4) [15 U.S.C. 80 b-3(b)(4)]. Moreover, based on a review of a sampling of requests for proposals from state and municipal governments for investment advisory services, a common requirement is that the adviser be registered with the SEC or a state. See, e.g., Request for Information Vermont Pension Investment Committee – Vermont Manager Program RFI (Feb. 27, 2009) (stating that eligible investment advisers must be SEC-registered with at least $100 million in assets under management), available at: http://www.vermonttreasurer.gov/documents/rfp/20090316_VPICVermontManagerProgram.pdf. It also is our understanding from discussions with representatives of the state securities regulators that a very small percentage of state-registered advisers have state or municipal government clients.

commodity trading advisors)?[65] To the extent that they are able to have government clients at all, are any of these advisers likely to engage in pay to play?

We note that proposed rule 206(4)-5 would regulate the activities of investment advisers – business organizations over which we have clear regulatory authority under the Advisers Act. The rule would have no effect on state laws, codes of ethics or other rules governing the activities of state and municipal officials or employees of public pension plans over whom we have no regulatory jurisdiction.[66]

2. Relationship with MSRB Rules; Alternative Approaches

As discussed above, we modeled proposed rule 206(4)-5 on MSRB rules G-37 and G-38, which we believe have successfully addressed pay to play in the municipal bond market. This approach should minimize the compliance burdens on firms that would be subject to both rule regimes because firms that are already subject to MSRB rules would already have developed policies and systems for compliance that could be adapted to meet investment adviser requirements. Certain provisions of our proposed rule, however, are somewhat different in ways that reflect the different statutory framework under which the rule would be adopted and the differences between municipal underwriting and asset management. Comment is requested on

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65 Our 1999 proposed rule would have applied to all investment advisers not prohibited from registering with the Commission. See 1999 Proposing Release, supra note 17.

66 A number of commenters in 1999, including those representing state and local officials, argued that the rule would be an intrusion on state sovereignty. We disagree. We have a responsibility to regulate the activities of investment advisers. Our objectives in the proposed rule do not relate to campaign finance, but rather to prohibiting fraudulent activity by investment advisers. We believe our proposed rule is appropriately tailored to those ends.

whether we should use rules G-37 and G-38 as the models for proposed rule 206(4)-5.[67] If not, are there alternative models that would be more appropriate? Are there significant differences in governments' selection process for municipal underwriters and investment advisers that we have not addressed but that should be reflected in the rule? Would our approach adequately protect public pension plans, their sponsors and participants against the adverse effects of pay to play practices?

We understand many advisers have established restrictions on pay to play practices in their codes of ethics and compliance policies. Instead of, or in addition to, adopting a new rule to address pay to play practices, should we amend our code of ethics rule[68] or our compliance rule[69] to require all registered advisers to adopt policies and procedures designed to prevent them from engaging in pay to play practices?[70] Should we instead, or also, require an executive officer of

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67 For instance, in 1999, we requested comment on our use of MSRB rule G-37 as a model, and several commenters responded that, because of distinctions between the investment adviser profession and the municipal securities industry, we should not follow the approach of MSRB rule G-37. Some commenters asserted that, unlike municipal underwriters, advisers' business relationships with state and municipal clients are ongoing and long-term and thus the two-year ban is much more harsh a consequence. While municipal underwritings themselves tend to be episodic, underwriting relationships are often longstanding. As a result, the rules' time outs may have similar effects.

68 Rule 204A-1 under the Advisers Act [17 CFR 275.204A-1].

69 Rule 206(4)-7 under the Advisers Act [17 CFR 275.206(4)-7].

70 Some commenters in 1999 suggested that the better approach would be to require advisers to adopt codes of ethics designed to prevent pay to play practices. The Investment Counsel Association of America (subsequently renamed the Investment Advisers Association) submitted to the comment file relating to our 1999 proposal "<u>Best Practice Pay-to-Play Guidelines for Adviser Codes of Ethics,</u>" advocating such an approach as an alternative to our 1999 proposal. <u>See</u> http://www.sec.gov/rules/proposed/s71999/tittswo2.htm. The ICAA offered the following three alternative policies on political contributions, and suggested that advisers should tailor these policies to fit their respective circumstances: (1) a contribution ban above a certain <u>de minimis</u> amount (either with respect to all political contributions or ones that fall within certain specified parameters); (2) a pre-clearance process for contributions; or (3) a disclosure policy with respect to contributions. At that time, codes of ethics were voluntary. However, in 2004,

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each adviser to certify annually that the adviser or its covered associates did not participate in pay to play? Should some other employee of the adviser, such as the chief compliance officer, make the certification?

In 1999, we considered proposing a different approach to address pay to play, which would have required an adviser to disclose information about its political contributions to officials of government entities to which it provided or was seeking to provide investment advisory services. We decided not to propose such an approach at that time because we thought that disclosure would not be effective to protect public pension plan clients.[71] Disclosure to a pension plan's trustees might be insufficient because, in some cases, the trustees would have received the contributions. Disclosure to plan beneficiaries also would likely be insufficient because they are generally unable to act on the information by moving their pension assets to a

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the Commission adopted a requirement that advisers adopt and implement codes of ethics that include a standard of conduct that reflects the adviser's fiduciary obligations, although the code of ethics rule does not directly address pay to play practices. See Advisers Act rule 204A-1 [17 CFR 275.204A-1]; Investment Adviser Codes of Ethics, Investment Advisers Act Release No. 2256 (July 2, 2004) [69 FR 41696 (July 9, 2004)]. See also Investment Counsel Association of America, Report on Pay-to-Play and the Investment Advisory Profession (May 15, 2000), available at http://www.investmentadviser.org/eweb/docs/Publications_News/PublicDocs_UsefulWebsites/PubDoc/report (condemning practices by which investment professionals try to gain access to business through political contributions, and urging its members to adopt codes of ethics designed to prevent pay to play).

71 In response to our 1999 Proposal, some commenters suggested requiring advisers to disclose publicly their contributions to state and local officials. Statutes requiring disclosure of political contributions are designed to inform voters about a candidate's financial supporters; an informed electorate can then use the information to vote for or against a candidate. But, as several other commenters correctly pointed out, our goal is not campaign finance reform, and how voters might react to such disclosure is not, for us, the relevant concern. Our primary concern is the protection of advisory clients and investors who are affected by pay to play practices whom we have the responsibility to protect under the Advisers Act.

different plan or reversing adviser hiring decisions. Moreover, disclosure requirements may not stop pay to play practices and can be circumvented.[72] Accordingly, we do not believe that relying on disclosure is sufficient to address these problematic practices.[73] We request comment on whether we should, nonetheless, consider this approach, as well as potential alternative approaches that may be more effective or less costly.

3. Pay to Play Restrictions

(a) Two-Year "Time Out" for Contributors

Proposed rule 206(4)-5(a)(1) would prohibit investment advisers from providing advice for compensation to a "government entity"[74] within two years after a "contribution" to an "official" of the government entity has been made by the investment adviser or by any of its "covered associates."[75] We are proposing that the time out be two years long because the duration needs to be sufficiently long to have a deterrent effect. We recognize, however, that a longer ban could be overly harsh.[76] We note that MSRB rule G-37 contains a two-year time out,

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72 See infra note 158 and accompanying text regarding swap arrangements that may used to circumvent public disclosure.

73 MSRB rule G-37, however, does establish a reporting and disclosure system for broker-dealers subject to that rule. MSRB rule G-37(e)(ii).

74 "Government entity" is defined by the proposed rule as "any State or political subdivision of a State, including any agency, authority, or instrumentality of the State or political subdivision, a plan, program, or pool of assets sponsored or established by the State or political subdivision or any agency, authority or instrumentality thereof; and officers, agents, or employees of the State or political subdivision or any agency, authority or instrumentality thereof, acting in their official capacity." Proposed rule 206(4)-5(f)(5).

75 Proposed rule 206(4)-5(a)(1).

76 We note that, notwithstanding the proposed duration of the rule's "time out" – two years – the reach of the time out is relatively narrow in the sense that it only prohibits advisers from receiving compensation for providing advice from the particular government entities to whose officials triggering contributions have been made. It does not limit the adviser from receiving

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which appears, based on the success of the MSRB rules, to have operated as an effective deterrent in the municipal securities context.[77] We request comment on whether two years is an appropriate length of time.[78]

(1) Prohibition on Compensation

Investment advisers making contributions covered by the proposed rule would not be prohibited from providing advisory services to a government client, even after triggering the two-year time out. Instead, an adviser would be prohibited from receiving compensation for providing advisory services to the government client during the time out. This approach is intended to avoid requiring an adviser to abandon a government client after the adviser or any of its covered associates makes a political contribution covered by the rule. An adviser subject to the prohibition would likely, at a minimum, be obligated to provide (uncompensated) advisory

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compensation from other government entities as to which triggering contributions have not been made.

77 See supra note 24. Several commenters in 1999 suggested that, because advisers' business relationships with state and municipal clients are ongoing and long-term, as compared to the relationships between municipal underwriters and their clients, the two-year ban is much more harsh a consequence. As we note above, while municipal underwritings themselves tend to be episodic, underwriting relationships are often longstanding, which may result in the rules' time outs having similar effects. See supra note 67.

78 Some commenters in 1999 objected to two years as being too long a period of time (arguing, for example, that because changing investment advisers can be so disruptive to a pension fund that such a fund would be extremely unlikely to return to an adviser after a "time out," thereby rendering the two-year ban tantamount to a permanent one), whereas others suggested that the period be longer or that it track the remainder of the term of the government official to whom the contribution was made.

services for a reasonable period of time[79] until the government client finds a successor to ensure its withdrawal did not harm the client, or the contractual arrangement between the adviser and the government client might obligate the adviser to continue to perform under the contract at no fee.[80] We request comment on our proposed approach. Is there another approach that would cause less disruption to the government client?

(2) Officials of a Government Entity

The prohibitions in the rule would be triggered by a contribution to an "official" of a "government entity." Government entities under the proposed rule include all state and local governments, their agencies and instrumentalities, and all public pension plans and other

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79 Some commenters in 1999 indicated concern that government entities that retain advisers who trigger the two-year time out – and would therefore be unable to receive compensation for two years – might try to delay an adviser's ability to withdraw in order to enjoy the benefits of investment advice for free. We believe that while an adviser's fiduciary obligations require it to act in the best interests of its clients, they do not require it to provide uncompensated advice indefinitely because it is prohibited from receiving compensation under the rule – rather, the adviser may need to continue to provide advice for only a reasonable period of time.

80 An investment adviser that violates the rule may be required, under its fiduciary duties, to continue providing advisory services to the public pension plan, for a reasonable period of time, until the plan obtains a new adviser. See Temporary Exemption for Certain Investment Advisers, Investment Advisers Act Release No. 1846 (Nov. 29, 1999) [64 FR 68019, 68024 (Dec. 6, 1999)] (describing an investment adviser's fiduciary duties to an investment company in the case of an assignment of the advisory contract).

We note that the two-year time out in MSRB rule G-37 operates to prohibit a broker, dealer or municipal securities dealer from engaging in all municipal securities business; it does not distinguish between providing compensated and uncompensated services. MSRB Rule G-37(b)(i). See also MSRB Rule G-37 Interpretive Notices, Interpretation of Prohibition on Municipal Securities Business Pursuant to Rule G-37 (Feb. 21, 1997) (determining that once a dealer enters into contract and a subsequent contribution results in a prohibition, the dealer "should not be allowed to continue with the municipal securities business, subject to an orderly transition to another entity to perform such business"). But see infra note 189 (discussing MSRB's approach to transitions in the context of pre-existing engagements relating to municipal fund securities, such as interests in Section 529 plans).

collective government funds.[81] An official would include an incumbent, candidate or successful candidate for elective office of a government entity if the office is directly or indirectly responsible for, or can influence the outcome of, the selection of an investment adviser or has authority to appoint any person who is directly or indirectly responsible for or can influence the outcome of the selection of an investment adviser.[82] Generally, executive or legislative officers who hold a position with influence over the hiring of an investment adviser are government officials under the proposed rule.[83] These definitions are substantively the same as those in MSRB rule G-37.[84]

We request comment on our proposed definition of "official." For instance, a candidate for federal office may be an "official" under the rule, just as such a person may be under MSRB rule G-37, not because of the office he or she is running for, but as a result of an office he or she currently holds.[85] As a preliminary matter, we do not believe that an incumbent state or local

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81 See supra note 74.

82 Proposed rule 206(4)-5(f)(6). The two-year time out would be triggered by contributions, not only to elected officials who have legal authority to hire or select the adviser, but to elected officials (such as persons with appointment authority) who can influence the hiring of the adviser. A person who serves at the will of an elected official is likely to be subject to that official's influences and recommendations. We note that MSRB rule G-37 also applies to elected officials empowered to appoint persons with the authority to select which broker-dealers will receive government business.

83 It is the scope of authority of the particular office of an official, not the influence actually exercised by the individual, that would determine whether the individual has influence over the awarding of an investment advisory contract under the definition.

84 See MSRB rule G-37(g)(ii) and (g)(vi).

85 Proposed rule 206(4)-5(f)(6), in relevant part, defines "official" as any person . . . who was, at the time of the contribution, an incumbent, candidate or successful candidate for elective office of a government entity . . . ," and a "government entity," in relevant part, as "any state or political subdivision of a state" (emphasis added). Accordingly, any person, including a person running for federal office, who meets the definition of "official" would be covered under the rule. See also MSRB rule G-37(g)(ii) and (g)(vi) (defining "issuer" and "official of an issuer",

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official should be excluded from the definition solely because he or she is running for federal office, but we request comment on this aspect of the proposed rule. Should such a candidate for federal office be excluded?[86] Are there other persons to whom an adviser or its covered associates might make a contribution to influence the selection of that adviser? For example, should we expand the rule's prohibitions to apply expressly in cases where an adviser or a covered associate gives a contribution to others closely associated with the official – such as an official's political action committee ("PAC"), his or her inauguration or transition committee,[87] a local or state political party that provides assistance to such official,[88] or a foundation or other charitable institution associated with such official?[89]

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respectively); MSRB Qs & As, Question IV.2 and IV.3, available at http://www.msrb.org/msrb1/rules/QAG-372003.htm (explaining how G-37 applies to candidates for federal office).

86 Some 1999 commenters urged that contributions to candidates for federal office be excluded from the rule, while others agreed these contributions should be covered. In particular, certain commenters asserted that this aspect of the proposed rule would have a disparate effect on candidates for federal office because state and local politicians would experience limitations on their ability to receive federal campaign contributions while their opponents would be subject to no such limitations. These commenters also claimed the rule would have little effect because if the candidate for federal office was successful, he or she would quickly lose his or her ability to influence the selection of an investment adviser at the state or local level. Other commenters thought it appropriate that the rule apply to candidates for federal office. As noted above, our emphasis in the proposed rule remains on the current office of an elected official and his or her ability to affect the selection of an investment adviser, regardless of what outside positions that official may seek.

87 A contribution to an official, as opposed to a committee, for inauguration or transition expenses would be a contribution under the proposed rule. See infra note 93 and accompanying text. This approach is consistent with the approach in MSRB rule G-37. We are proposing a similar approach for reasons of regulatory consistency; nonetheless, we have included this request for comment on whether we should include contributions to such committees.

88 Under the proposed rule, such contributions or payments by an adviser (or its covered associates) would only trigger the rule's provisions to the extent that an adviser was trying to do indirectly what it is prohibited from doing directly. See infra section II.A.3(d) of this Release. In contrast,

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(3) Contributions

The proposed rule covers "contributions" made by an investment adviser and its covered associates. The proposed rule uses the same definition of contribution as MSRB rule G-37.[90] A contribution would generally be any gift, subscription, loan, advance, deposit of money, or anything of value[91] made for the purpose of influencing an election for a federal, state or local office, including any payments for debts incurred in such an election.[92] It would also include

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the prohibition on advisers soliciting contributions or payments from others in proposed rule 206(4)-5(a)(2)(ii) would expressly include payments to a political party of a state or locality where the investment adviser is providing or seeking to provide investment advisory services to a government entity. See infra section II.A.3(c) of this Release. Further, our proposed amendments to rule 204-2 (in particular, rule 204-2(a)(18)(i)(D)) would expressly include a requirement that an adviser subject to the rule make and keep records of, among other things, all direct or indirect contributions or payments made by the investment adviser or any of its covered associates to a political party of a State or political subdivision thereof. Our proposed approach to these provisions generally tracks the MSRB approach.

89 For a discussion of associated recordkeeping requirements, see infra note 206 and accompanying text.

90 MSRB rule G-37(g)(i).

91 Commenters to our 1999 proposal raised concerns that volunteer campaign work by advisory employees could trigger the proposed rule's time out provision. We would not consider volunteer campaign work by an individual to be a contribution, provided the adviser has not solicited the individual's efforts and the adviser's resources, such as office space, are not used. Cf. MSRB Qs & As, Question II.12, available at http://www.msrb.org/msrb1/rules/QAG-372003.htm.

92 Proposed rule 206(4)-5(f)(1). Commenters in 1999 expressed concern that the scope of our proposed rule was too broad. These commenters, many of whom represented investment advisers, raised concerns that the rule as proposed could unnecessarily restrict their employees from making any political contributions. Some commenters questioned the constitutionality of our proposal, arguing that the proposed rule would violate First Amendment protections for free speech. In Blount, supra note 16, a federal appeals court upheld a First Amendment challenge to MSRB rule G-37. The Court left open the question of the appropriate level of scrutiny to be applied, but concluded that the rule satisfied even a strict scrutiny test. We believe that the rule we are proposing today similarly is consistent with the First Amendment. Absent provisions to limit the application of the rule's prohibitions, it could result in frequent inadvertent violations that would carry harsh consequences for advisers. Accordingly, we refined the categories of

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transition or inaugural expenses incurred by a successful candidate for state or local office.[93] We request comment on our proposed definition of "contribution."[94] Are there additional items of value that, as with transitional or inaugural expenses, should be specified in and covered by the definition? For instance, should we include the expenses an investment adviser would incur in organizing or sponsoring a conference at which a government official is invited to attend or is a speaker?[95] If so, how should our rule distinguish legitimate conferences or meetings from those that are more akin to fundraising events?[96] Are there items that should be excluded from the definition?

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persons whose personal political contributions would be covered under the rule and provided for a self-executing exception that should prevent many inadvertent violations. We believe these changes will address many of the commenters' concerns about the rule we proposed in 1999.

93 Proposed rule 206(4)-5(f)(1)(iii). Transition or inaugural expenses of a successful candidate for federal office are not included. Contributions to political parties are not specifically covered by the definition and thus would not trigger the proposed rule's two-year timeout unless they are a means to do indirectly what the proposed rule would prohibit if done directly (for example, the contributions are earmarked or known to be provided for the benefit of a particular political official). See proposed rule 206(4)-5(d). Contributions to state and local political parties are, however, subject to the proposed rule's recordkeeping requirements. See infra section II.B and proposed rule 204-2(a)(18)(i)(D).

94 Commenters in 1999 urged us to adopt a rule prohibiting only political contributions intended to influence, or made for the purpose of influencing, adviser selection. This approach, they argued, would eliminate the risk that innocent campaign contributions would trigger application of the "two-year time out." Political contributions are made ostensibly to support a candidate, however, and the burden of proving a different intent is very difficult absent unusual evidence. As one court noted, "actors in this field are presumably shrewd enough to structure their relations rather indirectly." Blount, supra note 16. As a result, requiring proof of such an intent would greatly diminish, if not eliminate, the prophylactic value of the proposed rule.

95 Under the proposed rule, an adviser would be prohibited from soliciting contributions for the official. Proposed rule 206(4)-5(a)(2)(ii).

96 Cf. Supervision When Sponsoring Meetings and Conferences Involving Issuer Officials, MSRB Rule G-37 Interpretive Notice (Mar. 26, 2007), available at http://www.msrb.org/msrb1/rules/notg37.htm (rather than addressing meetings and conferences

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(4) Covered Associates

Contributions made to influence the selection process are typically made not by the firm itself, but by officers and employees of the firm who have a direct economic stake in the business relationship with the government client. For this reason, MSRB rule G-37 limits its prohibitions to contributions made by "municipal finance professionals" employed by a broker-dealer. No group analogous to municipal finance professionals, however, exists within the typical investment advisory firm. In many of the pay to play enforcement actions we have brought involving investment advisers, we have alleged that political contributions or other payments were made to influence the selection of the advisory firm by executives of the adviser or persons who solicit government clients on behalf of the adviser.[97] We therefore are proposing to limit application of

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of this nature in its rules directly, the MSRB applies a facts-and-circumstances test on a case-by-case basis).

97 See, e.g., In the Matter of Barrett N. Wissman, Investment Advisers Act Release No. 2879 (May 22, 2009) (in a settled action, the Commission alleged that managing director of registered investment adviser engaged in a fraudulent scheme involving undisclosed kickback payments made by investment management firms and others in connection with the sale of securities to the New York Common Retirement Fund and the investment of the fund's assets in the purchase and sale of securities); In the Matter of Thayer Capital Partners, TC Equity Partners IV, L.L.C., TC Management Partners IV, L.L.C., and Frederick V. Malek, Investment Advisers Act Release No. 2276 (Aug. 12, 2004) (in a settled action, the Commission alleged that unregistered adviser, through its chairman, agreed to hire an inexperienced associate of the Connecticut Treasurer as a consultant as a condition to securing a state pension fund investment); In the Matter of Frederick W. McCarthy, Investment Advisers Act Release No. 2218 (Mar. 5, 2004) (in a settled action, the Commission alleged that principal and chairman of investment management firm provided $2 million in consulting contracts to associates of the Connecticut Treasurer in order to secure the Treasurer's decision to invest). We have also observed this pattern of contributions in pay to play arrangements in other contexts, including those involving union pension funds. See, e.g., In the Matter of William M. Stephens, Investment Advisers Act Release No. 2076 (Nov. 4, 2002) (in a settled action, the Commission alleged that executive vice president and chief investment strategist of registered investment adviser met with people who offered to introduce him to the trustees of union pension funds, and he agreed that after he and his firm became the funds' adviser, he would arrange to divert a portion of the funds into investments controlled by the

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the rule's "time out" provision to contributions made by the adviser and its "covered associates," which would include the adviser's general partners, managing members, executive officers, or other individual with a similar status or function.[98] Any employee of the adviser who solicits[99] government entity clients for the investment adviser would also be a covered associate,[100] as

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people who made the introductions, who would, in turn, pay kickbacks to the pension fund trustees who hired him and his firm); In the Matter of Chris Woessner, Investment Advisers Act Release No. 2164 (Aug. 26, 2003) (Commission alleged that former vice president of sales at registered investment adviser who was in charge of marketing to pension plans caused his firm to direct client commissions for the benefit of a broker-dealer and pension consultant in exchange for the referral of a union pension fund client to the firm).

98 Proposed rule 206(4)-5(f)(2)(i). Under our 1999 proposal, the rule would have applied more broadly to "partners" (not just a general partner or equivalent) and "executive officers" (which we proposed to define as "the president, any vice president in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy-making function, or any other person who performs similar policy-making functions, for the investment adviser"). See 1999 Proposing Release, supra note 17, at section II.A.1. Commenters in 1999 suggested that, instead of applying the rule to all partners, we narrow the rule to apply only to a firm's general partner (or equivalent) and other owners that have a significant ownership interest in the firm. Commenters also suggested that we either exclude executive officers of divisions unrelated to the firm's solicitation and/or advisory functions or limit the rule's application to only the most senior officers of an adviser, such as persons required to be listed on Schedule A of Form ADV. In light of these comments, we have included in our proposed definition of "covered associates" only those persons associated with an investment adviser who we believe are more likely to have an economic incentive to make contributions to influence the advisory firm's selection and who we have found, in our enforcement actions, typically make contributions.

99 See proposed rule 206(4)-5(f)(10) (defining "solicit").

100 Proposed rule 206(4)-5(f)(2)(ii). Several commenters in 1999 argued that we would have included too broad a category of solicitors because our definition of "solicitor" would have included any person who solicited any client for or referred any client to the adviser. The two-year time out would have been triggered, for example, by registered representatives who solicited brokerage business for a firm dually registered as a broker-dealer and as an adviser, even though the registered representatives had no involvement with government clients. See 1999 Proposing Release, supra note 17, at section II.A.1. We have included a narrower category of solicitors in our current proposed rule; the two-year time out provisions would be triggered by a contribution by a person who solicits government entities for advisory services. Many commenters also urged that the definition of "solicitor" exclude third-party solicitors. They asserted that it was unfair to hold advisers responsible for the actions of these solicitors, arguing that the advisers did not

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would any PAC controlled by the investment adviser or any of the adviser's covered associates.[101]

Under the proposed rule, the term "executive officer" includes the adviser's president and any vice president in charge of a principal business unit, division or function (such as sales, administration or finance) or any other executive officer who, in each case, in connection with his or her regular duties: (i) performs investment advisory services (or supervises someone who performs them) for an adviser; (ii) solicits (or supervises someone who solicits) for an adviser, including with respect to investors for a covered investment pool;[102] or (iii) supervises, directly or indirectly, executive officers described in (i) or (ii).[103] Accordingly, for instance, the proposed rule would cover contributions by a portfolio manager who is an executive officer, as well as contributions by anyone in the portfolio manager's chain of supervision up to and including the president of the adviser. The rule would also cover contributions by an executive officer who supervises personnel who solicit advisory clients and contributions by anyone in that executive's

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control their activities. We have excluded third-party solicitors from this two-year time out provision; instead we are proposing to prohibit advisers from soliciting government business through third parties, as discussed in detail in section II.A.3(b) of this Release.

101 Proposed rule 206(4)-5(f)(2)(iii). Our 1999 proposal would also have included PACs controlled by the investment adviser and the individuals associated with the investment adviser whose contributions would have triggered the "time out." See 1999 Proposing Release, supra note 17, at section II.A.1. We have proposed to include PACs because these vehicles, which may be regulated by state and/or federal election law, are often used by corporations, interest groups, or others to make political contributions. See, e.g., Tennessee Registry of Election Finance, PACs FAQ, available at http://www.state.tn.us/tref/pacs/pacs_faq.htm; Federal Election Commission, Quick Answers to PAC Questions, available at http://www.fec.gov/ans/answers_pac.shtml.

102 See discussion of covered investment pools, infra, section II.A.3(e).

103 Proposed rule 206(4)-5(f)(4). Our proposed definition of "executive officer" in rule 206(4)-5(f)(4) is based on the same considerations as a similar definition in Advisers Act rule 205-3 [17 CFR 275.205-3]. Whether a person is an executive officer depends on his or her function, not title; a chief executive officer whose title does not include "president" is clearly an executive officer.

chain of supervision. The rule would not, however, cover contributions by the adviser's other executives, such as its comptroller, its head of human resources, or its director of information services, unless the contribution is an indirect contribution for the adviser, because the compensation of these individuals is likely to be tied less directly to obtaining or retaining clients.

Contributions by non-executive employees (other than those who solicit government entity clients) would not trigger the rule's prohibitions, unless the adviser or any of its covered associates used the person to indirectly make a contribution.[104] This could occur, for example, if a firm paid a non-executive employee a bonus with the understanding that the bonus would be used by the employee to make a political contribution that, if made by the firm, would trigger the rule's prohibition.[105]

As noted above, the Commission has drafted the proposed rule so that its prohibitions are triggered by political contributions by persons who, in the context of an advisory firm, are likely to have an economic incentive to make contributions to influence the advisory firm's selection and the categories of executives and employees of an adviser that we have seen, most typically, to make political contributions and payments in pay to play situations. We are mindful of the burdens the proposed rule would place on advisory firms and on the ability of persons associated with an adviser to participate in civic affairs. We thus have narrowly tailored the rule to achieve our goal of preventing adviser participation in pay to play practices.

We request comment on the scope of the proposed rule and, in particular, those persons associated with the advisers whose political contributions would trigger the application of the

104 Proposed rule 206(4)-5(d).

105 See id. See also discussion of indirect contributions, infra section II.A.3(c).

two-year "time out" and would be prohibited from soliciting political contributions from others. Have we included persons most likely to have an economic incentive to make political contributions for the purpose of influencing the selection of the adviser?

Have we covered too many persons? If so, how should we narrow the rule? For example, are there certain executive officers of the adviser we should not include? The proposed rule would cover all executive officers who, as part of their regular duties, perform investment advisory services or supervise someone who performs them. Should we instead limit the scope to a subset of such officers? If so, how should we define that subset?[106] Should we extend the rule to cover all portfolio managers, or just those portfolio managers responsible for managing government client assets? Are there other types of employees whose contributions should trigger the time out?

Have we too narrowly drawn the rule to achieve our goals? Should we, for example, include employees of companies that are related persons of an adviser who solicit government entity clients for the investment adviser? As discussed further below, we propose permitting payments to these persons under the proposed ban on payments to third parties because we recognize that an adviser may rely on them to assist it in seeking government clients.[107] Would that same rationale support including them as "covered associates" of the adviser (whose contributions would be subject the proposed rule's two-year time out provision)? Would not

[106] Many 1999 commenters argued that our proposal included too many persons whose activities are unconnected to managing public pension money, making it too likely that an innocent political contribution would trigger a two-year time out. We considered these comments in narrowing the scope of persons covered by our current proposed rule, as described above.

[107] See discussion at section II.A.3(b), infra.

including them be likely to encourage circumvention of the rule's requirements?[108] We also request comment on whether we should, for example, include certain family members who, and related businesses that, might give political contributions on the adviser's behalf to try to influence officials of government entities?[109] Under the proposed rule, political contributions by such persons would only result in a violation under the rule if the adviser or its covered associates were acting through them to do indirectly what they cannot do directly under the rule.[110] MSRB rule G-37 addresses this matter similarly. Should we include beneficial owners of the adviser because they have a direct economic stake in the adviser's business relationship with the government client? If so, should the definition include all owners, or only those with a significant ownership stake in an adviser, such as those who have contributed (or that have the right to receive upon dissolution) ten percent or more of the company's capital?

(5) "Look Back"

Under the proposed rule, the two-year time out would continue in effect after the covered associate who made the triggering contribution left the advisory firm. Moreover, a contribution made by a covered associate of an adviser would be attributed to any other adviser that employs or engages the person who made the contribution within two years after the date the contribution

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108 See proposed rule 206(4)-5(d), however.

109 See, e.g., Martin Z. Braun et al., A Political Family Affair?, THE BOND BUYER (Oct. 21, 2002) (noting that spouses of municipal finance professionals in dealer firms are making campaign contributions to issuer officials who can influence the award of bond business).

110 Paragraph (d) of proposed rule 206(4)-5. See section II.A.3(d) of this Release.

was made.[111] As a result, an investment adviser would be required to "look back" in time to determine whether it would be subject to any business restrictions under the proposed rule when employing or engaging a covered associate. This provision, which tracks MSRB rule G-37,[112] would prevent advisers from circumventing the rule by channeling contributions through departing employees, or by influencing the selection process by hiring persons who have made political contributions. Comment is requested on the proposed look-back requirement. For example, would a shorter period be sufficient to prevent circumvention of the rule?[113] If so, what period would be appropriate? Would our proposed look-back provision inappropriately deter politically active individuals from joining advisory firms that provide investment advice to government entities or are seeking to do so?

(6) Exception for De Minimis Contributions

111 Proposed rule 206(4)-5(a)(1). In no case would the prohibition imposed by the proposed rule be longer than two years from the date the covered associate makes a covered contribution. If, for example, a covered associate becomes employed by an investment adviser one year and six months after making a contribution, the new employer would be subject to the proposed rule's prohibition for the remaining six months of the two-year period. The covered associate's employer at the time of the contribution would be subject to the proposed rule's prohibition for the entire two-year period regardless of whether the covered associate remains employed by the adviser. See infra section II.B.

112 MSRB rule G-37(g)(iv). Cf. MSRB Qs & As, Question II.12, available at http://www.msrb.org/msrb1/rules/QAG-372003.htm.

113 Commenters in 1999 urged us to reduce the look back period, arguing that politically active individuals might be discouraged from joining advisory firms. However, we are concerned about the prospect of advisers seeking to circumvent the rule by hiring individuals shortly after they have made significant contributions that could influence government officials.

Proposed rule 206(4)-5 contains a de minimis exception that would permit each covered associate who is an individual[114] to make aggregate contributions of $250 or less, per election, to an elected official or candidate without triggering the rule's prohibitions if the person making the contribution is entitled to vote for the official or candidate.[115] We have proposed $250 because we believe that contributions of $250 or less are typically made without the intent or ability to influence the selection process for investment advisers and thus do not involve the conflicts of interest the rule is intended to prevent, as well as for reasons of regulatory consistency. The $250 amount is the same as the de minimis amount excepted from MSRB rule G-37.[116] Comment is requested on the scope of the exception.[117] Should the amount be increased or decreased, and if

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114 Under the proposed rule, each covered associate, taken separately, would be subject to the $250 de minimis exception for elections in which he or she is entitled to vote. In other words, the $250 limit applies per covered associate and is not an aggregate limit for all of an adviser's covered associates.

115 Proposed rule 206(4)-5(b)(1). Under the proposed rule, primary and general elections would be considered separate elections. Accordingly, a covered person of an investment adviser could, without triggering the prohibitions of the rule, contribute up to $250 in both the primary election campaign and the general election campaign (up to $500) of each official for whom the person making the contribution would be entitled to vote. For purposes of this rule, a person would be "entitled to vote" for an official if the person's principal residence is in the locality in which the official seeks election. See, e.g., In the Matter of Pryor, McClendon, Counts & Co., Inc. et al., Exchange Act Release No. 48095 (June 26, 2003) (noting that Rule G-37 allows a person to contribute $250 to a candidate's campaign in the primary and in the general election, for a total of $500 during the election cycle, and clarifying that contributions must be limited to $250 before the primary, with an additional $250 allowed after the primary for the general election). See also MSRB Qs & As, Question II.8, available at http://www.msrb.org/msrb1/rules/QAG-372003.htm.

116 See MSRB rule G-37(b)(i).

117 Some commenters in 1999 suggested that the amount be substantially higher. Some commenters thought we should raise the de minimis amount to $1,000 to be consistent with the limits on private contributions for candidates for federal office. We believe that a higher threshold – such as $1,000 – would be significantly more likely to enable a contributor to seek to exert influence over an official with the ability to select an investment adviser, especially in a local election. We also believe a lower amount might be too restrictive – it could preclude individuals from

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so, on what basis? For instance, the MSRB has not adjusted its de minimis amount for inflation since it was established in 1994. We have not adjusted the $250 for inflation because of ease of reference to a round number and because an inflation adjustment would result in an amount not significantly higher. We request comment, however, on whether we should adjust our amount for inflation. Should we provide a de minimis exception for contributions to officials for whom an individual is not entitled to vote, and if so, what would be an appropriate de minimis amount?[118]

(7) Exception for Certain Returned Contributions

We are proposing a second exception from the two-year compensation ban intended to address situations in which the adviser triggers the ban inadvertently.[119] We have attempted to limit the scope of this exception to the types of contributions that we believe are unlikely to raise pay to play concerns. This exception would be available only with respect to contributions made by a covered associate of the investment adviser to officials other than those for whom the covered associate was entitled to vote at the time of the contributions and which, in the

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supporting candidates for whom they are able to vote at levels that are less likely to facilitate undue influence.

118 Our proposed de minimis exception only applies to contributions to a candidate for whom the contributor is entitled to vote. Whereas the outcome of an election in which a contributor is eligible to vote is likely to have a greater personal impact on the contributor, there is a significantly greater likelihood that a contributor's contribution in an election in which he or she is not entitled to vote could be motivated by other factors, which might include influencing a candidate. In 1999, there was a mixture of support and criticism for limiting the exception to contributions to officials or candidates for whom the contributor is entitled to vote, and one commenter advocated expanding it to a $100 de minimis exception for candidates for whom the contributor is not entitled to vote.

aggregate, do not exceed $250 to any one official, per election.[120] Further, the adviser must have discovered the contribution which resulted in the prohibition within four months of the date of such contribution[121] and, within 60 days after learning of the triggering contribution, must cause the contribution to be returned to the contributor.[122] We believe this exception should only be available when the adviser discovered the triggering contribution, and caused it to be returned, promptly. Our proposal generally tracks MSRB rule G-37's "automatic exemption" provision.[123]

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119 Proposed rule 206(4)-5(b)(2).

120 Proposed rule 206(4)-5(b)(2)(i). To the extent that the contribution by a covered associate of the adviser was less than $250 and was for an official for whom the covered associate was entitled to vote at the time of the contributions, the contribution would not have triggered the two-year ban on account of the exception contained in paragraph (b)(1) of the proposed rule.

121 Id. We believe that requiring that the adviser must have discovered the contribution within four months provides an appropriate time limit for the exception. On one hand, we do not believe the exception should be available where it takes longer for advisers to discover contributions made by covered associates because they might enjoy the benefits of a contribution's potential influence for too long a period of time. On the other hand, we believe it makes sense to give advisers sufficient time to discover contributions made by covered associates if, for example, their covered associates disclose their contributions to the adviser on a quarterly basis. Also, this provision is consistent with the approach taken in MSRB rule G-37(j)(i).

122 Proposed rule 206(4)-5(b)(2)(i). The prompt return of the contribution would provide some indication that the contribution would not affect an official of a government entity's decision-making process with regard to choosing an adviser. We have proposed that the contribution must be returned within 60 days to give contributors sufficient time to seek its return, but still require that they do so in a timely manner. Also, this provision is consistent with MSRB rule G-37(j)(i). If the recipient will not return the contribution, the adviser would still have available the opportunity to apply for an exemption under paragraph (e) of the proposed rule. Paragraph (e), which sets forth factors we would consider in determining whether to grant an exemption, includes as a factor whether the adviser "has taken all available steps to cause the contributor involved in making the contribution which resulted in such prohibition to obtain a return of the contribution."

123 MSRB rule G-37(j). We did not include an equivalent provision in our 1999 proposal, and MSRB rule G-37 contained no such provision at that time. However, the MSRB added an "automatic exemption" provision in 2003. Exchange Act Release No. 47814 (May 8, 2003) [68 FR 25917 (May 14, 2003)]. Several of the comments we received on our 1999 proposal, while supporting the exemptive provision we proposed at that time, expressed concern that the scope

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To ensure that the exception for certain returned contributions does not encourage an investment adviser to relax its efforts to promote compliance with the rule's prohibitions, no adviser would be entitled to rely on the exception more than twice per 12-month period.[124] And an investment adviser would not be permitted to rely on the exception more than once with respect to contributions by the same covered associate of the investment adviser,[125] regardless of the time period.

We request comment on the proposed criteria for, and limitations on, the exception for certain returned contributions. Are the various time periods we proposed (discovery of contribution within four months of it being made, return of contribution within 60 days of

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and breadth of the rule would expose advisers to the risk of inadvertent violations, which would necessitate frequent exemptive applications. See, e.g., Comment Letter of the Securities Industry Association (Oct. 29, 1999) ("SIA Comment Letter"); Comment Letter of Morgan Stanley Dean Witter Investment Management Inc. (Nov. 1, 1999) ("MSDW Comment Letter"); Comment Letter of Fidelity Investments (Nov. 1, 1999); Investment Counsel Association of America Comment Letter (Nov. 1, 1999) ("Nov. ICAA Comment Letter"); Comment Letter of Scudder Kemper Investments (Nov. 8, 1999) ("Scudder Kemper Comment Letter"); Comment Letter of Nicholas-Applegate Capital Management (Oct. 26, 1999) ("Nicholas-Applegate Comment Letter"); Comment Letter of Smith Barney Asset Management and Salomon Brothers Asset Management Inc. (Nov. 1, 1999) ("Smith Barney Comment Letter") (suggesting, alternatively, that the time out period be 30 days for inadvertent violations); Comment Letter of Davis Polk & Wardwell (Nov. 1, 1999) ("Davis Polk Comment Letter"); and Comment Letter of American Bar Association, Subcommittees on Investment Companies and Investment Advisers and on Private Investment Entities of the Committee on Federal Regulation of Securities, Section of Business Law (Jan. 5, 2000) ("ABA Comment Letter"). The exception we have proposed would help address these concerns.

124 Proposed rule 206(4)-5(b)(2)(ii). We wanted to give each adviser more than one opportunity to refine its compliance procedures to avoid further violations of the proposed rule but, as noted, did not want to allow an adviser to relax its standards by making multiple exceptions available. This will generally create some flexibility to accommodate a covered associate's inadvertent violation.

125 Proposed rule 206(4)-5(b)(2)(iii). Once a covered associate has been made aware of an "inadvertent" violation, a justification for a second violation is more questionable.

discovery, and limitation of reliance on the exception twice per adviser per 12-month period) reasonable? Would they be effective? Are there other circumstances under which an adviser should be able to avail itself of an exception? Alternatively, should we require that an adviser institute special supervisory procedures (after it relies on the exception for certain returned contributions) for the covered associate making the contribution, including requiring pre-clearance of all contributions, for a specified period of time?

(b) Ban on Using Third Parties To Solicit Government Business

After the adoption of rule G-37 in 1994, the MSRB observed that municipal securities dealers sought to circumvent rule G-37 by hiring third-party consultants to solicit government clients on their behalf.[126] These third-party consultants would make political contributions or otherwise seek to exert influence designed to secure municipal business for the municipal securities firm.[127] Two years later, in 1996, the Commission approved, and the MSRB adopted, rule G-38, which required municipal dealers to disclose publicly the terms of their agreements with consultants.[128] In 2005, after concluding that the required disclosure was neither adequate

126 See In the Matter of Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Consultants, Exchange Act Release No. 36522 (Nov. 28, 1995) [60 FR 62275 (Dec. 5, 1995)] ("The Board believes that rules G-37 and G-20 [regarding gifts and gratuities] . . . along with [the rule on fair dealing] set appropriate standards for dealer conduct in the municipal securities industry. However, the Board is concerned about dealers' increasing use of consultants to obtain or retain municipal securities business. While the Board believes that in many instances the use of consultants is appropriate, it also believes that, in a number of instances, the use of consultants may be in response to limitations placed on dealer activities by rule G-37 and rule G-20. While both of these rules prohibit dealers from doing indirectly what they are precluded from doing directly, indirect activities often are difficult to prove." (footnotes omitted)).

127 See id.

128 See In the Matter of Self-Regulatory Organizations; Order Approving Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Consultants, Exchange Act Release No. 36727 (Jan. 17, 1996) [61 FR 1955 (Jan. 24, 1996)] ("The rule approved today is intended to

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to prevent circumvention of rule G-37, nor consistently being made,[129] the MSRB (with the Commission's approval) amended rule G-38 to impose a complete ban on the use of third-party consultants to solicit government clients.[130]

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provide additional information to issuers and to the public to assist in determining the extent to which payments to consultants influence the issuer's selection process in connection with municipal securities business. . . . ") ("MSRB Rule G-38 Adoption Order"). See also Municipal Securities Rulemaking Board, Request for Comments on Revised Draft Amendments to Rule G-38 Relating to Solicitation of Municipal Securities Business (as modified on Oct. 12, 2004) (Sept. 29, 2004), available at http://www.msrb.org/msrb1/archive/2004/RevRuleG-38Solicitation.htm#revised1 (noting, with regard to MSRB rule G-38, "As initially adopted, the rule required . . . that the dealer disclose information about its consulting arrangements to any issuer from which a consultant would solicit municipal securities business on its behalf [and that the dealer disclose] to the MSRB . . . the terms of the consulting agreements and the business obtained by the consultants . . . [with] such disclosures made available to the public through the MSRB web site . . . ."(footnotes omitted)).

129 See Municipal Securities Rulemaking Board, Amendments Relating to Solicitation of Municipal Securities Business Under Rule G-38, SR-MSRB-2005-04 (Mar. 17, 2005), available at http://www.msrb.org/msrb1/rulesandforms/sec/SR-MSRB-2005-04.pdf ("The MSRB began its current rulemaking initiative on the solicitation on behalf of brokers, dealers and municipal securities dealers ("dealers") of municipal securities business by consultants early last year because of certain practices that could present challenges to maintaining the integrity of the municipal securities market. These practices include, among other things, significant increases in recent years in the number of consultants being used, the amount these consultants are being paid and the level of reported political giving by consultants. The MSRB has been concerned that increases in levels of compensation paid to consultants for successfully obtaining municipal securities business may be motivating consultants, who currently are not subject to the basic standards of fair practice and professionalism embodied in MSRB rules, to use more aggressive or questionable tactics in their contacts with issuers.").

130 See In the Matter of Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 to the Proposed Rule Change Relating to Solicitation of Municipal Securities Business under MSRB Rule G-38, Exchange Act Release No. 52278 (Aug. 17, 2005) [70 FR 49342 (Aug. 23, 2005)]. As amended, MSRB rule G-38(a) states, "Subject to section (c) of this rule [regarding transitional payments], no broker, dealer or municipal securities dealer may provide or agree to provide, directly or indirectly, payment to any person who is not an affiliated person of the broker, dealer or municipal securities dealer for a solicitation of municipal securities business on behalf of such broker, dealer or municipal securities dealer."

We are concerned that our adoption of a rule addressing pay to play practices by advisers would lead to a similar use of consultants or solicitors by investment advisers to circumvent the rule. Indeed, we have alleged that third-party solicitors have played a central role in each of the enforcement actions against investment advisers that we have brought in the past several years involving pay to play schemes.[131] Government authorities in New York and other jurisdictions have prohibited, or are considering prohibiting, the use of consultants, solicitors, or placement agents by investment advisers to solicit government investment business.[132]

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131 See, e.g., SEC v. Henry Morris, et al., Litigation Release No. 20963 (Mar. 19, 2009) (the Commission's complaint alleges that investment advisers and a placement agent, among others, engaged in a fraudulent scheme to extract kickbacks from investment management firms seeking to manage assets of the New York State Common Retirement Fund); In the Matter of Kent D. Nelson, Investment Advisers Act Release No. 2765 (Aug. 1, 2008); Initial Decision Release No. 371 (Feb. 24, 2009); Investment Advisers Act Release No. 2868 (Apr. 17, 2009) (an administrative law judge found that an investment adviser funneled payments through a third party to the New Mexico state treasurer in exchange for being retained as an adviser by the state treasurer's office); SEC v. Paul J. Silvester et al., Litigation Release No. 16759 (Oct. 10, 2000); Litigation Release No. 16834 (Dec. 19, 2000); Litigation Release No. 18461 (Nov. 17, 2003); Litigation Release No. 19583 (Mar. 1, 2006); Litigation Release No. 20027 (Mar. 2, 2007) (alleging that, in order to obtain investment contracts, investment adviser firms made payments to associates of the Connecticut state treasurer, a portion of which were kicked back to the treasurer). See also supra notes 31-40 (discussing other cases related to these enforcement actions).

132 See, e.g., Aaron Elstein, NY Pension Fund Bans Controversial Middlemen, CRAIN'S NEW YORK BUSINESS (Apr. 22, 2009) (describing the New York State Comptroller's ban on placement agents); Press Release, Office of the New York City Comptroller, Thompson Moves to Ban Placement Agents, Asks State AG to Investigate Quadrangle Transaction, PR-09-04-095 (Apr. 22, 2009), available at http://www.comptroller.nyc.gov/press/2009_releases/pr09-04-095.shtm (describing the New York City Comptroller's calls on the New York City Pension Funds to ban placement agents); Henry Goldman, New York City Police Pension Bans Placement Agent Use, BLOOMBERG (May 5, 2009) (describing the New York City Police Pension Fund's suspension on the use of placement agents); Martin Z. Braun, New York City's Fire Pension Bans Middlemen, Joining Two Others, BLOOMBERG (May 16, 2009) (describing the New York City Fire Pension Fund's suspension on the use of placement agents); Barry Massey, NM Agency Bans Placement Agents on Investments, BUSINESSWEEK (May 26, 2009) (describing the New Mexico State Investment Council's ban on placement agents). See also In the Matter of the Carlyle Group, AGNY Investigation No. 2009-071, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (May 14, 2009), available at

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In our 1999 proposal, contributions to a government official by an adviser's third-party solicitor, engaged by the adviser to obtain clients, would have triggered a two-year "time out" for the adviser.[133] Several commenters opposed inclusion of contributions by third-party solicitors as a trigger for the "time out." Most argued that this aspect of the rule was unfair and created significant compliance challenges because these solicitors were not, according to the commenters, controlled by advisers.[134]

In light of these considerations, including the apparent difficulties for advisers to monitor the activities of their third-party solicitors, we are proposing to prohibit investment advisers from

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http://www.oag.state.ny.us/media_center/2009/may/pdfs/Carlyle%20AOD.pdf; In the Matter of Riverstone Holdings, LLC, AGNY Investigation No. 2009-091, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (June 11, 2009), available at http://www.oag.state.ny.us/media_center/2009/june/pdfs/Riverstone%20AOD%20FINAL%20EXECUTED.pdf; and In the Matter of PCG Corporate Partners Advisors II, LLC, AGNY Investigation No. 2009-101, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (July 1, 2009), available at http://www.oag.state.ny.us/media_center/2009/july/pdfs/PCG%20AOD%20FINAL%20EXECUTED.pdf (in each case, banning the use of third-party placement agents pursuant to a "Public Pension Fund Reform Code of Conduct" in connection with the New York Attorney General's findings that "private equity firms and hedge funds frequently use placement agents, finders, lobbyists, and other intermediaries. . . to obtain investments from public pension funds . . . , that these placement agents are frequently politically-connected individuals selling access to public money, . . . and that the use of placement agents to obtain public pension fund investments is a practice fraught with peril and prone to manipulation and abuse.").

133 See 1999 Proposing Release, supra note 17, at section II.A.1.

134 See, e.g., SIA Comment Letter; T. Rowe Comment Letter; MSDW Comment Letter; Comment Letter of Legg Mason, Inc. (Nov. 1, 1999); American Bankers Association Comment Letter (Nov. 1, 1999); Nov. ICAA Comment Letter; Scudder Kemper Comment Letter; Nicholas-Applegate Comment Letter; Smith Barney Comment Letter; Davis Polk Comment Letter; and ABA Comment Letter. We note that rule 206(4)-3 (the "cash solicitation rule") under the Advisers Act, among other things, requires an adviser that engages a third-party solicitor for clients: (i) to make a bona fide effort to ascertain whether the solicitor has complied with the adviser's agreement with the solicitor; and (ii) to have a reasonable basis for believing that the solicitor has so complied. Advisers Act rule 206(4)-3(a)(2)(iii)(C) [17 CFR 275.206(4)-3(a)(2)(iii)(C)].

using third-party solicitors to obtain government clients.[135] Proposed rule 206(4)-5 would make it unlawful for any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act [15 U.S.C. 80b-3(b)(3)], or any of its covered associates, to provide or agree to provide, directly or indirectly, "payment" to any person to solicit a government entity for investment advisory services unless such person is: (i) a "related person" of the investment adviser or, if the related person is a company, an employee of that related person; or (ii) any of the adviser's employees, general partners, LLC managing members, executive officers (or other person with a similar status or function, as applicable).[136] The rule's prohibition on an adviser's payments to third-party solicitors may apply to persons commonly called "finders," "solicitors," "placement agents," or "pension consultants."[137]

135 Although rule 206(4)-3 under the Advisers Act (the "Cash Solicitation Rule") contemplates that certain client solicitation activities of third parties can be undertaken where certain conditions are met and the adviser both "makes a bona fide effort to ascertain whether" and "has a reasonable basis for believing that" the solicitor has complied with certain aspects of the rule (Advisers Act rule 206(4)-3(a)(2)(iii)(C) [17 CFR 275.206(4)-3(a)(2)(iii)(C)]), commenters' concerns about the inability of advisers to control the political contribution activity of their solicitors (which is not restricted under the Cash Solicitation Rule) persuade us that a different approach is appropriate for solicitation of government clients.

136 Proposed rule 206(4)-5(a)(2)(i). Advisers making payments to solicitors must comply with the cash solicitation rule under the Advisers Act. If this component of proposed rule 206(4)-5 is adopted as proposed, investment advisers registered or required to be registered with us would no longer be able to rely on the cash solicitation rule to pay third-party solicitors to obtain government clients. For a discussion of proposed amendments to the cash solicitation rule, see infra section II.C.

137 Pension consultants provide advice to pension plans (public or private) and their trustees with respect to their investments, selection of money managers and other service providers, and other investment-related matters. Many pension plans rely heavily on the expertise and guidance of their pension consultant in helping them to manage pension plan assets. Pension consultants may act as third-party solicitors. Others may act as investment advisers subject to our rule. In 2005, our Office of Compliance Inspections and Examinations published a report highlighting concerns relating to the Advisers Act stemming from examinations of 24 pension consultant firms,

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The proposed rule would only apply to "third-party" solicitors who solicit government entities for investment advisory services.[138] The prohibition on payments to third-party solicitors would not cover solicitations on behalf of an investment adviser by a person who is a "related person" of the adviser, any of the related person's employees if the related person is a company,[139] or any executive officer or partner of the adviser.[140] A contribution to a government

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including conflicts of interest that arise with respect to pension consultants that provide products and services to both pension plan advisory clients and money managers and mutual funds on an ongoing basis. Office of Compliance Inspections and Examinations, U.S. Securities and Exchange Commission, Staff Report Concerning Examinations of Select Pension Consultants (May 16, 2005), available at http://www.sec.gov/news/studies/pensionexamstudy.pdf. Commission staff also published on the Commission's Web site, in cooperation with the U.S. Department of Labor, tips to assist fiduciaries of employee benefit plans in reviewing conflicts of interest of pension consultants. Selecting and Monitoring Pension Consultants: Tips for Plan Fiduciaries (June 1, 2005), available at http://www.sec.gov/investor/pubs/sponsortips.htm.

Although the terms are sometimes used interchangeably, "finders" typically locate buyers and/or sellers for a security on behalf of a broker-dealer, "solicitors" typically locate investment advisory clients on behalf of an investment adviser, and "placement agents" typically specialize in finding investors (often institutional investors or high net worth investors) that are willing and able to invest in a private offering of securities on behalf of the issuer of such privately offered securities.

138 Proposed rule 206(4)-5(a)(2)(i).

139 We would define "related person" as any person, directly or indirectly, controlling or controlled by the investment adviser, and any person that is under common control with the investment adviser. Proposed rule 206(4)-5(f)(9). The term "company" is defined in the Advisers Act, in relevant part, as "a corporation, a partnership, an association, a 'joint-stock' company, a trust, or any organized group of persons, whether incorporated or not." 15 U.S.C. 80b-2(a)(5).

140 More specifically, we do not include any of the following within the prohibition on payments for solicitation of government clients: executive officers, general partners, managing members (or, in each case, persons with similar status or function), employees, or "related persons" of the investment adviser. Proposed rule 206(4)-5(a)(2)(i). We make this distinction because related person solicitors are subject to an adviser's (or its affiliates') control and thus should not present the compliance challenges that advisers pointed to with respect to third-party solicitors. See supra note 134 and accompanying text. MSRB rule G-38's exclusions are based on two similar definitions – of "affiliated person of the broker, dealer or municipal securities dealer" and of "affiliated company of the broker, dealer or municipal securities dealer." MSRB rule G-38(b)(i) and (b)(ii).

official by certain of these persons would instead trigger the two-year "time out" under paragraph (a) of the proposed rule, during which the investment adviser could not provide investment advisory services for compensation to the government entity whose selection of an adviser that official could influence.[141] We have proposed to include related persons and their employees (if the related persons are companies) in order to enable advisers to compensate parent companies and other owners, subsidiaries and sister companies – as well as employees of related companies – for government entity solicitation activities because we recognize that there may be efficiencies in allowing advisers to rely on these particular types of persons to assist them in seeking clients.[142] We request comment on whether we should include employees of an adviser's related persons that are companies within the group of persons not subject to the ban on payments to third parties. Should we include only employees of certain related persons of the adviser? If so, how should we make that determination? We also request comment on whether there are other types of persons associated with an investment adviser who should not be subject to the ban on payments to third parties. We would define "payment" as any gift, subscription, loan, advance or

141 Pursuant to proposed rule 206(4)-5(a)(1), certain contributions by the investment adviser and its covered associates would trigger the two-year time out. For a discussion of the two year "time out" provision of the proposed rule, see supra section II.A.3(a). We are not proposing that contributions by "related persons" and their employees would trigger the two-year time out, although we request comment on whether to include in the definition of "covered associate" an employee of a related person who solicits a government entity for the adviser. See discussion at section II.A.3(a)(4), supra. See also proposed rule 206(4)-5(d)

142 For example, if an adviser's sister company has an office in a given location, the adviser might seek the assistance of a sister company's employee at that location to solicit local government business on its behalf rather than relying on its own personnel who might be located a significant distance away.

deposit of money or anything of value.[143] We are proposing this definition to cover the various means by which an adviser and its covered associates may seek to compensate a third-party solicitor.[144] A "finder's fee" paid for a third-party solicitation would be an example of a prohibited payment. It could also include payments made to pension consultants for performing various services, such as attending or sponsoring conferences, if those services are intended to obtain government clients.[145] Are there other types of payments we should explicitly include in the definition? Are there others that we should exclude, and, if so, why?

We would broadly define "solicit" to mean: (i) with respect to investment advisory services, to communicate, directly or indirectly, for the purpose of obtaining or retaining a client for, or referring a client to, an investment adviser; and (ii) with respect to a contribution or payment, to communicate, directly or indirectly, for the purpose of obtaining or arranging a contribution or payment. We are proposing this definition to capture the types of communications in which an investment adviser might engage that we believe should trigger application of the rule's prohibitions – communications for the purpose of obtaining or retaining

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143 Proposed rule 206(4)-5(f)(7). MSRB rule G-38 incorporates the definition of "payment," as well as the definitions of "issuer" and "municipal securities business" from MSRB rule G-37(g).

144 As well as the various means by which an adviser and its covered associates may seek to solicit other persons or coordinate donations to political parties. <u>See infra</u> section II.A.3(d).

145 The proposed rule's prohibition on making payments to third-party solicitors of government clients would apply expressly only to investment advisers and their covered associates. <u>But see</u> proposed rule 206(4)-5(d) (the proposed rule's prohibitions on an adviser and its covered associates doing indirectly what cannot be done directly). For a discussion of this provision, see <u>infra</u> section II.A.3.(d) of this Release. The proposed rule would not prohibit government entities from retaining "pension consultants" (or other third-parties) and paying them to recommend particular investment advisers for the management of public funds.

a client or a contribution.[146] Whether a particular communication constitutes a "solicitation," therefore, depends on the specific facts and circumstances relating to the communication. The nature of information conveyed in any communication and the manner in which it is presented would be relevant factors to consider. Does our proposed definition effectively capture the appropriate scope of communications? If not, what types of communications should we exclude, and why?

We request comment on our proposal to prohibit the use of third-party solicitors of government business. Is our proposed prohibition on the use of third-party solicitors an appropriate means to deter pay to play practices? We propose to prohibit only third-party solicitors as likely posing a significant threat to investor protection; certain related-party solicitors would, instead, be subject to the time out limitations of proposed rule 206(4)-5(a)(1). Is this differentiation appropriate? If not, should we instead subject advisers to the two-year time out for contributions made by their third party solicitors although, as noted above, commenters in 1999 indicated that such a requirement may impose significant compliance challenges?[147] If the differentiation is appropriate, should we also have a two-year look back restriction for any contributions made by the third party? Is there a different approach that would be effective at eliminating circumvention of the rule through the use of third parties? For example, should we consider narrowing the prohibition to accommodate government solicitation activities by third parties if such third parties (and their related persons) commit not to contribute to (or solicit contributions for) officials of any government entity from which any adviser that hires them is

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146 See proposed rule 206(4)-5(f)(10). MSRB rule G-38 contains a similar definition. See MSRB rule G-38(b)(i).

seeking business? To what extent might the proposed ban on using third parties to solicit government business disproportionately impact the ability of certain investment advisers, such as those that are smaller and less established, to compete in the market to provide advisory services to government clients? Conversely, to what extent might the proposed ban benefit smaller or less established advisers who are currently unable or unwilling to engage in pay to play practices to compete for government business?

(c) Restrictions on Soliciting and Coordinating Contributions and Payments

Another way an adviser can attempt to influence the selection process is by coordinating contributions for an elected official or payments to a political party, or by soliciting others to make contributions to an elected official or payments to a political party.[148] Therefore, proposed rule 206(4)-5(a)(2)(ii) would prohibit an adviser and its covered associates from soliciting any person or PAC to make, or from coordinating, any contribution to an official of a government entity to which the adviser is providing or seeking to provide investment advisory services, or

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(. . . continued)

147 See supra note 134.

148 For examples of solicitation or coordination of contributions in the municipal securities dealer context, see In the Matter of Pryor, McClendon, Counts & Co., Inc. et al., Exchange Act Release No. 48095 (June 26, 2003) (Commission alleged that a broker-dealer violated rule G-37(c) because its president delivered three $250 money orders (in other people's names) in addition to his own personal check for $250 to the campaign of a New York City mayoral candidate during a period when the firm was engaged in municipal securities business with New York City); In the Matter of FAIC Securities, Inc., Exchange Act Release No. 36937 (Mar. 7, 1996) (Commission alleged that the broker-dealer willfully violated G-37(c) because the firm's municipal finance professionals approved its affiliated companies' political contributions to candidates for office who could influence the awarding of municipal securities business by the State of Florida and by Dade County, Florida, and during the two-year period following those contributions, the firm continued to seek, and was selected, to participate in negotiated underwritings of certain municipal securities by both Dade County and a state agency).

any payment[149] to a political party of a state or locality where the investment adviser is providing or seeking to provide investment advisory services to a government entity.[150] Our proposed restrictions on soliciting and coordinating contributions and payments generally track MSRB rule G-37.[151] The MSRB amended its rule in 2005, with Commission approval, to expand its prohibition on soliciting others to make, and on coordinating, payments to state and local

149 See supra note 143 and accompanying text for the definition of "payment." This definition is derived from the definition of "contribution," but does not include the limits on the purposes for which such money is given, as currently set forth in the proposed definition of contribution. We are including "payments," as opposed to "contributions," here to deter an adviser from circumventing the rule's prohibitions by coordinating indirect contributions to government officials through payments to political parties. We noted similar concerns in the context of MSRB Rule G-37 when we approved a recordkeeping provision in rule G-8 to require persons subject to that rule to keep records relating to political party payments. See SEC Order Approving Proposed Rule Change by the Municipal Securities Rulemaking Board Relating to Rule G-37 on Political Contributions and Prohibitions on Municipal Securities Business, and Rule G-8, on Recordkeeping, Exchange Act Release No. 35446 (Mar. 6, 1995) ("[S]ome [industry participants] currently are urging dealers to make payments to political parties earmarked for expenses other than political contributions (such as administrative expenses or voter registration drives). Since these payments would not constitute "contributions" under the rule, the recordkeeping and reporting provisions would not apply. The MSRB is concerned, based upon this information, that the same pay-to-play pressures that motivated the MSRB to adopt rule G-37 may be emerging in connection with the fundraising practices of certain political parties described above.").

150 Proposed rule 206(4)-5(a)(2)(ii). An investment adviser would be seeking to provide advisory services to a government entity when it responds to a request for proposal, communicates with a government entity regarding that entity's formal selection process for investment advisers, or engages in some other solicitation of investment advisory business of the government entity. A violation of paragraph (a)(2)(ii) of the proposed rule would not trigger a two-year ban on the provision of investment advisory services for compensation, but would be a violation of the rule. This provision would prohibit, for example, an adviser's solicitation of a payment to the political party of the state in which the adviser was seeking to provide advisory services to a government entity of the state, but would not preclude that adviser from soliciting a payment to a local political party, unless the adviser was doing so as a means to do indirectly what the adviser could not do directly under the proposed rule (for example, if the adviser was soliciting the payment as a means to funnel payments to an official of the government entity from which the adviser was seeking business). See proposed rule 206(4)-5(d).

151 See MSRB rule G-37(c). We note, however, that G-37 did not contain a prohibition on soliciting or coordinating payments to political parties in 1999, and our 1999 proposal did not contain such a provision. 1999 Proposing Release, supra note 17.

political parties to close what the MSRB identified as a gap in which contributions were being made indirectly to officials through payments to political parties for the purposes of influencing their choice of municipal securities dealers.[152] The MSRB had not previously been able to deter this misconduct, despite issuing informal guidance in both 1996 and in 2003.[153] We are proposing a similar prohibition on soliciting or coordinating payments to political parties in states or localities where the investment adviser is providing or seeking to provide investment advisory services to a government entity because we are concerned that our adoption of a rule that only prohibits advisers from soliciting others to make, or coordinating, contributions to

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152 See Rule G-37: Request for Comments on Draft Amendments to Rule G-37(c), Relating to Prohibiting Solicitation and Coordination of Payments to Political Parties, and Draft Question and Answer Guidance Concerning Indirect Rule Violations, MSRB Notice 2005-11 (Feb. 15, 2005), available at http://www.msrb.org/msrb1/archive/2005/2005-11.asp ("G-37(c) Notice") ("[T]he MSRB is especially troubled by the emergence of recent media and other reports that issuer agents have informed dealers and [municipal finance professionals] that, if they are prohibited from contributing directly to an issuer official's campaign, they should contribute to the affiliated party's "housekeeping" account. The MSRB is concerned that dealers or [municipal finance professionals] who make such payments may be doing so in an effort to avoid the political contribution limitations embodied in Rule G-37."); Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Approving Proposed Rule Change Concerning Solicitation and Coordination of Payments to Political Parties and Question and Answer Guidance on Supervisory Procedures Related to Rule G-37(d) on Indirect Violations, Exchange Act Release No. 52496 (Sept. 22, 2005) (SEC order approving change to MSRB G-37 to prohibit soliciting or coordinating payments to political parties).

153 See G-37(c) Notice, supra note 152. ("Both the 1996 Q&A guidance and the 2003 Notice were intended to alert dealers and [municipal finance professionals] to the realities of political fundraising and guide them toward developing procedures that would lead to compliance with both the letter and the spirit of the Rule. The MSRB continues to be concerned, however, that dealer, [municipal finance professional], and affiliated persons' payments to political parties, including "housekeeping", "conference" or "overhead" type accounts, and PACs give rise to at least the appearance that dealers may be circumventing the intent of Rule G-37.").

officials would lead to the development of a similar gap in which advisers could circumvent the rule by making payments to political parties to influence an official.[154]

Proposed rule 206(4)-5(a)(2)(ii) would also prohibit advisers from seeking to influence the selection process by, for example, "bundling"[155] contributions or payments from its employees or others or by making or coordinating contributions or payments through a third party, such as a "gatekeeper."[156] In a gatekeeper arrangement, political contributions or payments are arranged by an intermediary, typically a pension consultant, which distributes or

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154 We note that a direct contribution to a political party by an adviser or its covered associates would not trigger the two-year time out provision of the proposed rule (although we request comment on our proposed definition of "contribution"), unless the contribution was a means for the adviser to do indirectly what the proposed rule would prohibit if done directly (for example, if the contribution was earmarked or known to be provided for the benefit of a particular government official). See supra note 93. We are proposing, however, that an adviser be prohibited from soliciting others to make, or coordinating, payments to political parties because, as the MSRB's experience has shown, advisers could otherwise use such means to circumvent the proposed rule's limitations on direct contributions to government officials.

155 An employee or person acting on an adviser's behalf "bundles" contributions or payments by coordinating small contributions or payments from several employees of the adviser or others to create one large contribution or payment. For an example of this in the context of the municipal securities industry, see In the Matter of Pryor, McClendon, Counts & Co., Inc. et al., Securities Act Release No. 48095 (June 26, 2003) ("Counts[, the president of the broker-dealer firm,] gave his administrative assistant $750 in cash, told her to purchase three separate money orders, and told her to make them payable for $250 each to the candidate's campaign. Counts instructed his assistant to make out one of the money orders as if it were from the assistant herself, and to make out the other two as if they were from the wife of a [firm] employee and a friend of Counts', respectively. Counts then caused those money orders to be delivered to the candidate's campaign together with Counts' own personal check for $250. [When two of the three money orders were subsequently returned,] Counts instructed his assistant to deposit the returned $500 into [the firm]'s bank account, which she did.").

156 We are proposing that solicitation of contributions of others for an official of a government entity to which an adviser is providing or seeking to provide investment advisory services by an adviser or its covered associates be subject to a flat prohibition under the rule, rather than trigger a two-year "time out," because we recognize it may be more difficult for an adviser to monitor solicitation activities (as opposed to direct contribution activity). For a discussion of an adviser's obligation to adopt policies and procedures reasonably designed to prevent violations of the Advisers Act pursuant to our "compliance rule," see infra note 207 and accompanying text.

directs contributions or payments to elected officials or candidates.[157] The gatekeeper ensures that advisers not making a requisite amount of contributions or payments are not included among the final candidates for advisory contracts. In addition, a gatekeeper could arrange "swaps" of contributions or payments between elected officials in order to obscure the significance of the contributions or payments from public disclosure or to circumvent plan restrictions on contributions to trustees.[158] Under the proposed rule, the gatekeeper in these arrangements would be coordinating political contributions or payments and, if the gatekeeper is an investment adviser, would itself violate the proposed rule's restrictions on coordinating contributions or

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157 See, e.g., SEC v. Morris et al., Litigation Release No. 21001 (Apr. 15, 2009) (the Commission's complaint alleges that placement agents acted as gatekeepers by directing investment management firms to funnel kickbacks through various entities); In the Matter of Kent D. Nelson, Initial Decision Release No. 371 (Feb. 24, 2009) (an administrative law judge found that an investment adviser funneled payments through a third party to the New Mexico state treasurer, acting as gatekeeper by extracting $4.4 million in finder's fees from broker-dealers and siphoning $2.9 million to the state treasurer's office to influence the office's discretionary commitment of funds, in exchange for being retained as an adviser by the state treasurer's office); (Investment Advisers Act Release No. 2868 (Apr. 17, 2009). Similar types of arrangements exist outside of the context of government investments, such as in the area of union pension funds. See, e.g., In the Matter of Duff & Phelps Investment Management Co., Inc., Investment Advisers Act Release No. 1984 (Sept. 28, 2001) and related case In re Performance Analytics, et al., Investment Advisers Act Release No. 2036 (June 17, 2002) (in a settled action, the Commission alleged that an investment adviser entered into an arrangement with gatekeeper broker-dealer in which the adviser would direct its trades to broker-dealer if the broker-dealer would continue to recommend the adviser to the union pension fund board, and the broker-dealer allegedly funneled payments to certain trustees on the pension fund board to preserve its role as gatekeeper and to preserve the adviser's role as adviser to the fund).

158 For example, Adviser A advises Plan X, while Adviser B advises Plan Y. The "gatekeeper" may direct a political contribution from Adviser A to the elected official, who is a trustee to Plan Y, and from Adviser B to the elected official, who is a trustee to Plan X, agreeing to place both advisers on each plan's approved list. Persons reviewing records of the political contributions would have no way of determining that the contributions were swapped and that they created conflicts of interest on the part of the advisers as well as the elected officials.

payments.[159] The adviser would also violate the proposed rule if it paid the third-party solicitor to coordinate political contributions or payments in order to obtain business.

We request comment on this aspect of the proposed rule, including our proposed definitions. Is it appropriate to differentiate between "contributions" to officials and "payments" to political parties? Are there alternative approaches that would effectively deter these types of indirect pay to play arrangements? Do commenters believe that our proposed inclusion of payments to state and local political parties closes an important gap in which contributions might be made indirectly to officials for the purposes of influencing their choice of investment advisers? Alternatively, do commenters believe that our proposed inclusion of political parties is unnecessary?

(d) Direct and Indirect Contributions or Solicitations

Rule 206(4)-5(d) would also prohibit acts done indirectly, which, if done directly, would result in a violation of the rule.[160] Thus, an adviser and its covered associates could not circumvent the rule by directing or funding contributions through third parties, including, for example, consultants, attorneys, family members, friends or companies affiliated with the adviser. This provision would also cover, for example, situations in which contributions by an adviser are made, directed or funded through a third party with an expectation that, as a result of the contribution, another contribution is likely to be made by a third party to an "official of the

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159 Regardless of whether the gatekeeper is an investment adviser, a person participating in such a scheme could, if the rule is adopted, be considered to be aiding and abetting an adviser's violation of the rule. See section 209(d) of the Act [15 U.S.C. 80b-9(d)] (authorizing Commission enforcement action for aiding and abetting a violation of the Advisers Act or any Advisers Act rule).

government entity," for the benefit of the adviser. Contributions made through gatekeepers (described above) thus would be considered made "indirectly" for purposes of the proposed rule. We request comment on this aspect of the proposed rule.

(e) Investment Pools

(1) Application of the Rule to Pooled Investment Vehicles

Pay to play activities in the context of investment pools[161] also raise concerns about the potential for fraud.[162] The fraud that may result from pay to play practices can occur in a number of circumstances involving the government official and the pooled investment vehicle. The

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160 Proposed rule 206(4)-5(d). See also section 208(d) of the Advisers Act [15 U.S.C. 80b-8(d)]; MSRB rule G-37(d).

161 Investment pools may include, but are not limited to: mutual funds, hedge funds, private equity funds, and venture capital funds.

162 See, e.g., SEC v. Paul J. Silvester et al., Litigation Release No. 16759 (Oct. 10, 2000) (action in which investment adviser allegedly paid third party solicitors who kicked back a portion of the money to the former Connecticut State Treasurer in order to obtain public pension fund investments in a hedge fund managed by the adviser); SEC v. William A. DiBella et al., Litigation Release No. 20498 (Mar. 14, 2008) (consultant was found to have aided and abetted the former Connecticut State Treasurer in a pay to play scheme involving an investment adviser to a private equity fund who had paid third-party solicitors to obtain public pension fund investments in the fund); In the Matter of the Carlyle Group, AGNY Investigation No. 2009-071, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (May 14, 2009), available at http://www.oag.state.ny.us/media_center/2009/may/pdfs/Carlyle%20AOD.pdf; In the Matter of Riverstone Holdings, LLC, AGNY Investigation No. 2009-091, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (June 11, 2009), available at http://www.oag.state.ny.us/media_center/2009/june/pdfs/Riverstone%20AOD%20FINAL%20EXECUTED.pdf; and In the Matter of PCG Corporate Partners Advisors II, LLC, AGNY Investigation No. 2009-101, Assurance of Discontinuance Pursuant to Executive Law § 63(15) (July 1, 2009), available at http://www.oag.state.ny.us/media_center/2009/july/pdfs/PCG%20AOD%20FINAL%20EXECUTED.pdf (three settled actions brought by New York Attorney General in which advisers allegedly paid third-party solicitors who kicked back a portion of the money to the former New York Deputy State Treasurer in order to obtain public pension investments in private equity funds managed by the advisers).

following are examples of pay to play relationships involving investment pools that implicate the concerns underlying this rulemaking:

- When an investment adviser to a pooled investment vehicle makes a contribution to a government official and the government official directs that public monies (e.g., pension plan assets) be invested in that adviser's pooled investment vehicle;
- When an investment adviser to a pooled investment vehicle makes a contribution to a government official and that government official chooses that investment adviser to be an adviser to a government sponsored plan, such as a "529 plan;"[163] and
- When an investment adviser to a pooled investment vehicle makes a contribution to a government official and that government official chooses that adviser's pooled investment vehicle as an investment option in a government sponsored plan, such as a "529 plan,"[164] regardless of whether the adviser is also chosen to be the adviser to the plan.

Pay to play activities can harm public pension plans and their beneficiaries. Such activities can cause competition in the market for investments to be manipulated, which can distort the process by which investment decisions regarding public investments are made, and

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163 This practice would be covered under (a)(1) of the proposed rule. See supra section II.A.3.(a) of this release. For a specific discussion of the application to "529 plans," see discussion below at footnotes 176-189 and related text.

164 See Elliot Blair Smith, Fund Scandal Worries Tuition Plan Investors, USA TODAY (Nov. 19, 2003), at B1 (reporting that the former governor of Wisconsin received campaign contributions from the founder of a mutual fund company, and subsequently the then-governor's staff created a panel of four state employees that selected the founder's firm to manage the state's 529 plan and provide the plan's investment options).

can result in public pension plans making inferior investments. In addition, the pension plan may pay higher fees because advisers must recoup the contributions, or because the contract negotiations are not handled on an arm's-length basis.

An adviser's participation in pay to play activities may also defraud other investors in a pooled investment vehicle. For example, in a pay to play kickback scheme, the government investor in the pooled vehicle would receive a kickback payment from the adviser while other investors in the pool may pay higher advisory fees as a result of the adviser trying to recoup the cost of the kickback. As another example, a government investor that has engaged in a pay to play scheme with an investment adviser may leverage the fact of the adviser's payment to obtain additional benefits for itself that may operate as a fraud on other investors in the pooled vehicle.

Therefore, the proposed prophylactic rule seeks to address pay to play practices by advisers managing pooled investment vehicles.[165] The proposed rule would subject an adviser to a covered investment pool to the prohibitions of proposed rule 206(4)-5[166] so that the government entities, the pooled investment vehicles, and the other investors in that vehicle are also protected against the harms that may result when advisers engage in pay to play practices.

(2) Covered Investment Pools

The proposed rule's prohibitions would be applicable only with respect to an adviser that manages a covered investment pool.[167] The proposed rule would generally define "covered

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165 See proposed rule 206(4)-5(c).

166 Id.

167 See proposed rule 206(4)-5(c). As described below, proposed rule 206(4)-5 narrows this definition to exclude certain investment companies for the purposes of paragraph (a)(1) of the proposed rule.

investment pool"[168] as: (i) any investment company as defined in section 3(a) of the Investment Company Act of 1940 ("Investment Company Act");[169] or (ii) any company that would be an investment company under section 3(a) of that Act but for the exclusion provided from that definition by section 3(c)(1), section 3(c)(7) or section 3(c)(11) of that Act.[170]

Our 1999 proposal would have applied the rule only to advisers managing private funds, such as hedge funds and private equity funds,[171] that are typically excepted from the definition of investment company by either section 3(c)(1) or 3(c)(7) of the Investment Company Act.[172] We have expanded upon that proposal to include advisers managing investment companies[173] (which are registered under the Investment Company Act[174]) as well as collective investment trusts (which are excepted from the definition of investment company by section 3(c)(11)).[175] Both of these types of collective investment pools today are used as either funding vehicles for, or investments of, government-sponsored savings and retirement plans. These plans include, for

168 Proposed rule 206(4)-5(f)(3).

169 15 U.S.C. 80a-3(a).

170 15 U.S.C. 80a-3(c)(1), (7) or (11).

171 See 1999 Proposing Release, supra note 17, at section II.A.4.

172 15 U.S.C. 80a-3(c)(1) and (7).

173 15 U.S.C. 80a-3(a).

174 15 U.S.C. 80a-8.

175 15 U.S.C. 80a-3(c)(11). We note that a bank maintaining a collective investment trust would not be subject to the proposed rule if the bank falls within the exclusion from the definition of "investment adviser" in Section 202(a)(11)(A) of the Advisers Act [15 U.S.C. 80b-2(a)(11)(A)]. A person who falls within the definition of an investment adviser that provides advisory services with respect to a collective investment trust in which a government entity invests, however, would be subject to the rule's prohibitions.

example, college savings plans (such as "529 plans"[176]) and retirement plans (such as "403(b) plans"[177] and "457 plans"[178]). They typically allow participants to select among pre-established investment "options," or particular investment pools (often invested in registered investment companies or funds of funds, such as target date funds), that a government official has directly or indirectly selected to include as investment choices for participants.[179]

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176 A 529 plan is a "qualified tuition plan" established under Section 529 of the Internal Revenue Code of 1986 [26 U.S.C. 529]. States generally establish 529 plans as state trusts which are considered instrumentalities of states for federal securities law purposes. As a result, the plans themselves are generally not regulated under the federal securities laws and many of the protections of the federal securities laws do not apply to investors in them. See Section 2(b) of the Investment Company Act [15 U.S.C. 80a-2(b) and Section 202(b) of the Advisers Act [15 U.S.C. 80b-2(b) (exempting state-owned entities from those statutes). However, the federal securities laws do generally apply to, and the Commission does generally regulate, the brokers, dealers, and municipal securities dealers that effect transactions in interests in 529 plans. See generally Sections 15(a)(1) and 15B of the Securities Exchange Act of 1934 [15 U.S.C. 78a-15(a)(1) and 15B] ("Exchange Act"). A bank effecting transactions in 529 plan interests may be exempt from the definition of "broker" or "municipal securities dealer" under the Exchange Act if it can rely on an exception from the definition of broker in the Exchange Act. In addition, state sponsors of 529 plans may hire third-party investment advisers either to manage 529 plan assets on their behalf or to act as investment consultants to the agency responsible for managing plan assets. These investment advisers, unless they qualify for a specific exemption from registration under the Advisers Act, are generally required to be registered with the Commission and would therefore be subject to our proposed rule.

177 A 403(b) plan is a tax-deferred employee benefit retirement plan established under Section 403(b) of the Internal Revenue Code of 1986 [26 U.S.C. 403(b)].

178 A 457 plan is a tax-deferred employee benefit retirement plan established under Section 457 of the Internal Revenue Code of 1986 [26 U.S.C. 457].

179 For example, many 529 plans allow plan participants to select among various underlying investment options to direct the investment of their contributions. The participants' contributions are then invested in options of the 529 plan and the plan, in turn, invests its assets in the investment companies or other investments on which the plan options are based. The Internal Revenue Code requires that in order to set up a 529 plan investor contributions must be held in a qualified trust. See 26 U.S.C.§ 529(b). Often, the adviser to the 529 plan also advises the registered investment companies that serve as the underlying investment options for the plan. Sometimes, however, registered investment companies advised by investment advisers that do not provide advisory services directly to the government entity may serve as the underlying investment options for the plan.

Government-sponsored savings plans have grown enormously in recent years.[180] Competition for an adviser's fund to be selected as an investment option in government-sponsored savings plans is keen,[181] and we are concerned that advisers to pooled investment vehicles are making political contributions to influence the decision by government entities of the funds to be included as options in such plans. Of course, as discussed above,[182] proving such a direct quid pro quo or intent to influence in a specific case often will not be possible. As previously stated, it is precisely because of that difficulty that a prophylactic rule is needed.[183] We are concerned about the harmful effects pay to play activities may have in this context on these government-sponsored plans and their beneficiaries. Plans and their beneficiaries may be harmed, for example, if because of an adviser's political contributions, a government official causes a government-sponsored plan to invest in a fund managed by that adviser that charges

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180 See Investment Company Institute, 529 Plan Program Statistics, Dec. 2008 (May 22, 2009), available at http://www.ici.org/research/stats/529s/529s_12-08 (indicating that 529 plan assets have increased from \$8.6 billion in 2000 to \$104.9 billion in the fourth quarter of 2008, and that 529 plan participants have increased from 1.3 million in 2000 to 11.2 million in the fourth quarter of 2008); Investment Company Institute, The U.S. Retirement Market, 2008, 18 RESEARCH FUNDAMENTALS, No. 5 (June 2009), available at http://www.ici.org/pdf/fm-v18n5.pdf (indicating that 403(b) plan and 457 plan assets have increased from \$627 billion in 2000 to \$712 billion in the fourth quarter of 2008); SEI, Collective Investment Trusts: The New Wave in Retirement Investing (May 2008), available at https://longjump.com/networking/RepositoryPublicDocDownload?id=80031025axe139509557&docname=SEI%20CIT%20White%20Paper%205.08.pdf&cid=80031025&encode=application/pdf (citing Morningstar data indicating that collective investment trust assets nearly tripled from 2004 to 2007 and grew by more than 150 percent between 2005 and 2007 alone).

181 See, e.g., Charles Paikert, TIAA-CREF Stages Comeback in College Savings Plans, CRAIN'S NEW YORK BUSINESS (Apr. 23, 2007) (depicting TIAA-CREF's struggle to remain a major player in managing State 529 plans because of increasing competition from the industry's heavyweights); Beth Healy, Investment Giants Battle for Share of Exploding College-Savings Market, BOSTON GLOBE (Oct. 29, 2000), at F1 (describing the increasing competition between investment firms for state 529 plans and increasing competition to market their plans nationally).

182 See supra notes 16 and 55 and accompanying text.

183 See, e.g. Blount, supra note 16, at 945.

higher fees or is less well managed than a fund that may have been chosen on the basis of pure merit. In addition, pay to play practices could be particularly damaging in the 529 context if a state offers only one, or very few, investment options to its participants.[184] Accordingly, we are proposing to include these other pooled investment vehicles often managed by investment advisers.

Under the rule, each of the pay to play prohibitions (with one exception discussed below) would be equally applicable to an investment adviser that manages assets of a government entity through the entity's investment in a covered investment pool managed by that adviser. For example, if an investment adviser subject to our rule makes a campaign contribution to an official of a government entity in a position to influence the decision to invest government assets in a private equity fund managed by that adviser, the investment adviser would be prohibited from receiving compensation with respect to the government entity's investment in the private equity fund.

In the case of an adviser to a publicly-offered registered investment company, however, we propose to apply the two-year "time out" provision only when the investment company is included in a plan or program of a government entity (e.g., a 529 plan).[185] When a government

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184 See, e.g., Restrictions Lessen Benefits of State College Savings Plans, USA TODAY (Dec. 1, 2003), at A20 ("[M]any states offer only a few investment options . . . [and] limit investors to a single fund company. . . . While plans vary, states typically have negotiated an exclusive deal with one fund company.").

185 Proposed rule 206(4)-5(c), (f)(3). Accordingly, the time out provision would be applicable, for example, if a particular mutual fund is selected to be an investment option for participants in a 529 plan; the time out provision would not be applicable if a state government invested its pension fund assets in that same mutual fund. We define a "plan or program of a government entity" in the proposed rule as any investment program or plan sponsored or established by a government entity, including, but not limited to, a "qualified tuition plan," such as a 529 plan, a

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entity invests in publicly-offered securities of a registered investment company, we are generally less concerned that the investment company's adviser would be motivated by pay to play considerations if, for example, the adviser has not bid for, or solicited, the government entity's business. Moreover, in many circumstances in which a government entity determines to make an investment in an investment company for cash management or other purposes, the adviser may not even be aware that a government entity has made an investment.[186] We are mindful that subjecting advisers and their covered associates to the two-year "time out" in these situations could create substantial compliance challenges because the adviser would have to monitor investments by these government entities in its investment companies to ensure that a contribution by the adviser or its covered associates did not trigger a time out. In contrast, we have included an exception that would subject to the two-year time out provision an adviser to a publicly offered registered investment company that is included in a plan or program of a government entity because we believe pay to play concerns are more likely to be present in that situation, and advisers will clearly know that the government entity is a client or investor in the adviser's investment company. As noted above, significant competition exists among advisers to

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retirement plan, such as a 403(b) plan or 457 plan, or any similar program or plan. Proposed rule 206(4)-5(f)(8).

186 In contrast, where securities are privately placed, such as securities of a private fund, the adviser (and through its compliance program, its personnel) should be aware that an investment from a government entity is being solicited and should therefore be in a position to refrain from making contributions that would trigger a "time out" with respect to receiving compensation from that government entity.

have their funds selected as investment options in government-sponsored savings plans, which we believe may contribute to the risk of pay to play.[187]

We believe it is appropriate, however, to apply the other two substantive prohibitions of the proposed rule[188] to advisers to pooled investment vehicles regardless of whether it is included in a plan or program of a government entity. We believe the same concerns regarding pay to play are raised under those prohibitions whether the adviser is managing the government entities' assets directly or through a pooled investment vehicle.

For example, an investment adviser subject to our proposed rule that manages a registered investment company would be prohibited from compensating a third party to solicit an investment by a government entity in the fund or soliciting others to make contributions to officials of a government entity that the adviser seeks to have invest in the fund. For purposes of the two-year time out, however, a mutual fund adviser would not need to screen for investments from government entities to determine if a disqualifying campaign contribution has been made if the fund is used for investment of a state government's general assets or for investment by the state's pension fund. If the registered investment company is to be included in that state's 529 plan, however, the investment adviser would be subject to the two-year time out on contributions.[189]

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187 See supra note 180 and accompanying text.

188 Proposed rule 206(4)-5(a)(2)(i) and (ii).

189 The proposed rule would prohibit the receipt of compensation from the investment company by the investment adviser, not the inclusion of the investment company in the 529 plan, and would also prohibit the receipt of any advisory fee to which the adviser is entitled if it is also a direct adviser to the 529 plan.

We note that a firm retained by a government entity to distribute interests in a 529 plan (i.e., municipal fund securities) may be subject to MSRB rules. See Municipal Securities Rulemaking

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We request comment on the definition of covered investment pool under the proposed rule. Should we also apply the rule in the context of government investments in structured finance vehicles in which public funds may invest?[190] Should we, alternatively or in addition, limit the applicability of the proposed rule's prohibitions in the context of registered investment companies to circumstances under which the government entity's investment is of a sufficiently large size such that the fund adviser is more likely to have an incentive to attempt to influence the government entity's decision-making process? If so, how should we define that threshold? Should we, for example, base it on the amount of assets in the fund, such as 5 percent of the fund's assets? Should we treat differently under the rule advisers to funds in plans where the

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Board, Interpretive Notice: Rule D-12: Interpretation Relating to Sales of Municipal Fund Securities in the Primary Market (Jan. 18, 2001), available at http://www.msrb.org/msrb1/rules/NewRuleD-12Interpretation.htm. Such a distributor may have an affiliated investment adviser that is retained by the government entity to provide investment advice to the 529 plan. Thus, the distributor could be subject to MSRB rules G-37 and G-38, while the affiliated investment adviser could be subject to our proposed rule, if adopted. As we note above, the investment adviser's fiduciary obligations could require it to continue to provide investment advice without compensation after it or a covered associate gives a contribution that triggers our proposed rule's two-year "time out" while MSRB rule G-37 typically would ban a firm from continuing to engage in municipal securities business for two years after a triggering contribution is made. See supra note 80. However, the MSRB has provided additional flexibility in the context of contracts to distribute securities such as interests in 529 plans. See Municipal Securities Rulemaking Board, Interpretation on the Effect of a Ban on Municipal Securities Business under Rule G-37 Arising During a Pre-Existing Engagement Relating to Municipal Fund Securities (Apr. 2, 2002), available at http://www.msrb.org/msrb1/rules/notg37.htm (allowing a dealer that has become subject to G-37's ban on new municipal securities business to continue receiving compensation throughout the duration of the ban if certain conditions are met). We are not proposing a similar approach under our rule because it would undermine the deterrent effect of having a two-year time out.

190 These might include, for example, pools exempt from the definition of "investment company" under Section 3(c)(5) or (6) of the Investment Company Act [15 U.S.C. 80a-3(c)(5) and (6)] and pools relying on rule 3a-7 under the Investment Company Act. [17 CFR 270.3a-7]. Pursuant to our proposed definition of "covered investment pool," the rule would apply to an investment by a

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adviser is not the sole or primary adviser to the plan or where a different adviser's funds are included as investment options under the plan? For example, are there sub-advisory arrangements in which a sub-adviser would not know or be able to influence whether, or which, government entities are being solicited for a covered investment pool? If so, how should we define those sub-advisers? Should we circumscribe the rule's applicability so it is not triggered in the context of government entity investments in particular types of funds, such as money market funds, where the ability of the adviser to profit might be attenuated because, for example, those particular types of funds tend to generate lower margin or investments tend to be for relatively short terms? Should we provide exceptions to the provision subjecting an adviser to a two-year "time out" from receiving compensation in the context of specific types of government entity investments (such as short-term investments for cash management)?

(3) Applying the Compensation Limit to Covered Investment Pools

If a government entity is an investor in a covered investment pool at the time the contribution triggering a two-year "time out" is made, the proposed rule would require the adviser to forgo any compensation related to the assets invested or committed by that government entity.[191] We recognize the provisions of the proposed rule that would require the adviser to

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government entity in a structured finance vehicle that relies on Section 3(c)(1) or 3(c)(7) of the Investment Company Act [15 U.S.C. 80a-3(c)(1) and (7)]. See proposed rule 206(4)-5(f)(3).

191 See discussion at Section II.A.3.(a)(1), supra. We note that the phrase "for compensation" includes both profits and the recouping of costs, so the proposed rule would not permit an adviser to continue to manage assets at cost after a disqualifying contribution is made.

either waive its fee or terminate the relationship raise different issues for investment pools than for separately managed accounts due to various structural and legal differences.

In the case of a private fund, the adviser typically could waive or rebate the related fees and any performance allocation or carried interest.[192] The adviser may also seek to cause the pooled investment vehicle to redeem the investment of the government entity. For many private funds, such as venture capital and private equity funds, it may not be possible for a government entity to withdraw its capital or cancel its commitment without harm to the other investors. We request comment on ways to prevent advisers to these funds from benefitting from contributions covered by the two-year time out, while protecting other investors in the funds.

The options for restricting compensation involving government investors in registered investment companies are more limited, due to both Investment Company Act provisions and potential tax consequences.[193] One approach that would meet the requirements of the proposed rule would be for the adviser of a registered investment company to waive its advisory fee for the fund as a whole in an amount approximately equal to fees attributable to the government

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192 Some commenters on our 1999 Proposal noted that a performance fee waiver raises various calculation issues. An adviser making a disqualifying contribution could comply with the proposed rule by waiving a performance fee or carried interest determined on the same basis as the fee or carried interest is normally calculated, e.g., on a mark-to-market basis. For arrangements like those typically found in private equity and venture capital funds where the fee or carry is calculated based on realized gains and losses and mark-to-market calculations are not feasible, advisers could use a straight line method of calculation which assumes that the realized gains and losses were earned over the life of the investment.

193 See, e.g., Rule 18f-3 under the Investment Company Act. Moreover, other regulatory considerations, such as the Employee Retirement Income Security Act of 1974 [29 U.S.C. 18] ("ERISA"), may impact these arrangements with respect to collective investment trusts.

entity.[194] We request comment on other options that may be available, including alternatives that might require us to revise the proposed rule.

An adviser to a covered investment pool that serves as an investment option in a government program such as a 529 plan might seek to eliminate its investment pool as an option in order to comply with or mitigate costs arising from the rule's two-year "time out." As a result, plan investors may be denied an appropriate investment alternative. Would elimination of the option be an inappropriate consequence we should seek to prevent? Have we appropriately applied the rule to curb pay to play activities (that may be effectuated, for example, through revenue sharing arrangements) while still permitting funds to be marketed and distributed to government entities in the ordinary course of business through compensated third parties, such as registered broker-dealers?

(f) Exemptions

We are proposing a provision under which an adviser may apply to us for an order exempting it from the two-year compensation ban.[195] Under the proposed rule, the Commission could exempt advisers from the rule's "time out" requirement where the adviser discovers contributions that trigger the compensation ban only after they have been made or when imposition of the prohibitions is unnecessary to achieve the rule's intended purpose.[196]

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194 This may also be done at the class level or series level for private funds organized as corporations.

195 Rules 0-4, 0-5, and 0-6 under the Advisers Act [17 CFR 275.0-4, 0-5, and 0-6] provide procedures for filing applications under the Act, including applications under the proposed rule.

196 This provision is similar to our 1999 proposal.

In determining whether to grant an exemption from the two-year compensation ban, we would take into account the varying facts and circumstances that each application presents. Further, we would consider: (i) whether the exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Advisers Act; (ii) whether the investment adviser, (A) before the contribution resulting in the prohibition was made, adopted and implemented policies and procedures reasonably designed to prevent violations of this section; (B) prior to or at the time the contribution which resulted in such prohibition was made, had no actual knowledge of the contribution; and (C) after learning of the contribution, (1) has taken all available steps to cause the contributor involved in making the contribution which resulted in such prohibition to obtain a return of the contribution; and (2) has taken such other remedial or preventive measures as may be appropriate under the circumstances; (iii) whether, at the time of the contribution, the contributor was a covered associate or otherwise an employee of the investment adviser, or was seeking such employment; (iv) the timing and amount of the contribution which resulted in the prohibition; (v) the nature of the election (e.g., federal, state or local); and (vi) the contributor's apparent intent or motive in making the contribution which resulted in the prohibition, as evidenced by the facts and circumstances surrounding such contribution.[197]

These factors are similar to those considered by FINRA and the appropriate bank regulators in determining whether to grant an exemption under MSRB rule G-37(i).[198] As suggested above, when applying the criteria, we expect to take into account, among other things,

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[197] Proposed rule 206(4)-5(e). If the proposed rule is adopted, we would grant such exemptions pursuant to our authority under Section 206A of the Advisers Act [15 U.S.C. 80b-6a].

the varying facts and circumstances presented by each application. The factors are intended to assist us in determining whether granting relief is appropriate. For example, one factor relates to whether the adviser had and implemented reasonably designed policies and procedures. Several other factors relate to the adviser's knowledge of the contribution and its conduct after the contribution was discovered. The remaining factors largely relate to the particular facts surrounding the contribution that may affect whether it is appropriate for us to grant relief in that situation. For example, the same amount of money contributed in a local election may have a much greater impact than in a federal election. Facts regarding the timing and amount of the contribution, the contributor's employment status at the time of the contribution, as well as the contributor's apparent intent or motive may suggest whether the contribution was made to influence the selection of the adviser. We would apply these exemptive provisions with sufficient flexibility to avoid consequences disproportionate to the situation, while effecting the policies underlying the rule.[199] Should we provide for additional exemptions from the proposed rule? We request comment on the proposed criteria for exemptions by application. Are there additional criteria the Commission should explicitly consider when determining whether to grant an exemption?

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198 See MSRB rule G-37(i).

199 An adviser applying for an exemption could place advisory fees earned between the date of the contribution triggering the prohibition and the date on which we determine whether to grant an exemption in an escrow account. The escrow account would be payable to the adviser if the Commission grants the exemption. If the Commission does not grant the exemption, the fees contained in the account must be returned to the public fund.

B. Recordkeeping

We are also proposing amendments to rule 204-2[200] to require an investment adviser that is registered or required to be registered with us and (i) has or seeks government clients or (ii) provides investment advisory services to a covered investment pool in which a government entity investor invests or is solicited to invest, to make and keep certain records of contributions made by the adviser and its covered associates. We believe these records would be necessary to allow us to examine for compliance with rule 206(4)-5, if adopted.

The proposed amendments would require an adviser to make and keep the following records: (i) the names, titles and business and residence addresses of all covered associates of the investment adviser; (ii) all government entities for which the investment adviser or any of its covered associates is providing or seeking to provide investment advisory services, or which are investors or are solicited to invest in any covered investment pool to which the investment adviser provides investment advisory services, as applicable;[201] (iii) all government entities to which the investment adviser has provided investment advisory services, along with any related covered investment pool(s) to which the investment adviser has provided investment advisory services and in which the government entity has invested, as applicable, in the past five years, but not prior to the effective date of the proposed rule;[202] and (iv) all direct or indirect contributions or payments made by the investment adviser or any of its covered associates to an official of a

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200 17 CFR 275.204-2.

201 We note that an adviser may identify its clients on its books through the use of codes. See Advisers Act rule 204-2(d) [17 CFR 275.204-2(d)].

202 See id.

government entity, a political party of a state or political subdivision thereof, or a PAC.[203] The adviser's records of contributions and payments would be required to be listed in chronological order identifying each contributor and recipient, the amounts and dates of each contribution or payment and whether such contribution or payment was subject to the exception for certain returned contributions pursuant to proposed rule 206(4)-5(b)(2).[204] These requirements are generally consistent with the MSRB recordkeeping rule for broker-dealers.[205]

Should we exclude de minimis contributions from the recordkeeping requirement? Should we expand our recordkeeping requirements to cover records of contributions or payments not just to government officials and political parties, but also persons associated with officials of government entities, regardless of whether contributions or payments to these individuals trigger the prohibitions contained in our proposed pay to play rule?[206]

To manage compliance with the proposed rule effectively, we would expect that the adviser would adopt sufficient internal procedures – which would include keeping certain records

203 Proposed rule 204-2(a)(18)(i). We note that this provision is intended to include records of direct contributions an adviser or its covered associates makes under proposed rule 206(4)-5(a)(1), as well as records of contributions or payments an adviser or its covered associates coordinates or solicits another person or PAC to make under proposed rule 206(4)-5(a)(2)(ii), which would be considered indirect contributions or payments.

204 Proposed rule 204-2(a)(18)(ii).

205 MSRB rule G-8(a)(xvi). Like rule G-37, the proposed rule requires an investment adviser to keep, in addition to records of political contributions, records of any other "payments" made to officials, political parties or PACs. See proposed amendment to rule 204-2(a)(18)(i)(D). See also supra note 149 and accompanying text for an explanation of how the rule distinguishes between contributions and payments. The MSRB also requires certain records to be made and kept in accordance with disclosure requirements that our proposed rule does not contain.

206 See supra note 89 and accompanying text.

– to prevent the rule's prohibitions from being triggered.[207] As discussed above, a single contribution could, under the rule, lead to a two-year suspension of compensated advisory activities for a government client. Therefore, we anticipate that many, if not all, of the records that we propose to require registered advisers make and keep under our proposed amendments would be those an adviser undertaking a serious compliance effort would ordinarily make and keep. We request that commenters opposing the new recordkeeping requirements suggest alternative means that would be sufficient to aid examinations for compliance with the proposed rule.

C. Amendment to Cash Solicitation Rule

We are also proposing a technical amendment to rule 206(4)-3 under the Advisers Act, the "cash solicitation rule." That rule makes it unlawful, except under specified circumstances and subject to certain conditions, for an investment adviser to make a cash payment to a person who directly or indirectly solicits any client for, or refers any client to, an investment adviser.[208]

Because paragraph (iii) of rule 206(4)-3 contains provisions regarding more general restrictions on third-party solicitors that would cover solicitation activities directed at any client – whether a government entity client or not – our proposed technical amendment would be designed to note the specialized provisions prohibiting payments by an adviser to third-party solicitors of government clients that are contained in proposed rule 206(4)-5. Specifically, we propose to add a new paragraph (e) to rule 206(4)-3 to alert advisers and others that special

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[207] See Advisers Act rule 206(4)-7 [17 CFR 275.206(4)-7] (setting forth guidelines for advisers' compliance policies and procedures).

[208] 17 CFR 275.206(4)-3.

prohibitions apply to solicitation activities involving government entity clients under our proposed pay to play rule.[209]

D. Transition Period

The prohibition and recordkeeping requirements under the proposed rule would arise from contributions made on or after the effective date of the rule, if adopted. As a result, firms would need to have developed and adopted appropriate procedures to track contributions and would need to begin monitoring contributions made by their covered associates on that date. The Commission requests comment on whether firms would require additional time to develop procedures to comply with the proposed rule and, if so, how long of a transition period following the rule's adoption would be necessary? For example, if a transition period is necessary, would 90 days be an appropriate amount of time? Would longer be necessary, e.g., six months, and if so, why?

E. General Request for Comment

Any interested persons wishing to submit written comments on the proposed rule and rule amendment that are the subject of this Release, or to suggest additional changes or submit comments on other matters that might have an effect on the proposals described above, are requested to do so. Commenters suggesting alternative approaches are encouraged to submit proposed rule text.

III. COST/BENEFIT ANALYSIS

We are sensitive to the costs and benefits imposed by our rules, and understand that there would be compliance costs with proposed rule 206(4)-5 and the proposed amendment to rule

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209 Proposed rule 206(4)-3(e).

204-2.[210] We are mindful of the burdens the proposed rule would place on advisory firms and limitations it would place on the ability of certain persons associated with an adviser to make contributions to candidates for certain offices and to solicit contributions for certain candidates and payments to political parties. We thus have narrowly tailored the rule to achieve our goal of ending adviser participation in pay to play practices, while seeking to limit these burdens.

The proposed rule and rule amendments would address "pay to play" practices by investment advisers that provide, or are seeking to provide, advisory services to government entity clients and to certain covered investment pools in which a government entity invests. The proposed rule would prohibit an investment adviser from providing advisory services for compensation to a government client for two years after the adviser or certain of its executives or employees make a contribution to certain elected officials or candidates. The proposed rule would also prohibit an adviser from providing or agreeing to provide, directly or indirectly, payment to any third party for a solicitation of advisory business from any government entity, or for a solicitation of a government entity to invest in certain covered investment pools, on behalf of such adviser. Additionally, the proposed rule would prevent an adviser from coordinating or soliciting from others contributions to certain elected officials or candidates or payments to certain political parties. Our proposed amendment to rule 204-2 would require a registered adviser (or adviser required to be registered) to maintain certain records of the political contributions made by the adviser or certain of its executive or employees.

210 We are also proposing to make a conforming technical amendment to rule 206(4)-3 to address potential areas of conflict with proposed rule 206(4)-5. We do not expect that this technical amendment will affect the costs associated with the rulemaking.

A. Benefits

As discussed extensively throughout this release, we expect that proposed rule 206(4)-5 would yield several important direct and indirect benefits. At its core, the rulemaking addresses practices that undermine the integrity of our markets. Overall, the proposed rule is intended to address pay to play relationships that interfere with the legitimate process by which advisers are chosen based on the merits rather than on their contributions to political officials. The potential for fraud to invade the various, intertwined relationships created by pay to play arrangements is without question. Accordingly, we believe that the proposed rule will achieve its goals of protecting public pension plans, beneficiaries, and other investors from the resulting harms.

Curtailing pay to play practices will help protect public pension plans and investments of the public in government-sponsored savings and retirement plans and programs by addressing situations in which a more qualified adviser may not be selected, potentially leading to inferior management, diminished returns or greater losses. By addressing pay to play practices, we would be leveling the playing field so that the advisers selected to manage retirement funds and other investments for the public are more likely to be selected based on their skills and the quality of their advisory services. These benefits could result in substantial savings and better performance for the public pension plans, their beneficiaries, and participants.[211]

By leveling the playing field among advisers competing for state and local government business, the proposed rule could also eliminate or minimize manipulation of the market for advisory services provided to state and local governments. Payments made to third-party

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211 According to US census data as of 2007, there are 2,547 state and local government employee retirement systems.

solicitors as part of pay to play practices create artificial barriers to competition for firms that cannot, or will not, make those contributions or payments. They also create increased costs for firms that may feel they have no alternative but to pay to play. Additionally, pay to play practices potentially expose an adviser to other costs, such as liability, defense costs and distraction from its duties. Curtailing pay to play arrangements enables advisory firms, particularly smaller advisory firms, to compete on merit, rather than their ability or willingness to make contributions.

Moreover, the absence of arm's-length negotiations may enable advisers to obtain greater ancillary benefits, such as "soft dollars," from the advisory relationship, which may be directed for the benefit of the adviser, potentially at the expense of the pension plan, thereby using a pension plan asset for the adviser's own purposes.[212] Additionally, taxpayers could benefit because they might otherwise bear the financial burden of bailing out a government pension fund that has ended up with a shortfall due to poor performance or excessive fees that might result from pay to play.

Applying the proposed rule to government entity investments in certain pooled investment vehicles or where a pooled investment vehicle is an investment option in a government-sponsored plan or program would extend the same benefits regardless of whether an adviser subject to the proposed rule is providing advice directly to the government entity or is managing assets for the government entity indirectly through a pooled investment vehicle. By addressing distortions in the process by which investment decisions are made regarding public investments, we will provide important protections to public pension plans and their beneficiaries, as well as participants in other important plans or programs sponsored by government entities. Other investors in a pooled investment vehicle also will be better protected from, among other things, the effects of fraud that may result from an adviser's participation in pay to play activities, such as higher advisory fees.

Finally, the proposed amendments to rule 204-2 would benefit the public plans and their beneficiaries and participants in state plans or programs as well as investment advisers that keep the required records. The public pension plans, beneficiaries, and participants would benefit from these amendments because the records required to be kept would provide Commission staff with information to review an adviser's compliance with proposed rule 206(4)-5 and thereby may promote improved compliance. Advisers would benefit from the proposed amendments to the recordkeeping rule as these records would assist the Commission in enforcing the rule against, for example, competitors whose pay to play activities, if not uncovered, could adversely affect the competitive position of a compliant adviser.

B. Costs

The proposed rule and rule amendments would impose costs on advisers that provide advisory services to government clients, though we have tried to minimize the costs associated with an inadvertent violation of proposed rule 206(4)-5 by including an exception for certain returned contributions. The proposed rule would require an adviser with government clients, and an adviser that solicits business from government clients, to incur costs to monitor contributions made by the adviser and its covered associates, and to establish procedures to comply with the

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212 See supra note 51.

proposed rule and rule amendments. The initial and ongoing compliance costs imposed by the proposed rule would vary significantly among firms, depending on a number of factors. These include the number of covered associates of the adviser, the degree to which compliance procedures are automated, the extent to which an adviser has a pre-existing policy under its code of ethics or compliance program,[213] and whether the adviser is affiliated with a broker-dealer firm that is subject to rules G-37 and G-38. A smaller adviser, for example, would likely have a small number of covered associates, and thus expend less resources to comply with the proposed rule and rule amendments than a larger adviser.

A large adviser is likely to spend more resources to comply with the rule than a smaller adviser. However, based on staff observations, a large adviser is more likely to have an affiliated broker-dealer that is required to comply with MSRB rules G-37 and G-38.[214] Such a large adviser could likely use some or all of the compliance procedures established by its broker-dealer affiliate to facilitate its compliance with proposed rule 206(4)-5. As a result, many advisers with

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213 See Investment Counsel Association of America Comment Letter (May 15, 2000) ("May ICAA Comment Letter") ("According to our members, many investment advisers already have policies and procedures in place to report contributions under state and local law and to avoid pay to play issues.").

214 According to registration information available from Investment Adviser Registration Depository ("IARD") as of July 1, 2009, there are 1,312 SEC-registered investment advisers (or 11.57% of the total 11,340 registered advisers) that indicate in Item 5.D.(9) of Form ADV that they have state or municipal government clients. Of those 1,312 advisers, 108 (or 82.4%) of the largest 10% have one or more affiliated broker-dealers or are, themselves, also registered as a broker-dealer; and 202 of the largest 20% (or 87.1%) have one or more affiliated broker-dealers or are, themselves, also registered as a broker-dealer. Conversely, only 46 (or 35.1%) of the smallest 10% have one or more affiliated broker-dealers or are, themselves, also registered as a broker-dealer; and only 72 of the smallest 20% (or 31.0%) have one or more affiliated broker-dealers or are, themselves, also registered as a broker-dealer. With respect to broker-dealer affiliates, however, we note that our IARD data does not indicate whether the affiliated broker-dealer is a municipal securities dealer subject to MSRB rules G-37 and G-38..

broker-dealer affiliates may spend less resources to comply with the proposed rule and rule amendments.[215]

We anticipate that advisory firms subject to proposed rule 206(4)-5 would develop compliance procedures to monitor the political contributions made by the adviser and its covered associates. We estimate that the costs imposed by the proposed rule would be higher initially, as firms establish and implement procedures and systems to comply with the rule and rule amendments. It is anticipated that compliance expenses would then decline to a relatively constant amount in future years, and annual expenses are likely to be lower for small advisers as the systems and processes should be less complex than for a large adviser.

We estimate that approximately 1,764 investment advisers registered with the Commission may be affected by the proposed rule and rule amendments.[216] Of the 1,764

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215 Cf. Comment Letter of US Bancorp Piper Jaffray (Nov. 15, 1999) ("US Bancorp Letter") ("[T]he more the Rule mirrors G-37, the more firms can borrow from or build upon compliance procedures already in place. . . . [H]owever, [there are] many differences between the rules that would result in significant new burdens.").

216 This number is based on registration information available from IARD as of July 1, 2009. As noted previously, there are 1,312 SEC-registered investment advisers (or 11.57% of the total 11,340 registered advisers) that indicate in Item 5.D.(9) of Form ADV that they have state or municipal government clients. Based on this data point and other responses to Item 5.D., we further estimate that 289 (or 11.57%) of the 2,502 registered investment advisers that manage "other pooled investment vehicles" (and do not also indicate that they have state or municipal government clients) are advising pooled investment vehicles in which government clients invest, and we estimate that 79 (or 11.57%) of the 679 registered investment advisers that manage registered investment companies (and do not also indicate that they have state or municipal government clients) are advising registered investment companies that are available as an investment option in a government plan or program. The sum of 1,312, 289 and 79 is 1,680. The proposed rule also applies to those advisers that seek to obtain government clients, and we do not know the precise number of such advisers. We believe, however, that the percentage of advisers is likely not great because, according to IARD data, there has not been any appreciable growth or shrinkage over the past five years in the percentage of SEC-registered advisers who have state or municipal government clients; the percentage has been almost unchanged. Accordingly, we estimate that an additional 5% (or 84) of SEC-registered advisers are seeking government clients, for a total of 1,764 (1,680 + 84) registered advisers subject to the proposed rule.

advisers, we estimate that approximately 1,300 advisers have fewer than five covered associates that would be subject to the proposed rule each, a "smaller firm"; approximately 328 advisers have between five and 15 covered associates each, a "medium firm"; and approximately 136 advisers have more than 15 covered associates that would be subject to the prohibitions of the proposed rule each, a "larger firm".[217]

Advisers that are unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act [15 U.S.C. 80b-3(b)(3)] would be subject to proposed rule 206(4)-5.[218] Based on our review of registration information on IARD and outside sources and reports, we estimate that there are approximately 2,000 advisers that are unregistered in reliance on section 203(b)(3).[219] Applying the same principles we used with respect to registered investment advisers, we estimate that 231 of those advisers manage pooled investment vehicles in which government client assets are invested and would therefore be subject to the proposed rule.[220]

For purposes of this analysis, it is assumed that each exempt advisory firm that would be subject to the proposed rule would likely either be smaller firms or medium firms, in terms of

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217 These estimates are based on IARD data, specifically the responses to Item 5.B.(1) of Form ADV, that 967 (or 73.7%) of the 1,312 registered investment advisers that have government clients have fewer than five employees who perform investment advisory functions related to those government clients, 244 (or 18.6%) have five to 15 such employees, and 101 (or 7.7%) have more than 15 such employees. We then applied those percentages to the 1,764 advisers we believe will be subject to the proposed rule for a total of 1,300 smaller, 328 medium and 136 larger firms.

218 The proposed amendments to rules 204-2 and 206(4)-3 would apply only to advisers that are registered, or required to be registered, with the Commission.

219 This number is based on our review of registration information on IARD as of July 1, 2009, IARD data from the peak of hedge fund adviser registration in 2005, and a distillation of numerous third-party sources including news organizations and industry trade groups.

220 11.57% of 2000 is 231.4. See supra note 216.

number of covered associates because it is unlikely that an adviser that is limited to fewer than 15 clients would have a large number of advisory personnel that would be covered associates.[221]

Although the time needed to comply with the proposed rule would vary significantly from adviser to adviser, the Commission staff estimates that firms with government clients would spend between 8 hours and 250 hours to establish policies and procedures to comply with the proposed rule. Commission staff further estimates that ongoing compliance with the proposed rule would require between 10 and 1,000 hours, annually. These estimates are derived in part from conversations with industry professionals regarding broker-dealer compliance with rule G-37 and G-38 and representatives of investment advisers that have pay to play policies in place. In addition, advisory firms may incur one-time costs to establish or enhance current systems to assist in their compliance with the proposed rule. These costs would vary widely among firms. Small advisers may not incur any system costs if they determine a system is unnecessary due to the limited number of employees they have or the limited number of government entity clients they have. Large firms likely already have devoted significant resources into automating compliance and reporting and the new rule could result in enhancements to these existing systems. We believe such system costs could range from the tens of thousands of dollars for simple reporting systems, to hundreds of thousands of dollars for complex systems used by the large advisers. As we noted previously, large advisers are more likely to have broker-dealer affiliates that may already have compliance systems in place for MSRB rules G-37 and G-38 that could be used by an adviser.

221 See section 203(b)(3) of the Advisers Act [15 U.S.C. 80b-3(b)(3)].

Initial compliance procedures would likely be designed, and ongoing administration of them performed, by compliance managers and compliance clerks. We estimate that the hourly wage rate for compliance managers is $258, including benefits, and for compliance clerks, $63 per hour, including benefits.[222] To establish and implement adequate compliance procedures, we estimate that the proposed rule would impose initial compliance costs of approximately $2,064[223] per smaller firm, approximately $26,156[224] per medium firm, and approximately $52,313[225] per larger firm.[226] It is estimated that the proposed rule would impose annual, ongoing compliance

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222 Our hourly wage rate estimate for a compliance manager and compliance clerk is based on data from the Securities Industry Financial Markets Association's Management & Professional Earnings in the Securities Industry 2008, modified by Commission staff to account for an 1800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

223 The per firm cost estimate is based on our estimate that development of initial compliance procedures for smaller firms would take 8 hours of compliance manager time (at $258 per hour).

224 With respect to our estimated range of 8-250 hours, we assume a medium-sized firm would take 125 hours to develop initial compliance procedures, and such a firm would likely have support staff. We also anticipate that a compliance manager would do approximately 75% of the work because he/she is responsible for implementing the policy for the entire firm. Accordingly, the per firm cost estimate is based on our estimate that development of initial compliance procedures for medium firms would take 93.75 hours of compliance manager time (at $258 per hour) and 31.25 hours of clerical time (at $63 per hour).

225 With respect to our estimated range of 8-250 hours, we assume a larger firm would take 250 hours to develop initial compliance procedures, and such a firm would likely have support staff. We also anticipate that a compliance manager would do approximately 75% of the work because he/she is responsible for implementing the policy for the entire firm. Accordingly, the per firm cost estimate is based on our estimate that development of initial compliance procedures for larger firms would take 187.50 hours of compliance manager time (at $258 per hour) and 62.5 hours of clerical time (at $63 per hour).

226 Some commenters in 1999 suggested that our cost estimates, then, were too low. See US Bancorp Letter ("[W]e believe the initial compliance cost estimates in the [1999] Release of $285 for a small firm, $13,387.50 for a medium firm and $22,312.50 for a large firm underestimate by orders of magnitude the initial costs of compliance."); Comment Letter of American Council of Life Insurance (Nov. 1, 1999) ("Many of our member companies have observed that the proposal's compliance cost projections are speculative and unrealistic, especially when applied to large diversified financial institutions like life insurers. . . . Moreover, the cost estimates are greatly understated when the proposed rule is applied to large diversified

(continued . . .)

expenses of approximately $2,580[227] per smaller firm, $104,625[228] per medium firm, and $209,250[229] per larger firm.

We further anticipate that approximately one-third of advisers that we estimate would be subject to the rule may also engage outside legal services to assist in drafting policies and procedures.[230] We estimate the cost associated with such an engagement would include fees for approximately three hours of outside legal review for a smaller firm, 10 hours for a medium firm, and 30 hours for a large firm, at a rate of $400 per hour. For a smaller firm we estimate a total of $1,200 in outside legal fees for each of the estimated 325 advisers that would seek assistance, for a medium firm we estimate a total of $4,000 for the estimated 164 advisers that would seek assistance, and for each of the 102 larger firms we estimate a total of $12,000.[231] Thus, we

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life insurers offering investment advice as one of several products and services. . . . One of our larger diversified member companies has estimated that it would cost approximately $200,000 per year to administer compliance with the proposed rule for the approximately 200-300 people the rule would encompass. The company developing these estimates based its estimate of hours and labor costs on its actual compliance with Rule G-37."). We have significantly increased our cost estimates from our 1999 proposal. We also note that the scope of persons covered under the current rule proposal is narrower than the scope of persons proposed to be covered in 1999. See supra note 98 and accompanying text.

227 The per firm cost estimate is based on our estimate that ongoing compliance procedures for smaller firms would take 10 hours of compliance manager time (at $258 per hour) per year.

228 The per firm cost estimate is based on our estimate that ongoing compliance procedures for medium firms would take 375 hours of compliance manager time (at $258 per hour) and 125 hours of clerical time (at $63 per hour), per year.

229 The per firm cost estimate is based on our estimate that ongoing compliance procedures for larger firms would take 750 hours of compliance manager time (at $258 per hour) and 250 hours of clerical time (at $63 per hour), per year.

230 Based on staff observations, we estimate 75% of larger firms, 50% of medium firms, and 25% of smaller firms would seek to outsource all or a portion of this type of legal work.

231 As noted above, we estimate 75% of larger firms, 50% of medium firms, and 25% of smaller firms would seek the assistance of outside counsel.

estimate that approximately 591 investment advisers will incur these additional costs, for a total cost of $2,270,000 among advisers affected by the proposed rule amendments.

Additionally, we expect that on average approximately five advisers annually will apply to the Commission for an exemption from the proposed rule.[232] We estimate that a firm that applies for an exemption will hire outside counsel to prepare an exemptive request, and that counsel will spend 16 hours preparing and submitting an application for review at a rate of $400 per hour. As a result, each application will cost approximately $6,400, and the total estimated cost for five applications annually will be $32,000.

The prohibitions of the proposed rule may also impose other costs on advisers, covered associates, third-party solicitors, and political officials. An adviser that becomes subject to the prohibitions of the proposed rule would no longer be eligible to receive advisory fees from its government client. This could limit the number of advisers able to provide services to potential government entity clients. The adviser, however, may be obligated to provide (uncompensated) advisory services for a reasonable period of time until the government client finds a successor to ensure its withdrawal did not harm the client, or the contractual arrangement between the adviser and the government client might obligate the adviser to continue to perform under the contract at no fee. An adviser that provides uncompensated advisory services to a government client would incur the direct cost of providing uncompensated services, and may incur opportunity costs if the adviser is unable to pursue other business opportunities for a period of time. Advisers to government clients, as well as covered associates of the adviser, also may be less likely to make

232 This estimate is based on staff discussions with Financial Industry Regulatory Authority staff responsible for reviewing exemptive applications submitted under MSRB rule G-37.

political contributions to political officials, possibly imposing costs on the officials if they are unable to secure alternate funding. Under the proposed rule, covered associates and executives may face new limitations on the amounts and to whom they can contribute. In addition, these same individuals could be prohibited from soliciting others to contribute or from coordinating contributions to government officials or political parties in certain circumstances. These limitations and prohibitions, including if a firm chose to adopt policies or procedures that are more restrictive than the proposed rule, could be perceived by the individuals subject to them as costs imposed on their ability to express their support for certain candidates for elected office and government officials.

Because the proposed rule would prohibit advisers from compensating third parties to solicit government entities for advisory services, advisers that currently rely on third-party solicitors to obtain government clients may have to bear the expense of hiring and training in-house staff in order to continue their solicitation activities. While third-party solicitors are not subject to the proposed rule, the proposed ban on advisers' use of third-party solicitors may have a substantial negative impact on persons who provide third-party solicitation services, and if their businesses consists solely of soliciting government entities on behalf of investment advisers, the proposed rule could result in these persons instead being employed directly by advisers or shifting the focus of their solicitation activities. In addition, small investment advisers and new investment advisers that do not have the capital to hire employees to obtain government clients may find it difficult to enter the market to provide advisory services to government pension plans or to obtain additional government clients.

We also anticipate that the proposed amendment to rule 204-2 would impose additional costs. The proposed amendments to rule 204-2 would require that SEC-registered advisers maintain certain records of campaign contributions by certain advisory personnel.[233] For purposes of the Paperwork Reduction Act, we have estimated that Commission-registered advisers would incur approximately 3,528 additional hours annually to comply with the proposed amendments to rule 204-2.[234] Based on this estimate, we anticipate that advisers would incur an aggregate cost of approximately $222,264 per year for the total hours advisory personnel would spend in complying with the proposed recordkeeping requirements.[235] Unregistered advisers that would be subject to proposed rule 206(4)-5 would not be subject to the proposed amendments to rules 204-2 and 206(4)-3.

C. Request for Comment

The Commission requests comment on the effects of the proposed rule and rule amendments on pension plan beneficiaries, participants in government plans or programs, investors in pooled investment vehicles, investment advisers, the advisory profession as a whole, government entities, third party solicitors, and political action committees. We request data to quantify the costs and value of the benefits associated with the proposed rule. Specifically,

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233 One commenter in 1999 expressed the view that our proposed amendments to the recordkeeping rule would be burdensome. See Nov. ICAA Comment Letter ("The proposed rule, in effect, requires firms to keep an ongoing, continuously updated list of prospective government clients. . . . [I]t is logistically unclear how a firm should compile this list. . . . [T]he burden of continuously compiling this list would be significant.") We have increased our burden estimate from our 1999 proposal. We note that records are a critical component of proposed rule 206(4)-5. In particular, such records are necessary for examiners to inspect advisers for compliance with the terms of the proposed rule. We also note that it is typical for advisers seeking business from government entities to do so through a request for proposal or similar process, which would typically generate a record.

234 See infra note 242.

235 We expect that the function of recording and maintaining records of political contributions would be performed by a compliance clerk at a cost of $63 per hour. See supra note 222. Therefore the total costs would be $222,264 (3,528 hours x $63 per/hour).

comment is requested on the costs of establishing compliance procedures to comply with the proposed rule, both on an initial and ongoing basis. Comment also is requested on the costs of using compliance procedures of an affiliated broker-dealer that the broker-dealer established as a result of rule G-37 and G-38.[236] In addition, we request data regarding our assumptions about the number of unregistered advisers that would be subject to the proposed rule, and the number of covered associates of these exempt advisers. As discussed below, section 202(c)(1) of the Advisers Act does not apply to proposed new rule 206(4)-5 or the proposed amendments to rule 206(4)-3. Nonetheless, in the context of the objectives of this rulemaking, we are interested in comments that address whether these proposed rules will promote efficiency, competition and capital formation. We solicit comment on the effect the proposed rule would have on the market for investment advisory services and third-party solicitation services. Commenters should provide analysis and empirical data to support their views on the costs and benefits associated with this proposal.

IV. PAPERWORK REDUCTION ACT

A. Rule 204-2

The proposed amendment to rule 204-2 contains a new "collection of information" requirement within the meaning of the PRA, and the Commission has submitted the proposed amendment to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for the collection of information is "Rule 204-2

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236 See ABA Comment Letter ("Any cost-benefit analysis of the Rule logically should begin, by analogy, with an analysis of the costs that have been borne by Municipal Securities Professionals in complying with MSRB Rule G-37, bearing in mind that the proposed Rule contains no reporting requirements.").

under the Advisers Act of 1940." Rule 204-2 contains a currently approved collection of information number under OMB control number 3235-0278. 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.

Section 204 of the Advisers Act provides that investment advisers registered or required to be registered with the Commission must make and keep certain records for prescribed periods, and make and disseminate certain reports. Rule 204-2 sets forth the requirements for maintaining and preserving specified books and records. This collection of information is mandatory. The Commission staff uses this collection of information in its examination and oversight program, and the information generally is kept confidential.[237]

The current approved collection of information for rule 204-2 is based on an average of 181.15 burden hours each year, per Commission-registered adviser, for a total of 1,954,109 burden hours. The current total burden is based on an estimate of 10,787 registered advisers.

The proposed amendments to rule 204-2 would require every investment adviser registered or required to be registered that provides or seeks to provide advisory services to government entities to maintain certain records of contributions made by the adviser or any of its covered associates. The proposed amendments would require an adviser to make and keep the following records: (i) the names, titles and business and residence addresses of all covered associates of the investment adviser; (ii) all government entities for which the investment adviser or any of its covered associates is providing or seeking to provide investment advisory services, or which are investors or are solicited to invest in any covered investment pool to which the investment adviser provides investment advisory services, as applicable; (iii) all government entities to which the investment adviser has provided investment advisory services, along with any related covered investment pool(s) to which the investment adviser has provided investment advisory services and in which the government entity has invested, as applicable, in the past five years, but not prior to the effective date of the proposed rule; and (iv) all direct or indirect contributions or payments made by the investment adviser or any of its covered associates to an official of a government entity, a political party of a state or political subdivision thereof, or a PAC. An adviser to a covered investment pool in which a government entity invests or is solicited to invest would be treated as though that investment adviser were providing or seeking to provide investment advisory services directly to the government client. The adviser's records of contributions and payments would be required to be listed in chronological order identifying each contributor and recipient, the amounts and dates of each contribution or payment and whether such contribution or payment was subject to the exception for certain returned contributions pursuant to proposed rule 206(4)-5(b)(2). These records would be required to be maintained in the same manner, and for the same period of time, as other books and records under rule 204-2(a). This collection of information would be found at 17 CFR 275.204-2. Advisers that are exempt from Commission registration under section 203(b)(3) of the Advisers Act would not be subject to the recordkeeping requirements.

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[237] See section 210(b) of the Advisers Act [15 U.S.C. 80b-10(b)].

Commission records indicate that currently there are approximately 11,340 registered investment advisers subject to the collection of information imposed by rule 204-2.[238] As a result of the increase in the number of advisers registered with the Commission since the current total burden was approved, the total burden has increased by 100,176 hours (553 additional advisers[239] x 181.15 hours). We estimate that approximately 1,764 Commission-registered advisers provide, or seek to provide, advisory services to government clients and to certain pooled investment vehicles in which government entities invest, and would thus be affected by the proposed rule amendments.[240] Under the proposed amendments, each respondent would be required to retain the records in the same manner and for the same period of time as currently required under rule 204-2. The proposed amendments to rule 204-2 are estimated to increase the burden by approximately two hours per Commission-registered adviser with government clients annually for a total increase of 3,528 hours.[241] The revised annual aggregate burden for all respondents to the recordkeeping requirements under rule 204-2 thus would be 2,057,813 hours.[242] The revised weighted average burden per Commission-registered adviser would be 181.46 hours.[243]

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238 This figure is based on registration information from IARD as of July 1, 2009.

239 11,340 – 10,787 = 553

240 See supra note 216.

241 This increased burden relates only to the recordkeeping requirements we are proposing to amend. See supra section III.B. of this release for an explanation of other estimated costs associated with complying with the proposed rule and rule amendments.

242 1,954,109 (current approved burden) + 100,176 (burden for additional registrants) + 3,528 (burden for proposed amendments) = 2,057,813 hours.

243 2,057,813 (revised annual aggregate burden) divided by 11,340 (total number of registrants) = 181.46.

Additionally, we expect advisory firms may incur one-time costs to establish or enhance current systems to assist in their compliance with the proposed amendments to rule 204-2. These costs would vary widely among firms. Small advisers may not incur any system costs if they determine a system is unnecessary due to the limited number of employees they have or the limited number of government entity clients they have. Large firms likely already have devoted significant resources into automating compliance and reporting and the new rule could result in enhancements to these existing systems. We believe they could range from the tens of thousands of dollars for simple reporting systems, to hundreds of thousands of dollars for complex systems used by the large advisers.

B. Rule 206(4)-3

The proposed amendment to rule 206(4)-3 contains a revised "collection of information" requirement within the meaning of the PRA, and the Commission has submitted the proposed amendment to the OMB for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for the collection of information is "Rule 206(4)-3 – Cash Payments for Client Solicitations." Rule 206(4)-3 contains a currently approved collection of information number under OMB control number 3235-0242.

Section 206(4) of the Advisers Act provides that it shall be unlawful for any investment adviser to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative. Rule 206(4)-3 generally prohibits investment advisers from paying cash fees to solicitors for client referrals unless certain conditions are met. The rule requires that an adviser pay all solicitors' fees pursuant to a written agreement that the adviser is required to retain. This collection of information is mandatory. The Commission staff uses this collection of information in its examination and oversight program, and the information generally is kept confidential.[244]

The current approved collection of information for rule 206(4)-3 is based on an estimate that 20% of the 10,817 Commission-registered advisers (or 2,163 advisers) rely on the rule, at an average of 7.04 burden hours each year, per respondent, for a total of 15,228 burden hours (7.04 x 2,163).

The proposed amendments to rule 206(4)-3 would require every investment adviser that relies on the rule and that provides or seeks to provide advisory services to government entities to also abide by the limitations provided in proposed rule 206(4)-5. This collection of information would be found at 17 CFR 275.206(4)-3. Advisers that are exempt from Commission registration under section 203(b)(3) of the Advisers Act would not be subject to rule 206(4)-3.

Commission records indicate that currently there are approximately 11,340 registered investment advisers,[245] 20% of which (or 2,268) are likely subject to the collection of information imposed by rule 206(4)-3. As a result of the increase in the number of advisers registered with the Commission since the current total burden was approved, the total burden has increased by 739.2 hours (105 additional advisers[246] x 7.04 hours). We assume that approximately 20% of the Commission-registered advisers that use rule 206(4)-3 (or 454 advisers) provide, or seek to provide, advisory services to government clients and would thus be

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244 See section 210(b) of the Advisers Act [15 U.S.C. 80b-10(b)].

245 This figure is based on registration information from IARD as of July 1, 2009.

246 2,268 (20% of current registered investment advisers) – 2,163 (20% of registered investment advisers when burden estimate was last approved by OMB) = 105.

affected by the proposed rule amendments.[247] Under the proposed amendments, each respondent would be prohibited from certain solicitation activities with respect to government clients,[248] which would eliminate the need to enter into and retain the written agreement required under rule 206(4)-3 with respect to those clients. Accordingly, the proposed amendments to rule 206(4)-3 are estimated to decrease the burden by 20%, or approximately 1.4 hours, per Commission-registered adviser that uses the rule and has or is seeking government clients annually, for a total decrease of 635.6 hours. The revised annual aggregate burden for all respondents to the recordkeeping requirements under rule 206(4)-3 thus would be 15,331.6 hours.[249] The revised weighted average burden per Commission-registered adviser would be 6.76 hours.[250]

C. Request for Comment

Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments to: (i) evaluate whether the proposed amendments to the collection 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 collection 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

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247 In light of the 11.57% of registered investment advisers that indicate they have state or municipal government clients, we conservatively estimate that 20% of the advisers who rely on rule 206(4)-3 are soliciting government entities to be advisory clients or to invest in covered investment pools those advisers manage. See supra note 214.

248 See proposed rule 206(4)-3(a).

249 15,228 (current approved burden) + 739.2 (burden for additional registrants) - 635.6 (reduction in burden for proposed amendments) = 15,331.6 hours.

250 15,331.6 (revised annual aggregate burden) divided by 2,268 (total number of registrants who rely on rule) = 6.76.

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.

Persons desiring to submit comments on the collection of information requirements 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 3208, Washington, DC 20503, and also should send a copy of their comments to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090 with reference to File No. S7-18-09. Requests for materials submitted to OMB by the Commission with regard to this collection of information should be in writing, refer to File No. S7-18-09, 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 collections of information between 30 and 60 days after publication. A comment to OMB is best assured of having its full effect if OMB receives it within 30 days after publication of this release.

V. INITIAL REGULATORY FLEXIBILITY ANALYSIS

The Commission has prepared the following Initial Regulatory Flexibility Analysis ("IRFA") regarding proposed rule 206(4)-5 and the amendments to rules 204-2 and 206(4)-3 in accordance with section 3(a) of the Regulatory Flexibility Act.[251]

A. Reasons for Proposed Action

Investment advisers that seek to influence the award of advisory contracts by government entities, by making or soliciting political contributions to those officials who are in a position to influence the awards violate their fiduciary obligations. These practices – known as "pay to play" – distort the process by which investment advisers are selected and, as discussed in greater detail above, can harm advisers' public pension plan clients, and thereby beneficiaries of those plans, which may receive inferior advisory services and pay higher fees. In addition, the most qualified adviser may not be selected, potentially leading to inferior management, diminished returns or greater losses for the public pension plan. Pay to play is a significant problem in the management of public funds by investment advisers. Moreover, we believe that advisers' participation in pay to play is inconsistent with the high standards of ethical conduct required of them under the Advisers Act. The proposed rule and rule amendments are designed to prevent fraud, deception and manipulation by reducing or eliminating adviser participation in pay to play practices.

B. Objectives and Legal Basis

Proposed rule 206(4)-5, the "pay to play" rule, would prohibit an adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act, from providing advisory services for compensation to a government client for two years after the adviser, or any of its covered associates, make a contribution to public officials (and candidates) such as state treasurers, comptrollers or other elected executives or administrators who can influence the selection of the adviser.[252] In addition, we are proposing to prohibit an adviser or any of its covered associates

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[251] 5 U.S.C. 603(a).

[252] Proposed rule 206(4)-5(a)(1).

from soliciting contributions for an elected official or candidate or payments to a political party of a state or locality where the adviser is providing or seeking to provide advisory services to a government entity,[253] and from providing or agreeing to provide, directly or indirectly, payment to any third party engaged to solicit advisory business from any government entity on behalf of the adviser.[254] Further, the prohibitions in the proposed rule also would apply to advisers to certain investment pools in which a government entity invests.[255] The proposed rule amendment to rule 204-2 is designed to provide Commission staff with records to review compliance with proposed rule 206(4)-5, and the proposed amendment to rule 206(4)-3 would clarify the application of the cash solicitation rule as a result of proposed rule 206(4)-5.

The Commission is proposing new rule 206(4)-5 and proposing to amend rule 206(4)-3 pursuant to the authority set forth in sections 206(4) and 211(a) of the Advisers Act [15 U.S.C. 80b-6(4) and 80b-11(a)]; to amend rule 204-2 pursuant to the authority set forth in sections 204 and 211 of the Advisers Act [15 U.S.C. 80b-4 and 80b-11]. Section 206(4) gives us authority to prescribe means reasonably designed to prevent fraudulent, deceptive, or manipulative acts or practices. Section 211 gives us authority to classify, by rule, persons and matters within our jurisdiction and to prescribe different requirements for different classes of persons, as necessary or appropriate to the exercise of our authority under the Act. Section 204 gives us authority to prescribe, by rule, such records and reports that an adviser must make, keep for prescribed

253 Proposed rule 206(4)-5(a)(2)(ii).

254 Proposed rule 206(4)-5(a)(2)(i).

255 Proposed rule 206(4)-5(c).

periods, or disseminate, as necessary or appropriate in the public interest or for the protection of investors.

C. Small Entities Subject to Rule

Under Commission rules, for the purposes of the Advisers Act and the Regulatory Flexibility Act, an investment adviser generally is a small entity if it: (i) has assets under management having a total value of less than $25 million; (ii) did not have total assets of $5 million or more on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of $25 million or more, or any person (other than a natural person) that had $5 million or more on the last day of its most recent fiscal year.[256]

The Commission estimates that as of July 2009 there are approximately 706 small SEC-registered investment advisers.[257] Of these 706 advisers, 57 indicate on Form ADV that they have state or local government clients. The proposed rule also would apply to those advisers that are exempt from registration with the Commission in reliance on section 203(b)(3) of the Advisers Act. We estimate that approximately 231 such unregistered advisers may manage pooled investment vehicles in which government client assets are invested and would be subject to the proposed rule.[258] We do not have data and are not aware of any databases that compile information regarding how may advisers that are exempt from registration with the Commission in reliance on section 203(b)(3) of the Advisers Act and that have state or local government

256 17 CFR 275.0-7(a).

257 This estimate is based on registration information from IARD as of July 1, 2009.

258 See supra notes 217 and 220.

clients. It is unclear how many of these advisers that are exempt from registration that would be subject to the rule are small advisers for purposes of this analysis.

D. Reporting, Recordkeeping, and other Compliance Requirements

The proposed rule would impose certain reporting, recordkeeping and compliance requirements on advisers, including small advisers. The proposed rule imposes a new compliance requirement by: (i) prohibiting an adviser from providing advisory services for compensation to government clients for two years after the adviser or any of its covered associates makes a contribution to certain elected officials or candidates; (ii) prohibiting an adviser from providing or agreeing to provide, directly or indirectly, payment to any third party engaged to solicit advisory business from any government entity on behalf of the adviser; and (iii) prohibiting an adviser or any of its covered associates from soliciting contributions for an elected official or candidate or payments to a to a political party of a state or locality where the adviser is providing or seeking to provide advisory services to a government entity .

The proposed rule amendments would impose new recordkeeping requirements by requiring an adviser to maintain certain records about its covered associates, its advisory clients, government entities invested in certain pooled investment vehicles managed by the adviser, and its political contributions as well as the political contributions of its covered associates. An investment adviser that does not provide or seek to provide advisory services to a government entity, or to a covered investment pool in which a government entity invests, would not be subject to the proposed rule and rule amendments.

As noted above, we believe that a limited number of small advisers will have to comply with the proposed rule and rule amendments. Moreover, to the extent small advisers tend to have fewer clients and fewer employees that would be covered associates for purposes of the rule, the proposal should impose lower costs on small advisers as compared to large advisers as variable costs, such as the requirement to make and keep records relating to contributions, should be lower as there should be fewer records to make and keep.[259]

E. Duplicative, Overlapping, or Conflicting Federal Rules

The Commission believes that there are no other federal rules that duplicate, overlap, or conflict with the proposed rule amendments. As discussed above, to make clear the relationship between our rules, we propose making a technical amendment to rule 206(4)-3 to specify that solicitation activities involving government entity clients under our proposed rule 206(4)-5 are subject to limitations set forth in that rule.

F. Significant Alternatives

The Regulatory Flexibility Act directs the Commission to consider significant alternatives that would accomplish the stated objective, while minimizing any significant impact on small entities.[260] In connection with the proposed rule amendments, the Commission considered the following alternatives: (i) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (ii) the clarification, consolidation, or simplification of compliance and reporting requirements under the proposed rule and rule amendments for such small entities; (iii) the use of performance rather than design

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259 However, as noted above, many larger advisers with broker-dealer affiliates may spend less resources to comply with the proposed rule and rule amendments because they may be able to rely on compliance procedures and systems that the broker-dealer already has in place to comply with MSRB rules G-37 and G-38. See supra note 214 and accompanying text.

260 As noted above, we considered two alternatives to certain aspects of proposed rule 206(4)-5: a disclosure obligation and a two-year time out for third-party solicitors. We do not believe either alternative would accomplish our stated objective of curtailing pay to play activities and thereby address potential harms from those activities. See section II.A.2., as well as notes 133 and 134 and accompanying text.

standards; and (iv) an exemption from coverage of the proposed rule and rule amendments, or any part thereof, for such small entities.

Regarding the first alternative, the Commission is not proposing different compliance or reporting requirements for small advisers as it may be inappropriate under the circumstances. The proposal is designed to reduce or eliminate adviser participation in pay to play, a practice that can distort the process by which investment advisers are selected to manage public pension plans that can harm public pension plan clients and cause advisers to violate their fiduciary obligations. To establish different requirements for small advisers could diminish the protections the proposal would provide to public pension plan clients and their beneficiaries.

Regarding the second alternative, we will continue to consider whether further clarification, consolidation, or simplification of the compliance requirements is feasible or necessary, but we believe that the current proposal is clear. The proposed rule and rule amendments contain an approach to curtailing pay to play practices that is modeled on established MSRB rules that have already been implemented by financial firms of varying sizes. However, we note that we are proposing an amendment to rule 206(4)-3, the cash solicitation rule, to clarify that the requirements of new proposed rule 206(4)-5 apply to solicitation activities involving government clients.

Regarding the third alternative, we consider using performance rather than design standards with respect to pay to play practices of investment advisers to be neither consistent with the objectives for this rulemaking nor sufficient to protect investors in accordance with our statutory mandate of investor protection. Design standards, which we have employed, provide a base line for advisory conduct as it relates to contributions and other pay to play activities, which is consistent with a rule designed to prohibit pay to play. The use of design standards also is important to ensure consistent application of the rule among investment advisers to which the rule and rule amendments will apply.

Regarding the fourth alternative, exempting small entities could compromise the overall effectiveness of the proposed rule and related rule amendments. Since we intend to extend the benefit of banning pay to play practices to clients of both small and large advisers, it would be inconsistent to specify different requirements for small advisers.

G. Solicitation of Comments

We encourage written comments on matters discussed in this IRFA. In particular, the Commission seeks comment on:

- the number of small entities, particularly small advisers, to which the proposed rule and rule amendments would apply and the effect on those entities, including whether the effects would be economically significant; and
- how to quantify the number of small advisers, including those that are unregistered, that would be subject to the proposed rule and rule amendments.

Commenters are asked to describe the nature of any effect and provide empirical data supporting the extent of the effect.

VI. EFFECTS ON COMPETITION, EFFICIENCY AND CAPITAL FORMATION

The Commission is proposing to amend rule 204-2 pursuant to its authority under sections 204 and 211. Section 204 requires the Commission, when engaging in rulemaking pursuant to that authority, to consider whether the rule is "necessary or appropriate in the public interest or for the protection of investors."[261] Section 202(c) of the Advisers Act[262] requires the Commission, when engaging in rulemaking that requires it 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.[263]

We are proposing to amend rule 204-2 to require an adviser to make and keep a list of its covered associates, the government entities the adviser provides advisory services to or seeks to provide advisory services to, and the contributions made by the firm and its covered associates, as applicable, to government officials and candidates.[264] The proposed amendment is designed to provide our examiners important information about the adviser and its covered associates' contributions to government officials and the government entities that the adviser provides advisory services to or seeks to provide those services. We believe that the proposed amendment to the Advisers Act recordkeeping rule would not materially increase the compliance burden on advisers under rule 204-2. Similarly, we do not believe that the proposed amendments to the recordkeeping rule would disproportionately affect advisers with government entity clients or potential government clients. The amendments will apply equally to all SEC-registered advisers. All registered advisers are already subject to a variety of recordkeeping requirements in the course of their business and, therefore, the proposed amendments to the recordkeeping rule

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261 15 U.S.C. 80b-4(a).

262 15 U.S.C. 80b-2(c).

263 In contrast, the Commission is proposing new rule 206(4)-5 and amendments to rule 206(4)-3 pursuant to its authority under sections 206(4) and 211, neither of which requires us to consider the factors identified in section 202(c)(1).

264 Proposed rule 204-2(a)(18)(i).

should not affect efficiency. We do not anticipate that the proposed recordkeeping rule amendments would affect capital formation.

The Commission requests comment whether the proposed amendment to rule 204-2, if adopted, would promote efficiency, competition, and capital formation. Commenters are requested to provide empirical data to support their views.

VII. CONSIDERATION OF IMPACT ON THE ECONOMY

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"[265] the Commission must advise OMB whether a proposed regulation constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results in or is likely to result in: (1) an annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers or individual industries; or (3) significant adverse effects on competition, investment or innovation.

We request comment on the potential impact of the proposed new rule and proposed rule amendments on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

VIII. STATUTORY AUTHORITY

The Commission is proposing new rule 206(4)-5 and amendments to rule 206(4)-3 of the Advisers Act pursuant to the authority set forth in sections 206(4) and 211(a) of the Investment Advisers Act of 1940 [15 U.S.C. 80b-6(4), 80b-11(a)].

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265 Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

The Commission is proposing amendments to rule 204-2 of the Advisers Act pursuant to the authority set forth in sections 204 and 211(a) of the Advisers Act [15 U.S.C. 80b-4 and 80b-11(a)].

List of Subjects in 17 CFR Part 275

Reporting and recordkeeping requirements; Securities.

For the reasons set out in the preamble, Title 17 Chapter II of the Code of Federal Regulations is proposed to be amended as follows.

PART 275 -- RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

1. The authority citation for Part 275 continues to read in part as follows:

Authority: 15 U.S.C. 80b-2(a)(11)(G), 80b-2(a)(17), 80b-3, 80b-4, 80b-4a, 80b-6(4), 80b-6a, and 80b-11, unless otherwise noted.

* * * * *

2. Section 275.204-2 is amended by adding paragraph (a)(18) and by revising paragraph (h)(1) to read as follows:

§ 275.204-2 -- Books and records to be maintained by investment advisers.

(a) * * *

(18)(i) Books and records that pertain to § 275.206(4)-5 containing a list or other record of:

(A) The names, titles and business and residence addresses of all covered associates of the investment adviser;

(B) All government entities for which the investment adviser or any of its covered associates is providing or seeking to provide investment advisory services, or which are investors or are solicited to invest in any covered investment pool to which the investment adviser provides investment advisory services, as applicable;

(C) All government entities to which the investment adviser has provided investment advisory services, along with any related covered investment pool(s) to which the investment adviser has provided investment advisory services and in which the government entity has invested, as applicable, in the past five years, but not prior to [effective date of this section]; and

(D) All direct or indirect contributions or payments made by the investment adviser or any of its covered associates to an official of a government entity, a political party of a state or political subdivision thereof, or a political action committee.

(ii) Records relating to the contributions and payments referred to in paragraph (a)(18)(i)(D) of this section must be listed in chronological order and indicate:

(A) The name and title of each contributor;

(B) The name and title (including any city/county/state or other political subdivision) of each recipient of a contribution or payment;

(C) The amount and date of each contribution or payment; and

(D) Whether any such contribution was the subject of the exception for certain returned contributions pursuant to § 275.206(4)-5(b)(2).

(iii) For purposes of this section, the terms "contribution," "covered associate," "covered investment pool," "government entity," "official," "payment," and "solicit" have the same meanings as set forth in § 275.206(4)-5.

(iv) For purposes of this section, an investment adviser to a covered investment pool in which a government entity invests or is solicited to invest shall be treated as though that investment adviser were providing or seeking to provide investment advisory services directly to the government entity.

*   *   *   *   *

(h)(1) Any book or other record made, kept, maintained and preserved in compliance with §§ 240.17a-3 and 240.17a-4 of this chapter under the Securities Exchange Act of 1934, or with rules adopted by the Municipal Securities Rulemaking Board, which is substantially the same as the book or other record required to be made, kept, maintained and preserved under this section, shall be deemed to be made, kept, maintained and preserved in compliance with this section.

*   *   *   *   *

3. Section 275.206(4)-3 is amended by adding paragraph (e) and removing the authority citation following the section to read as follows:

§ 275.206(4)-3 Cash payments for client solicitations.

*   *   *   *   *

(e) Special rule for solicitation of government entity clients. Solicitation activities involving a government entity, as defined in § 275.206(4)-5, shall be subject to the additional limitations set forth in that section.

4. Section 275.206(4)-5 is added to read as follows:

§ 275.206(4)-5 Political contributions by certain investment advisers.

(a) Prohibitions. As a means reasonably designed to prevent fraudulent, deceptive or manipulative acts, practices, or courses of business within the meaning of section 206(4) of the Act (15 U.S.C. 80b-6(4)), it shall be unlawful:

(1) For any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act (15 U.S.C. 80b-3(b)(3)) to provide investment advisory services for compensation to a government entity within two years after a contribution to an official of the government entity is made by the investment adviser or any covered associate of the investment adviser (including a person who becomes a covered associate within two years after the contribution is made); and

(2) For any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act (15 U.S.C. 80b-3(b)(3)) or any of the investment adviser's covered associates:

(i) To provide or agree to provide, directly or indirectly, payment to any person to solicit a government entity for investment advisory services on behalf of such investment adviser unless:

(A) Such person is a related person of the investment adviser or, if the related person is a company, an employee of that related person; or

(B) Such person is an executive officer, general partner, managing member (or, in each case, a person with a similar status or function), or employee of the investment adviser; and

(ii) To coordinate, or to solicit any person or political action committee to make, any:

(A) Contribution to an official of a government entity to which the investment adviser is providing or seeking to provide investment advisory services; or

(B) Payment to a political party of a state or locality where the investment adviser is providing or seeking to provide investment advisory services to a government entity.

(b) <u>Exceptions</u>.

(1) De minimis exception. Paragraph (a)(1) of this section does not apply to contributions made by a covered associate, if a natural person, to officials for whom the covered associate was entitled to vote at the time of the contributions and which in the aggregate do not exceed $250 to any one official, per election.

(2) Exception for certain returned contributions.

(i) An investment adviser that is prohibited from providing investment advisory services for compensation pursuant to paragraph (a)(1) of this section as a result of a contribution made by a covered associate of the investment adviser is excepted from such prohibition, subject to paragraphs (b)(2)(ii) and (b)(2)(iii) of this section, upon satisfaction of the following requirements:

(A) The investment adviser must have discovered the contribution which resulted in the prohibition within four months of the date of such contribution;

(B) Such contribution must not have exceeded $250; and

(C) The contributor must obtain a return of the contribution within 60 calendar days of the date of discovery of such contribution by the investment adviser.

(ii) An investment adviser is entitled to no more than two exceptions pursuant to paragraph (b)(2)(i) of this section per 12-month period.

(iii) An investment adviser may not rely on the exception provided in paragraph (b)(2)(i) of this section more than once with respect to contributions by the same covered associate of the investment adviser regardless of the time period.

(c) Prohibitions as applied to covered investment pools. For purposes of this section, an investment adviser to a covered investment pool in which a government entity invests or is solicited to invest shall be treated as though that investment adviser were providing or seeking to provide investment advisory services directly to the government entity.

(d) Further prohibition. As a means reasonably designed to prevent fraudulent, deceptive or manipulative acts, practices, or courses of business within the meaning of section 206(4) of Advisers Act (15 U.S.C. 80b-6(4)), it shall be unlawful for any investment adviser registered (or required to be registered) with the Commission, or unregistered in reliance on the exemption available under section 203(b)(3) of the Advisers Act (15 U.S.C. 80b-3(b)(3)) or any of the investment adviser's covered associates to do anything indirectly which, if done directly, would result in a violation of this section.

(e) Exemptions. The Commission, upon application, may conditionally or unconditionally exempt an investment adviser from the prohibition under paragraph (a)(1) of this section. In determining whether to grant an exemption, the Commission will consider, among other factors:

(1) Whether the exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of Advisers Act (15 U.S.C. 80b);

(2) Whether the investment adviser:

(i) Before the contribution resulting in the prohibition was made, adopted and implemented policies and procedures reasonably designed to prevent violations of this section; and

(ii) Prior to or at the time the contribution which resulted in such prohibition was made, had no actual knowledge of the contribution; and

(iii) After learning of the contribution:

(A) Has taken all available steps to cause the contributor involved in making the contribution which resulted in such prohibition to obtain a return of the contribution; and

(B) Has taken such other remedial or preventive measures as may be appropriate under the circumstances;

(3) Whether, at the time of the contribution, the contributor was a covered associate or otherwise an employee of the investment adviser, or was seeking such employment;

(4) The timing and amount of the contribution which resulted in the prohibition;

(5) The nature of the election (e.g, federal, state or local); and

(6) The contributor's apparent intent or motive in making the contribution which resulted in the prohibition, as evidenced by the facts and circumstances surrounding such contribution.

(f) Definitions. For purposes of this section:

(1) Contribution means any gift, subscription, loan, advance, or deposit of money or anything of value made for:

(i) The purpose of influencing any election for federal, state or local office;

(ii) Payment of debt incurred in connection with any such election; or

(iii) Transition or inaugural expenses of the successful candidate for state or local office.

(2) Covered associate of an investment adviser means:

(i) Any general partner, managing member or executive officer, or other individual with a similar status or function;

(ii) Any employee who solicits a government entity for the investment adviser; and

(iii) Any political action committee controlled by the investment adviser or by any person described in paragraphs (f)(2)(i) and (f)(2)(ii) of this section.

(3) Covered investment pool means any investment company, as defined in section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)), or any company that would be an investment company under section 3(a) of that Act but for the exclusion provided from that definition by either section 3(c)(1), section 3(c)(7) or section 3(c)(11) of that Act (15 U.S.C. 80a-3(c)(1), (c)(7) or (c)(11)), except that for purposes of paragraph (a)(1) of this section, an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a), the shares of which are registered under the Securities Act of 1933 (15 U.S.C. 77a), shall be a covered investment pool only if it is an investment or an investment option of a plan or program of a government entity.

(4) Executive officer of an investment adviser means the president, any vice president in charge of a principal business unit, division or function (such as sales, administration or finance), or any other executive officer of the investment adviser who, in each case, in connection with his or her regular duties:

(i) Performs, or supervises any person who performs, investment advisory services for the investment adviser;

(ii) Solicits, or supervises any person who solicits, for the investment adviser, including with respect to investors for a covered investment pool; or

(iii) Supervises, directly or indirectly, any person described in paragraph (f)(4)(i) or (f)(4)(ii) of this section.

(5) Government entity means any state or political subdivision of a state, including:

(i) Any agency, authority, or instrumentality of the state or political subdivision;

(ii) A plan, program, or pool of assets sponsored or established by the state or political subdivision or any agency, authority or instrumentality thereof; and

(iii) Officers, agents, or employees of the state or political subdivision or any agency, authority or instrumentality thereof, acting in their official capacity.

(6) Official means any person (including any election committee for the person) who was, at the time of the contribution, an incumbent, candidate or successful candidate for elective office of a government entity, if the office:

(i) Is directly or indirectly responsible for, or can influence the outcome of, the hiring of an investment adviser by a government entity; or

(ii) Has authority to appoint any person who is directly or indirectly responsible for, or can influence the outcome of, the hiring of an investment adviser by a government entity.

(7) Payment means any gift, subscription, loan, advance, or deposit of money or anything of value.

(8) Plan or program of a government entity means any investment program or plan sponsored or established by a government entity, including, but not limited to, a "qualified tuition plan" authorized by section 529 of the Internal Revenue Code (26 U.S.C. 529), a retirement plan authorized by section 403(b) or 457 of the Internal Revenue Code (26 U.S.C. 403(b) or 457), or any similar program or plan.

(9) Related person of an investment adviser means any person, directly or indirectly, controlling or controlled by the investment adviser, and any person that is under common control with the investment adviser.

(10) Solicit means:

(i) With respect to investment advisory services, to communicate, directly or indirectly, for the purpose of obtaining or retaining a client for, or referring a client to, an investment adviser; and

(ii) With respect to a contribution or payment, to communicate, directly or indirectly, for the purpose of obtaining or arranging a contribution or payment.

(g) Effective date. The prohibitions on providing investment advisory services and payments to solicit, in each case as described in this section, arise only from contributions and payments, respectively, made on or after [the effective date of this section].

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Dated: August 3, 2009

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 248

[Release Nos. 34-60423, IC-28842, IA-2911; File No. S7-29-04]

RIN 3235-AJ24

Regulation S-AM: Limitations on Affiliate Marketing

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission ("Commission") is adopting Regulation S-AM to implement Section 624 of the Fair Credit Reporting Act as amended by Section 214 of the Fair and Accurate Credit Transactions Act of 2003, which required the Commission and other federal agencies to adopt rules implementing limitations on a person's use of certain information received from an affiliate to solicit a consumer for marketing purposes, unless the consumer has been given notice and a reasonable opportunity and a reasonable and simple method to opt out of such solicitations. The final rules implement the requirements of Section 624 with respect to investment advisers and transfer agents registered with the Commission, as well as brokers, dealers and investment companies.

DATES: Effective Date: [insert 30 days after publication in the Federal Register].

Compliance Date: Compliance will be mandatory as of January 1, 2010.

FOR FURTHER INFORMATION CONTACT: For information regarding the regulation as it relates to brokers, dealers, or transfer agents, contact Brice Prince, Special Counsel, or Ignacio Sandoval, Attorney, Office of Chief Counsel, Division of Trading and Markets, (202) 551-5550, or regarding the regulation as it relates to investment companies or investment advisers, contact Penelope Saltzman, Assistant Director, Office of Regulatory Policy, Division of Investment

Management, (202) 551-6792, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

The Commission today is adopting Regulation S-AM, 17 CFR 248.101 through 248.128, under the Fair and Accurate Credit Transactions Act of 2003 ("FACT Act"),[1] the Securities Exchange Act of 1934 (the "Exchange Act"),[2] the Investment Company Act of 1940 (the "Investment Company Act"),[3] and the Investment Advisers Act (the "Advisers Act").[4]

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1 Pub. L. No. 108-159, Section 214, 117 Stat. 1952, 1980 (2003).

2 15 U.S.C. 78q, 78w, and 78mm.

3 15 U.S.C. 80a-30 and 80a-37.

4 15 U.S.C. 80b-4 and 80b-11.

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I. Background

Section 214 of the FACT Act added Section 624 to the Fair Credit Reporting Act ("FCRA").[5] This new section of the FCRA gives consumers the right to restrict a person from making marketing solicitations to them using certain information about them obtained from the person's affiliate. Section 214 also required the Office of the Comptroller of the Currency ("OCC"), the Board of Governors of the Federal Reserve System ("Board"), the Federal Deposit Insurance Corporation ("FDIC"), the Office of Thrift Supervision, the National Credit Union Administration ("NCUA") (collectively, the "Banking Agencies") and the Federal Trade Commission ("FTC") (collectively with the Banking Agencies, the "Agencies"), and the Commission, in consultation and coordination with one another, to issue rules implementing Section 624 of the FCRA.

Commission staff consulted and coordinated with staff of the Agencies in drafting rules to implement Section 624. As required by Section 214 of the FACT Act, Regulation S-AM is, to the extent possible, consistent with and comparable to the implementing regulations adopted by the Agencies.[6] Regulation S-AM contains rules of general applicability that are substantially similar to the rules that have been adopted by the Agencies. Regulation S-AM also contains

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5 See Pub. L. No. 108-159, Section 214, 117 Stat. 1952, 1980 (2003); 15 U.S.C. 1681s-3 and note. The FCRA sets standards for the collection, communication, and use of information bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living.

A portion of Section 214 of the FACT Act amended the FCRA to add a new Section 624, while other provisions of Section 214 were not incorporated into the FCRA. Throughout this release, references to "Section 214" or "Section 624 of the FCRA" are used depending on whether the reference is to Section 624 or to a portion of Section 214 not incorporated into the FCRA.

6 See Banking Agencies, Fair Credit Reporting Affiliate Marketing Regulations, 72 FR 62910 (Nov. 7, 2007) ("Joint Rules"). Citations to particular provisions of the "Joint Rules" refer to the numbering system used in the Board's final rules. See 12 CFR 222.1 to 222.28. See also FTC, Affiliate Marketing Rule, 72 FR 61424 (Oct. 30, 2007) ("FTC Rule").

examples that illustrate the application of the general rules. These examples differ from those used by the Agencies in order to provide more meaningful guidance to financial institutions subject to the Commission's jurisdiction.

II. Overview of Comments Received and Explanation of Regulation S-AM

A. Overview of Comments Received

On July 8, 2004, the Commission proposed Regulation S-AM (the "proposal" or "proposed rules").[7] The Commission received 15 comments on the proposed rules from financial institutions and their representatives.[8] While a number of commenters generally supported the

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7 Limitations on Affiliate Marketing (Regulation S-AM), Exchange Act Release No. 49985 (July 8, 2004), 69 FR 42302 (July 14, 2004) ("Proposing Release").

8 The Securities Industries Association, n/k/a the Securities Industry and Financial Markets Association ("SIFMA") submitted two comment letters. We consider these letters to be one comment. See Letters from Alan E. Sorcher, Vice President and Associate General Counsel, SIFMA to Jonathan G. Katz, Secretary, Commission (Aug. 13, 2004) ("SIFMA Letter I") and from Alan E. Sorcher, Vice President and Associate General Counsel, SIFMA to Jonathan G. Katz, Secretary, Commission (Aug. 18, 2004) ("SIFMA Letter II") (together "SIFMA Letters"). Unless otherwise noted, all letters referred to below were addressed to the Secretary of the Commission.

See Letter from Michael E. Bleier, General Counsel, Mellon Financial Corporation (July 26, 2004) ("Mellon Letter"); Letter from Ira Friedman, Senior Vice President, Chief Privacy Officer and Special Counsel, Metropolitan Life Insurance Company (Aug. 3, 2004) ("MetLife Letter"); Letter from Larkin Fields, Senior Vice President and Chief Privacy Officer, United Services Automobile Association (Aug. 11, 2004) ("USAA Letter"); Letter from Jeffrey A. Tassey, Executive Director, Coalition to Implement the FACT Act (Aug. 12, 2004) ("Coalition Letter"); Letter from Monique S. Botkin, Counsel, Investment Counsel Association of America, Inc., n/k/a Investment Adviser Association (Aug. 12, 2004) ("IAA Letter"); Letter from Robert G. Rowe, III, Regulatory Counsel, Independent Community Bankers of America (Aug. 12, 2004) ("ICBA Letter"); Letter from Peter L. McCorkell, Senior Counsel, Wells Fargo & Company (Aug. 12, 2004) ("Wells Fargo Letter"); Letter from Roberta B. Meyer, Senior Counsel, Risk Classification, American Counsel of Life Insurers ("ACLI") (Aug. 13, 2004) ("ACLI Letter"); Letter from Tamara K. Salmon, Senior Associate Counsel, Investment Company Institute ("ICI") (Aug. 13, 2006) ("ICI Letter"); Letter from Henry H. Hopkins, Chief Legal Counsel, and Karen Nash-Goetz, Associate Legal Counsel, T. Rowe Price Associates, Inc. (Aug. 13, 2004) ("T. Rowe Price Letter"); Letter from J. Stephen Zielezienski, Vice President & Associate General Counsel, American Insurance Association ("AIA") (Aug. 15, 2004) ("AIA Letter"); Letter from Beth L. Climo, Executive Director, American Bankers Association Securities Association ("ABASA") (Aug. 16, 2004) ("ABASA Letter"); Letter from Robert C. Drozdowski, Vice President,

(continued)

Commission's proposals,[9] others expressed concerns regarding particular provisions of the proposed rules. The most significant areas of concern raised by the commenters related to: (1) proposed restrictions on "constructive sharing"; (2) which affiliate would be responsible for providing the notice; (3) the proposed definitions for terms such as "affiliate," "eligibility information," "clear and conspicuous," "pre-existing business relationship," and "marketing solicitation"; and (4) the scope of certain proposed exceptions to the proposed rules' notice and opt out requirements.[10] A more detailed discussion of the comments is contained in the Section-by-Section analysis below.

B. Explanation of Regulation S-AM

Regulation S-AM will allow a consumer, in certain limited situations, to block affiliates of a person subject to Regulation S-AM that the consumer does business with from soliciting the consumer based on certain "eligibility information" (i.e., certain financial information, such as information regarding the consumer's transactions or experiences with the person) received from the person. Unlike Regulation S-P, the Commission's privacy rule,[11] Regulation S-AM does not

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Payments and Technology Policy, America's Community Bankers ("ACB") (Aug. 16, 2004) ("ACB Letter"); Letter from Richard M. Whiting, Executive Director and General Counsel, The Financial Services Roundtable ("FSR") (Aug. 16, 2004) ("FSR Letter"). Each of these letters is available at http://www.sec.gov/rules/proposed/s72904.shtml.

9 See, e.g., IAA Letter; ICI Letter; Mellon Letter; MetLife Letter.

10 See infra Part III.D.

11 Currently, Regulation S-P is codified at 17 CFR Part 248. With the adoption of Regulation S-AM, we are redesignating Regulation S-P as Subpart A of Part 248, and adopting Regulation S-AM as Subpart B of Part 248. We are also adopting technical and conforming amendments to Regulation S-P to reflect this change as detailed infra Part X. In particular, we are changing the current subpart designations within Regulation S-P to undesignated center headings, revising all references in Regulation S-P to "this part" to read "this subpart," and for consistency with the term used in Regulation S-AM, revising all references to "G-L-B Act" to read "GLBA." We are consolidating Regulation S-P and Regulation S-AM in Part 248 because both regulations address information sharing and safekeeping.

prohibit the sharing of information with another entity. Instead, Regulation S-AM prohibits a company from using eligibility information received from an affiliate to make marketing solicitations to consumers, unless: (1) the potential marketing use of the information has been clearly, conspicuously, and concisely disclosed to the consumer; (2) the consumer has been provided a reasonable opportunity and a simple method to opt out of receiving the marketing solicitation; and (3) the consumer has not opted out. Regulation S-AM also provides that a notice and opt out required under Regulation S-AM can be combined with other disclosures required by law, such as the initial and annual privacy notices required by Regulation S-P. Regulation S-AM also contains a number of exceptions to its notice and opt out requirements, such as when an affiliate making a marketing solicitation has a pre-existing business relationship with the consumer, or provides marketing material in response to an affirmative request by the consumer or in response to a communication initiated by the consumer. In addition, the Appendix to Regulation S-AM provides model forms that, when used properly, satisfy Regulation S-AM's requirement that an affiliate marketing notice be clear, conspicuous, and concise. Regulation S-AM also includes examples illustrating the applicability of the final rules to certain situations. The facts and circumstances of each individual situation, however, will determine whether compliance with an example, to the extent applicable, constitutes compliances with the final rules.

As adopted, Regulation S-AM differs from the proposed rules in several significant ways. First, an affiliate communicating eligibility information is not responsible for providing an affiliate marketing notice. Instead, the notice may be provided by any affiliate identified in the notice that has, or has previously had, a pre-existing business relationship with the consumer to whom the notice is provided. Second, the final rules do not apply to "constructive sharing" scenarios, as considered in the Proposing Release. Third, the Commission requested and received comment on the use of oral notices, and after careful consideration of the comments, the final rules provide that notices cannot be delivered orally, but instead, must be delivered electronically or in writing. While consumers can elect to opt out orally after receipt of the notice, they may not orally revoke their opt out. Fourth, unlike the proposal which referred to "making or sending" marketing solicitations, the final rules eliminate the reference to "send" because we concluded, based on comments, that "sending" and "making" marketing solicitations are different activities. Fifth, the final rules clarify that an opt out notice may apply to eligibility information obtained in connection with one or more continuing relationships the consumer establishes with an entity or its affiliates, as long as the notice adequately describes the relationships covered by the notice. Sixth, the final rules include a new section describing the conditions under which a service provider for both an entity that has a pre-existing business relationship with a consumer and the entity's affiliate would be acting for the entity rather than its affiliate whose products or services are being marketed. Finally, the definition of "affiliate," "control," "marketing solicitation," and "pre-existing business relationship" have been revised to reflect comments we received.[12]

III. Section-by-Section Analysis

While the Proposing Release placed Regulation S-AM in 17 CFR 247.1-247.28, the final rules are located in 17 CFR 248.101 through 248.128.[13]

[12] These and other changes are discussed in greater detail infra Part III.

[13] See supra note 11. This numbering system differs slightly from the one used by the Agencies, but is still consistent with the Joint Rules – Regulation S-AM uses section numbers that are higher by 100 than those used in the Joint Rules. For example, references to § 22 of the Joint Rules would correspond to § 122 of Regulation S-AM. In addition, the Commission believes that placing Regulation S-AM in the same part of the CFR as the Commission's privacy rules (continued)

A. Section 248.101 Purpose and Scope

We received no comments on proposed § 247.1, which identifies the purposes and scope of the rules, and we are adopting it as proposed, redesignated as § 248.101. Paragraph (a) of § 248.101 of Regulation S-AM provides that the purpose of Regulation S-AM is to implement the affiliate marketing provisions of Section 624 of the FCRA. Paragraph (b) of § 248.101 lists the entities to which the final rules apply. Although the FACT Act does not specifically identify the entities that are to be subject to the rules prescribed by the Commission,[14] Congress's inclusion of the Commission as one of the agencies required to adopt implementing regulations suggests that Congress intended that our rules apply to those entities that the Commission regulates, i.e., brokers, dealers, and investment companies, as well as to investment advisers and transfer agents that are registered with the Commission (respectively, "registered investment advisers" and "registered transfer agents," and, collectively, with brokers, dealers, and investment companies, "Covered Persons").[15] These entities are referred to as "you" throughout

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(i.e., Regulation S-P) will provide persons subject to the rules with an easier point of reference, especially since we expect that these persons would consolidate the notice and opt out requirements of the affiliate marketing rules together with those of the privacy rules.

14 Section 214(b) of the FACT Act directed that regulations implementing Section 624 of the FCRA be prescribed by the "Federal banking agencies, the National Credit Union Administration, and the [Federal Trade] Commission, with respect to the entities that are subject to their respective enforcement authority under Section 621 of the Fair Credit Reporting Act [15 U.S.C. 1681s] and the Securities and Exchange Commission . . . ." See 15 U.S.C. 1681s-3 note. Section 621(a)(1) of the FCRA grants enforcement authority to the FTC for all persons subject to the FCRA "except to the extent that enforcement . . . is specifically committed to some other government agency under subsection (b)" of Section 621. 15 U.S.C. 1681s(a)(1). The Commission is not one of the agencies included under subsection (b). The Commission was added to the list of federal agencies required by Section 214(b) to adopt regulations implementing Section 624 of the FCRA in conference committee. There is no legislative history on this issue.

15 The term "Covered Persons" is used for the purposes of this release and is not a defined term in Regulation S-AM. The application of Regulation S-AM to investment companies, brokers, dealers (other than notice-registered broker-dealers), and registered transfer agents and

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Regulation S-AM. We have excluded from the scope of the regulation broker-dealers registered by notice with the Commission under Section 15(b)(11) of the Exchange Act for the purpose of conducting business in security futures products ("notice-registered broker-dealers").[16]

B. Section 248.102 Examples

We are adopting as proposed § 247.2, which clarifies the effect of the examples used in the rules and model forms, redesignated as § 248.102. Given the wide range of possible situations covered by Section 624 of the FCRA, Regulation S-AM includes general rules, provides more specific examples, and includes model opt out notice forms. The examples, which are not exclusive, provide guidance concerning the rules' application in ordinary circumstances. The facts and circumstances of each individual situation, however, will determine whether compliance with an example, to the extent applicable, constitutes compliance with this subpart.[17]

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investment advisers is consistent with Regulation S-P. Not all transfer agents, investment companies or investment advisers are required to register with the Commission. Section 17A(c) of the Exchange Act requires that transfer agents register with the appropriate regulatory agency, which can be the Commission, the Board, the OCC or the FDIC. 15 U.S.C. 78c(a)(34) (defining "appropriate regulatory agency"); 15 U.S.C.78q-1(c) (describing the registration requirements for transfer agents). Section 6(f) of the Investment Company Act (15 U.S.C. 80a-6(f)) provides an exemption from registration for a closed-end investment company that elects to be regulated as a business development company pursuant to Section 54 of the Act (15 U.S.C. 80a-53). Sections 203 and 203A of the Advisers Act govern the registration of investment advisers with the Commission. See 15 U.S.C. 80b-3 and 80b-3a.

16 See discussion of definitions of "broker" and "dealer" infra Parts III.C.2 and III.C.9. Notice-registered broker-dealers are subject to primary oversight by the Commodity Futures Trading Commission ("CFTC") and are exempted from all but the core provisions of the laws administered by the Commission. We interpret Congress's exclusion of the CFTC from the list of financial regulators required by Section 214(b) of the FACT Act to prescribe regulations implementing Section 624 of the FCRA to mean that Congress did not intend for the Commission's rules under the FACT Act to apply to entities subject to primary oversight by the CFTC.

17 The Joint Rules and the FTC Rule provide that, to the extent applicable, compliance with an example constitutes compliance with the Joint Rules and the FTC Rule, respectively. See, e.g., 12 CFR 222.2. The examples in our final rules, however, do not provide the same safe harbor. The examples in Regulation S-AM are intended to describe the broad outlines of situations illustrating compliance with the applicable rule. However, the specific facts and circumstances

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Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise under this subpart. Similarly, the examples do not illustrate any issues that may arise under other laws or regulations. We received no comment on this section.

C. Section 248.120 Definitions

As noted, for consistency and ease of reference, Regulation S-AM generally follows the section numbering used in the Joint Rules and the FTC Rule. Therefore, the defined terms proposed under § 247.3 are now located in § 248.120. In addition, the examples corresponding to the definition of "pre-existing business relationship," in proposed § 247.20(d)(1), are now included in the definition of "pre-existing business relationship," which is redesignated as § 248.120(q)(2) in the final rules.[18]

1. Affiliate

We are revising the proposed definition of "affiliate" in response to issues raised by commenters. The proposal defined "affiliate" of a Covered Person as any person that is related by common ownership or common corporate control with the Covered Person. The proposed rule also provided that a Covered Person is considered an affiliate of another person for purposes of Regulation S-AM if: (1) the other person is regulated under Section 214 of the FACT Act by one of the Agencies; and (2) the rules adopted by that Agency treat the Covered Person as an affiliate of the other person.[19] The proposed definition followed the definition of "affiliates" in

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relating to a particular situation will determine whether compliance with an example constitutes compliance with the rules.

18 See supra note 13.

19 Proposed § 247.3(a)(1)–(2). This provision was designed to prevent the disparate treatment of affiliates within a holding company structure that are regulated by different federal regulators and to make this provision of Regulation S-AM consistent with comparable provisions of the Agencies.

Section 2 of the FACT Act, which encompasses "persons that are related by common ownership or affiliated by corporate control."[20]

Commenters noted with approval the proposed definition's general consistency with the definition of "affiliate" in the GLBA and Regulation S-P, but some suggested the definitions should be made more consistent.[21] Two commenters suggested that we eliminate the term "corporate" in the Regulation S-AM definition.[22] In addition, two commenters suggested that the Commission adopt the approach to the definition of affiliate taken under California's Financial Information Privacy Act ("California Privacy Law").[23]

After considering the comments, we are revising the definition of "affiliate" to eliminate the term "corporate" from the definition.[24] The final definition harmonizes the various FCRA and FACT Act formulations, and the GLBA definition, by defining "affiliate" to mean "any person that is related by common ownership or common control with" another person. While Section 2 of the FACT Act contains the term "corporate," we did not include it in the final rule in

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20 Several FCRA provisions apply to information sharing with persons "related by common ownership or affiliated by corporate control," "related by common ownership or affiliated by common corporate control," or "affiliated by common ownership or common corporate control." See, e.g., FCRA Sections 603(d)(2), 615(b)(2), and 625(b)(2). Each of these provisions was enacted as part of the 1996 amendments to the FCRA. Similarly, Section 2(4) of the FACT Act defines the term "affiliate" to mean "persons that are related by common ownership or affiliated by corporate control." In contrast, the Gramm-Leach-Bliley Act ("GLBA") defines "affiliate" to mean "any company that controls, is controlled by, or is under common control with another company." See 15 U.S.C. 6809(6).

21 See ACB Letter; FSR Letter; IAA Letter; ICBA Letter; ICI Letter; T. Rowe Price Letter; Wells Fargo Letter.

22 See ICI Letter; T. Rowe Price Letter.

23 See FSR Letter; Mellon Letter. These commenters noted that the California law places no restriction on information sharing among affiliates if they: (1) are regulated by the same or similar functional regulators; (2) are involved in the same broad line of business, such as banking, insurance, or securities; and (3) share a common brand identity. See Cal. Financial Code Section 4053(c).

recognition of other types of control relationships that may give rise to affiliation under the rule.[25] In contrast to the other regulators, we did not replace the term "person" with "company" in the definition because certain of our Covered Persons are natural persons. For example, some brokers-dealers and some investment advisers registered with the Commission are sole proprietors. In contrast, banking charters are held by entities other than natural persons. This change to the definition of "affiliate" is intended to promote consistency in the Commission's rules and to prevent gaps in the coverage of Regulation S-AM. We do not believe that there is a substantive difference between the definitions of "affiliate" in the FACT Act and in Section 509 of the GLBA.[26] We are not, however, incorporating elements of the California Privacy Law into the definition. To do so would be beyond our congressional mandate, especially given that Congress itself could have incorporated those elements when amending the FCRA.

2. Broker

We received no comments on the proposed definition of "broker" and are adopting it as proposed.[27] The definition incorporates the definition of "broker" in the Exchange Act and excludes notice-registered brokers.[28]

3. Clear and Conspicuous

We are adopting the definition of "clear and conspicuous" as proposed to mean reasonably understandable and designed to call attention to the nature and significance of the

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24 Section 248.120(a).

25 As discussed below, "control" is defined in Regulation S-AM to include control relationships that go beyond those based on corporate control. See infra Part III.C.8.

26 This approach is also consistent with the Agencies' final rules. See Joint Rules at 72 FR 62912; FTC Rule at 72 FR 61426.

27 See § 248.120(b), which was proposed as § 247.3(b).

information presented.[29] Persons may wish to consider a number of methods to make their notices clear and conspicuous, including those described below. Institutions are not required to implement any particular method or combination of methods to make their disclosures clear and conspicuous. Rather, the particular facts and circumstances will determine whether a disclosure is clear and conspicuous. Consistent with the Proposing Release, a notice or disclosure may be made reasonably understandable through various methods that include:

- using clear and concise sentences, paragraphs, and sections;
- using short explanatory sentences;
- using bullet lists;
- using definite, concrete, everyday words;
- using active voice;
- avoiding multiple negatives;
- avoiding legal and highly technical business terminology; and
- avoiding explanations that are imprecise and readily subject to different interpretations.[30]

A notice or disclosure could also use various design methods to call attention to the nature and significance of the information in it, including but not limited to:

- using a plain-language heading;
- using a typeface and type size that are easy to read;
- using wide margins and ample line spacing; and

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28 See supra note 16.

29 See § 248.120(c), proposed as § 247.3(c).

30 See Proposing Release at 69 FR 42305.

- using boldface or italics for key words.[31]

Persons who choose to provide the notice or disclosure by using an Internet Web site may use text or visual cues to encourage the reader to scroll down the page, if necessary, to view the entire document. Persons may also take steps to ensure that other elements on the Web site (such as text, graphics, hyperlinks, or sound) do not distract attention from the notice or disclosure.

If a notice or disclosure required under Regulation S-AM is combined with other information, methods for designing the notice or disclosure to call attention to the nature and significance of the information in it may include distinctive type sizes, styles, fonts, paragraphs, headings, graphic devices, and appropriate groupings of information. However, there is no need to use distinctive features, such as distinctive type sizes, styles, or fonts, to differentiate an affiliate marketing opt out notice from other components of a required disclosure. For example, the notice could be included in a GLBA privacy notice that combines several opt out disclosures in a single notice. Moreover, nothing in the clear and conspicuous standard requires segregation of the affiliate marketing opt out notice when it is combined with a GLBA privacy notice or other required disclosures.

We recognize that it will not be feasible or appropriate to incorporate all of the methods described above with respect to every affiliate marketing notice. We recommend, but do not require, that institutions consider the methods described above in designing their notices. We also encourage the use of consumer or other readability testing to devise notices that are understandable to consumers.

Five commenters addressed the proposed definition of "clear and conspicuous."[32] One

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31 Id.

commenter expressed approval of the proposed definition because of its similarity to the definition of the term found in Regulation S-P.[33] However, other commenters suggested that the definition could give rise to an increased risk of litigation and civil liability for financial institutions.[34] While these commenters recognized that the proposed definition was derived from the GLBA privacy regulations, they noted that compliance with the GLBA privacy regulations is enforced exclusively through administrative actions and not through private litigation. One commenter suggested the definition was unnecessary to ensure that consumers receive a clear and conspicuous notice as required by Section 624 of the FCRA, noting that other affiliate sharing notice and opt out requirements have operated in the FCRA for several years without a regulatory definition.[35] Commenters also pointed to the Board's withdrawal of a similar definition in other regulations as support for not including the definition.[36] In the alternative, one commenter suggested that the Commission and the Agencies issue questions and answers or non-exclusive examples indicating that compliance with one of these examples would satisfy the rule's

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32 See ACB Letter; Coalition Letter; IAA Letter; ICBA Letter; Wells Fargo Letter.

33 See IAA Letter. See also 17 CFR 248.3(c)(1) (defining "clear and conspicuous" for purposes of Regulation S-P).

34 See ACB Letter; ICBA Letter; Wells Fargo Letter.

35 See Coalition Letter. The FCRA contains "affiliate sharing" notice and opt out provisions that are distinct from the "affiliate marketing" provisions of Regulation S-AM. Section 603(d)(2)(A)(iii) of the FCRA provides that a person may communicate information that is not transaction or experience information among its affiliates without that information becoming a consumer report if the sharing is clearly and conspicuously disclosed to the consumer and the consumer is given an opportunity to opt out of the sharing. In contrast, Regulation S-AM limits the use of information by affiliates for marketing purposes, not the sharing of information among affiliates.

36 See Coalition Letter; Wells Fargo Letter. These commenters cited the Board's decision to withdraw a similar proposal to define "clear and conspicuous" for purposes of Regulations B, E, M, Z, and DD, in part because of concerns over civil liability.

requirements.[37] Another commenter suggested outlining reasonable expectations for what would be considered "clear and conspicuous" and suggested including reasonable protections against liability and administrative penalties when unintentional errors occur.[38]

Because the FACT Act requires that we provide specific guidance on how to comply with the clear and conspicuous standard,[39] we believe that it is important to both define "clear and conspicuous" in the final rules and provide specific guidance for how to satisfy that standard.[40] The Commission notes that an affiliate sharing opt out notice required under the FCRA, which may be enforced through private rights of action, must be included in a GLBA privacy notice.[41] Therefore, the affiliate sharing opt out notices generally are provided in a manner consistent with the clear and conspicuous standard set forth in the GLBA privacy regulations.[42] We believe that Covered Persons' experience in providing clear and conspicuous affiliate sharing notices should help them provide clear and conspicuous affiliate marketing notices under Regulation S-AM.

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37 See ICBA Letter. One commenter urged us to make clear that a person does not have to use specific terms for opt out and that this should be included as part of the account opening process. See SIFMA Letter I.

38 See ACB Letter; see also 12 U.S.C. 4301, et seq.

39 See 15 U.S.C. 1681s-3(a)(2)(B) ("Notwithstanding subparagraph (A), the notice required under paragraph (1) shall be clear, conspicuous, and concise . . . . The regulations prescribed to implement this section shall provide specific guidance regarding how to comply with such standards.").

40 The Commission is providing two types of specific guidance on satisfying the requirement to provide a clear and conspicuous affiliate marketing opt out notice. First, this release and § 248.121(a) describe certain techniques that may be used to make notices clear and conspicuous. Second, the Commission is adopting as part of Regulation S-AM the model forms set forth in the Appendix to Subpart B – Model Forms ("Appendix") that may, but are not required to, be used to facilitate compliance with the affiliate marketing notice requirements.

41 See 15 U.S.C. 6803(b)(4).

42 See, e.g., the definition and examples in Regulation S-P at 17 CFR 248.3(c).

Accordingly, we are adopting the definition of "clear and conspicuous" as proposed.[43] We urge Covered Persons to consider the guidance discussed above regarding practices and methods for making notices clear and conspicuous. Moreover, like the Agencies, we are adopting model forms that may, but are not required to, be used to facilitate compliance with the affiliate marketing notice requirements.[44] The requirement that a notice be clear and conspicuous would be satisfied by the appropriate use of one of the model forms. Accordingly, use of the model forms, although optional, should help alleviate risks from litigation related to the requirement that notices be clear and conspicuous, about which some commenters expressed concern.[45]

4. Commission

We received no comment on the definition of "Commission" to mean the Securities and Exchange Commission and are adopting it as proposed.[46]

5. Company

We received no comment on the definition of "company" and are adopting the term as proposed.[47]

6. Concise

We received no comment on the definition of "concise" and are adopting it as proposed.[48]

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43 See § 248.120(c), which was proposed as § 247.3(c).

44 See Appendix to Regulation S-AM.

45 See ACB Letter; ICBA Letter; Wells Fargo Letter.

46 See § 248.120(d), which was proposed as § 247.3(d).

47 See § 248.120(e), which was proposed as § 247.3(e).

48 See § 248.120(f), which was proposed as § 247.21(b)(3). The Appendix provides that the requirement for a concise notice would be satisfied by the appropriate use of one of the model (continued)

Section 248.120(f)(1) defines the term "concise" to mean a reasonably brief expression or statement. Paragraph (f)(2) provides that a notice required by Regulation S-AM may be concise even if it is combined with other disclosures required or authorized by federal or state law.[49]

7. Consumer

Proposed paragraph (f) of § 247.3 defined "consumer" to mean an individual, including an individual acting through a legal representative.[50] Some commenters suggested that the definition of "consumer" used in Regulation S-AM should track the definition in Regulation S-P.[51] Some also asked that the Commission include in the definition the examples that accompany the definition of "consumer" in Regulation S-P.[52]

The Commission is aware of the narrower definition of "consumer" in the privacy regulations enacted under Title V of the GLBA.[53] However, we believe that the use of distinct definitions of "consumer" reflects differences in the scope and objectives of the two statutes. Accordingly, we are adopting the definition of "consumer" as proposed.[54] For purposes of this definition, an individual acting through a legal representative would qualify as a consumer.

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forms contained in the Appendix, although use of the model forms is not required. See supra note 40.

49 Such disclosures include, but are not limited to, a GLBA privacy notice, an affiliate-sharing notice under Section 603(d)(2)(A)(iii) of the FCRA, and other consumer disclosures.

50 The proposed definition follows the statutory definition of Section 603(c) of the FCRA. See 15 U.S.C. 1681a(c).

51 See ACB Letter; IAA Letter; T. Rowe Price Letter.

52 See IAA Letter; T. Rowe Price Letter.

53 See Proposing Release at 69 FR 42305.

54 See § 248.120(g).

8. Control

We are adopting the definition of "control" as proposed.[55] Two commenters supported the proposed definition, indicating it was consistent with the one found in Regulation S-P and the GLBA.[56] For purposes of Covered Persons, "control" means the power to exercise a controlling influence over the management or policies of a company, whether through ownership of securities, by contract, or otherwise.[57] Ownership of more than 25 percent of a company's voting securities would create a presumption of control of the company.[58] As the Proposing Release explained, this definition would be used to determine when companies are affiliated[59] and would result in financial institutions being considered affiliates regardless of whether the control is exercised by a company or an individual.[60]

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55 See § 248.120(h), which was proposed as § 247.3(g).

56 See IAA Letter; T. Rowe Price Letter.

57 Section 248.120(h). This definition is consistent with definitions of control found elsewhere under the securities laws. See, e.g., 17 CFR 240.19g2-1(b)(2); 17 CFR 248.3(i); 15 U.S.C. 80a-2(a)(9); 15 U.S.C. 80b-2(a)(12).

58 This presumption may be rebutted by evidence, but in the case of an investment company, will continue until the Commission makes a decision to the contrary according to the procedures described in Section 2(a)(9) of the Investment Company Act. 15 U.S.C. 80a-2(a)(9).

59 See supra Part III.C.1; Proposing Release at 69 FR 42305.

60 In § 222.3(i) of their Joint Proposal, the Banking Agencies and the NCUA defined "control" as ownership of 25 percent of a company's voting securities, control over the election of a majority of the directors, trustees or general partners of the company, or the power to exercise a controlling influence over management or policies of a company, as determined by the particular agency. See Banking Agencies and NCUA, Fair Credit Reporting Affiliate Marketing Regulation; Proposed Rules, 69 FR 42502 (July 15, 2004) ("Joint Proposal"). However, as we emphasized in the Proposing Release, the definition of "control" in the proposed rules differed from the Agencies' definition in the Joint Proposal. See Proposing Release at 69 FR 42305. The Joint Rules incorporate the definition of "control" to mean "common ownership or common corporate control" as in the Agencies' final FCRA medical information rules. See Joint Rules at 72 FR 62913 (citing 70 FR 70664 (Nov. 22, 2005)).

9. Dealer

We received no comments on the definition of "dealer" and are adopting it as proposed.[61] Section 248.120(i) defines "dealer" to have the same meaning as in Section 3(a)(5) of the Exchange Act,[62] regardless of whether the dealer is registered under Section 15(b) of the Exchange Act.[63] The term includes a municipal securities dealer as defined in Section 3(a)(30) of the Exchange Act,[64] other than a bank (as defined in Section 3(a)(6) of the Exchange Act),[65] regardless of whether it is registered under Section 15(b) or 15B(a)(2) of the Exchange Act.[66] In addition, the term includes a government securities dealer as defined in Section 3(a)(44) of the Exchange Act,[67] regardless of whether it is registered under Section 15(b) or 15C(a)(2) of the Exchange Act.[68] The definition specifically excludes notice-registered broker-dealers.[69]

10. Eligibility Information

We are adopting the proposed definition of "eligibility information" to mean any information, the communication of which would be a consumer report, if the statutory exclusions from the definition of "consumer report" in Section 603(d)(2)(A) of the FCRA, for transaction or experience information and for "other" information that is subject to the affiliate-sharing opt out,

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61 See § 248.120(i), proposed as § 247.3(h).

62 15 U.S.C. 78c(a)(5).

63 15 U.S.C. 78o(b).

64 15 U.S.C. 78c(a)(30).

65 15 U.S.C. 78c(a)(6).

66 15 U.S.C. 78o(b), 78o-4(a)(2).

67 15 U.S.C. 78c(a)(44).

68 15 U.S.C. 78o(b), 78o-5(a)(2).

69 See discussion of the inapplicability of Regulation S-AM to notice-registered broker-dealers supra note 16 and accompanying text.

did not apply.[70] As under the proposal, eligibility information would include a Covered Person's own transaction or experience information, such as information about a consumer's account history with that Covered Person, and "other" information under Section 603(d)(2)(A)(iii), such as information from consumer reports or applications.[71]

We have revised the definition of "eligibility information" to clarify that the term does not apply to aggregate or blind data that does not contain personal identifiers.[72] Examples of personal identifiers listed in the definition include account numbers, names or addresses, and also could include Social Security numbers, driver's license numbers, telephone numbers, or other types of information that, depending on the circumstances or when used in combination, could identify the individual or individuals to whom the data relates. Other types of personal identifiers could include passwords, screen names, user names, e-mail addresses, or Internet Protocol addresses.

We recognized in the Proposing Release that it might be burdensome for Covered Persons to determine and track whether consumer report information is (1) "eligibility information" and thus subject to the notice and opt out provisions of Section 624 or (2) information that might be shared with affiliates under other exceptions to the FCRA (to which the notice and opt out provisions of Section 624 do not apply). We invited comment on whether

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70 See § 248.120(j). See also 15 U.S.C. 1681a(d)(2)(A)(iii). Under the FCRA, the term "consumer report" is defined to include any communication of information from a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living that is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for credit or insurance to be used primarily for personal, family or household purposes, employment purposes, or other purposes authorized elsewhere in the FCRA. 15 U.S.C. 1681a(d)(1).

71 See § 248.120(j).

the proposed definition of "eligibility information" appropriately reflected the scope of coverage of the FACT Act and provided meaningful guidance to Covered Persons.

Some commenters indicated that the proposed definition did not provide enough meaningful guidance as to what sort of information is covered.[73] Others suggested that the Commission should provide examples to illustrate the common types of information that would and would not constitute eligibility information.[74] One commenter requested examples specifically relevant to the securities industry.[75] Another commenter offered an alternative definition, stating that the proposed definition was unnecessarily complex and difficult to apply.[76] Another commenter noted that, unlike the Agencies, the Commission did not provide in the Proposing Release that the term was designed to "facilitate discussion, and not change the scope of the information covered by Section 624(a)(1)" of the FCRA.[77] The commenter expressed concern that the divergence may signal some other interpretation, but did not provide an example of a secondary interpretation.

The Commission believes that further clarification of, or exclusions from, the term "eligibility information" would implicate the definitions of "consumer report" and "consumer reporting agency" in Sections 603(d) and (f), respectively, of the FCRA. The Commission does

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72 Id.

73 See FSR Letter; SIFMA Letter I.

74 See ICI Letter; T. Rowe Price Letter.

75 See ICI Letter.

76 See ICBA Letter. The commenter proposed to define eligibility information as "any information that bears on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for credit or insurance to market products and services for personal, family or household purposes to that person."

not define the terms "consumer report" and "consumer reporting agency" in this rulemaking or construe terms therein, such as "transaction or experience" information. We note that financial institutions have relied on these statutory definitions for many years. Providing examples of information that would or would not be eligibility information would not necessarily reduce the complexity of the definition, and could create greater uncertainty with regard to information that is not covered by an example. The definition of "eligibility information" in Regulation S-AM is the same as the one found in the Joint Rules adopted by the Banking Agencies.[78]

11. FCRA

We received no comment on the term "FCRA" and are adopting it as proposed to mean the Fair Credit Reporting Act.[79]

12. GLBA

The proposed rule defined "GLB Act" to mean the Gramm-Leach-Bliley Act. We received no comment on this definition but are changing the term to "GLBA" to be more consistent with the way the Agencies refer to the Gramm-Leach-Bliley Act.[80]

13. Investment Adviser

We received no comment on the definition of "investment adviser" and are adopting it as proposed.[81] This definition incorporates the definition of "investment adviser" in the Investment Advisers Act.

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77 See Coalition Letter.

78 In adopting their final rules, the Banking Agencies stated that they anticipate addressing the definitions of "consumer report" and "consumer reporting agency" in a separate rulemaking after the required FACT Act rules have been completed. See Joint Rules at 72 FR 62915.

79 See § 248.120(k), which was proposed as § 247.3(j).

80 See § 248.120(l), proposed as § 247.3(k).

14. Investment Company

We received no comment on the definition of "investment company" and are adopting it as proposed.[82] This definition incorporates the definition of "investment company" in the Investment Company Act.

15. Marketing Solicitation

We are adopting the definition of "marketing solicitation," with modifications discussed below.[83] The proposed rule defined "marketing solicitation" to mean marketing initiated by a Covered Person to a particular consumer that is based on eligibility information communicated to that Covered Person by its affiliate, and that is intended to encourage the consumer to purchase or obtain a product or service. The definition included any form of communication, such as a telemarketing call, direct mail, or electronic mail that is directed to a specific consumer based on that consumer's eligibility information. It did not include communications that are directed at the general public without regard to eligibility information, even if those communications are intended to encourage consumers to purchase products and services. We noted in the Proposing Release that the definition tracked the definition in Section 624 of the FCRA but did not follow the statute exactly to prevent confusion with the term "solicitation" in the context of the federal securities laws.[84] Although Section 624 also authorizes the Commission to exclude other communications from the definition of "marketing solicitation," we did not propose to do so, but

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81 See § 248.120(m), proposed as § 247.3(l).

82 See § 248.120(n), proposed as § 247.3(m).

83 See § 248.120(o), proposed as § 247.3(n).

84 See Proposing Release at 69 FR 42306. In particular, Regulation S-AM uses the term "marketing solicitation" rather than "solicitation." Although "solicitation" is a defined term in Section 624 of the FACT Act, the operative phrase in Section 624(a) is "solicitation for marketing purposes." See 15 U.S.C. 1681s-3(a).

rather, sought comment on whether any other communications should be excluded from the statutory definition of "solicitation."[85] We also requested comment on whether, and to what extent, various tools used in Internet-based marketing, such as pop-up ads, could constitute marketing solicitations as opposed to communications directed at the general public.

Seven commenters addressed the definition of "marketing solicitation."[86] Some expressed concern that the proposed definition was not the same as the definition in Section 214 of the FCRA[87] and suggested including the phrase "of a product or service" in the introductory language to be consistent.[88] Other commenters favored the exclusion from the definition of marketing solicitation, solicitations made to the general public.[89] However, one commenter believed that the phrase "distributed without the use of eligibility information communicated by an affiliate" inadvertently misstated the types of general marketing that would not be marketing solicitations.[90] Another commenter asked the Commission to clarify that any communications directed at the general public are not marketing solicitations regardless of whether they were developed using specific eligibility information.[91]

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85 15 U.S.C. 1681s-3(d)(2).

86 See Coalition Letter; FSR Letter; ICBA Letter; ICI Letter; MetLife Letter; SIFMA Letter I; Wells Fargo Letter.

87 See FSR Letter; SIFMA Letter I.

88 Id. One commenter indicated that the lack of this phrase raised the possibility that the definition could be misinterpreted. See FSR Letter.

89 See Coalition Letter; ICBA Letter; Wells Fargo Letter.

90 See Coalition Letter.

91 See Wells Fargo Letter.

Several commenters also addressed Internet-based marketing and generally opposed including it in this rulemaking.[92] Some expressed the view that discussion of a particular delivery mechanism would be counterproductive and contrary to congressional intent, noting that the Internet was not specifically addressed in this legislation.[93] Another suggested that Internet issues should be addressed in a separate process to ensure that notice and opportunity to be heard are given to the parties affected.[94]

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92 See Coalition Letter; FSR Letter; MetLife Letter.

93 See Coalition Letter; MetLife Letter.

94 See MetLife Letter.

The commenter also opined that pop-up ads that appear automatically without the use of eligibility information or information from other affiliates are communications directed at the general public, and that a consumer visiting an Internet Web site is effectively making an inquiry which is tantamount to an affirmative request for information. In addition, the commenter asked for clarification that pre-recorded messages played while consumers are on hold when calling a call center should be construed as general marketing solicitations. Another commenter asked for a similar clarification for advertisements that appear on password-protected Web sites.[95]

The revised definition tracks the statutory language more closely by encompassing the marketing "of a product or service."[96] To ensure consistency with the definition of "pre-existing business relationship," the definition applies to marketing intended to encourage the consumer to purchase "or obtain" a product or service. In this way, the definition includes marketing for the rental or lease of goods or services, financial transactions, and financial contracts. The Commission is not adopting the reference to communications "distributed without the use of eligibility information communicated by an affiliate" in the exclusion for marketing directed at the general public because we do not believe it is necessary. Marketing that is undertaken without the use of eligibility information received from an affiliate is not covered by the affiliate marketing rules. Moreover, there is no restriction on using eligibility information received from an affiliate in marketing directed at the general public, such as radio, television, general circulation magazine, billboard advertisements, or publicly available Web sites that are not

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95 See ICI Letter.

96 For purposes of this release and the final rule, we interpret and use the term "products and services" to include shareholder investments in investment companies.

directed to particular consumers.[97]

The definition of "marketing solicitation" does not distinguish among different delivery methods or media. A determination of whether a marketing communication in any medium constitutes a marketing solicitation depends upon the facts and circumstances. The Commission declines to exclude categorically from the definition of "marketing solicitation," pre-recorded messages played while a consumer is on hold with a call center, or advertisements that appear solely on password-protected Web sites. Marketing delivered by such media may constitute a marketing solicitation if it is targeted to a particular consumer based on eligibility information received from an affiliate. For example, a pre-recorded message played while a consumer is on hold with a call center would be a marketing solicitation if it is targeted to a particular consumer based on eligibility information received from an affiliate, but would not be a marketing solicitation if it is played for all consumers who are on hold with the call center.

We note that the Agencies declined to exclude educational seminars, customer appreciation events, focus group invitations, and similar forms of communication from the definition of "solicitation" in their final rules.[98] While we received no comments on these types of activities, like the Agencies, we believe that such activities must be evaluated according to the facts and circumstances, and that some of these activities may be coupled with, or a prelude to, a marketing solicitation. For example, an invitation to a financial educational seminar when the invitees are selected based on eligibility information received from an affiliate may be a marketing solicitation if the seminar is used to solicit the consumer to purchase or obtain

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97 See supra text accompanying note 90. Similarly, visiting a publicly available Web site should not, by itself, constitute an "inquiry" for purposes of the pre-existing business relationship exception.

investment products or services.

16. Person

We received no comment on the definition of "person," and we are adopting it as proposed.[99] The proposed rule defined "person" to mean any individual, partnership, corporation, trust, estate, cooperative, association, government or governmental subdivision or agency, or other entity. A person could act through an agent, such as a licensed agent (in the case of an insurance company), a trustee (in the case of a trust), or any other agent. For purposes of Regulation S-AM, actions taken by an agent on behalf of a person that are within the scope of the agency relationship will be treated as actions of that person.

17. Pre-Existing Business Relationship

a. Definition

We are adopting the definition of "pre-existing business relationship" substantially as proposed,[100] with the modifications discussed below. The proposed rule contained a three-part definition of "pre-existing business relationship." Under the first part, a "pre-existing business relationship" would exist when there is a financial contract in force between a Covered Person and a consumer.[101] Under the second part, a "pre-existing business relationship" would exist when a consumer purchased, rented, or leased a Covered Person's goods or services, or entered into a financial transaction (including holding an active account or a policy in force or having another continuing relationship) with a Covered Person during the 18-month period immediately

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98 See Joint Rules at 72 FR 62919; FTC Rule at 72 FR 61432.

99 See § 248.120(p), proposed as § 247.3(o).

100 See § 248.120(q)(1), proposed as § 247.3(p).

101 See Proposed § 247.3(p)(1).

preceding the date on which a marketing solicitation is made.[102] Under the third part, a "pre-existing business relationship" would exist when, in certain circumstances, a consumer inquired about, or applied for, a product or service offered by a Covered Person during the three-month period immediately preceding the date on which a marketing solicitation is made to the consumer.[103] In the Proposing Release, we noted that the proposed definition tracked the definition in Section 624 of the FCRA but did not follow the statute exactly.[104] We also noted that while Section 624 authorizes the Commission to recognize any other circumstances that would constitute a pre-existing business relationship, we did not propose to exercise this authority.[105]

Ten commenters addressed the definition of "pre-existing business relationship."[106] Several commenters noted that the statutory reference to "a person's licensed agent" was not in the rule.[107] One commenter expressed the view that Congress intended the phrase to be included in any implementing rule because it is in the statute.[108] Two commenters noted the importance of licensed agents in the insurance industry, and stated that independent, licensed agents

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102 See Proposed § 247.3(p)(2).

103 See Proposed § 247.3(p)(3).

104 See Proposing Release at 42306 (citing 15 U.S.C. 1681s-3(d)(1)).

105 Id. (citing 15 U.S.C. 1681s-3(d)(1)(D)).

106 See ABASA Letter; ACB Letter; ACLI Letter; AIA Letter; Coalition Letter; FSR Letter; ICBA Letter; MetLife Letter; Wells Fargo Letter; SIFMA Letter I.

107 See ACB Letter; ACLI Letter; Coalition Letter; FSR Letter; ICBA Letter; MetLife Letter; SIFMA Letter I.

108 See Coalition Letter.

frequently act as the main point of contact between a consumer and an insurance company.[109] In light of these comments and to more closely track the statute, we have added the phrase "or a person's licensed agent" in the final definition of "pre-existing business relationship." For example, a person who is both a licensed agent for an insurance company and a registered representative for a broker-dealer may sell to a consumer a variable annuity issued by the insurance company. The licensed agent may use eligibility information that it obtains in connection with selling the variable annuity to the consumer to market the insurance company's life insurance policies to the consumer for the duration of the pre-existing business relationship without offering an opt out opportunity.

Some commenters questioned the requirement in the first part of the definition that a financial contract be in force "on the date on which the consumer is sent a marketing solicitation."[110] In their view, delays between the time when information is processed and prepared for a marketing solicitation and the time a marketing solicitation is made or sent would create an undue burden of having to synchronize the sending of the marketing solicitation with a contract that is in force. They recommended that a contract should only have to be in force when the information is prepared for a marketing solicitation and not when the marketing solicitation is made. We do not agree with these comments and are adopting the second part of the definition as proposed. This approach is consistent with the approach used in the other two parts of the

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109 See ACLI Letter; MetLife Letter. The ACLI Letter also noted that this type of role played by licensed agents would have implications for not only life insurers who issue variable life insurance and variable annuity contracts but also the broker-dealers who sell these products.

110 See ACLI Letter; SIFMA Letter I; Wells Fargo Letter.

statutory definition.[111] We also note that the second part of the definition alleviates these synchronization problems since a pre-existing business relationship would continue to exist for another 18 months after a financial contract ceases to be in force.

Some commenters addressed various parts of the second part of the definition.[112] One commenter suggested that "any account with outstanding contractual responsibilities on either side of an account relationship should be considered an active account, regardless of whether the individual transactions occur or do not occur under the account."[113] We decline to interpret an "active account" in this way. Section 603(r) of the FCRA defines an "account" to have the same meaning as in Section 903 of the Electronic Fund Transfer Act ("EFTA").[114] Section 903 of the EFTA defines the term "account" to mean a demand deposit, savings deposit, or other asset account established primarily for personal, family, or household purposes.[115] In addition, our view regarding the term "account" is analogous to the views expressed by the Agencies.

One commenter stated that when consumers pay in advance for future services, the 18-month exemption under the second part of the definition should not begin until after the last payment or shipment of the product.[116] Another commenter suggested that the 18-month period

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111 See 15 U.S.C. 1681s(d)(1)(A)–(C). As noted earlier, the definition of "pre-existing business relationship" in Regulation S-AM tracks the statutory definition. Although the statutory definition does not contain the term "sent" for the provision dealing with a contract that is in force (15 U.S.C.1681s(d)(1)(A)), the other two parts of the statutory definition do contain the term "sent" (15 U.S.C. 1681s(d)(1)(B)–(C)). Accordingly, we believe that the statutory definition is best implemented by including this concept in all three parts of the definition in Regulation S-AM.

112 See Coalition Letter; Wells Fargo Letter.

113 See Wells Fargo Letter.

114 See 15 U.S.C. 1681a(r)(4).

115 See 15 U.S.C. 1693(a)(2).

116 See Coalition Letter.

should begin at the time that all contractual responsibilities expire.[117] The Commission declines to adopt these suggestions because they could lead to consumers receiving marketing solicitations long after closing or transferring an account. For purposes of the final rule, a pre-existing business relationship terminates when an investor redeems or sells investment company shares or closes or transfers an account, and not when the investor receives the last statement relating to the account or when an obligation assumed by a Covered Person in an account opening document expires. The final rule includes examples to help clarify the scope of this part of the definition of a pre-existing business relationship.[118]

Two commenters discussed the third part of the definition of "pre-existing business relationship" – an inquiry or application by the consumer regarding a product or service offered by the person during the preceding three months.[119] These commenters generally stated that the exception should not depend on consumers providing contact information or on a consumer's expectations. One commenter indicated that an e-mail inquiry, a return address on an envelope, or the captured phone number of a consumer requesting information about products or services should qualify as a "pre-existing business relationship."[120]

Certain elements of the definition of "pre-existing business relationship" are substantially similar to the definition of "established business relationship" under the FTC's Telemarketing Sales Rule ("TSR").[121] The TSR definition was informed by Congress's intent that the "established business relationship" exemption to the "do not call" provisions of the Telephone

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117 See Wells Fargo Letter.

118 See §§ 248.120(q)(2) and 248.120(q)(3).

119 See Coalition Letter; Wells Fargo Letter.

120 See Wells Fargo Letter.

Consumer Protection Act[122] should be grounded on the reasonable expectations of the consumer.[123] Congress's incorporation of similar language in the definition of "pre-existing business relationship"[124] suggests that it is appropriate to consider the reasonable expectations of the consumer in determining the scope of this exception. For purposes of Regulation S-AM, an inquiry would include any affirmative request by a consumer for information after which the consumer would reasonably expect to receive information from the affiliate about its products or services.[125] A consumer would not reasonably expect to receive information from an affiliate if the consumer did not request information from or provide contact information to the affiliate. For this reason, the Commission does not believe that an automatically captured telephone number of a consumer is sufficient to create an inquiry, particularly when the financial institution could easily ask the consumer for contact information during the telephone call that captured the consumer's telephone number. Similarly, we do not believe that information such as an Internet Protocol address or data contained in an Internet "cookie" that is automatically collected about a consumer visiting a Covered Person's Web site is, by itself, sufficient to create an inquiry. We understand that industry practice in the case of telephone calls is to ask the consumer to provide or confirm his or her contact information.[126] To provide additional guidance to industry, we have

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121 See 16 CFR 310.2(n).

122 47 U.S.C. 227, et seq.

123 H.R. Rep. No. 102-317, at 14-15 (1991). See also FTC, Telemarketing Sales Rule, 68 FR 4580, 4591-94 (Jan. 29, 2003) ("TSR Adopting Release").

124 149 Cong. Rec. S13,980 (daily ed. Nov. 5, 2003) (statement of Senator Feinstein) (noting that the "pre-existing business relationship" definition "is the same definition developed by the Federal Trade Commission in creating a national 'Do Not Call' registry for telemarketers.").

125 See TSR Adopting Release at 68 FR 4594.

126 Similarly, the Commission does not believe that a return address on an envelope is sufficient to constitute an affirmative request by a consumer for information about a person's products or (continued)

provided additional examples in the definition that deal with consumer calls and e-mails.[127] These examples, along with other examples, are discussed below. One commenter urged the Commission to clarify that all three parts of the definition of "pre-existing business relationship" include a transaction-based relationship between a consumer and a securities affiliate regardless of the issuer of the security purchased by the consumer.[128] This commenter asserted that a consumer whose securities and investment transactions are managed through a bank-owned securities affiliate would not be surprised, and may later expect, to receive marketing solicitations for other securities products based on eligibility information the securities affiliate has received from the affiliated bank. Another commenter urged the Commission to expand the definition to include relationships arising out of the ownership of servicing rights, a participation interest in lending or other similar relationships.[129] Another commenter suggested that the definition should apply to manufacturers that make sales through dealers, such as an automobile manufacturer that sells vehicles not directly to consumers, but through franchised dealers.[130] The

services. A consumer would not have a reasonable expectation of being contacted about products and services simply by providing a return address on an envelope. In our view, a consumer provides a return address on an envelope to ensure that if a piece of mail is undeliverable, it is returned to the consumer and not because they are seeking to establish a business relationship. Accordingly, we consider a return address on an envelope analogous to an automatically captured telephone number.

127 See §§ 248.120(q)(2)(v)–(vii) and (q)(3).

128 See ABASA Letter (stating that the proposed rule supports the conclusion that a pre-existing business relationship exists between a securities affiliate and a consumer when the consumer purchases a proprietary securities product like a bank's own mutual fund and expressing concern that the purchase of non-proprietary securities products from the securities affiliate could be considered to be outside of the first two provisions of the definition of a pre-existing business relationship).

129 See Wells Fargo Letter.

130 See FSR Letter. The commenter further indicated that vehicle financing may be arranged through a manufacturer's captive finance company or independent sources of financing, and noted that manufacturers often provide consumers with information about warranty coverage,
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commenter urged the Commission to consider the relationship between a manufacturer and a consumer as a pre-existing business relationship based on the purchase, rental, or lease of the manufacturer's goods.

Like the Agencies, the Commission believes it is not necessary to add any additional bases for a pre-existing business relationship. Paragraph (q)(2)(i) of § 248.120 provides an example of a brokerage firm with a pre-existing business relationship using eligibility information from an affiliate to make marketing solicitations about products or services. This example should provide Covered Persons with sufficient guidance regarding a securities affiliate's use of eligibility information.

b. Examples

Paragraph (d)(1) of proposed § 247.20 provided four examples to illustrate the pre-existing business relationship exception. Proposed paragraphs (d)(1)(i) through (iii) contained examples illustrating each of the three parts of the definition.[131] Proposed paragraph (d)(1)(iv) provided an example of a consumer calling a centralized call center for a group of affiliated companies to inquire about the consumer's existing securities account with a broker-dealer, and indicated that such a call would not establish a pre-existing business relationship between the consumer and the broker-dealer's affiliates. We requested comment on these examples.

One commenter generally expressed approval of the examples we provided, other than

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recall notices, and other product information. This commenter stated that manufacturers also send solicitations to consumers about their products and services, drawing in part on transaction or experience information from the captive finance company.

131 See Proposed §§ 247.20(d)(1)(i) (illustrating the first part), (d)(1)(ii) (illustrating the second part) and (d)(1)(iii) (illustrating the third part).

the example in proposed § 247.20(d)(1)(iii).[132] Another commenter requested that the Commission provide further examples dealing with consumer calls to call centers to clarify what would and would not be considered subject to Regulation S-AM's opt out notice requirement.[133]

We are adopting seven examples of a pre-existing business relationship set out in § 248.120(q)(2).[134] In § 248.120(q)(3) we have provided three examples of the absence of a pre-

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132 The example in proposed § 247.20(d)(1)(iii) illustrated that a pre-existing business relationship would exist with a Covered Person's affiliate when a consumer made an inquiry about, or applied for, a product or service offered by the affiliate during the three-month period immediately preceding the date on which a marketing solicitation is made to the consumer based on eligibility information received from the Covered Person. The Coalition Letter stated that a consumer should not be required to provide contact information as part of an inquiry in order to establish a pre-existing business relationship. As stated above, however, we do not believe that a consumer would reasonably expect to have established a pre-existing business relationship in the absence of providing contact information. See also supra text accompanying notes 125 and 126.

133 See MetLife Letter.

134 Section 248.120(q)(2)(i) provides an example of a pre-existing business relationship based on a consumer's open account with a brokerage firm. Section 248.120(q)(2)(ii) provides a similar example of a pre-existing business relationship with a registered investment adviser. Section 248.120(q)(2)(iii) provides an example in which a pre-existing business relationship is established for 18 months after the date a consumer who was the record owner of investment company securities redeems all of those securities. Section 248.120(q)(2)(iv) provides an example in which a consumer applies for a product or service, but does not obtain the product or service for which she applied, and a pre-existing business relationship is established for three months after the date of the application. Contact information is not mentioned in this example because the consumer presumably would have supplied it on the application. Section 248.120(q)(2)(v) provides an example in which a consumer makes a telephone inquiry about a product or service offered by a brokerage firm and provides contact information to the institution, but does not obtain a product or service from or enter into a financial transaction with the institution. As noted earlier, we do not believe that, by itself, an institution's capture of a consumer's telephone number during a telephone conversation with the consumer about the institution's products or services is sufficient to create an inquiry. In these circumstances, to ensure that an inquiry has been made, the institution should ask the consumer to provide his or her contact information. Section 248.120(q)(2)(vi) provides an example in which pre-existing business relationships are established for three months after the date a consumer makes an e-mail inquiry to a broker-dealer about one of its affiliated investment company's products or services without providing any contact information other than the consumer's e-mail address. Unlike telephone communications, e-mail communications do not provide institutions with an opportunity to ask for additional contact information at the time of a consumer's initial request for information. Section 248.120(q)(2)(vii) provides an example in which a pre-existing business relationship between a consumer and a broker-dealer is established for three months by a

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existing relationship.[135]

18. Transfer Agent

We received no comment on the definition of "transfer agent" and are adopting it as proposed.[136] The rule defines "transfer agent" to have the same meaning as in Section 3(a)(25) of the Exchange Act.[137]

19. You

We received no comment on the definition of "you" and are adopting it substantially as proposed.[138] The one difference is that the final definition does not include notice-registered broker-dealers.[139]

D. Section 248.121 Affiliate Marketing Opt Out and Exceptions

Proposed § 247.20 set forth the requirement that a consumer be provided with notice and a reasonable opportunity to opt out before a receiving affiliate uses eligibility information to make marketing solicitations to the consumer. Proposed paragraphs (a) and (b) bifurcated duties

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consumer's telephone call to a centralized call center for the broker-dealer and an affiliated investment company with which the consumer has an existing relationship, and the consumer provides contact information to the call center and inquires about products and services offered by the broker-dealer, but does not obtain any products or services.

135 Section 248.120(q)(3)(i) is similar to § 248.120(q)(2)(vii) except that the consumer does not inquire about an affiliate's products or services but about an existing account with the broker-dealer. In this situation, a pre-existing business relationship with an affiliate of the broker-dealer is not established. Section 248.120(q)(3)(ii) is substantively similar to the example in proposed § 247.20(d)(2)(iii), whereby a pre-existing business relationship is not created by simply requesting information about retail hours and locations. Section 248.120(q)(3)(iii) illustrates that a call in response to an advertisement for a free promotional item is not an inquiry about a product or service that would establish a pre-existing business relationship.

136 See § 248.120(r), proposed as § 247.3(q).

137 15 U.S.C. 78c(a)(25).

138 See § 248.120(s), proposed as § 247.3(r).

139 See supra note 16.

between the "communicating affiliate" and "receiving affiliate" to resolve what we perceived as an ambiguity in the FCRA with regard to which affiliate was to provide the opt out notice to the consumer.[140] Proposed paragraph (c) contained exceptions to the requirements of Regulation S-AM and incorporated each of the statutory exceptions to the affiliate marketing notice and opt out requirements that are set forth in Section 624(a)(4) of the FCRA, and paragraph (d) illustrated those exceptions with examples. Proposed paragraph (e) provided that Regulation S-AM would not be applicable to marketing solicitations that were based on information received by an affiliate prior to the proposed mandatory compliance date.[141] Proposed paragraph (f) clarified the relationship between sharing information and becoming a credit reporting agency. The final rules modify many of these proposed provisions as discussed below.

1. Section 248.121(a)

Under proposed § 247.20(a)(1), before a receiving affiliate could use eligibility information to make or send marketing solicitations to a consumer, the communicating affiliate would have had to provide a notice to the consumer stating that the information may be communicated to and used by the receiving affiliate for marketing purposes. The consumer also would have had to have a reasonable opportunity to opt out through some simple method before the receiving affiliate could make a marketing solicitation. The notice and opt out requirements would have applied only if a receiving affiliate would use eligibility information for marketing

140 In the proposed rules, we differentiated between affiliates by referring to an affiliate that communicated eligibility information to an affiliate as the "communicating affiliate" and to the affiliate receiving the eligibility information as the "receiving affiliate."

141 This section, redesignated as § 248.128(c), is discussed below. See infra Part III.K.2.

purposes.[142] Proposed paragraph (a)(2) included two "rules of construction" to give further guidance regarding how affiliate marketing notices might be provided to consumers.[143]

Proposed § 247.20(b) set forth the general duties of a receiving affiliate. In particular, a receiving affiliate could not have used the eligibility information it received from its affiliate to make marketing solicitations to a consumer unless, prior to such use the consumer had: (1) been provided an opt out notice (as described in proposed paragraph (a) of § 247.20) that applied to that affiliate's use of eligibility information; (2) received a reasonable opportunity to opt out of that use through one or more simple methods; and (3) not opted out. The Commission solicited comment on these provisions. In addition, the Commission also solicited comment on whether there were situations where oral notices and opt outs should be allowed and, if so, how the

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142 Proposed paragraph (a)(1) would not have applied if no eligibility information was communicated to affiliates, or if no receiving affiliate would use eligibility information to make marketing solicitations. In the proposal, we provided an example in which paragraph (a) was inapplicable. In the example, a financing company affiliated with a broker-dealer asked the broker-dealer to include financing-company marketing materials in periodic statements sent to consumers by the broker-dealer without regard to eligibility information.

143 The first rule of construction would have permitted the notice to be provided either in the name of a person with which the consumer currently did or previously had done business, or by using one or more common corporate names shared by members of an affiliated group of companies that included the common corporate name used by that person. This rule of construction also would have provided three alternatives regarding the manner in which the notice could have been given. First, a communicating affiliate could have provided the notice to the consumer directly. Second, a communicating affiliate could have used an agent to provide the notice, so long as the agent provided the notice in the name of the communicating affiliate or by using a common corporate name. When using an agent however, the communicating affiliate would have remained responsible for any failure of the agent to fulfill the affiliate's notice obligations. Third, a communicating affiliate could have provided a joint notice with one or more of its affiliates. Of course, if the agent was an affiliate of the person that provides the notice, that affiliate could not have included any marketing solicitations of its own on or with the notice, unless one of the exceptions in paragraph (c) of proposed § 247.20 applied. Even if the agent sending the notice were not an affiliate, the agent would have been permitted to use the information only for limited purposes under Regulation S-P. See 17 CFR 248.11. The second rule of construction would have discussed how to avoid issuing duplicate notices when Affiliate A communicated information to Affiliate B, who in turn communicated information to Affiliate C.

statute's clear and conspicuous standard could be satisfied.[144]

Five commenters addressed the duties of the communicating affiliate and the receiving affiliate.[145] Some commenters supported having the communicating affiliate provide the notice and opt out, indicating that consumers may be more likely to expect a notice from the communicating affiliate and could unknowingly miss the opportunity to opt out if they do not have a pre-existing relationship with the company that is sending the notice and opt out.[146] Other commenters disagreed with the provision in the proposal that would have required the communicating affiliate provide the notice and opt out.[147] One commenter viewed the statute's lack of direction regarding which entity must provide the notice and opt out as evidence of Congressional intent to permit companies to structure the notice and opt out in a manner that meets their unique needs and situations.[148] Another commenter stated that the FCRA contemplates that the receiving affiliate would provide the notice, and that to require the communicating affiliate to provide it would create a basis for civil liability if a communicating affiliate does not provide notice and an opportunity to opt out before a receiving affiliate uses eligibility information to make a marketing solicitation.[149]

Six commenters addressed oral notices and supported permitting their use.[150] One

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144 The proposal also contemplated that the opt out notice would be provided to the consumer in writing or, if the consumer agreed, electronically. See Proposing Release at 69 FR 42308.

145 See ACLI Letter; ICBA Letter; ICI Letter; T. Rowe Price Letter; Wells Fargo Letter.

146 See ICI Letter; T. Rowe Price Letter.

147 See ACLI Letter; ICBA Letter; Wells Fargo Letter.

148 See ACLI Letter. One commenter also suggested allowing companies to decide the best method of providing the notice. See ICBA Letter.

149 See Wells Fargo Letter.

150 See Coalition Letter; IAA Letter; ICBA Letter; ICI Letter; T. Rowe Price Letter; Wells Fargo Letter.

commenter indicated that the use of oral notices would be an easier method by which consumers could exercise their rights under the proposed rules.[151] This commenter indicated that this was especially so for consumers who primarily conduct business over the telephone, suggesting that when information is provided over the phone, a consumer is less likely to disregard a privacy notice.[152] Another commenter generally noted the changing technological landscape and stated that limiting delivery of the notice to written form could create a barrier to improved customer service.[153] Another commenter asserted that the FTC, in its TSR, has permitted clear and conspicuous oral notices without any enforcement difficulties.[154] One commenter also stated that the clear and conspicuous standard could be more easily met with oral notices through the use of scripts or lists of frequently asked questions.[155]

After considering these comments regarding proposed paragraphs (a) and (b), the Commission is adopting these paragraphs, redesignated as § 248.121(a), with modifications. Section 248.121(a)(1) sets forth the general rule and contains the three conditions that must be met before a Covered Person may use eligibility information about a consumer that it receives from an affiliate to make a marketing solicitation to the consumer. First, it must be clearly and conspicuously disclosed to the consumer in writing or, if the consumer agrees, electronically, in a concise notice that the Covered Person may use shared eligibility information to make marketing

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151 See ICI Letter.

152 See ICI Letter. One commenter suggested that the regulation permit the notice to be given by an affiliate while the consumer is being called with a marketing solicitation. See Wells Fargo Letter. Another commenter suggested that delivery of the notice would be better effectuated if the affiliate representative and consumer engaged in a dialogue. See IAA Letter.

153 See ICBA Letter.

154 See Coalition Letter.

155 See IAA Letter.

solicitations to the consumer. Second, the consumer must be provided a reasonable opportunity and a reasonable and simple method to opt out of the use of that eligibility information to make marketing solicitations to the consumer. Third, the consumer must not have opted out. Section 248.121(a)(2) provides an example of the general rule.

The Commission has eliminated as unnecessary the rules of construction in proposed paragraph (a)(2) as well as the provisions in the proposal relating to notice provided by an agent. General agency principles, however, continue to apply. An affiliate that has a pre-existing business relationship with the consumer may direct its agent to provide the opt out notice on its behalf. In light of one commenter's concern about civil liability, the final rules do not impose duties on any affiliate other than the affiliate that intends to use shared eligibility information to make solicitations to the consumer. Although an opt out notice must be provided by or on behalf of an affiliate that has a pre-existing business relationship with the consumer (or as part of a joint notice), that affiliate has no duty to provide such a notice. Instead, the final rules provide that absent such a notice, an affiliate must not use shared eligibility information to make solicitations to the consumer.

Proposed paragraph (b) of § 247.20 has been deleted and replaced with paragraph (a)(3) in § 248.121. Section 248.121(a)(3) provides that the initial opt out notice must be provided either by an affiliate that has a pre-existing business relationship with the consumer, or as part of a joint notice from two or more members of an affiliated group of companies, provided that at least one of the affiliates on the joint notice has a pre-existing business relationship with the consumer. This follows the general approach taken in the proposal to ensure that the notice would be provided by an entity known to the consumer. While we used the terms "communicating affiliate" and "receiving affiliate" in the proposal and continue to use these terms in this release, the final rule text does not include these terms in order to avoid potential confusion.[156] The Commission has considered the comments regarding oral notices and opt outs and concluded that the opt out notice may not be provided orally. The Commission is required, under the FACT Act, to consider the affiliate-sharing notification practices employed on the date of enactment and to ensure that notices and disclosures may be coordinated and consolidated in promulgating regulations. Any affiliate-sharing notice required under Section 603(d)(2)(A)(iii) of the FCRA generally must be included in a GLBA privacy notice, which must be provided in writing, or if the consumer agrees, electronically. We find it consistent with existing affiliate-sharing notification practices to require the affiliate marketing opt out notice to be provided in writing, or if the consumer agrees, electronically. The Commission believes that this will promote coordination and consolidation of the FCRA affiliate marketing and sharing notice with the GLBA privacy notices. We are not persuaded that there are any circumstances in which an oral opt out notice would be necessary. While oral opt out notices are not permitted, a number of key exceptions to the initial notice and opt out requirement may be triggered by an oral communication with the customer. These include the: (1) pre-existing business relationship exception; (2) consumer-initiated communication exception; and (3) consumer authorization or request exception. We understand that some Covered Persons currently require consumers to

156 The Commission continues to believe that the statute's silence with regard to which affiliates may provide the opt out notice makes the statute ambiguous on this point. We agree with the commenters who indicated that consumers are less likely to disregard a notice provided by a person known to the consumer. We are concerned that a notice provided by an entity unknown to the consumer may not provide meaningful or effective notice because consumers are more likely to ignore or discard these notices. However, we note that while an agent unknown to the consumer may provide a notice, the notice itself would have to clearly indicate that it is on behalf of either the company the consumer has or had a pre-existing relationship with or be a joint notice from two or more members of an affiliated group of companies so long as one of the
(continued)

provide their Social Security numbers when exercising their existing GLBA or FCRA opt out rights. To combat identity theft and prevent "phishing," however, consumers have been advised not to provide sensitive personal information such as Social Security numbers to unknown entities. Furthermore, as one of the Federal agencies participating in the President's Identity Theft Task Force, the Commission has made a commitment to examine and recommend ways to limit the private sector's use of Social Security numbers. The approach recommended by some industry commenters would allow an entity unknown to the consumer to not only provide the affiliate marketing opt out notice, but also to require the consumer to reveal his or her Social Security number to that unknown entity in order to exercise the opt out. The Commission notes that requiring that a consumer reveal his or her Social Security number to an unknown entity in order to exercise his or her opt out right would send conflicting messages to consumers about providing Social Security numbers to unknown entities. This approach would be inconsistent with the Commission's current joint efforts with the Agencies to develop a comprehensive record on the uses of the Social Security number in the private sector and evaluate their necessity, as recommended by the President's Identity Theft Task Force.[157]

2. Section 248.121(b)

a. Making Marketing Solicitations

The proposed rules referred to "making or sending" marketing solicitations. One

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companies on the joint notice has or had a pre-existing relationship with the consumer. See § 248.121(a)(3).

157 See Combating Identity Theft: A Strategic Plan at 26-27 (April 2007) (available at www.idtheft.gov). See also Regulation S–P: Privacy of Consumer Financial Information and Safeguarding Personal Information, Exchange Act Release No. 57427 (Mar. 4, 2008); 73 FR 13692 (Mar. 13, 2008).

commenter urged us not to address "sending" marketing solicitations.[158] The commenter indicated that by making a reference to "sending" marketing solicitations, it appears that the rule encompasses entities that send a marketing solicitation on behalf of another entity. The general rule in Section 624(a)(1) of the FCRA, along with the duration provisions in Section 624(a)(3) and the pre-existing business relationship exception in Section 624(a)(4)(A), refer to "making" or "to make" a marketing solicitation. Other provisions of the FCRA, such as the consumer choice provision in Section 624(a)(2)(A), the service provider exception in Section 624(a)(4)(C), the non-retroactivity provision in Section 624(a)(5), and the definition of "pre-existing business relationship" in Section 624(d)(1), refer to "sending" or "to send" a marketing solicitation. The verb "to send," as used in the statute, refers to a ministerial act that a service provider, such as a mail house, performs for the person making the marketing solicitation,[159] or indicates the time after which marketing solicitations are no longer permitted.[160]

The Commission concludes that "making" and "sending" marketing solicitations are different activities and that the focus of the FCRA is primarily on the "making" of marketing solicitations.[161] Accordingly, the final rules refer to "making" a marketing solicitation, except where the FCRA specifically refers to "sending" a marketing solicitation. The FCRA, however, does not describe what a person must do in order "to make" a marketing solicitation. The

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158 See Wells Fargo Letter.

159 See 15 U.S.C. 1681s-3(a)(4)(C).

160 See 15 U.S.C. 1681s-3(d)(1)(B) and (C).

161 For example, a service provider may send a marketing solicitation to a consumer on behalf of another entity, but it is the entity on whose behalf the marketing solicitation is sent that is making the marketing solicitation and thus, is subject to the general prohibition on making a marketing solicitation without first giving the consumer an affiliated marketing notice and an opportunity to opt out.

legislative history is silent on this point. Nevertheless, the Commission believes it is important to provide clear guidance regarding what activities constitute making a marketing solicitation.

The Commission has added new § 248.121(b) in the final rules to clarify what constitutes "making" a marketing solicitation for purposes of Regulation S-AM. Section 248.121(b)(1) provides that a Covered Person makes a marketing solicitation to a consumer if: (1) it receives eligibility information from an affiliate; (2) it uses that eligibility information to identify the consumer or type of consumer to receive a marketing solicitation, establish the criteria used to select the consumer to receive a marketing solicitation, or decide which of its products or services to market to the consumer or tailor its marketing solicitation to that consumer; and (3) as a result of its use of the eligibility information, the consumer is provided a marketing solicitation.

The Commission understands that several common business practices may complicate application of this provision. Affiliated groups sometimes use a common database as the repository for eligibility information obtained by various affiliates, and information in that database may be accessible to multiple affiliates. In addition, affiliated companies sometimes use the same service providers to perform marketing activities, and some of those service providers may provide services for a number of different affiliates. Moreover, an affiliate may use its own eligibility information to market the products or services of another affiliate. Paragraphs (b)(2)–(5) of § 248.121 address these issues.

Section 248.121(b)(2) clarifies that a Covered Person may receive eligibility information from an affiliate in various ways, including by the affiliate placing that information into a common database that a Covered Person may access. Of course, receipt of eligibility information from an affiliate is only one element of making a marketing solicitation. In the case of a common database, use of the eligibility information will be important in determining whether a person has made a marketing solicitation.

To clarify the application of the concept of "making" a marketing solicitation in the context of a Covered Person using a service provider, § 248.121(b)(3) generally provides that a person receives or uses an affiliate's eligibility information if a service provider acting on behalf of the Covered Person receives or uses that information on the Covered Person's behalf.[162] Section 248.121(b)(3) also provides that all relevant facts and circumstances will determine whether a service provider is acting on behalf of a Covered Person when it receives or uses an affiliate's eligibility information in connection with marketing the Covered Person's products or services.

b. Constructive Sharing and Service Providers

In § 248.121(b)(4), we address the concept of "constructive sharing." In the proposing release, we illustrated the constructive sharing concept with an example in which a consumer has a pre-existing business relationship with a broker-dealer that is affiliated with a financing company. In the example, the financing company would provide the broker-dealer with specific eligibility criteria, such as consumers who have a margin loan balance in excess of $10,000, for the purpose of having the broker-dealer make marketing solicitations on behalf of the financing company to consumers that meet those criteria. A consumer who meets the eligibility criteria would contact the financing company after receiving the financing company marketing materials in the manner specified in those materials. We contemplated that the consumers' responses would provide the financing company with discernable eligibility information, such as through a

162 The service provider's activities would be those described in §§ 248.121(b)(1)(i) and (b)(1)(ii), discussed above. Section 248.121(b)(5), as discussed below, provides an exception to this general rule.

coded response form that would identify a consumer as an individual who meets the specific eligibility criteria.[163]

We solicited comment on whether, given the policy objectives of Section 214 of the FACT Act, the notice and opt out requirements of these rules should apply to circumstances that involve a constructive sharing of eligibility information to make marketing solicitations.

Commenters consistently opposed inclusion of the concept of constructive sharing in the final rules.[164] One commenter argued that inclusion of the proposed example of constructive sharing would restrict the ability of financial institutions to market products to their own customers.[165] Others stated that including the example was inconsistent with many of the exceptions provided in the proposed rules.[166] In general, commenters argued that constructive sharing was outside the scope of Regulation S-AM because the rules should address the making of marketing solicitations and not the sharing of information.[167]

After carefully considering the comments, we conclude that the FCRA only covers situations in which a person uses eligibility information that it received from an affiliate to make a marketing solicitation to the consumer about its products or services. In a constructive sharing scenario like that described in the proposal and above,[168] a pre-existing business relationship is

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163 See Proposing Release at 69 FR 42307.

164 See ABASA Letter; ACB Letter; Coalition Letter; FSR Letter; ICBA Letter; ICI Letter; MetLife Letter; SIFMA Letter I; T. Rowe Price Letter; Wells Fargo Letter.

165 See T. Rowe Price Letter.

166 See Coalition Letter; FSR Letter; ICBA Letter; Wells Fargo Letter; SIFMA Letter I.

167 See Coalition Letter; ICBA Letter; SIFMA Letter I; Wells Fargo Letter. Although the Commission did not receive comment from consumer groups, consumer groups argued to the Agencies that constructive sharing would contravene the intent of Congress and would amount to a loophole that should be fixed.

168 See supra note 163 and accompanying text.

established between the consumer and the financing company when the consumer contacts the financing company to inquire about or apply for products or services as a result of the consumer's receipt of the financing company's marketing materials from the broker-dealer. Thus, a pre-existing business relationship is established before the financing company uses any shared eligibility information to make marketing solicitations to the consumer. Because the financing company does not use shared eligibility information to make marketing solicitations to the consumer before it establishes a pre-existing business relationship with the consumer, the FCRA's affiliate marketing notice and opt out requirement does not apply.

The Commission acknowledges that the FCRA's affiliate marketing provisions only limit the use of eligibility information received from an affiliate to make marketing solicitations to a consumer. Separately, the affiliate sharing notice and opt out provisions of the FCRA (Section 603(d)(2)(A)(iii)) regulate the sharing of eligibility information other than transaction or experience information among affiliates and prohibit the sharing of such information among affiliates, unless the consumer is given notice and an opportunity to opt out.[169] The FCRA does not restrict the sharing of transaction or experience information (other than medical information) among affiliates.[170]

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169 Section 603(d)(2)(A)(iii) of the FCRA operates independently of FCRA's affiliate marketing provisions. Thus, the existence of a pre-existing business relationship between a consumer and an affiliate that seeks to use shared eligibility information, such as credit scores or income, to market to that consumer (or the applicability of another exception to these affiliate marketing rules) does not relieve the entity sharing the eligibility information from the requirement to comply with the affiliate sharing notice and opt out provisions of Section 603(d)(2)(A)(iii) of the FCRA before it shares with its affiliate eligibility information other than transaction or experience information. See 15 U.S.C. 1681a(d)(2)(A)(iii).

170 Information sharing occurs if a reference code included in marketing materials reveals one affiliate's information about a consumer to another affiliate upon receipt of a consumer's response.

Section 248.121(b)(4) describes two situations in which a Covered Person has not made a solicitation subject to Regulation S-AM. Both situations assume that the Covered Person has not used eligibility information received from an affiliate in the manner described in § 248.121(b)(1)(ii). In the first situation, the affiliate uses its own eligibility information that it obtained in connection with a pre-existing business relationship that it has or had with the consumer to market the Covered Person's products or services to the affiliate's consumers.[171] In the second situation, which builds on the first, a Covered Person's affiliate directs its service provider to use the affiliate's own eligibility information to market the Covered Person's products or services to the affiliate's consumer, and the Covered Person does not communicate directly with the service provider regarding that use of the eligibility information.

The core concept is that the affiliate that obtained the eligibility information in connection with a pre-existing business relationship with the consumer controls the actions of the service provider using that information. Therefore, the service provider's use of the eligibility information should not be attributed to the Covered Person whose products or services will be marketed to consumers. In such circumstances, the service provider is acting on behalf of the affiliate that obtained the eligibility information in connection with a pre-existing business relationship with the consumer, and not on behalf of the Covered Person whose products or services will be marketed to that affiliate's consumers.

In addition, the Commission recognizes that there may be situations in which the Covered

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171 As an example, a broker-dealer that sells investment company shares to a consumer has a pre-existing business relationship with the consumer (as does the investment company if the consumer is the record owner of its shares). The broker-dealer may make a marketing solicitation for an investment in an affiliated investment company based on eligibility information the broker-dealer obtained in connection with its pre-existing business relationship with the consumer.

Person whose products or services are being marketed does communicate with the affiliate's service provider.[172] To address these situations, the Commission has added § 248.121(b)(5) which describes the conditions under which a service provider would be deemed to be acting on behalf of the affiliate with the pre-existing business relationship, rather than the Covered Person whose products or services are being marketed, notwithstanding direct communications between the Covered Person and the service provider.[173]

Section 248.121(b)(5) provides that a Covered Person does not make a marketing solicitation subject to Regulation S-AM if a service provider (including an affiliated or third-party service provider that maintains or accesses a common database that the Covered Person may access) receives and uses eligibility information from the Covered Person's affiliate to market the Covered Person's products or services to the affiliate's consumer, so long as five conditions are met.

First, the Covered Person's affiliate must control access to and use of its eligibility information by the service provider (including the right to establish specific terms and conditions under which the service provider may use such information to market the Covered Person's products or services). This requirement must be set forth in a written agreement between the

172 For example, a service provider may perform services for various affiliates relying on information maintained in and accessed from a common database. In certain circumstances, the person whose products or services are being marketed may communicate with the service provider of the affiliate with the pre-existing business relationship, yet the service provider is still acting on behalf of the affiliate when it uses the affiliate's eligibility information in connection with marketing the person's products or services.

173 This section builds upon the concept of control of a service provider and thus is a natural outgrowth of § 248.121(b)(4). Under the conditions set forth in § 248.121(b)(5), the service provider is acting on behalf of an affiliate that obtained the eligibility information in connection with a pre-existing business relationship with the consumer because, among other things, the affiliate controls the actions of the service provider in connection with the service provider's receipt and use of eligibility information.

Covered Person's affiliate and the service provider. The Covered Person's affiliate may demonstrate control by, for example, establishing and implementing reasonable policies and procedures applicable to the service provider's access to and use of its eligibility information.[174]

Second, the Covered Person's affiliate must establish specific terms and conditions under which the service provider may access and use that eligibility information to market the Covered Person's products or services (or those of affiliates generally) to the affiliate's consumers, and periodically evaluates the service provider's compliance with those terms and conditions. These terms and conditions may include the identity of the affiliated companies whose products or services may be marketed to the affiliate's consumers by the service provider, the types of products or services of affiliated companies that may be marketed, and the number of times the affiliate's consumers may receive marketing materials. While the specific terms and conditions established by the Covered Person's affiliate must be set forth in writing, they are not required to be set forth in a written agreement between the affiliate and the service provider. If a periodic evaluation by the Covered Person's affiliate reveals that the service provider is not complying with those terms and conditions, the Commission expects the Covered Person's affiliate to take appropriate corrective action.[175]

Third, the Covered Person's affiliate must require the service provider to implement reasonable policies and procedures designed to ensure that the service provider uses the affiliate's eligibility information in accordance with the terms and conditions established by the affiliate relating to the marketing of the Covered Person's products or services. This requirement must be set forth in a written agreement between the Covered Person's affiliate and the service

[174] See § 248.121(b)(5)(i)(A).

provider.[176]

Fourth, the Covered Person's affiliate must be identified on or with the marketing materials provided to the consumer. This requirement will be construed flexibly. For example, the affiliate may be identified directly on the marketing materials, on an introductory cover letter, on other documents included with the marketing materials such as a periodic statement, or on the envelope that contains the marketing materials.[177]

Fifth, the Covered Person must not directly use the affiliate's eligibility information in the manner described in § 248.121(b)(1)(ii).[178]

Under these conditions, the service provider is acting on behalf of an affiliate that obtained the eligibility information in connection with a pre-existing business relationship with the consumer because, among other things, the affiliate controls the actions of the service provider in connection with the service provider's receipt and use of the eligibility information.[179] The five conditions together are intended to ensure that the service provider is acting on behalf of the affiliate that obtained the eligibility information in connection with a pre-existing business relationship with the consumer because that affiliate controls the service provider's receipt and use of that affiliate's eligibility information.

To provide additional guidance to Covered Persons, § 248.121(b)(6) provides six

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175 See § 248.121(b)(5)(i)(B).

176 See § 248.121(b)(5)(i)(C).

177 See § 248.121(b)(5)(i)(D).

178 See § 248.121(b)(5)(i)(E).

179 This provision is designed to minimize uncertainty that may arise from the application of the facts and circumstances test in § 248.121(b)(3) to situations that involve direct communications between a service provider and a Covered Person whose products and services will be marketed to consumers.

illustrative examples of the rules relating to making marketing solicitations.

3. Sections 248.121(c) and (d)

Proposed § 247.20(c) contained exceptions to the requirements of Regulation S-AM and incorporated each of the statutory exceptions to the affiliate marketing notice and opt out requirements that are set forth in Section 624(a)(4) of the FCRA. The Commission has revised the preface to the exceptions for clarity to provide that Regulation S-AM does not apply to "you" if a Covered Person uses eligibility information that it receives from an affiliate in certain circumstances. In addition, each of the exceptions has been moved to § 248.121(c) in the final rules and is discussed below.[180]

a. Pre-existing Business Relationship Exception

Proposed paragraph (c)(1) of § 247.20 clarified that the notice and opt out requirements of proposed Regulation S-AM would not apply when the receiving affiliate has a pre-existing business relationship with the consumer. We are adopting § 247.20(c)(1) substantially as proposed,[181] deleting the word "send" for the reasons discussed above and eliminating, as unnecessary, the cross-reference to the location of the definition of "pre-existing business

180 One commenter requested that the Commission delete the phrase "if you use eligibility information you receive from an affiliate" in the introductory words to Proposed § 247.20(c). The Commenter stated that this could inadvertently and mistakenly expose companies that share information with affiliates to potential liability. See SIFMA Letter II. That concern was addressed in the constructive sharing discussion above. See supra Part III.D.2.b.

181 Proposed § 247.20 (d)(1) provided examples of the pre-existing business relationship exception. As explained above, we have revised the examples from proposed § 247.20(d)(1) in the final rule and included them as examples of the definition of "pre-existing business relationship" rather than as examples of exceptions from the application of the rule. See § 248.120(q)(2); See also discussion of "pre-existing business relationship" and corresponding examples supra Part III.C.17.

relationship."[182] Commenters' views, and the scope of this exception, have been addressed above.[183] However, to help clarify the scope of the "pre-existing business relationship" exception, § 248.121(d)(1) provides an example to illustrate a situation in which the pre-existing business relationship exception would apply.[184]

b. Employee Benefit Plan Exception

Proposed § 247.20(c)(2) provided that Regulation S-AM would not apply to an affiliate using the information to facilitate communications to an individual for whose benefit the affiliate provided employee benefit or other services under a contract with an employer related to and arising out of a current employment relationship or an individual's status as a participant or beneficiary of an employee benefit plan. One commenter stated that the exception should be revised to permit communications "to an affiliate about an individual for whose benefit an entity provides employee benefit or other services pursuant to a contract with an employer related to and arising out of the current employment relationship or status of the individual as a participant or beneficiary of an employee benefit plan."[185] This commenter also suggested deleting the phrase "you receive from an affiliate" in the introduction to proposed § 247.20(c). In this commenter's view, the proposed exception should have permitted an employer or plan sponsor to share information with its affiliates in order to offer other financial services, such as brokerage accounts or IRAs, to its employees. This commenter also requested clarification on whether the exception applies only if related to products offered as an employee benefit.

182 See § 248.121(c)(1).

183 See supra Part III.C.17.

184 See §§ 248.120(q)(2)–(3) for examples illustrating situations in which a pre-existing business relationship exists and situations in which a pre-existing business relationship does not exist.

We decline to adopt the changes suggested by this commenter and adopt the employee benefit exception, redesignated as § 248.121(c)(2), as proposed. The focus of the rule is on facilitating communications "to an individual for whose benefit the [Covered Person] provides employee benefit or other services," which more closely tracks the statutory language than the alternative language proposed by the commenter.

Moreover, we note that the only type of Covered Person to whom Section 624 of the FCRA might apply is one that receives eligibility information from an affiliate.[186] The FCRA thus makes clear that the exceptions in Section 624(a)(4) were meant to apply to persons that otherwise would be subject to Section 624. In the case of the employee benefit exception, the person using the information is also "the person provid[ing] employee benefit or other services pursuant to a contract with an employer."[187] Therefore, this exception, like the other provisions of Regulation S-AM, should apply only to a Covered Person that uses eligibility information it receives from an affiliate to make marketing solicitations to consumers about its products or services.[188]

c. Service Provider Exception

Proposed § 247.20(c)(3) provided that the notice and opt out requirements of Regulation S-AM would not apply when the eligibility information is used to perform services for another affiliate. The exception would not have applied if the other affiliate was not permitted to make or send marketing solicitations on its own behalf, for example as a result of the consumer's prior

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185 See FSR Letter.

186 The statutory preface to the exceptions provides that "[t]his section shall not apply to a person" using information to do certain enumerated things. See 15 U.S.C. 1681s-3(a)(4).

187 15 U.S.C. 1681s-3(a)(4)(B).

decision to opt out. Thus, under the proposal, when the notice has been provided to a consumer and the consumer has opted out, a receiving affiliate subject to the consumer's opt out election could not circumvent the opt out by instructing the communicating affiliate or another affiliate to make or send marketing solicitations to the consumer on its behalf.[189]

One commenter urged the Commission to adopt this exception.[190] Others suggested conforming it to the statutory provision by deleting the references to marketing solicitations on behalf of service providers.[191] One of these commenters maintained that these references would impose additional burdens and costs on companies that use a single affiliate to provide various administrative services to other affiliates and would make it more difficult to provide general educational materials to consumers.[192] One commenter also asked the Commission to clarify that the limitation in FCRA Section 624(a)(4)(C) only applies to the service provider exception.[193]

We are adopting the service provider exception, redesignated as § 248.121(c)(3), substantially as proposed. We have eliminated the references to marketing solicitations made by a service provider on its own behalf. The general rule in § 248.121(a)(1) prohibits a service provider from using eligibility information it received from an affiliate to make marketing solicitations to a consumer about its own products or services unless the consumer is given notice and an opportunity to opt out and has not opted out, or unless one of the other exceptions applies.

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188 There is no corresponding example for this provision.

189 Similarly, this exception would not permit a service provider to make marketing solicitations on its own behalf if eligibility information is communicated and the FCRA's affiliate marketing notice and opt out provisions otherwise would apply.

190 See ICBA Letter.

191 See FSR Letter; MetLife Letter.

192 See FSR Letter.

193 See MetLife Letter.

The service provider exception simply allows a service provider to do what the affiliate on whose behalf it is acting may do, such as using shared eligibility information to make marketing solicitations to consumers to whom the affiliate is permitted to make such marketing solicitations.[194] Nothing in the service provider and pre-existing business relationship exceptions will prevent an affiliate that has a pre-existing business relationship with the consumer from relying upon the service provider exception, as long as the arrangement satisfies the requirements of the rule and applicable exceptions. To help clarify the scope of the service provider exception, § 248.121(d)(2) provides two examples.[195]

d. Consumer-Initiated Communication Exception

Proposed paragraph (c)(4) of § 247.20 provided that the notice and opt out requirements would not have applied when eligibility information was used in response to a communication initiated by the consumer. This exception could have been triggered by an oral, electronic, or written communication initiated by the consumer. To be covered by the proposed exception, any use of eligibility information would need to be responsive to the communication initiated by the consumer. Paragraph (d)(2) of the proposed rule provided three examples of situations that would and would not meet the exception.[196]

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194 As discussed above, the final rule does not include the word "make" because "making" and "sending" solicitations are distinct activities and this provision of the statute uses the verb "to send." See supra Part II.B.

195 Sections 248.121(b)(4) and 248.121(b)(5) are consistent with comparable provisions of the Joint Rules and the FTC Rule, 72 FR 62922-24 and 72 FR 61435-37, respectively.

196 Proposed § 247.20(d)(2)(i) provided that the exception would apply when a consumer holding an account with an institution calls the institution's affiliate for information about the affiliate's products and services, leaving contact information with the affiliate. Proposed § 247.20(d)(2)(ii) provided that the exception would not apply when a consumer did not initiate a communication but rather called an affiliate back after the affiliate made an initial marketing call and left a message for a consumer. Proposed § 247.20(d)(2)(iii) provided that the exception would not (continued)

Five commenters addressed this exception.[197] One commenter suggested that the Commission delete the phrase "orally, electronically, or in writing,"[198] while another suggested modifying it to read "whether orally, electronically, or in writing."[199] Other commenters objected to requiring the use of eligibility information to be "responsive" to the communication initiated by the consumer.[200] In their view, the concept of "responsiveness" would create a vague standard and encourage a narrow reading of the exception. Another commenter stated that the Commission did not and could not provide a clear definition of what would be "responsive" and opined that this standard would cause a Covered Person to be uncertain as to their compliance.[201] One commenter asserted that consumers may not be familiar with the various types of products or services available to them and the different affiliates that offer those products or services and may rely on the institution to inform them about available options.[202] For this reason, the commenter maintained that the exception should not limit an affiliate from responding with solicitations about any product or service. This commenter also stated that the Senate bill that preceded the FACT Act used more restrictive language in this exception than the final legislation passed by Congress.

Some commenters objected to the example in proposed § 247.20(d)(2)(ii), stating that a consumer responding to a call-back message should qualify as a consumer-initiated

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apply when a consumer called an affiliate asking for retail locations without asking about the affiliate's products and services.

197 See Coalition Letter; ICBA Letter; SIFMA Letter I; Wells Fargo Letter; USAA Letter.

198 See Coalition Letter.

199 See ICBA Letter.

200 See Wells Fargo Letter; USAA Letter.

201 See Coalition Letter.

communication and noting that the consumer has the option of not returning the call.[203] One commenter expressed concern about the example in proposed paragraph (d)(2)(iii) regarding the consumer who calls to ask for retail locations and hours, and stated that this would create a vague standard that would be difficult to apply and subject to differing interpretations.[204]

After considering the comments, we are adopting paragraphs (c)(4) and (d)(2) of proposed § 247.20 with some modifications, redesignated as §§ 248.121(c)(4) and (d)(3), respectively. The final rule eliminates the reference to oral, electronic, or written communications. Any form of communication may come within the exception as long as the consumer initiates the communication, whether in-person or by mail, e-mail, telephone, facsimile, or through other means.

Section 248.121(c)(4) provides that the communications covered by the exception must be consumer-initiated and must concern a Covered Person's products or services. The FCRA requires a person relying on the exception to use eligibility information only "in response to" a communication initiated by a consumer.[205] The Commission believes that the exceptions should be construed narrowly to avoid undermining the general rule requiring notice and opt out. Thus, consistent with the purposes of the FCRA, the Commission does not believe that a consumer-initiated communication unrelated to a Covered Person's products or services should trigger the

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202 See Wells Fargo Letter.

203 See SIFMA Letter I; Wells Fargo Letter; Coalition Letter.

204 See ICBA Letter. The commenter, however, did not explain why it thought the example was vague.

205 See 15 U.S.C. 1681s-3(a)(4)(D). The Commission believes this statutory language contemplates that the consumer-initiated communications will relate to a Covered Person's products or services, and that the marketing solicitations covered by the exception will be those made in response to that communication.

exception. A rule that allowed any consumer-initiated communication, no matter how unrelated to a Covered Person's products or services, to trigger the exception would not give meaning to the phrase "in response to" and could produce incongruous results. For example, if a consumer calls a broker-dealer to ask about retail locations and hours, but does not request information about its products or services, the broker-dealer may not use eligibility information it receives from an affiliate to make marketing solicitations to the consumer because the consumer-initiated communication does not relate to the broker-dealer's products or services. The use of eligibility information received from an affiliate would not be responsive to the communication, and the exception would not apply.

However, the Commission recognizes that if a consumer-initiated conversation turns to a discussion of products or services the consumer may need, marketing solicitations may be responsive if the consumer agrees to receive marketing materials and provides or confirms contact information by which he or she can receive those materials. For example, if a consumer calls a broker-dealer to ask about retail locations and hours, the broker-dealer's customer service representative asks the consumer if there is a particular product or service about which the consumer is seeking information, the consumer responds affirmatively and expresses an interest in mutual funds offered by the broker-dealer, the customer service representative offers to provide that information by telephone and mail additional information to the consumer, and the consumer agrees and provides or confirms contact information for receipt of the materials to be mailed, the broker-dealer may use eligibility information it receives from an affiliate to make marketing solicitations to the consumer about mutual funds because such marketing solicitations would respond to the consumer-initiated communication about mutual funds.

Likewise, if a consumer who has opted out of an affiliate's use of eligibility information to make marketing solicitations calls the affiliate for information about a particular product or service, (i.e., life insurance), marketing solicitations regarding that specific product or service could be made in response to that call, but marketing solicitations regarding other products or services could not. Because marketing solicitations will likely be made quickly, we do not believe it is appropriate to adopt a specific time limit for making solicitations following a consumer-initiated communication about products or services.

We are adopting the example in proposed § 247.20(d)(2)(i), redesignated as § 248.121(d)(3)(i), and modified to delete the references to a telephone call as the specific form of communication and the reference to providing contact information. As discussed above and illustrated in the examples in §§ 248.120(q)(2)(v) and (vi), the need to provide contact information may vary depending on the form of communication used by the consumer. A new example in § 248.121(d)(3)(ii) illustrates a situation involving a consumer-initiated communication in which a consumer does not know exactly what products, services, or investments he or she wants, but initiates a communication to obtain information about investing for a child's college education. We are adopting the call-back example in proposed § 247.20(d)(2)(ii), redesignated as § 248.121(d)(3)(iii) and modified to illustrate that when a Covered Person makes an initial marketing call without using eligibility information received from an affiliate and leaves a message that invites the consumer to receive information about the Covered Person's products and services by calling a toll-free number, the consumer's response qualifies as a consumer-initiated communication about a product or service. The modified example is intended to avoid requiring Covered Persons to track which calls are call-backs.[206]

We are adopting the retail hours example in proposed § 247.20(d)(2)(iii) substantially as proposed and redesignated as § 248.121(d)(3)(iv). We are also adopting a new example in § 248.121(d)(3)(v) to address the situation where a consumer calls to ask about retail locations and hours and a call center representative, after eliciting information about the reason the consumer wants to visit a retail location, offers to provide information about products of interest to the consumer by telephone and mail, and the consumer agrees and provides or confirms contact information. This example demonstrates how a conversation may develop to the point where making marketing solicitations would be responsive to the consumer's call.

e. Consumer Authorization or Request Exception

Proposed § 247.20(c)(5) provided that the notice and opt out requirements would not apply when the information is used to make marketing solicitations that have been affirmatively authorized or requested by the consumer.[207] We contemplated that this provision could be triggered by an oral, electronic, or written authorization or request by the consumer but indicated that a pre-selected check box would not constitute an affirmative authorization or request.[208] In addition, we noted that boilerplate language in a disclosure or contract would not have constituted an affirmative authorization.[209] The exception in proposed paragraph (c)(5) could have been triggered, for example, if a consumer opens a securities account with a broker-dealer

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206 Although the Commission received no specific comment regarding tracking call-backs, we have revised § 248.121(d)(3)(iii) in order to be consistent with the changes made by the Agencies in response to comments they received.

207 See Proposing Release at 69 FR 42309.

208 Id.

209 Id.

and authorizes or requests marketing solicitations about insurance from an insurance affiliate of the broker-dealer. Under the proposed exception, the consumer could have provided the authorization or made the request either through the Covered Person with whom he or she has a business relationship or directly to the affiliate that would make the marketing solicitation.[210] The duration of the authorization or request would have depended on the facts and circumstances. Proposed § 247.20(d)(3) provided an example of the affirmative authorization or request exception.

Some commenters noted that the proposed exception would have required an "affirmative" authorization or request but that the FCRA did not.[211] One commenter indicated that the proposal did not indicate how the authorization would be affirmative.[212] Another commenter indicated that inclusion of the term "affirmative" in the exception would have introduced uncertainty as to what would constitute an authorization or request by the consumer, and stated that the term should be deleted.[213] Other commenters asserted that a pre-selected check box should be sufficient to evidence a consumer's authorization or request for marketing solicitations.[214] In their view, a consumer's decision not to deselect a pre-selected check box should constitute a knowing act of the consumer to authorize or request marketing solicitations if

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210 Nothing in this exception supersedes the restrictions on telemarketing contained in rules of self-regulatory organizations, the Federal Communications Commission, or in the TSR, including the operation of the "Do-Not-Call List" established by the FTC and the Federal Communications Commission.

211 See ACLI Letter; SIFMA Letter I; Wells Fargo Letter. See also 15 U.S.C. 1681s-3(a)(4)(E).

212 See Wells Fargo Letter.

213 See SIFMA Letter I. However, the commenter did not provide an example of how this would create uncertainty.

214 See ICBA Letter; USAA Letter; Wells Fargo Letter.

the boxes are properly used.[215] Other commenters stated that preprinted language in a disclosure or contract should be sufficient to evidence a consumer's authorization or request for marketing solicitations.[216] Another commenter requested that the Commission clarify that a consumer's authorization or request does not have to refer to a specific product or service or to a specific provider of products or services in order for the exception to apply.[217]

We are adopting § 247.20(c)(5), redesignated as § 248.121(c)(5), substantially as proposed but without the word "affirmative." This change does not affect the meaning of the exception and the consumer still must take steps to "authorize" or "request" marketing solicitations. The GLBA and the implementing privacy rules include an exception to permit the disclosure of nonpublic personal information "with the consent or at the direction of the consumer."[218] Section 624 of the FCRA creates an exception to permit the use of shared eligibility information "in response to solicitations authorized or requested by the consumer." The Commission interprets the "authorized or requested" provision in the FCRA exception to require the consumer to take affirmative steps in order to trigger the exception despite deletion of the term from the rule. The Commission construes this exception, like the other exceptions, narrowly and in a manner that does not undermine Regulation S-AM's general notice and opt out requirement. In this regard, affiliated companies cannot avoid use of the FCRA's notice and opt out requirement by including preprinted boilerplate language in the disclosures or contracts they

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215 See USAA Letter; Wells Fargo Letter.

216 See Coalition Letter. This commenter cited case law and FTC informal staff opinion letters relating to a consumer's written instructions to obtain a consumer report pursuant to Section 604(a)(2) of the FCRA as support for allowing boilerplate language to constitute authorization or request.

217 See Wells Fargo Letter.

218 See 15 U.S.C. 6802 (e)(1)(A); 17 CFR 248.14(a)(1).

provide to consumers, such as a sentence (or a pre-selected box next to a sentence) stating that by applying to open an account, the consumer authorizes or requests to receive marketing solicitations from affiliates. Such an interpretation would permit the exception to swallow the rule, a result that cannot be squared with the intent of Congress to give consumers notice and an opportunity to opt out of marketing solicitations. We are adopting the consumer authorization or request example in proposed § 247.20(d)(3), redesignated as § 248.121(d)(4)(i), with conforming changes in light of the changes made to § 248.121(c)(5). In addition, to provide more guidance, we are adopting three additional examples. The example in § 248.121(d)(4)(ii) illustrates how a consumer can authorize or request solicitations by checking a blank check box. The examples in §§ 248.121(d)(4)(iii) and (iv) illustrate that preprinted boilerplate language and a pre-selected check box would not meet the authorization or request requirement. The Commission does not believe it is appropriate to set a fixed time period for an authorization or request. As noted in the proposal, the duration of the authorization or request depends on what is reasonable under the facts and circumstances.[219] Of course, an authorization to make marketing solicitations to the consumer terminates if the consumer revokes the authorization.

For the reasons discussed in connection with the consumer-initiated communication exception, we omitted the reference to oral, electronic, or written communications from this exception. We do not believe it is necessary to clarify the elements of an authorization or request. Section 624(a)(4)(E) of the FACT Act clearly refers to "solicitations authorized or requested by the consumer." The facts and circumstances will determine what marketing solicitations have been authorized or requested by the consumer.

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219 See Proposing Release at 69 FR 42310.

f. Compliance with Applicable Laws Exception

Proposed § 247.20(c)(6) clarified that the provisions of Regulation S-AM would not apply to an affiliate if compliance with the requirements of Section 624 by the affiliate would prevent that affiliate from complying with any provision of state insurance law pertaining to unfair discrimination in a state where the affiliate is lawfully doing business.[220] The Commission received no comments on this provision and is adopting it as proposed, redesignated as § 248.121(c)(6). There is no corresponding example for this exception.

4. Relation to Affiliate-Sharing Notice and Opt Out

Proposed paragraph (f) of § 247.20 clarified the relationship between the affiliate-sharing notice and opt out opportunity required under Section 603(d)(2)(A)(iii) of the FCRA and the affiliate marketing notice and opt out opportunity required by new Section 624 of the FCRA.[221]

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220 See FCRA Section 624(a)(4).

221 In general, Section 603(d)(2)(A) of the FCRA governs the sharing of creditworthiness and similar information among affiliates. As discussed in note 5 above, the FCRA sets standards for the collection, communication, and use of information bearing on a consumer's creditworthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living. The FCRA provides that a person who communicates these forms of information to others could become a "consumer reporting agency," which is subject to substantial statutory obligations. However, a person may communicate information about its own "transactions or experiences" with a consumer without becoming a consumer reporting agency. This transaction and experience information may be communicated among affiliated persons without any of them becoming a consumer reporting agency. See FCRA Sections 603(d)(2)(A)(i) and (ii); 15 U.S.C. 1681a(d)(2)(A)(i) and (ii).

The FCRA provides that a person may communicate to its affiliates information other than transaction and experience information without becoming a consumer reporting agency if the person first gives the consumer a clear and conspicuous notice that such information may be communicated to its affiliates and an opportunity to "opt out," or block the person from sharing the information. See FCRA Section 603(d)(2)(A)(iii); 15 U.S.C. 1681a(d)(2)(A)(iii). There is some overlap between this "affiliate sharing" provision of the FCRA and the "affiliate marketing" rules that we are adopting. The two provisions are distinct, however, and they serve different purposes. Nothing in these rules regarding the limitations on affiliate marketing under Section 624 of the FCRA supersedes or replaces the affiliate sharing notice and opt out requirement contained in Section 603(d)(2)(A)(iii) of the FCRA.

Specifically, proposed paragraph (f) provided that nothing in proposed Regulation S-AM would have limited the responsibility of a company to comply with the notice and opt out provisions of Section 603(d)(2)(A)(iii) of the FCRA before it shares information other than transaction and experience information with affiliates if it wishes to avoid becoming a consumer reporting agency.

One commenter urged the Commission to delete this provision as unnecessary.[222] In the alternative, this commenter asked the Commission to confirm that Section 603(d)(2)(A)(iii) of the FCRA applies to the sharing of information that would otherwise meet the definition of a "consumer report," and that the sharing affiliate does not automatically become a consumer reporting agency, but risks becoming a consumer reporting agency.[223] In response, the Commission is clarifying that the FCRA, not Regulation S-AM, establishes the standard for defining a person as a consumer reporting agency. Accordingly, we are adopting proposed § 247.20(f), redesignated as § 248.121(e) and modified to replace the reference to becoming a consumer reporting agency with the phrase "where applicable," in order to highlight this clarification.

E. Section 248.122 Scope and Duration of Opt Out

1. Section 248.122(a)

The scope of the opt out was addressed in various sections of the proposal. Proposed § 247.21(c) provided that the notice could have allowed a consumer to choose from a menu of alternatives when opting out, such as opting out of receiving marketing solicitations from certain types of affiliates, or from receiving marketing solicitations that use certain types of information

222 See Coalition Letter.

or are delivered using certain methods of communication. If a Covered Person provided a menu of alternatives, one of the alternatives would have had to allow the consumer to opt out with respect to all affiliates, all eligibility information, and all methods of delivering marketing solicitations. Proposed § 247.25(d) described how the termination of a consumer relationship would have affected the consumer's opt out. Under the proposal, if a consumer's relationship with a Covered Person terminated for any reason when the consumer's opt out election was in force, the opt out would have continued to apply indefinitely unless revoked by the consumer. The Proposing Release indicated that the opt out would have been tied to the consumer, rather than to the information used for the marketing solicitations.[224]

Some commenters were critical of the provision requiring Covered Persons that provide a menu of alternatives, to provide the consumer with the ability to opt out with respect to all affiliates, all eligibility information, and all methods of delivery.[225] One commenter stated that this requirement should be eliminated, arguing that this requirement does not appear in the FCRA.[226] Another commenter indicated that the reference to "all eligibility information" made the provision confusing because it implied that there were various forms of eligibility information.[227] One commenter opined that this universal opt out was not Congress's intent and stated that a notice should allow opt outs on an account basis rather than an individual basis.[228]

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223 Id.

224 See Proposing Release at 69 FR 42311.

225 See ACLI Letter; Coalition Letter; FSR Letter.

226 See ACLI Letter. See also 15 U.S.C. 1681s-3(a)(2).

227 See FSR Letter. Another commenter also indicated that the "option for all eligibility information" could be interpreted to mean all eligibility information pertaining to the consumer in perpetuity. This commenter sought clarification. See Coalition Letter.

228 See Coalition Letter.

Several commenters generally opposed the indefinite opt out requirement for consumers that terminate a relationship with a person.[229]

After considering the comments, we are adopting the provision relating to the scope of the opt out, with modifications, as § 248.122(a) of Regulation S-AM. Under this section, which is modeled on Section 624(a)(2)(A) of the FCRA, the scope of the opt out depends upon the content of the opt out notice. Under § 248.122(a)(1), except as otherwise provided in that section, a consumer's election to opt out prohibits any affiliate covered by the opt out notice from using the eligibility information received from another affiliate as described in the notice to make marketing solicitations to the consumer.

Section 248.122(a)(2)(i) clarifies that, in the context of a continuing relationship, an opt out notice may apply to eligibility information obtained in connection with a single continuing relationship, multiple continuing relationships, continuing relationships established subsequent to delivery of the opt out notice, or any other transaction with the consumer. Section 248.122(a)(2)(ii) provides examples of continuing relationships. These examples are substantially similar to the examples used in the GLBA privacy rules, with added references to relationships between consumers and affiliates.[230]

Section 248.122(a)(3)(i) limits the scope of an opt out notice that is not connected with a continuing relationship. This section provides that if there is no continuing relationship between a consumer and a Covered Person or its affiliate, and if the Covered Person or its affiliate provides an opt out notice to a consumer that relates to eligibility information obtained in connection with a transaction with the consumer, such as an isolated transaction or a credit

229 See ACLI Letter; Coalition Letter; FSR Letter; ICBA Letter; SIFMA Letter I.

application that is denied, the opt out notice only applies to eligibility information obtained in connection with that transaction. The notice cannot apply to eligibility information that may be obtained in connection with subsequent transactions or a continuing relationship that may be subsequently established by the consumer with the Covered Person or its affiliate. Section 248.122(a)(3)(ii) provides examples of isolated transactions.

Section 248.122(a)(4) provides that a consumer may be given the opportunity to choose from a menu of alternatives when electing to prohibit marketing solicitations. An opt out notice may give the consumer the opportunity to elect to prohibit marketing solicitations from certain types of affiliates covered by the opt out notice but not other types of affiliates covered by the notice, marketing solicitations based on certain types of eligibility information but not other types of eligibility information, or marketing solicitations by certain methods of delivery but not other methods of delivery, so long as one of the alternatives is the opportunity to prohibit all marketing solicitations from all of the affiliates that are covered by the notice. We continue to believe that Section 624(a)(2)(A) of the FCRA requires the opt out notice to contain a single opt out option for all marketing solicitations within the scope of the notice. The Commission recognizes that consumers could receive a number of different opt out notices, even from the same affiliate. Accordingly, we anticipate monitoring industry notice practices and evaluating whether further action is needed.

Section 248.122(a)(5)(i) contains a special rule that explains the obligations with respect to notice following the termination of a continuing relationship. Under this rule, a consumer must be given a new opt out notice if, after all continuing relationships with a person or its

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[230] See, e.g., 17 CFR 248.4(c)(3).

affiliate have been terminated, the consumer subsequently establishes a new continuing relationship with that person or the same or a different affiliate and the consumer's eligibility information is to be used to make a marketing solicitation.[231] This will afford the consumer and the Covered Person a fresh start following termination of all continuing relationships by requiring a new opt out notice if a new continuing relationship is subsequently established. The new opt out notice must apply, at a minimum, to eligibility information obtained in connection with the new continuing relationship. The new opt out notice may apply more broadly to information obtained in connection with a terminated relationship and give the consumer the opportunity to opt out with respect to eligibility information obtained in connection with both the terminated and the new continuing relationships. A consumer's failure to opt out does not override a prior, but still in-effect, opt out election made by the consumer and applicable to eligibility information obtained in connection with a terminated relationship. The prior opt out would still be in effect regardless of whether the new opt out notice provided to the consumer applies to eligibility information that was obtained in connection with the terminated relationship.[232] Section 248.122(a)(5)(ii) contains an example of this special rule. The Commission notes, however, that when a consumer was not given an opt out notice in connection with the initial continuing relationship because eligibility information obtained in connection

231 This provision was designed to address comments regarding consumers that terminate a continuing relationship with a Covered Person.. See supra note 229.

232 The Agencies received comment that it was inappropriate to tie the opt out to the consumer, rather than to the information used for making marketing solicitations. Upon further examination, we conclude that tying the opt out to the consumer could have had unintended consequences. For example, if the opt out were tied to the consumer, a Covered Person would have to track the consumer indefinitely, even if the consumer's relationship with the Covered Person terminated and a new relationship with that Covered Person was not established until years later. We do not believe that Covered Persons should be required to track consumers indefinitely following termination of a relationship.

with that continuing relationship was not shared with affiliates for use in making marketing solicitations, an opt out notice provided in connection with a new continuing relationship would have to apply to any eligibility information obtained in connection with the terminated relationship that is to be shared with affiliates for use in making future marketing solicitations.

2. Section 248.122(b) Duration and Timing of Opt Out

Proposed § 247.25 addressed the duration and effect of a consumer's opt out election. Section 247.25(a) provided that a consumer's election to opt out is effective for the opt out period, which is a period of at least five years beginning as soon as reasonably practicable after the consumer's opt out election is received. Nothing in the paragraph limited the ability of Covered Persons to set an opt out period of longer than five years, including an opt out period that does not expire unless revoked by the consumer. We also stated that if for some reason, a consumer elects to opt out again while the opt out period remains in effect, a new opt out period of at least five years would begin upon receipt of each successive opt out election.

Proposed § 247.25(b) provided that a receiving affiliate could not make or send marketing solicitations to a consumer during the opt out period based on eligibility information it receives from an affiliate, except as provided in the exceptions in proposed § 247.20(c) or if the consumer had revoked his or her opt out.[233] The proposal would have tied the opt out to the consumer, not to the information.[234] Proposed § 247.25(c) clarified that a consumer could opt

233 As discussed above, proposed § 247.20(c) provided exceptions from Regulation S-AM's notice and opt out requirements in several situations, including when the receiving affiliate has a pre-existing business relationship with the consumer or receives an affirmative request for marketing solicitations from the consumer or when the receiving affiliate provides employee benefits to the consumer or performs certain services on behalf of another affiliate. See supra Part III.D.3.

234 Thus, under the proposed rules, if a consumer initially elected to opt out but did not extend the opt out upon expiration of the opt out period, the receiving affiliate could use all of the eligibility information it had received about the consumer from its affiliate, including eligibility

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out at any time. Thus, even if the consumer did not opt out in response to the initial opt out notice or if the consumer's election to opt out was not prompted by an opt out notice, the consumer could still have opted out. Regardless of when the consumer opted out, the opt out would be effective for at least five years.

Commenters generally favored the five-year opt out provisions.[235] As discussed above, most commenters were concerned with the indefinite opt out provision when a consumer terminates a relationship with a person.[236] One commenter suggested that consumers should be allowed to revoke their opt outs orally, stating this would be consistent with the FCRA's flexible approach.[237] Another commenter stated that the opt out should not be broadly tied to a consumer but should be done on an account basis.[238] This commenter also asked for clarification on the implementation date, suggesting that the "reasonably practicable" language in the provision should be clarified to mean the opt out would begin on the date the opt out is received.

We are adopting the provisions addressing the duration of the opt out as redesignated § 248.122(b), with some modifications. The final rule clarifies that the opt out period expires if the consumer revokes his or her opt out in writing, or, if the consumer agrees, electronically.

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information that it received during the opt out period. However, if the consumer subsequently opted out again some time after the initial opt out period has lapsed, the receiving affiliate could not use any eligibility information about the consumer it received from an affiliate on or after the mandatory compliance date, including any information it received during the period in which no opt out election was in effect. See Proposing Release at 69 FR 42311.

Section 624(a)(5) of the FCRA contains a non-retroactivity provision, which provides that nothing shall prohibit the use of information that was received prior to the date on which persons are required to comply with the regulations implementing Section 624. 15 U.S.C. 1681s-3(a)(5).

235 See ACLI Letter; Coalition Letter; FSR Letter; ICBA Letter; SIFMA Letter I.

236 See supra Part III.E.1.

237 See ACLI Letter.

238 See Coalition Letter.

This is consistent with the approach taken in the GLBA privacy rules. We do not believe it is necessary or appropriate to permit oral revocations. Many of the exceptions to Regulation S-AM's notice and opt out provisions may be triggered by oral communications, as discussed above, which would permit the use of shared eligibility information to make marketing solicitations pending receipt of a written or electronic revocation. Also, as noted in the proposal, nothing prohibits setting an opt out period longer than five years, including an opt out period that does not expire unless revoked by the consumer.[239]

The Commission does not agree that the opt out period should begin on the date the consumer's election to opt out is received. We interpret the FACT Act requirement to mean that the consumer's opt out election must be honored for a period of at least five years from the date the election is implemented. We believe that Congress did not intend for the opt out period to be shortened to a period of less than the five years specified in the statute to reflect the time between the date the consumer's opt out election is received and the date the consumer's opt out election is implemented.

The Commission also believes that it is neither necessary nor appropriate to set a mandatory deadline for implementing the consumer's opt out election. A general standard better reflects that the time it will reasonably take to implement a consumer's opt out election may vary depending on the facts and circumstances of the situation.

Consistent with the special rule for a notice following termination of a continuing relationship, the duration of the opt out is not affected by the termination of a continuing relationship. When a consumer opts out in the course of a continuing relationship and that

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239 See Proposing Release at 69 FR 42322.

relationship is terminated during the opt out period, the opt out remains in effect for the remainder of the opt out period. If the consumer subsequently establishes a new continuing relationship while the opt out period remains in effect, the opt out period may not be shortened with respect to information obtained in connection with the terminated relationship by sending a new opt out notice to the consumer when the new continuing relationship is established, even if the consumer does not opt out upon receipt of the new opt out notice. A person may track the eligibility information obtained in connection with the terminated relationship and provide a renewal notice to the consumer, or may choose not to use eligibility information obtained in connection with the terminated relationship to make marketing solicitations to the consumer.

3. Section 248.122(c)

Proposed § 247.25(c) clarified that a consumer could opt out at any time.[240] As explained in the proposal, even if the consumer did not opt out in response to the initial opt out notice or if the consumer's election to opt out was not prompted by an opt out notice, a consumer could still opt out. Regardless of when the consumer opted out, the opt out would have had to be effective for a period of at least five years. We received no comment on this provision and are adopting it as proposed, redesignated as § 248.122(c).

F. Section 248.123 Contents of Opt Out Notice; Consolidated and Equivalent Notices

1. Section 248.123(a)

a. Joint Notice

Proposed § 247.21 addressed the contents of the affiliate marketing opt out notice, and proposed § 247.24(c) permitted joint notices with affiliates identified in the notice with respect to

240 See Proposing Release at 69 FR 42311.

which the notice was accurate. Proposed § 247.21(a) would have required the opt out notice to be clear, conspicuous, and concise, and to accurately disclose: (1) that the consumer may elect to limit a person's affiliate from using eligibility information about the consumer that the affiliate obtains from the person to make marketing solicitations to the consumer; and (2) if applicable, that the consumer's election will apply for a specified period of time and that the consumer will be allowed to extend the election once that period expires. The notice also would have had to provide the consumer with a reasonable and simple method to opt out.[241] Under the proposal, use of the proposed model forms in the proposed Appendix A, while not required, would have complied with proposed § 247.21(a) in appropriate circumstances. We received one comment on this section that urged the Commission to clarify that a Covered Person would not have to send an additional notice if the Covered Person initially provided an opt out of limited duration and then determined to increase the length of time of the duration or make the opt out permanent.[242]

We are adopting proposed § 247.21(a), redesignated as § 248.123(a) with some modifications to enhance the clarity and usability of the model notices. We are also incorporating provisions of proposed § 247.24(c), pertaining to joint notices.[243] Paragraph (a)(1)(i) provides that all opt out notices must provide the name of the affiliate or affiliates

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241 Proposed § 247.21(a) reflected the intent of Congress, as expressed in Section 624(a)(2)(B) of the FCRA, that a notice required by Section 624(a)(2)(B) must be "clear, conspicuous, and concise," and the method for opting out be "simple."

242 See T. Rowe Price Letter.

243 Proposed § 247.24(c)(1) permitted a person to provide a joint opt out notice with one or more of its affiliates, so long as the notice is accurate with respect to each affiliate that issues the joint notice. Section 248.123(a)(1)(i) incorporates the substance of proposed § 247.24(c)(1) and clarifies ways in which affiliates that share a name may be identified. Proposed § 247.24(c)(2) would have permitted affiliates to provide a joint notice if the affiliates shared a common name. One commenter suggested that the rule make clear that if in a joint notice some affiliates share a (continued)

providing the notice, and allows for a joint notice by a group of affiliates. If affiliates share a common name, such as "ABC," then the notice may indicate that it is being provided by the family or group of companies with the "ABC" name. The notice may identify the companies by stating that it is being provided by "all of the ABC companies," "the ABC banking, credit card, insurance, and securities companies," or by listing the name of each affiliate providing the notice. A representation that the notice is provided by "the ABC banking, credit card, insurance, and securities companies" applies to all companies in those categories and not just to some of those companies. If the affiliates providing the notice do not all share a common name, then the notice must either separately identify each affiliate by name or identify each of the common names used by those affiliates. For example, if the affiliates providing the notice do business under both the ABC name and the XYZ name, then the notice could list each affiliate by name or indicate that the notice is being provided by "all of the ABC and XYZ companies" or by "the ABC banking and securities companies and the XYZ insurance companies." Section 248.123(a)(1)(ii) provides that an opt out notice must contain a list of the affiliates or types of affiliates covered by the notice. The notice may apply to multiple affiliates and to companies that become affiliates after the notice is provided to the consumer. The rules for identifying the affiliates covered by the notice are substantially similar to the rules for identifying the affiliates providing the notice in § 248.123(a)(1)(i) described above.

Sections 248.123(a)(1)(iii)–(vii) require the opt out notice to include: (1) a general description of the types of eligibility information that may be used to make marketing solicitations to the consumer; (2) a statement that the consumer may elect to limit the use of

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common name and other affiliates do not, the notice may identify those affiliates with a common (continued) eligibility information to make marketing solicitations to the consumer; (3) a statement that the consumer's election will apply for the specified period of time stated in the notice and, if applicable, that the consumer will be allowed to renew the election once that period expires; (4) if the notice is provided to consumers who may have previously opted out, such as if a notice is provided to consumers annually, a statement that the consumer who has chosen to limit marketing offers does not need to act again until the consumer receives a renewal notice; and (5) a reasonable and simple method for the consumer to opt out. The requirement in § 248.123(a)(1)(vi) to include a statement regarding consumers who may have previously opted out would be satisfied by appropriate use of the model forms in the Appendix.[244] These forms, unlike the model forms in the proposed Appendix, include a statement that can be used in a notice given to a consumer who may have previously opted out to advise the consumer that he or she does not need to act again until he or she receives a renewal notice. The Commission continues to believe that the opt out notice must specify the length of the opt out period, if one is provided. However, an institution that subsequently chooses to increase the duration of the opt out period that it previously disclosed or honor the opt out in perpetuity has no obligation to provide a revised notice to the consumer. In that situation, the result is the same as if the institution established a five-year opt out period and then did not send a renewal notice at the end of that period. A person receiving eligibility information from an affiliate would be prohibited from using that information to make marketing solicitations to a consumer unless a renewal

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name as a group. See T. Rowe Price Letter.

244 The Commission, the Agencies, and the CFTC have proposed a model privacy form in a joint rulemaking. See Interagency Proposal for Model Privacy Form Under the Gramm-Leach-Bliley Act, Exchange Act Release No. 55497 (Mar. 20, 2007); 72 FR 14940 (Mar. 29, 2007). This model privacy form is intended to meet the notice content requirements of Regulation S-AM.

notice is first provided to the consumer and the consumer does not renew the opt out. So long as no marketing solicitations are made using eligibility information received from an affiliate, there would be no violation of the FCRA or Regulation S-AM for failing to send a renewal notice in this situation.

b. Joint Relationships

Proposed § 247.24(d)(1) set out rules that would have applied when two or more consumers (referred to in the proposed regulation as "joint consumers") jointly obtained a product or service, such as a joint securities account.[245] It also provided several examples. Under the proposed rules, a Covered Person could have provided a single opt out notice to joint accountholders that would have had to indicate whether the Covered Person would treat an opt out election by one joint accountholder as applying to all of the associated accountholders, or whether each accountholder would have to opt out separately. The Covered Person could not have required all accountholders to opt out before honoring an opt out direction by one of the joint accountholders. In addition, we provided an example in proposed paragraph (d)(2) to explain how the rules would operate and noted that while the example was patterned after similar provisions in the GLBA privacy rules as promulgated in Regulation S-P,[246] they differed from the GLBA privacy rules in that Section 624 of the FCRA deals with the use of information for marketing by affiliates, rather than the sharing of information among affiliates.

In the proposal, we requested specific comment on proposed paragraph (d)(1)(vii) and the example in paragraph (d)(2)(iii) that addressed the situation in which only one of two joint consumers had opted out. Under those paragraphs, in a joint consumer situation, if A had opted

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[245] See Proposing Release at 69 FR 42321.

out only for A, and B did not opt out, we indicated that a Covered Person's affiliate could use eligibility information about B to send marketing solicitations to B as long as the eligibility information was not based on A and B's joint consumer relationship. One commenter argued that this approach would be overly restrictive and challenging to implement because exclusion of joint account information could block information about both a customer who had decided to opt out and one that had not.[247] According to this commenter, Covered Persons should be able to use information about joint accounts to make marketing solicitations to the consumer who had decided not to opt out.

We are adopting proposed paragraphs (d)(1) and (d)(2) of § 247.24 with modifications, redesignated as § 248.123(a)(2). However, in light of the comment received, we are not adopting the example of joint relationships in proposed § 247.24(d)(2) because it addressed, in part, the sharing of information rather than the use of information to make marketing solicitations, and thus would be beyond the scope of this rulemaking. In addition, we have also made some technical changes to improve readability and promote consistency with the GLBA privacy rules.[248]

c. Alternative Contents

Proposed § 247.21(d) provided that if a person chose to give consumers a broader opt out

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246 See 17 CFR 248.7(d).

247 See T. Rowe Price Letter.

248 Some implementation issues may arise from providing a single opt out notice to joint consumers in the context of this rule (which focuses on the use of information) and in the context of other privacy rules (which focus on the sharing of information). For example, a consumer may opt out with respect to affiliate marketing in connection with an individually-held account, but not opt out with respect to affiliate marketing in connection with a joint consumer account. In that situation, it could be challenging to identify which consumer information may and may not be used by affiliates to make marketing solicitations to the consumer.

right than required by law, the person could modify the contents of the opt out notice to reflect accurately the scope of the opt out right it had provided. Proposed Model Form A-3 of Appendix A provided guidance for Covered Persons wishing to allow consumers to prevent all marketing from that person and its affiliates. We received no comments on this provision and are adopting it as proposed, redesignated as § 248.122(a)(3). We are adopting proposed Model Form A-3, redesignated as Model Form A-5 with slight modifications for clarity.

d. Model Notices

Section 248.123(a)(4) provides that model notices are in the Appendix. The Commission has provided model notices to facilitate compliance with the rule, although the final rules do not require their use.

2. Coordinated, Consolidated, and Equivalent Notices

Proposed § 247.27 provided that a notice required by proposed Regulation S-AM could be coordinated and consolidated with any other notice or disclosure required to be issued under any other provision of law.[249] We indicated that these notices could include but were not limited to the affiliate sharing and opt out notices described in Section 603(d)(2)(A)(iii) of the FCRA[250] and the privacy notices required by Title V of the GLBA. We further noted that a notice or other disclosure that was equivalent to the notice required by the proposal, and that was provided to a consumer together with disclosures required by any other provision of law, would satisfy the requirements of the proposed rule.

We requested comment on whether persons subject to the proposed rules would plan to consolidate their affiliate marketing notices with GLBA privacy notices or affiliate sharing opt

249 This is consistent with Section 624(b) of the FCRA. See also 15 U.S.C. 1681s-3 note.

out notices, whether we provided sufficient guidance on consolidated notices, and whether consolidation would be helpful or confusing to consumers. While one commenter expressed general support for the provision,[251] another stated that, while financial institutions may consider consolidating the affiliate marketing notice with the GLBA privacy notice, the decision to consolidate would be affected by the five-year duration of the affiliate marketing opt out.[252] However, the commenter did not specify whether this would make a firm more or less likely to consolidate notices. However, because Covered Persons are only encouraged to consolidate affiliate marketing notices with other notices they are required to provide, the Commission is, with the exception of technical changes made for clarity, adopting the consolidated and equivalent notice provisions as proposed, redesignated as §§ 248.123(b) and (c).

We encourage Covered Persons to consolidate their affiliate marketing opt out notice with GLBA privacy notices, including any affiliate sharing opt out notice under Section 603(d)(2)(A)(iii) of the FCRA, so that consumers receive a single notice they can use to review and exercise all applicable opt outs. We recognize, however, that special issues arise when these notices are consolidated. For example, the affiliate marketing opt out may be limited to a period of at least five years, subject to renewal, while the GLBA privacy and affiliate sharing opt out notices are not time-limited. This difference, if applicable, must be made clear to the consumer. Thus, if a Covered Person uses a consolidated notice and the affiliate marketing opt out is limited in duration, the notice must inform consumers that if they previously opted out, they do not need to opt out again until they receive a renewal notice when the opt out expires or is about to expire.

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250 See discussion of FCRA Section 603(d)(2)(A)(iii) supra note 221.

251 See Coalition Letter.

252 See FSR Letter.

In addition, as discussed more fully below, the Commission and the Agencies, in a joint rulemaking, have proposed a model privacy form that includes an affiliate marketing opt out.[253] The proposed model privacy form is designed to satisfy the requirement to provide an affiliate marketing opt out notice.

G. Section 248.124 Reasonable Opportunity to Opt Out

1. Section 248.124(a)

Proposed § 247.22(a) provided that the communicating affiliate would have to provide a consumer a "reasonable opportunity to opt out" after delivery of the opt out notice but before a marketing solicitation based on eligibility information is sent. We noted that because of the various circumstances in which opt out rights are provided, a "reasonable opportunity to opt out" should be generally construed to avoid setting a mandatory waiting period. A general standard would provide flexibility to allow receiving affiliates to use eligibility information to make marketing solicitations at an appropriate point in time, while assuring that the consumer is given a realistic opportunity to prevent such use of the information. We received no comments on proposed § 247.22(a) and are adopting it substantially as proposed, redesignated as § 248.124(a) with technical changes for clarity.

2. Section 248.124(b)

Proposed §§ 247.22(b)(1) through (5) provided examples of what might constitute a reasonable opportunity to opt out in different situations. Proposed §§ 247.22(b)(1) and (2) provided examples of reasonable opportunities to opt out by mail or by electronic means

[253] See supra note 244.

consistent with the examples used in the GLBA privacy rules.[254] Both examples illustrated that giving consumers 30 days in which to decide whether to opt out would be reasonable in most cases. Proposed § 247.22(b)(3) provided an example of a reasonable opportunity to opt out when the consumer was required to decide as a necessary part of proceeding with an electronic transaction, whether to opt out before completing the transaction.[255] Proposed paragraph (b)(4) of § 247.22 provided that including the affiliate marketing opt out notice in a notice under the GLBA privacy rules could satisfy the reasonable opportunity standard.[256] Proposed paragraph (b)(5) provided that an "opt-in" would satisfy the reasonable opportunity to opt out requirement, as long as a consumer's affirmative consent is documented.[257] We sought comment on whether additional guidance or examples were needed regarding the reasonable opportunity to opt out.

A number of commenters addressed the 30-day safe harbor.[258] Some commenters stated

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254 See 17 CFR 248.7(a)(3)(i)–(ii).

255 Under this proposed example, the Covered Person provided a simple process of opting out at the Internet Web site where the transaction was occurring. The opt out notice was automatically provided to the consumer, such as through the use of a mandatory link to an intermediate Web page, or "speed bump." The consumer was given a choice of either opting out or not opting out at that time through a simple process conducted at the Internet Web site. In this situation we indicated that a consumer could be required to check a box on the Internet Web site in order to opt out or decline to opt out before continuing with the transaction. However, this example would not have included a situation in which the consumer was required to send a separate e-mail or visit a different Internet Web site in order to opt out.

256 In this situation, the consumer would be allowed to exercise the opt out in the same manner and with the same amount of time to exercise the opt out as with respect to the GLBA privacy notice. This example takes into account the statutory requirement that we consider methods for coordinating and combining notices. See FACT Act Section 214(b)(3).

257 In the proposal, we noted that some persons subject to Regulation S-AM might have a policy of not allowing affiliates to use eligibility information for marketing purposes unless a consumer affirmatively consented, or "opted in," to receiving such marketing solicitations. However, we also noted that a pre-selected check box on a Web form or boilerplate language in a standard contract or disclosure document would not be evidence of the consumer's affirmative consent.

258 See Coalition Letter; FSR Letter; ICBA Letter.

that it would provide consumers with a reasonable opportunity to opt out.[259] Others were concerned that the time period would be viewed as a de facto minimum even though we had stated it would not.[260] Most commenters however, objected to informing the consumer that he or she has a specific period of time by which to respond,[261] citing a lack of Congressional intent,[262] customer confusion,[263] and unnecessary compliance burdens if Covered Persons decided to consolidate the GLBA notices with the Regulation S-AM notice.[264] While we received no specific comment on the opportunity to opt out by mail provision, one commenter stated that requiring consumers to acknowledge receipt of notices sent electronically, as in proposed § 247.22(b)(2), would violate the Electronic Signatures in Global and National Commerce Act ("E-Sign Act").[265] In addition, one commenter suggested broadening the scope of proposed § 247.22(b)(3) to include all transactions.[266] This commenter also opined that proposed paragraphs (b)(4) and (b)(5) were inconsistent, appearing to equate an opt in with obtaining an opt out for the purposes of the proposal, and urged the Commission to omit the opt-in example. Another commenter did not agree that pre-selected boxes would be an unacceptable method for obtaining customer authorization, if used properly.[267]

We are adopting §§ 247.22(b)(1) and (b)(3) substantially as proposed, redesignated as

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259 See FSR Letter; Wells Fargo Letter.

260 See Coalition Letter; ICBA Letter.

261 See ACLI Letter; Coalition Letter; FSR Letter; ICBA Letter.

262 See Coalition Letter.

263 See ACLI Letter; ICBA Letter.

264 See Coalition Letter.

265 See ACB Letter. The E-Sign Act is codified at 15 U.S.C. Chapter 96.

266 See Coalition Letter.

267 See USAA Letter.

§§ 248.124(b)(1) and (3). We are retaining the 30-day safe harbor because it helps afford certainty to entities that choose to follow the 30-day waiting period. We understand, however, that shorter waiting periods may be adequate under certain facts and circumstances in accordance with the general test for a reasonable opportunity to opt out.

The final rule divides proposed § 247.22(b)(2) into two subparts, redesignated as §§ 248.124(b)(2)(i) and (ii), to illustrate the different means of delivering an electronic notice. The example illustrates that for notices provided electronically, such as at an Internet Web site at which the consumer has obtained a product or service, a reasonable opportunity to opt out would include giving the consumer 30 days after the consumer acknowledges receipt of the electronic notice to opt out by any reasonable means. The acknowledgement of receipt aspect of this example is consistent with an example in the GLBA privacy regulations.[268] The example also illustrates that for notices provided by e-mail to a consumer who had agreed to receive disclosures by e-mail from the person sending the notice, a reasonable opportunity to opt out would include giving the consumer 30 days after the e-mail is sent to elect to opt out by any reasonable means. Consumer acknowledgement is not necessary when the consumer has agreed to receive disclosures by e-mail. Moreover, the electronic delivery of affiliate marketing opt out notices does not require consumer consent in accordance with the E-Sign Act because neither Section 624 of the FCRA nor these final rules require that the notice be provided in writing. Persons that provide electronic affiliate marketing opt out notices under Regulation S-AM may do so pursuant to the agreement of the consumer, as specified in these rules, or in accordance with the requirements of the E-Sign Act.

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268 See 17 CFR 248.9(b)(1)(iii).

We agree with commenters that the example regarding electronic transactions in redesignated § 248.124(b)(3) is limited in scope, and have added a new example for in-person transactions in § 248.124(b)(4). Together, these examples illustrate that an abbreviated opt out period is appropriate when the consumer is given a "yes" or "no" choice and is not permitted to proceed with the transaction unless he or she makes a choice.[269]

We received no comments on proposed § 247.22(b)(4), which provides that an affiliate marketing opt out notice can be included in a GLBA privacy notice, and are adopting it substantially as proposed, redesignated as § 248.124(b)(5). We are not adopting the example in proposed § 247.22(b)(5) that would have illustrated the option of providing a consumer with an opportunity to "opt in" to affiliate marketing because the example was unnecessary and confusing.

H. Section 248.125 Reasonable and Simple Methods of Opting Out

Proposed § 247.23(a) provided guidance on how a person could provide consumers with reasonable and simple methods of opting out. These examples generally track the examples of reasonable opt out means from Section 7(a)(2)(ii) of the GLBA privacy rules,[270] with certain modifications to give effect to Congress's mandate in the FACT Act that the method of opting out of affiliate marketing must also be "simple." Accordingly, the example in proposed § 247.23(a)(2) contemplated the use of a self-addressed envelope with which the consumer could mail his or her reply form and opt out notice. If consumers were given the choice of calling a

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269 For in-person transactions, consumers could be provided with a form that requires them to write "yes" or "no" to indicate their opt out preference, or a form that contains two blank check boxes: one to opt out and one not to opt out. Of course, if an opportunity to opt out is to be reasonable, a consumer must be permitted to choose freely whether to opt out or not, and must not be induced to forego his or her right to opt out.

270 See, e.g., 17 CFR 248.7(a)(2)(ii).

toll-free telephone number to opt out, the example contemplated that the system would be adequately designed and staffed to enable consumers to opt out with a single phone call.[271]

Proposed § 247.23(b) provided examples of opt out methods that would not be considered reasonable and simple. These methods include requiring the consumer to write a letter or to call or write to obtain an opt out form that was not included with the notice. A consumer who agrees to receive the opt out notice in electronic form only, such as by electronic mail or at an Internet Web site, would have to be allowed to opt out by the same or a substantially similar electronic form and should not be required to opt out solely by telephone or paper mail.

Eight commenters addressed these examples,[272] and generally agreed that the examples of the use of oral opt outs were reasonable and simple methods.[273] One commenter stated that consumers should also be able to orally revoke their opt outs.[274] Some commenters requested that the Commission clarify that this section is intended only to provide examples and is not mandatory.[275] Another commenter suggested that we delete the examples of methods that did not provide a reasonable and simple method of opting out, stating that these examples could expose Covered Persons to civil liability.[276] Other commenters objected to the reference to self-

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271 See Proposed § 247.23(a)(4).

272 See ACLI Letter; Coalition Letter; FSR Letter; IAA Letter; ICBA Letter; ICI Letter; T. Rowe Price Letter; Wells Fargo Letter.

273 See FSR Letter; IAA Letter; ICI Letter; T. Rowe Price Letter.

274 See FSR Letter.

275 See ICBA Letter; Coalition Letter.

276 See Wells Fargo Letter.

addressed envelopes.[277] One stated that a self-addressed envelope was unnecessary and inconsistent with Congress's intent because it was not required by the statute or necessary for GLBA notices.[278] Another commenter asserted that Covered Persons would view the use of a self-addressed envelope as a requirement.[279] This commenter opined that consumers would use the envelopes for other purposes, like sending remittances or address change forms, which would have "disastrous" consequences including unavoidable delays and lapsed notices.

Other commenters addressed electronic opt outs.[280] One commenter viewed the proposed requirement for the opt out to be electronic when the notice is electronic as arbitrary, stating that a similar requirement is not imposed on opt out notices sent by mail.[281] Another commenter opined that this requirement was not intended by Congress and requested that we adopt the GLBA rule examples.[282] Finally, some commenters believed that a company that provides a reasonable and simple method of opting out should not be required to honor an opt out through a different mechanism.[283]

We are adopting § 247.23, redesignated as § 248.125, revised as discussed below. Paragraph (a) provides the general rule that Covered Persons must not use eligibility information from an affiliate in order to make marketing solicitations to a consumer unless the consumer has been provided with a reasonable and simple method to opt out. Paragraph (b) provides examples

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277 See ACLI Letter; FSR Letter.

278 See FSR Letter.

279 See ACLI Letter.

280 See Coalition Letter; Wells Fargo Letter.

281 See Wells Fargo Letter.

282 See Coalition Letter.

283 See Coalition Letter; ICBA Letter.

illustrating opt out methods that are reasonable and simple, as well as examples that are not.[284]

We decline to follow commenters' suggestion that we adopt the GLBA examples without change. Section 624 of the FCRA requires the Commission to ensure that the consumer is given reasonable and simple methods of opting out. The GLBA did not require simple methods of opting out, although the Commission sought to provide examples of simple methods in the GLBA privacy rules. Most of the examples we are adopting are substantially similar to those in proposed § 247.23, but have been revised for clarity. We are retaining the examples in proposed §§ 247.23(a)(1) and (3), redesignated as § 248.125(b)(1)(i) and (iii), respectively. The example in § 248.125(b)(1)(ii) has been revised to reflect our understanding that the reply form and self-addressed envelope would be included together with the opt out notice and to clarify that the example is not mandatory. We do not find commenters' other views on this example to be persuasive. As in the proposal, the example in § 248.125(b)(1)(iv) contemplates that a toll-free telephone number that consumers may call to opt out would be adequately designed and staffed to enable consumers to opt out in a single phone call. In setting up a toll-free telephone number that consumers may use to exercise their opt out rights, institutions should minimize extraneous marketing or other messages directed to consumers who are in the process of opting out.

One new example in § 248.125(b)(1)(v) illustrates that reasonable and simple methods include allowing consumers to exercise all of their opt out rights described in a consolidated opt out notice that includes GLBA privacy, FCRA affiliate sharing, and FCRA affiliate marketing opt outs, by a single method, such as calling a single toll-free telephone number. This example furthers the Commission's statutory directive to ensure that notices and disclosures may be

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284 The examples of specific methods identified in the final rules are not an exhaustive list of (continued)

coordinated and consolidated.[285]

We have retained the examples of opt out methods that are not reasonable and simple in proposed §§ 247.23(b)(1) through (b)(3), redesignated as §§ 248.125(b)(2)(i) through (b)(2)(iii) respectively. The example redesignated as § 248.125(b)(2)(iii) has been slightly modified to illustrate that it is not reasonable or simple to require a consumer who receives the opt out notice in electronic form, such as through posting at an Internet Web site, to opt out solely by paper mail or solely by visiting a different Web site without providing a link to that site. We did not find the commenters' views on these examples to be persuasive.

In order to be consistent with the Joint Rules and the FTC rule,[286] the Commission has added new § 248.125(c), which clarifies that a consumer may be required to opt out through a specific means, as long as that means is reasonable and simple for the consumer. This section corresponds to a provision in Regulation S-P.[287]

I. Section 248.126 Delivery of Opt Out Notices

Paragraph (a) of proposed § 247.24 provided that a person covered by the proposed rule would have needed to deliver its opt out notice so that each consumer reasonably could be expected to receive actual notice. An electronically delivered opt out notice could have been delivered either in accordance with the electronic disclosure provisions in proposed Regulation S-AM or in accordance with the E-Sign Act.[288] The proposed rule included an example where a Covered Person could e-mail its affiliate marketing notice to consumers who had previously

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permissible methods.

285 See 15 U.S.C. 1681s(b).

286 See Joint Rules at 72 FR 62935; FTC Rule at 72 FR 61448.

287 See 17 CFR 248.7(a)(2)(iv).

agreed to the electronic delivery of information and could provide the notice on its Internet Web site for consumers who obtain products or services electronically through that Web site. One commenter expressed concern over the proposed requirement that the consumer acknowledge receipt of the notice as a necessary step to obtaining a particular product or service.[289] The commenter viewed this as inconsistent with the E-Sign Act.

Proposed § 247.24(b) provided examples of fulfilling the expectation of actual notice. We indicated that the "reasonable expectation of delivery" standard is a lesser standard than actual notice. For instance, if a communicating affiliate mailed a printed copy of its notice to the last known mailing address of a consumer, it would have met its obligation even if the consumer has changed addresses and never received the notice. One commenter expressed support for this standard.[290]

We are adopting § 247.24, redesignated as § 248.126, with modifications. We retained the reasonable expectation of actual notice standard, and the examples of a reasonable expectation of actual notice for an electronic notice have been revised and divided into two sets of examples of what does and does not meet the requirement.[291] The examples in paragraphs (b)(3)–(4) of § 248.126 illustrate that a consumer may reasonably be expected to receive actual notice if the affiliate providing the notice provides a notice by e-mail to a consumer who has agreed to receive electronic disclosures by e-mail from the affiliate providing the notice, or posts the notice on the Internet Web site at which the consumer obtained a product or service

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288 See 15 U.S.C. 7001, et seq.

289 See ACB Letter.

290 See Coalition Letter.

291 This is consistent with the approach taken in paragraph (b) of § 248.124.

electronically and requires the consumer to acknowledge receipt of the notice. Conversely, the examples in paragraphs (c)(2)–(c)(3) of § 248.126 illustrate that a consumer may not reasonably be expected to receive actual notice if the affiliate providing the notice sends the notice by e-mail to a consumer who has not agreed to receive electronic disclosures by e-mail from the affiliate providing the notice, or posts the notice on an Internet Web site without requiring the consumer to acknowledge receipt of the notice.

As discussed above, the Commission has determined that the electronic delivery of opt out notices does not require consumer consent in accordance with the E-Sign Act because nothing in Section 624 of the FCRA requires the notice to be provided in writing. Thus, we believe that requiring an acknowledgement of receipt is not inconsistent with the E-Sign Act. Moreover, this example is consistent with an example in the GLBA privacy rules and is appropriate, particularly where the notice is posted on an Internet Web site.

Unlike the Agencies, the Commission did not receive requests to require the mandatory delivery of electronic notices by e-mail. Like the Agencies, however, we decline to do so. The Commission agrees with the Agencies that concerns about unsolicited e-mail and the security of e-mail make it inappropriate to require e-mail as the only permissible form of electronic delivery for opt out notices.

J. Section 248.127 Renewal of Opt Out Elections

Proposed § 247.26 described procedures for extending an opt out. Proposed paragraph (a) of § 247.26 required consumers to be provided with a new notice and a reasonable opportunity to extend their opt out before a receiving affiliate could make marketing solicitations based on the consumer's eligibility information upon expiration of the opt out period. The affiliate that initially provided the notice, or its successor, would provide the extension notice. If an extension notice were not provided to the consumer, the opt out period would continue indefinitely. The requirement to provide an extension notice upon expiration of the opt out period would apply to any opt out – even if, for example, the consumer failed to opt out initially and informed the communicating affiliate of his or her opt out at some later time. The consumer could extend the opt out at the expiration of each successive opt out period. Proposed paragraph (b) of § 247.26 provided that each opt out extension would be effective for a period of at least five years, in compliance with proposed § 247.25.

Proposed § 247.26(c) addressed the contents of an extension notice.[292] Like the initial notice, an extension notice would have to be clear, conspicuous, and concise. Proposed paragraph (c) provided some flexibility in the design and contents of the notice. Under one approach, the notice could have accurately disclosed the same items required to be disclosed in the initial opt out notice under proposed § 247.21(a), along with a statement explaining that the consumer's prior opt out had expired or was about to expire, as applicable, and that the consumer would have to opt out again if he or she wished to keep the opt out election in force. Under another approach, the extension notice could have provided: (1) that the consumer previously elected to limit affiliates from using eligibility information about the consumer to make marketing solicitations to the consumer; (2) that the consumer's election had expired or was about to expire, as applicable; (3) that the consumer could have elected to extend his or her previous election; and (4) a reasonable and simple method for the consumer to extend the opt out. We requested comment regarding whether persons subject to proposed Regulation S-AM would plan to limit the duration of the opt out, and on the relative burdens and benefits of providing limited or unlimited opt out periods.

Proposed § 247.26(d) addressed the timing of the extension notice and provided that an extension notice could be delivered to the consumer either a reasonable period of time before an opt out period expired, or any time after the opt out period expired, but before covered marketing solicitations were made to the consumer. Requiring the extension notice a reasonable period of time before the opt out period expired was intended to facilitate the smooth transition of consumers who choose to change their elections. An extension notice given too far in advance of the expiration of the opt out period might confuse consumers. We did not propose to set a fixed time for what would constitute a "reasonable period of time," noting that a reasonable period of time could depend upon the amount of time given to the consumer for a reasonable opportunity to opt out, the amount of time necessary to process opt outs, and other factors. Nevertheless, we stated that providing an extension notice in combination with the last annual privacy notice required by the GLBA that was provided to the consumer before expiration of the affiliate marketing opt out period would have been reasonable in all cases. Proposed § 247.26(e) made clear that sending an extension notice to a consumer before the expiration of the opt out period would not shorten the five-year opt out period.

We also noted that opt out elections under the GLBA do not expire, and that GLBA notices typically state that a consumer need not opt out again if the consumer previously opted out. We recognized that including an affiliate marketing opt out notice or an extension notice in combination with an initial or annual notice under the GLBA required complying with both FCRA and GLBA requirements as applicable. Under the proposal, if a person chose to make the

[292] Covered Persons are not required to provide extension notices if they treat the consumer's opt (continued)

affiliate marketing opt out effective in perpetuity, the statement in the GLBA notice would have remained correct. However, the GLBA notice would not have been accurate with respect to the extension notice if the affiliate marketing opt out were limited to a defined period of five or more years. In that case, the extension notice regarding affiliate marketing would have had to make clear to the consumer the necessity of opting out again in order to extend the opt out. We requested comment on this interaction between the FACT Act and GLBA notices, including whether the Commission should provide further guidance regarding how a communicating affiliate might ensure that the difference in opt out rights is clear to consumers.

Commenters expressed concern that the extension notice would differ from the initial notice because the extension notice would be required to inform the consumer that the consumer's prior opt out had expired or was about to expire, as applicable, and that the consumer would have to opt out again to keep the opt out election in force.[293] In their view, this additional disclosure would have been costly and have provided little benefit to consumers. One commenter maintained that the additional disclosure would make it difficult, if not impossible, to combine the extension notice with the GLBA privacy notice.[294]

The Commission is adopting proposed § 247.26, redesignated as § 248.127, with modifications as discussed below. The final rules also replace the references to "extension" with references to a "renewal" notice.

Section 248.127(a) provides that after an opt out period expires, a person may not make marketing solicitations to a consumer who previously opted out unless the consumer has been

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out election as valid in perpetuity unless revoked by the consumer.

293 See Coalition Letter; ICBA Letter.

294 See ICBA Letter.

given a compliant renewal notice and a reasonable opportunity to opt out, and the consumer does not renew the opt out. This section also clarifies that a person can make marketing solicitations to a consumer after expiration of the opt out period if one of the exceptions in § 248.121(c) applies.

Section 248.127(a)(2) addresses the opt out renewal period. We continue to believe it is not necessary to set a fixed minimum period of time for a reasonable opportunity to renew the opt out, and that doing so would be inconsistent with the approach taken in other sections of Regulation S-AM and in the GLBA privacy rules. We received no comment regarding the minimum five-year period duration of the renewed opt out and are adopting this provision as proposed. Section 248.127(a)(3) states that a renewal notice must be provided either by the affiliate (or its successor) who provided the previous opt out notice, or as part of a joint renewal notice from two or more members of an affiliated group of companies, or their successors, that jointly provided the previous opt out notice. This provision balances the goal of ensuring that the notice is provided by an entity known to the consumer with the need to provide a degree of flexibility to recognize changes in corporate structure that may occur over time.

In the proposal, we recognized that the content of the extension or renewal notice would differ from the content of the initial notice. We note that while the statute does not require that affiliate marketing initial and opt out renewal notices be identical, it does require that the Commission provide guidance to ensure that opt out notices are clear, conspicuous, and concise. We find it unreasonable to expect a consumer, after receiving a renewal notice, to remember that he or she previously opted out five years ago (or longer). We also find it unreasonable to expect a consumer who remembers opting out to know that he or she must opt out again in order to renew that decision. To ensure that a consumer receives a meaningful renewal notice, the consumer must be: (1) reminded that he or she previously opted out; (2) informed that the previous opt out has expired or is about to expire; and (3) advised that to continue to limit solicitations from affiliates, he or she must renew the previous opt out. The renewal notice can state that "the consumer's election has expired or is about to expire." The final rule omits the words "as applicable" to clarify that the notice does not have to be tailored to differentiate consumers for whom the election "has expired" from those for whom the election "is about to expire."

The Commission does not agree with the commenters who indicated that the renewal notice's additional content frustrates the combination of FCRA affiliate marketing opt out notices with GLBA privacy notices. Even if the language of the renewal notice were identical to the initial notice, it still could be difficult to avoid honoring a consumer's opt out in perpetuity if the opt out notice is incorporated into the GLBA privacy notice. GLBA privacy notices often state that if a consumer has previously opted out, it is not necessary for the consumer to opt out again. This statement is accurate for affiliate marketing if the consumer's opt out will be honored in perpetuity, but is inaccurate if an affiliate marketing opt out, included as part of the notice, will be effective only for a limited period of time, subject to renewal by the consumer in five-year intervals. Thus, if an affiliate marketing opt out notice were consolidated with a GLBA privacy notice and affiliate marketing opt outs were effective only for a limited period of time, the notice would have to be modified to make clear that statements about the consumer not needing to opt out again do not apply to the affiliate marketing renewal notice. Therefore, the Commission does not believe that requiring a renewal notice to contain information not included in an initial notice will significantly affect the ability to incorporate affiliate marketing opt out notices into GLBA privacy notices because consolidation of the notices is most likely to occur when the affiliate marketing opt out will be honored in perpetuity. Entities that prefer not to provide renewal notices may do so by honoring the consumer's opt out in perpetuity. We therefore are adopting § 247.26(b) substantially as proposed, but redesignated as § 248.127(b) with revisions that reflect the changes to § 248.123, as discussed above.[295]

Proposed § 247.26(d) addressed the timing of the extension or renewal notice. We received no comment on this section and are adopting it substantially as proposed, redesignated as § 248.127(d).[296] Proposed § 247.26(e) addressed the effect of an extension or renewal notice on the existing opt out period. We received no comment on this section and are adopting it substantially as proposed, redesignated as § 248.127(d), with some modifications.[297]

K. Section 248.128 Effective Date, Compliance Date, and Prospective Application

1. Section 248.128(a) and (b)

In the Proposing Release, we recognized that some institutions may want to combine their affiliate marketing opt out notice with their next annual GLBA privacy notice. Twelve commenters addressed the effective and mandatory compliance dates.[298] These commenters believed that the mandatory compliance date should be delayed until some time after the effective date of the final rules. The commenters suggested various periods for delaying the

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295 These changes relate to identification of the affiliates or group of affiliates providing the opt out, descriptions of the types of eligibility information that may be used and the ability of the consumer to limit the use of that information, as well as other requirements that make the opt out notice reasonable and simple.

296 We have changed the reference from "extension" to "renewal" of a notice and deleted "before any affiliate makes or sends" as unnecessary. Proposed § 247.26(d)(2) is now referred to as "Combination with annual privacy notice" in § 248.127(c)(2) and clarified for ease of reference.

297 The phrase "to a period of less than 5 years" has been omitted as unnecessary.

298 See ACB Letter; ACLI Letter; AIA Letter; Coalition Letter; FSR Letter; IAA Letter; ICBA Letter; ICI Letter; Metlife Letter; SIFMA Letter I; T. Rowe Price Letter; USAA Letter.

mandatory compliance date from six, 12,[299] 15,[300] and 18 months.[301] In addition, they argued that a delayed mandatory compliance date was necessary in order to make significant changes to business practices and procedures, to implement necessary operational and systems changes, and to design and provide affiliate marketing opt out notices. Commenters also noted that many institutions would like to send the affiliate marketing notices with their initial or annual GLBA privacy notices, both to minimize costs and to avoid consumer confusion. These commenters noted that many large institutions provide GLBA privacy notices on a rolling basis, and indicated that a delayed mandatory compliance date was necessary to enable institutions to introduce affiliate marketing opt out notices into this cycle. A few industry commenters believed that Congress knew that an effective date is not necessarily the same as a mandatory compliance date because banking regulations commonly have effective dates and mandatory compliance dates that differ.

Regulation S-AM becomes effective approximately 30 days after publication in the Federal Register.[302] Compliance with Regulation S-AM is required not later than January 1, 2010.[303] The mandatory compliance date is delayed to give Covered Persons a reasonable amount of time to include the affiliate marketing opt out notice with their initial and annual privacy notices.[304] This is consistent with the FCRA's directive that notices may be consolidated

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299 See ACB Letter; AIA Letter; Coalition Letter; ICBA Letter; Metlife Letter.

300 See IAA Letter; T. Rowe Price Letter.

301 See ACLI Letter.

302 See § 248.128(a).

303 See § 248.128(b).

304 In the proposal, we indicated that the final rules would become effective six months after the date on which they were issued in final form. This was consistent with the requirements of Section 624 of the FCRA. See Proposing Release at 69 FR 42302.

and coordinated. The Commission believes that delaying the mandatory compliance date until January 1, 2010 will give Covered Persons adequate time to develop and distribute opt out notices, as well as provide Covered Persons sufficient time to develop and distribute consolidated notices.

2. Section 248.128(c)

Proposed § 247.20(e) provided that Regulation S-AM would not apply to eligibility information received by a receiving affiliate prior to the required compliance date. Some commenters argued that the proposed rule did not track the statutory language or reflect the intent of Congress.[305] These commenters asserted the final rules should grandfather all information received by any financial institution or affiliate in a holding company before the mandatory compliance date, rather than grandfather only that information received before the mandatory compliance date by a person that intends to use the information to make solicitations to the consumer. In the alternative, one commenter requested that, if we adopted the rule as proposed, we clarify that any information placed into a common database by an affiliate be considered to have been provided to an affiliated person.[306] The commenter argued that without such a clarification, affiliated companies would have to undertake costly deconstruction of existing databases to ensure compliance.

We are adopting § 247.20(e) substantially as proposed, redesignated as § 248.128(c), with modifications discussed below. To address concerns expressed by commenters, the final rules clarify that a Covered Person receives eligibility information from an affiliate when the affiliate places that information in a common database that is accessible by a Covered Person, even if the

305 See ACLI Letter; Coalition Letter; Wells Fargo Letter.

Covered Person has not accessed or used that information as of the compliance date. The final rules do not apply to eligibility information placed in a common database before the mandatory compliance date by an affiliate who has a pre-existing business relationship with a consumer. The rules do apply if eligibility information is obtained by an affiliate before the mandatory compliance date and is not, before the mandatory compliance date: (1) placed into a common database that is accessible to other affiliates; or (2) provided to another affiliate. The final rules also apply to new or updated eligibility information placed in a common database after the mandatory compliance date.

IV. Appendix to Subpart B – Model Forms

Proposed Appendix A provided model forms as examples to illustrate how Covered Persons could comply with the notice and opt out requirements of Section 624 of the FCRA and proposed Regulation S-AM.[307] Proposed Appendix A included three proposed model forms. Model Form A-1 was an initial opt out notice. Model Form A-2 was an extension notice that could be used when a consumer's prior opt out has expired or was about to expire. Model Form A-3 was for persons subject to proposed Regulation S-AM to use if they offered consumers a broader right to opt out of marketing than required by law.

We stated that use of the proposed model forms would not be mandatory.[308] We also noted that persons subject to proposed Regulation S-AM could use the model forms, modify them to suit particular circumstances, or use some other form, so long as the requirements of the proposed rules were met. We noted that although Model Forms A-1 and A-2 used five years as

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306 See Coalition Letter.

307 See Proposing Release at 69 FR 42322.

308 See Proposing Release at 69 FR 42312.

the duration of the opt out period, communicating affiliates could have chosen an opt out period longer than five years and substituted the longer time period in the opt out notices. The proposal also provided an illustration in which the communicating affiliates chose to treat the consumer's opt out as effective in perpetuity and thereby omitted from the initial notice any reference to the limited duration of the opt out period or the right to extend the opt out.

Each of the proposed model forms was designed as a stand-alone form. We anticipated that some Covered Persons might want to combine the affiliate marketing opt out notice with a GLBA privacy notice. We noted that if the notices were combined, we expected that Covered Persons would integrate the affiliate marketing opt out notice with other required disclosures and avoid repetition of information such as the methods for opting out. Finally, we noted that the development of a model form that would combine the various opt out notices was beyond the scope of the proposed rulemaking. We received one comment on the model forms that generally supported the development of templates.[309] This commenter also suggested there should be a safe harbor for companies that use the model forms.

We are adopting the model forms in Appendix A of the proposal substantially as proposed, redesignated as Appendix to Subpart B – Model Forms, with additions and revisions to reflect changes incorporated in the final rules, discussed above. The model forms are designed to be helpful for entities that give notices and beneficial for consumers. As under the proposal, the model forms are provided as stand-alone documents. Persons may also choose to combine their affiliate marketing notices with other consumer disclosures, such as GLBA privacy notices.[310]

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309 See ICBA Letter.

310 On March 31, 2006, the Commission and the Agencies released a report entitled Evolution of a Prototype Financial Privacy Notice prepared by Kleimann Communication Group, Inc.,
(continued)

Creating a consolidated model form is beyond the scope of this rulemaking. However, as discussed above, institutions can combine affiliate marketing opt out notices with other disclosures, including GLBA privacy and opt out notices. If a combined model notice is adopted, we would expect the use of that model to satisfy the requirement to provide an initial affiliate marketing opt out notice.[311] As adopted, the Appendix includes five model forms. Model Form A-1 is for an initial notice provided by a single affiliate. Model Form A-2 is for an initial notice provided as a joint notice from two or more affiliates. Model Form A-3 is for a renewal notice provided by a single affiliate. Model Form A-4 is for a renewal notice provided as a joint notice from two or more affiliates. Model Form A-5 is for a voluntary "no marketing" opt out.

While use of the model forms is not mandatory, appropriate use of the model forms satisfies the requirement in Section 624 of the FCRA that Covered Persons provide notices that are "clear, conspicuous, and concise."[312] As adopted, the model forms state that a consumer's opt out election applies either for a fixed number of years or for "at least 5 years." This revision

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summarizing research that led to the development of a prototype short-form GLBA privacy notice. This report is available at http://www.ftc.gov/privacy/privacyinitiatives/FTCFinalReportExecutiveSummary.pdf. That prototype included an affiliate marketing opt out notice. The prototype assumed that the notice would be provided by the affiliate that is sharing eligibility information. The Commission believes that providing model forms in this rule for stand-alone opt out notices that may be used in a more diverse set of circumstances than a model privacy form is appropriate and consistent with efforts to develop a model privacy form. On March 29, 2007, the Commission, the Agencies, and the CFTC published for public comment in the Federal Register a model privacy form based on the prototype that includes the affiliate marketing opt out notice. See supra note 244.

311 See supra Part III.F.

312 Persons may use or not use the model forms, or modify the forms, so long as the requirements of the regulation are met. For example, although some of the model forms use five years as the duration of the opt out period, an opt out period of longer than five years may be used and the longer time substituted in the opt out notices. However, Covered Persons that modify the forms or use different forms for their notice requirements should take care to ensure that their notices are clear, conspicuous, and concise.

permits Covered Persons that use a longer opt out period or that subsequently extend their opt out period to rely on the model language. The model forms also contain a reference to the consumer's right to revoke an opt out, and the model forms clarify that, with an opt out of limited duration, the consumer does not have to opt out again until a renewal notice is sent.

V. Cost-Benefit Analysis

The Commission is sensitive to the costs and benefits of its rules and understands that the rules may impose costs on Covered Persons. Regulation S-AM's requirement to provide consumers with notice and an opportunity to opt out of receiving affiliate marketing solicitations is designed to benefit consumers by enabling them to limit certain marketing solicitations from affiliated companies. In addition, the notice requirement should enhance the transparency of each Covered Person's affiliate marketing and information sharing practices.

In the proposal, we noted that the proposed rules would impose costs upon Covered Persons[313] that wish to engage in affiliate marketing based on the communication of eligibility information. Absent an exception, a Covered Person is prohibited from <u>using</u> eligibility information received from an affiliate to make marketing solicitations to consumers, unless: (1) the potential marketing use of the information has been clearly, conspicuously and concisely disclosed to the consumer; (2) the consumer has been provided a reasonable opportunity and a simple method to opt out of receiving the marketing solicitation; and (3) the consumer has not opted out.

In proposing the rules, we estimated that approximately 6,768 broker-dealers, 5,182

313 "Covered Persons" include brokers, dealers (except notice-registered broker-dealers), and investment companies, as well as investment advisers and transfer agents that are registered with the Commission.

investment companies, 7,977 registered investment advisers, and 443 registered transfer agents would be required to comply with Regulation S-AM.[314] We also indicated that a Covered Person's obligation to provide notice and opportunity to opt out would depend on the information sharing policies of that person and the marketing policies of its affiliates.[315] After considering a number of factors,[316] we estimated in the Proposing Release that approximately 10% of Covered Persons, or 2,037 respondents, would be required to provide consumers with notice and an opt out opportunity under Regulation S-AM.[317] We further estimated that 14,259 Covered Persons each would require 1 hour on average to review its information sharing and affiliate marketing policies and practices to determine whether notice and an opt out opportunity would be necessary. After assuming a cost of $125 per hour for managerial staff time, we estimated that the total one-time cost of review would be approximately $1,782,375 (14,259 x $125). We

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314 See Proposing Release at 69 FR 42313.

315 For purposes of the Paperwork Reduction Act analysis in the Proposing Release, we estimated that approximately 70% of Covered Persons have affiliates. Updated statistics reported in registration forms filed by investment advisers show that approximately 56% of registered investment advisers have a corporate affiliate, and we estimated that other Covered Persons would report a rate of affiliation similar to that reported by registered investment advisers. Id.

316 In the Proposing Release we indicated that: (1) a Covered Person that does not have affiliates or that does not communicate eligibility information to its affiliates would not be required to comply with the proposed notice and opt out requirements; (2) even if a communicating affiliate shared eligibility information, notice and opt out would not be required if the receiving affiliate did not use the information as a basis for marketing solicitations; (3) because the proposed rules allowed for a single, joint notice on behalf of a common corporate family, Covered Persons would not be required to independently provide affiliate marketing notices and opt out opportunities if they were included in an affiliate's notice; and (4) the proposed rules incorporated a number of statutory exceptions that would further reduce the number of persons required to provide affiliate marketing notices. In addition, in the Proposing Release we noted that if an institution were required to provide consumers notice and an opportunity to opt out, the notice could be combined with GLBA privacy notices or with any other document, including other disclosure documents or account statements. We expressed our expectation that most institutions that would be required to provide an affiliate marketing notice would combine that notice with some other form of communication. Id.

317 Id. at 42313-14.

estimated that, upon completion of the review, 2,037 Covered Persons actually would be required to provide a notice and an opt out opportunity, and that those persons would need an average of 6 hours to develop an initial notice and opt out form and 2 hours to design notices for new customers to receive on an ongoing basis (a total of 8 hours per affected Covered Person, or 16,296 hours). We assumed this time would be divided between senior staff, computer professionals, and secretarial staff, with review by legal professionals. Assuming an average per-hour staff cost of $95, we estimated the total cost to be $1,548,120 (16,296 x $95) in the first year. We also estimated that each of the 2,037 affected Covered Persons would spend approximately 2 hours per year (or 4,074 hours) delivering notices to new consumers and recording any opt outs that are received on an ongoing basis. Finally, we noted that these tasks would not require managerial or professional involvement; thus, we estimated an average staff cost of $40 per hour, for a total annual cost of $162,960 (4,074 x $40).[318]

We received one comment on the cost-benefit analysis, which stated that the estimates understated the compliance burden associated with Regulation S-AM.[319] The commenter indicated that the Banking Agencies estimated that it would take approximately 18 hours to prepare and distribute the initial notice to customers. It also indicated that reprogramming costs could run into the millions of dollars for the securities industry. The commenter stated that, based on the experience of the securities industry in complying with the GLBA, each firm would have to spend several hundred hours to review its information sharing and affiliate marketing policies, to provide initial notice and opt out, to design notices to be sent to new customers on an ongoing basis, to deliver the notices to customers and to record any opt outs that are received.

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318 Id. at 42314

The commenter did not provide us with specific data regarding its estimates.

The Commission recognizes that costs for developing and maintaining records of delivery of affiliate marketing notices and recording opt out elections, and costs for personal training, will vary greatly, depending on the size of a financial institution, its customer base, number of affiliates, and the extent to which the institution intends to share information. Accordingly, we have revised our estimates to make them consistent with the compliance estimates provided by the Banking Agencies in their Joint Rules,[320] to update the number of entities subject to Regulation S-AM and make the dollar costs economically current. For the purposes of the final rules, we estimate that approximately 5,561 broker-dealers, 4,586 investment companies, 11,300 registered investment advisers, and 413 registered transfer agents will be required to comply with Regulation S-AM.[321] After considering a number of factors, we estimate that approximately 10% of Covered Persons, or 2,186 respondents, will be required to provide consumers with notice and an opt out opportunity under Regulation S-AM. Moreover, we estimate that 12,242[322] Covered Persons each will require 1 hour on average to review its information sharing and affiliate marketing policies and practices to determine whether notice and an opt out opportunity is

319 See SIFMA Letter I.

320 The Banking Agencies estimated that 18 hours was reasonable but expected that figure to vary among Covered Persons. See 69 FR 42513. In the Proposing Release, the Commission estimated that the "hour burden for developing, sending and tracking the opt out notices would range from 2-20 hours, with an average of 6 hours." See Proposing Release at 69 FR 42315.

321 A Covered Person's obligation to provide notices and opt out opportunities will depend on the information sharing policies of that person and the marketing policies of its affiliates. For purposes of the Paperwork Reduction Act, we now estimate that approximately 56% of Covered Persons have affiliates. Statistics reported in registration forms filed by investment advisers show that approximately 56% of registered investment advisers have a corporate affiliate, and we estimate that other Covered Persons would report a rate of affiliation similar to that reported by registered investment advisers.

necessary. Assuming a cost of $180 per hour for managerial staff time,[323] the staff estimates that the total one-time cost of review will be approximately $2,203,560 (12,242 x $180). Once the review is complete, we estimate that 2,186 Covered Persons will be required to provide an affiliate marketing notice and an opt out opportunity, and that those persons will need an average of 18 hours to prepare an initial notice and distribute it to consumers (a total of 39,348 hours). We assume that this time will be divided between senior staff, computer professionals, and secretarial staff, with review by legal professionals. We estimate an average per-hour staff cost of $256,[324] with an estimated total cost of $10,073,088 (39,348 x $256) in the first year. We also estimate that each of the 2,186 Covered Persons will spend approximately 4 hours per year (or 8,744 hours) for creating and delivering notices to new consumers and recording any opt outs that are received on an ongoing basis. Finally, as in the Proposing Release, we note that these tasks should not require managerial or professional involvement. Thus, we estimate an average staff cost of $56 per hour,[325] for a total annual cost of $489,664 (8,744 hours x $56).[326]

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322 This estimate is based on the following calculation: (5,561 + 4,586 + 11,300 + 413 = 21,860 x .56 = 12,242).

323 This is the per hour cost of Senior Compliance Officer, who we feel will be the appropriate person to review notices. This figure is derived from See Securities Industry and Financial Markets Association, Report on Management and Professional Earnings in the Securities Industry – 2007 (2007) ("SIFMA Report"), modified by the Commission's Office of Economic Analysis to account for an 1800-hour work year, bonuses, firm size, employee benefits, and overhead.

324 This estimate is derived from averaging the per hour costs of a Programmer Analyst ($194), a Senior Database Administrator ($266), a Compliance Manager ($245), a Director of Compliance ($394), a Paralegal ($168) and a Compliance Attorney ($270). See SIFMA Report.

325 This estimate is derived from averaging the per hour costs of a Senior General Clerk ($52), a General Clerk ($40), an Administrative Assistant ($65), a Compliance Clerk ($62) and a Data Entry Clerk ($61). See SIFMA Report.

326 We note that Regulation S-AM includes several considerations that should minimize compliance costs for affected persons. First, as required by the FACT Act, Regulation S-AM allows Covered Persons to combine their affiliate marketing opt out notices with any other notice required by (continued)

VI. Paperwork Reduction Act

Certain provisions of Regulation S-AM may constitute a "collection of information" within the meaning of the Paperwork Reduction Act of 1995.[327] The Commission submitted Regulation S-AM to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11, and the OMB approved the collection of information. The title for the collection of information is "Regulation S-AM: Limitations on Affiliate Marketing," its expiration date is November 30, 2010, and its OMB control number is 3235-0609. 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.[328] Responses to these collections of information will not be kept confidential. The Commission received no comments on the PRA analysis included in its proposal to adopt Regulation S-AM.[329] We do not believe that any differences between Regulation S-AM as proposed and Regulation S-AM as adopted, including the increase in average estimated burden hours, would significantly affect the collection of information or the estimated hour burden associated with the collection of information.

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law, including the privacy notices required under the GLBA. Covered Persons are already required to provide privacy notices and to accept consumer opt out elections related to information sharing. Second, Regulation S-AM allows Covered Persons some flexibility to develop and distribute the affiliate marketing opt out notices, and to record opt out elections in the manner best suited to their business and needs. Third, Regulation S-AM is consistent and comparable with the rules proposed by the Agencies, which should provide greater certainty to Covered Persons that are part of a family of affiliated companies because such affiliated companies are subject to consistent requirements. Finally, Regulation S-AM includes examples that provide specific guidance regarding what types of policies and procedures Covered Persons could develop.

327 As amended, codified at 44 U.S.C. Chapter 35.

328 44 U.S.C. 3512.

329 See Proposing Release at 69 FR 42314-16.

A. Collection of Information

Before an affiliate may use eligibility information received from another affiliate to make marketing solicitations to a consumer, the consumer must be provided with a notice informing the individual of his or her right to opt out of such marketing. In addition, as a practical matter, Covered Persons must keep records of any opt out elections in order for the opt outs to be effective. The opt out period must last at least five years. At the end of the opt out period, the consumer must be provided with a renewal notice and a new chance to opt out before the resumption of marketing solicitations to the consumer based on the consumer's eligibility information.

Notice and opt out are only required if a Covered Person uses eligibility information from an affiliate for use in marketing solicitations. Covered Persons that do not have affiliates, or whose affiliates do not make marketing solicitations based on eligibility information received from a Covered Person, are not required to provide notice and opt out. Regulation S-AM contains a number of other exceptions as directed by Section 214 of the FACT Act, such as for situations in which the affiliate has a pre-existing business relationship with the consumer or in which the consumer requests marketing information. In the final rules, we have attempted to retain procedural flexibility and to minimize compliance burdens except as required by the terms of the FACT Act.

B. Use of Information

Section 624 of the FCRA is intended to enhance the protection of consumer financial information in the affiliate marketing context and to enable consumers to limit Covered Persons from using eligibility information they receive from an affiliate to make marketing solicitations. Regulation S-AM is necessary to fulfill the statutory mandate, in Section 214 of the FACT Act, that the Commission prescribe regulations to implement Section 624.

C. Respondents

We estimate that approximately 5,561 broker-dealers, 4,586 investment companies, 11,300 registered investment advisers, and 413 registered transfer agents will be required to comply with Regulation S-AM. However, we expect that only a fraction of all Covered Persons will be required to provide notices and opt out opportunities to consumers. First, the rules only apply to Covered Persons that have affiliates, and then only if affiliates receiving eligibility information make marketing solicitations based on the eligibility information received from a Covered Person. Based on a review of forms filed with the Commission, we estimate that approximately 56% of Covered Persons have an affiliate.[330] However, we assume that many of those Covered Persons do not communicate eligibility information to their affiliates for marketing purposes and thus will not be subject to the notice and opt out requirements of Regulation S-AM.[331] The rules also incorporate a number of statutory exceptions that further reduce the number of Covered Persons required to provide affiliate marketing notices. In addition, any notices required by Regulation S-AM can be combined with notices already required by Regulation S-P. Further, if notice is required, Regulation S-AM allows all affiliates under common ownership or control to provide a single, joint notice. Accordingly, Covered Persons that are required to provide affiliate marketing notices could be covered by a notice sent

330 This estimate is based upon statistics reported on Form ADV, the Universal Application for Investment Adviser Registration, which contains specific questions regarding affiliations between investment advisers and other persons in the financial industry. We estimate that other Covered Persons would report a rate of affiliation similar to that reported by registered investment advisers.

331 For example, professional standards require investment advisers to preserve the confidentiality of information communicated by clients or prospects. See Association for Investment Management and Research, Standards of Practice Handbook 123, 125 (1996).

by one or more affiliates, and may not be required to provide a notice independently. In light of these factors, we estimate that approximately 10% of Covered Persons, or approximately 2,186 respondents, will be required to provide consumers with notices and an opportunity to opt out under Regulation S-AM.

D. Total Annual Reporting and Recordkeeping Burdens

Every Covered Person that has one or more affiliates likely would incur a one-time burden in reviewing its policies and business practices to determine the extent to which it communicates eligibility information to affiliates for marketing purposes and whether those affiliates make marketing solicitations based on that eligibility information. This determination should be straightforward for most entities, in part because GLBA privacy regulations already require Covered Persons other than transfer agents to review their information sharing practices and disclose whether they share information with affiliates.[332] We estimate that approximately 56% of all Covered Persons, or approximately 12,242, have an affiliate. The amount of time required to review their policies will vary widely, from a few minutes for those that do not share eligibility information with affiliates to 4 hours or more for Covered Persons with more complex information sharing arrangements. We estimate that each Covered Person will require 1 hour on average to review its policies and practices, for a total one-time burden of 12,242 hours. We estimate that 2,186 Covered Persons will be required to provide notice and opt out opportunities under the rules. This process consists of several steps. First, an affiliate marketing notice would have to be created. The amount of time required to develop a notice should be reduced

332 See 17 CFR 248.6(a)(3) (initial, annual, and revised GLBA privacy notices must include "the categories of affiliates . . . to whom you disclose nonpublic personal information"). Transfer agents are subject to consistent and comparable requirements promulgated by the Agencies.

significantly by the inclusion of model forms in Regulation S-AM. Second, the notices will need to be delivered. The final rules allow that affiliate marketing notices may be combined with any other notice or disclosure required by law. We expect that most Covered Persons will combine their affiliate marketing notices with some other form of communication, such as an account statement or an annual privacy notice under the GLBA. Because those communications are already delivered to consumers, adding a brief affiliate marketing notice should not result in added costs for processing or for postage and materials.[333] Notices may be delivered electronically to consumers who have agreed to electronic communications, which should further reduce the costs of delivery. Third, as a practical matter, Covered Persons will need to keep accurate records in order to honor any opt out elections and to track the expiration of the opt out period. The number of actual notice mailings in any given year will depend on the number of consumers who do business with each affected person. For purposes of the PRA, we estimate that the hour burden for developing, sending, and tracking the opt out notices will range from 2-50 hours, with an average of 18 hours for each Covered Person (39,348 hours total).[334] We estimate that postage and materials costs for the notices would be negligible because the notices likely will be combined with other required mailings.[335]

Because the notice and opt out requirements are a prerequisite to conducting covered forms of affiliate marketing, most Covered Persons would provide notice within the first year after which compliance with Regulation S-AM is required. However, additional notices will be

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333 Because we assume that most affiliate marketing notices will be combined with other required mailings, we base our estimates on the resources required to integrate an affiliate marketing notice into another mailing, rather than on the resources required to create and send a separate mailing.

334 See discussion of new cost estimates and burden hours supra Part V.

required as new customer relationships are formed. We anticipate that many Covered Persons will ensure delivery to new consumers with a minimum of additional effort by providing or combining the notices with other documents such as account opening documents or initial GLBA privacy notices. Accordingly, we estimate an ongoing annual burden of 4 hours per year (or 8,744 hours total) for creating and delivering notices to new consumers and recording any opt outs that are received on an ongoing basis.[336]

A consumer opt out may expire at the end of five years, as long as the person that provided the initial notice provides the consumer with renewed notice and an opportunity to extend his or her opt out election before any affiliate marketing may begin.[337] Designing, sending, and recording opt out renewal notices will require additional hours and costs. However, because the initial opt out period must last for at least five years, any burden related to renewal notices would not arise within the first four years of the collection of information.

In sum, we estimate that each of approximately 12,242 Covered Persons will require an average one-time burden of 1 hour to review affiliate marketing practices (12,242 hours total). We estimate that the approximately 2,186 Covered Persons required to provide notices and opt out opportunities will incur an average first-year burden of 18 hours to provide notices and allow for consumer opt outs, for a total estimated first-year burden of 39,348 hours. With regard to

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335 See discussion of consolidated notices supra Part III.F.2.

336 See discussion of new cost estimates and burden hours supra Part V.

337 In order to ease the burden of tracking each opt out period, many affiliated persons may decide to implement an opt out period of longer than five years, including a period that never expires.

continuing notice burdens, we estimate that each of the approximately 2,186 Covered Persons required to provide notices and opt out opportunities will incur an annual burden of 2 hours to develop notices for new consumers (4,372 hours total) and an annual burden of 2 hours to deliver the notices and record any opt outs for new consumers (4,372 hours total). These estimates represent a total one-time burden of 51,590 hours (12,242 hours plus 39,348 hours) and an ongoing annual burden of 8,744 hours (4,372 hours plus 4,372 hours). We do not expect that Covered Persons will incur start-up or materials costs in addition to the staff time discussed above.

E. Retention Period for Recordkeeping Requirements

Regulation S-AM does not contain express provisions governing the retention of records related to opt outs. However, as noted above, a person subject to Regulation S-AM would need to keep some record of consumer opt outs in order to know which consumers should not receive marketing solicitations based on eligibility information. These records would need to be retained for at least as long as the opt out period of five or more years, so that the person responsible for providing the renewal notice would know when that notice is required.

F. Collection of Information is Mandatory

As noted, Covered Persons that use eligibility information from their affiliates for marketing purposes will be required to comply with the notice and opt out provisions of Regulation S-AM. Assuming that no other exception applies, the disclosure and recordkeeping requirements will be mandatory with respect to those Covered Persons.

VII. Final Regulatory Flexibility Analysis

The Commission has prepared this Final Regulatory Flexibility Analysis for Regulation S-AM in accordance with 5 U.S.C. 604.

A. Need for the Rule

Regulation S-AM implements Section 214 of the FACT Act (which added new Section 624 to the FCRA) that, in general, prohibits a person from using certain information received from an affiliate to make marketing solicitations to a consumer, unless the consumer is given notice, as well as an opportunity and a simple method to opt out, of the possibility of receiving such solicitations. Section 214 also required the Agencies and the Commission, in consultation and coordination with one another, to issue implementing regulations that are consistent and comparable to the extent possible. The objectives of Regulation S-AM are discussed in detail in the Background, Overview of Comments Received and Explanation of Regulation S-AM, and Section-by-Section Analysis at Sections I through III above. The legal basis for Regulation S-AM is Section 214 of the FACT Act,[338] as well as Sections 17, 17A, 23, and 36 of the Exchange Act,[339] Sections 31 and 38 of the Investment Company Act,[340] and Sections 204 and 211 of the Investment Advisers Act.[341] The Commission received no comments regarding the Initial Regulatory Flexibility Analysis.

B. Description of Small Entities to Which the Final Rules Will Apply

Regulation S-AM applies to any Covered Person that uses eligibility information for the purpose of making marketing solicitations. Of the entities registered with the Commission, 896 broker-dealers, 197 investment companies, 671 registered investment advisers, and 76 registered

338 Pub. L. No. 108-159, 117 Stat. 1952 (2003).

339 15 U.S.C. 78q, 78q-1, 78w, and 78mm.

340 15 U.S.C. 80a-30 and 80a-37.

341 15 U.S.C. 80b-4 and 80b-11.

transfer agents are considered small entities.[342] Only affiliated entities are subject to Regulation S-AM. We estimate that 56% of all Covered Persons have affiliates, although it is not clear whether small entities differ significantly from larger entities in their rates of corporate affiliation. While we invited comment from small entities that would be subject to the proposed rules as well as general comment regarding information that would help us to quantify the number of small entities that may be affected by Regulation S-AM, we received none.

C. Projected Reporting, Recordkeeping, and Other Compliance Requirements

Regulation S-AM requires Covered Persons to provide consumers with notice and an opportunity to opt out of affiliated persons' use of eligibility information for marketing purposes. The final rule prohibits a Covered Person from using eligibility information received from an affiliate to make marketing solicitations to consumers, unless: (1) the potential marketing use of the information has been clearly, conspicuously and concisely disclosed to the consumer; (2) the consumer has been provided a reasonable opportunity and a simple method to opt out of receiving the marketing solicitation; and (3) the consumer has not opted out.

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342 For purposes of the Regulatory Flexibility Act, under the Exchange Act a small entity is a broker or dealer that had total capital of less than $500,000 on the date of its prior fiscal year and is not affiliated with any person that is not a small entity. 17 CFR 240.0-10. Under the Investment Company Act a "small entity" is an investment company that, 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. 17 CFR 270.0-10. Under the Investment Advisers Act, a small entity is an investment adviser that: (i) manages less than $25 million in assets, (ii) has total assets of less than $5 million on the last day of its most recent fiscal year, and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that manages $25 million or more in assets, or any person that had total assets of $5 million or more on the last day of the most recent fiscal year. 17 CFR 275.0-7. A small entity in the transfer agent context is defined to be any transfer agent that (i) received less than 500 items for transfer and less than 500 items for processing during the preceding six months: (ii) transferred only items of issuers that would be deemed "small businesses" or "small organizations" under Rule 0-10 under the Exchange Act; (iii) maintained master shareholder files that in the aggregate contained less than 1,000 shareholder accounts at all times during the
(continued)

For those entities that provide the Section 624 notice in consolidation with other documents such as notices provided under the GLBA or other federally mandated disclosures, the final rules impose very limited additional reporting or recordkeeping requirements. However, for Covered Persons that choose to send the notices separately, the reporting and recordkeeping requirements and other compliance requirements may be more substantial. Although the final rules do not include specific recordkeeping requirements, in practice some system of recordkeeping must exist to ensure that any consumer opt outs are honored.

There are a number of features of the FACT Act's affiliate marketing provisions as implemented by Regulation S-AM that limit its scope. First, the law only applies to the use of eligibility information by affiliates for the purpose of making marketing solicitations. Thus, affiliates that make marketing solicitations based solely upon their own information or without regard to eligibility information are not affected by this law. Second, the law provides exceptions to its notice and opt out requirements that permit Covered Persons to market to consumers with whom they have a "pre-existing business relationship" or from whom they have received a request for information. Third, § 248.123(a)(1)(i) allows a single, joint notice to be sent to a consumer on behalf of multiple affiliates.

A number of alternatives exist that could reduce the costs associated with compliance with Regulation S-AM. First, significant cost savings may be obtained by consolidating affiliate marketing notices with GLBA privacy notices or with other documents provided to consumers such as account statements. In addition, the model forms could be used for opt out notices that comply with the requirements of the rules. Regulation S-AM also permits Covered Persons to

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preceding fiscal year; and (iv) is not affiliated with any person (other than a natural person) that (continued) reduce the need for ongoing tracking by offering a permanent opt out from both the sharing of information between affiliates and from receiving marketing based on such sharing, which would be consistent with both the GLBA and FCRA notice and opt out requirements as well as with the FACT Act's notice and opt out requirements. Small entities may wish to consider whether consolidation of their privacy and affiliate marketing notices and opt out forms can reduce their compliance costs. Similar considerations can reduce the burden of providing affiliate marketing notices to new consumers. For example, as long as the notices remain clear, conspicuous, and concise,[343] small entity Covered Persons can combine affiliate marketing notices with account opening documents or initial privacy notices provided under the GLBA in order to ensure that affiliate marketing notices are delivered to new consumers without substantial additional efforts on the part of the Covered Person.

The Commission was concerned about the potential impact of the proposed rules on small entities and requested comment on: (1) the potential impact of any or all of the provisions in the proposed rules, including any benefits and costs, that the Commission should consider; (2) the costs and benefits of any alternatives, paying special attention to the effect of the proposed rules on small entities in light of the above analysis; (3) costs to implement and to comply with the proposed rules, including any expenditure of time or money for, for example, employee training, legal counsel, or other professional time, for preparing and processing the notices; and (4) costs to record and track consumers' elections to opt out. We received no comments on these issues.

D. Identification of Other Duplicative, Overlapping, or Conflicting Federal Rules

With the exception of the opt out for affiliate sharing under Section 603(d)(2)(A)(iii) of

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is not a small business or small organization under Rule 0-10. 17 CFR 240.0-10.

the FCRA, we have not identified any federal statutes or regulations that duplicate, overlap, or conflict with Regulation S-AM. As discussed previously, while there is some overlap between Regulation S-AM and the affiliate sharing provisions of the FCRA and the notice provisions of Regulation S-P, we expect that Covered Persons will consolidate the notice provisions of Regulation S-AM, the affiliate sharing provisions of the FCRA and the privacy notice provisions of Regulation S-P.[344] We sought and received no comment regarding any other statute or regulation, including state or local statutes or regulations, that would duplicate, overlap, or conflict with the proposed rules.

E. Agency Actions to Minimize Effects on Small Entities

The Regulatory Flexibility Act directs the Commission to consider significant alternatives that would accomplish the stated objectives of a rule while minimizing any significant adverse impact on small businesses. In connection with Regulation S-AM, the Commission considered the following alternatives: (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance and reporting requirements under the proposed rules for small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the proposed rules, or any part thereof, for small entities.

The Commission does not believe that an exemption from coverage or special compliance or reporting requirements for small entities would be consistent with the mandates of the FACT Act. Section 214 of the FACT Act addresses the protection of consumer privacy, and consumer

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343 See § 248.123(a).

344 See discussion of overlap of Regulation S-AM with the affiliate sharing provisions of the FCRA supra Parts II.B and III.

privacy concerns do not depend on the size of the entity involved. However, we have endeavored throughout the final rules to minimize the regulatory burden on all Covered Persons, including small entities, while meeting the statutory requirements. Small entities should benefit from the existing emphasis on performance rather than design standards throughout the final rules and the use of examples, including model forms for affiliate marketing notices. The Commission solicited and received no comment on any alternative system that would be consistent with the FACT Act but would minimize the impact on small entities.

VIII. Consideration of Burden on Competition, and Promotion of Efficiency, Competition, and Capital Formation

Section 23(a)(2) of the Exchange Act[345] requires the Commission, in adopting rules under the Exchange Act, to consider the impact that the rules may have upon competition. Regulation S-AM, which implements Section 214 of the FACT Act, applies to all brokers, dealers, investment companies, registered investment advisers, and registered transfer agents. Each of these entities must provide notice and an opportunity to opt out to customers before an affiliate uses eligibility information to make marketing solicitations to consumers. Because other entities will be subject to substantially similar affiliate marketing and opt out notice rules adopted by the Agencies,[346] all financial institutions will have to bear costs of implementing the rules or substantially similar rules. We do not believe the rules will result in anti-competitive effects. Other affiliated persons that make marketing solicitations using eligibility information received from a Covered Person subject to Regulation S-AM or the substantially similar rules of the Agencies will be subject to substantially similar requirements. Therefore, all persons that engage

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345 15 USC 78w(a)(2).

346 <u>See</u> Joint Rules and FTC rule.

in affiliate marketing based on eligibility information will be required to bear the costs of implementing the rules or substantially similar rules. Although these costs may vary among persons subject to the various affiliate marketing rules, we do not believe that the costs would be significantly greater for any particular entity or entities based on which affiliate marketing rule applies to that entity.

Section 3(f) of the Exchange Act,[347] Section 202(c) of the Investment Advisers Act, and Section 2(c) of the Investment Company Act[348] require the Commission, when engaging in rulemaking to consider or determine whether an action is necessary or appropriate in the public interest, to consider whether the action will promote efficiency, competition, and capital formation. We solicited comment on these issues but received none.[349] The rules will result in additional costs for Covered Persons and their affiliates, which may affect their efficiency. As discussed above, however, the rules and the model forms should promote efficiency by minimizing compliance costs. The ability of Covered Persons and their affiliates to use joint notices should further promote efficiency by facilitating the use of notices already prepared by affiliates and the allocation of compliance and notice delivery costs among affiliates. The rules and model forms also should promote competition among Covered Persons and between Covered Persons and other types of entities subject to the affiliate marketing rules of the Agencies by providing a common set of requirements relating to the use of eligibility information for affiliate marketing purposes. We are not aware of any effect the final rules will have on capital formation.

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347 15 USC 78c(f).

348 15 USC 80a-2(c).

349 See Proposing Release at 69 FR 42318.

IX. Statutory Authority

The Commission is adopting Regulation S-AM and making conforming, technical amendments to Regulation S-P under the authority set forth in Section 214 of the FACT Act,[350] Sections 17, 17A, 23, and 36 of the Exchange Act,[351] Sections 31 and 38 of the Investment Company Act,[352] and Sections 204 and 211 of the Investment Advisers Act.[353]

X. Text of Final Rules

List of Subjects in 17 CFR Part 248

Affiliate marketing, Brokers, Consumer protection, Dealers, Investment advisers, Investment companies, Privacy, Reporting and recordkeeping requirements, Securities, Transfer agents.

For the reasons stated in the preamble, the Securities and Exchange Commission amends 17 CFR part 248 as follows:

1. The authority citation for part 248 is revised to read as follows:

Authority: 15 U.S.C. 78q, 78q-1, 78w, 78mm, 80a-30, 80a-37, 80b-4, 80b-11, 1681s-3 and note, 1681w(a)(1), 6801-6809, and 6825.

2. The heading for part 248 is revised to read as follows:

Part 248 – REGULATIONS S-P AND S-AM

3. In part 248, remove each reference to "this part" and add the reference "this subpart" in its place.

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350 Pub. L. No. 108-159, Section 214, 117 Stat. 1952 (2003).

351 15 U.S.C. 78q, 78q-1, 78w, and 78mm.

352 15 U.S.C. 80a-30 and 80a-37.

353 15 U.S.C. 80b-4 and 80b-11.

§ 248.3 [Amended]

4. In § 248.3, amend paragraphs (a)(1), (a)(2) and (p) by removing the reference "G-L-B Act" and adding the reference "GLBA" in its place.

5. Remove the heading of subpart A of part 248 and add in its place the following undesignated center heading: "Privacy and Opt Out Notices".

6. Remove the heading of subpart B of part 248 and add in its place the following undesignated center heading: "Limits on Disclosures".

7. Remove the heading of subpart C of part 248 and add in its place the following undesignated center heading: "Exceptions".

8. Remove the heading of subpart D of part 248 and add in its place the following undesignated center heading: "Relation to Other Laws; Effective Date".

Subpart A – Regulation S-P: Privacy of Consumer Financial Information and Safeguarding Personal Information

9. Designate §§ 248.1 through 248.30 as subpart A by adding the heading to read as set forth above.

10. Reserve §§ 248.31 through 248.100 in subpart A.

Appendix B to Subpart A – Sample Clauses

11. Appendix A to part 248 is redesignated as Appendix B to subpart A and the heading is revised to read as set forth above.

12. New Appendix A to Subpart A is added and reserved to read as follows:

Appendix A to Subpart A – Forms

[Reserved]

13. Subpart B (§§ 248.101 through 248.128 and Appendix to Subpart B) is added to

part 248 to read as follows:

Subpart B – Regulation S-AM: Limitations on Affiliate Marketing

248.101 Purpose and scope.

248.102 Examples.

248.103 – 248.119 [Reserved]

248.120 Definitions.

248.121 Affiliate marketing opt out and exceptions.

248.122 Scope and duration of opt out.

248.123 Contents of opt out notice; consolidated and equivalent notices.

248.124 Reasonable opportunity to opt out.

248.125 Reasonable and simple methods of opting out.

248.126 Delivery of opt out notices.

248.127 Renewal of opt out elections.

248.128 Effective date, compliance date, and prospective application.

Appendix to Subpart B – Model Forms

Subpart B – Regulation S-AM: Limitations on Affiliate Marketing.

§ 248.101 Purpose and scope.

(a) Purpose. The purpose of this subpart is to implement section 624 of the Fair Credit Reporting Act, 15 U.S.C. 1681, et seq. ("FCRA"). Section 624, which was added to the FCRA by section 214 of the Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159, 117 Stat. 1952 (2003) ("FACT Act" or "Act"), regulates the use of consumer information received from an affiliate to make marketing solicitations.

(b) Scope. This subpart applies to any broker or dealer other than a notice-registered broker or dealer, to any investment company, and to any investment adviser or transfer agent registered with the Commission. These entities are referred to in this subpart as "you."

§ 248.102 Examples.

The examples in this subpart are not exclusive. The examples in this subpart provide guidance concerning the rules' application in ordinary circumstances. The facts and circumstances of each individual situation, however, will determine whether compliance with an example, to the extent applicable, constitutes compliance with this subpart. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise under this subpart. Similarly, the examples do not illustrate any issues that may arise under other laws or regulations.

§§ 248.103 – 248.119 [Reserved]

§ 248.120 Definitions.

As used in this subpart, unless the context requires otherwise:

(a) Affiliate of a broker, dealer, or investment company, or an investment adviser or transfer agent registered with the Commission means any person that is related by common ownership or common control with the broker, dealer, or investment company, or the investment adviser or transfer agent registered with the Commission. In addition, a broker, dealer, or investment company, or an investment adviser or transfer agent registered with the Commission will be deemed an affiliate of a company for purposes of this subpart if:

(1) That company is regulated under section 214 of the FACT Act, Pub. L. No. 108-159, 117 Stat. 1952 (2003), by a government regulator other than the Commission; and

(2) Rules adopted by the other government regulator under section 214 of the FACT Act treat the broker, dealer, or investment company, or investment adviser or transfer agent registered

with the Commission as an affiliate of that company.

(b) Broker has the same meaning as in section 3(a)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(4)). A "broker" does not include a broker registered by notice with the Commission under section 15(b)(11) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)(11)).

(c) Clear and conspicuous means reasonably understandable and designed to call attention to the nature and significance of the information presented.

(d) Commission means the Securities and Exchange Commission.

(e) Company means any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization.

(f) Concise. (1) In general. The term "concise" means a reasonably brief expression or statement.

(2) Combination with other required disclosures. A notice required by this subpart may be concise even if it is combined with other disclosures required or authorized by federal or state law.

(g) Consumer means an individual.

(h) Control of a company means the power to exercise a controlling influence over the management or policies of a company whether through ownership of securities, by contract, or otherwise. Any person who owns beneficially, either directly or through one or more controlled companies, more than 25 percent of the voting securities of any company is presumed to control the company. Any person who does not own more than 25 percent of the voting securities of any company will be presumed not to control the company. Any presumption regarding control may be rebutted by evidence, but, in the case of an investment company, will continue until the

Commission makes a decision to the contrary according to the procedures described in section 2(a)(9) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(9)).

(i) Dealer has the same meaning as in section 3(a)(5) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(5)). A "dealer" does not include a dealer registered by notice with the Commission under section 15(b)(11) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)(11)).

(j) Eligibility information means any information the communication of which would be a consumer report if the exclusions from the definition of "consumer report" in section 603(d)(2)(A) of the FCRA did not apply. Eligibility information does not include aggregate or blind data that does not contain personal identifiers such as account numbers, names, or addresses.

(k) FCRA means the Fair Credit Reporting Act (15 U.S.C. 1681, et seq.).

(l) GLBA means the Gramm-Leach-Bliley Act (15 U.S.C. 6801, et seq.).

(m) Investment adviser has the same meaning as in section 202(a)(11) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(11)).

(n) Investment company has the same meaning as in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3) and includes a separate series of the investment company.

(o) Marketing solicitation. (1) In general. The term "marketing solicitation" means the marketing of a product or service initiated by a person to a particular consumer that is:

(i) Based on eligibility information communicated to that person by its affiliate as described in this subpart; and

(ii) Intended to encourage the consumer to purchase or obtain such product or service.

(2) Exclusion of marketing directed at the general public. A marketing solicitation does not include marketing communications that are directed at the general public. For example, television, general circulation magazine, billboard advertisements and publicly available Web sites that are not directed to particular consumers would not constitute marketing solicitations, even if those communications are intended to encourage consumers to purchase products and services from the person initiating the communications.

(3) Examples of marketing solicitations. A marketing solicitation would include, for example, a telemarketing call, direct mail, e-mail, or other form of marketing communication directed to a particular consumer that is based on eligibility information received from an affiliate.

(p) Person means any individual, partnership, corporation, trust, estate, cooperative, association, government or governmental subdivision or agency, or other entity.

(q) Pre-existing business relationship. (1) In general. The term "pre-existing business relationship" means a relationship between a person, or a person's licensed agent, and a consumer based on:

(i) A financial contract between the person and the consumer which is in force on the date on which the consumer is sent a solicitation covered by this subpart;

(ii) The purchase, rental, or lease by the consumer of the person's goods or services, or a financial transaction (including holding an active account or a policy in force or having another continuing relationship) between the consumer and the person, during the 18-month period immediately preceding the date on which the consumer is sent a solicitation covered by this subpart; or

(iii) An inquiry or application by the consumer regarding a product or service offered by that person during the three-month period immediately preceding the date on which the consumer is sent a solicitation covered by this subpart.

(2) Examples of pre-existing business relationships. (i) If a consumer has a brokerage account with a broker-dealer that is currently in force, the broker-dealer has a pre-existing business relationship with the consumer and can use eligibility information it receives from its affiliates to make solicitations to the consumer about its products or services.

(ii) If a consumer has an investment advisory contract with a registered investment adviser, the investment adviser has a pre-existing business relationship with the consumer and can use eligibility information it receives from its affiliates to make solicitations to the consumer about its products or services.

(iii) If a consumer was the record owner of securities issued by an investment company, but the consumer redeems these securities, the investment company has a pre-existing business relationship with the consumer and can use eligibility information it receives from its affiliates to make solicitations to the consumer about its products or services for 18 months after the date the consumer redeemed the investment company's securities.

(iv) If a consumer applies for a margin account offered by a broker-dealer, but does not obtain a product or service from or enter into a financial contract or transaction with the broker-dealer, the broker-dealer has a pre-existing business relationship with the consumer and can therefore use eligibility information it receives from its affiliates to make solicitations to the consumer about its products or services for three months after the date of the application.

(v) If a consumer makes a telephone inquiry to a broker-dealer about its products or services and provides contact information to the broker-dealer, but does not obtain a product or service from or enter into a financial contract or transaction with the institution, the broker-dealer has a pre-existing business relationship with the consumer and can therefore use eligibility information it receives from its affiliates to make solicitations to the consumer about its products or services for three months after the date of the inquiry.

(vi) If a consumer makes an inquiry by e-mail to a broker-dealer about one of its affiliated investment company's products or services but does not obtain a product or service from, or enter into a financial contract or transaction with the broker-dealer or the investment company, the broker-dealer and the investment company both have a pre-existing business relationship with the consumer and can therefore use eligibility information they receive from their affiliates to make solicitations to the consumer about their products or services for three months after the date of the inquiry.

(vii) If a consumer who has a pre-existing business relationship with an investment company that is part of a group of affiliated companies makes a telephone call to the centralized call center for the affiliated companies to inquire about products or services offered by a broker-dealer affiliated with the investment company, and provides contact information to the call center, the call constitutes an inquiry to the broker-dealer. In these circumstances, the broker-dealer has a pre-existing business relationship with the consumer and can therefore use eligibility information it receives from the investment company to make solicitations to the consumer about its products or services for three months after the date of the inquiry.

(3) Examples where no pre-existing business relationship is created. (i) If a consumer makes a telephone call to a centralized call center for a group of affiliated companies to inquire about the consumer's existing account at a broker-dealer, the call does not constitute an inquiry to any affiliate other than the broker-dealer that holds the consumer's account and does not establish a pre-existing business relationship between the consumer and any affiliate of the

account-holding broker-dealer.

(ii) If a consumer who has an advisory contract with a registered investment adviser makes a telephone call to an affiliate of the investment adviser to ask about the affiliate's retail locations and hours, but does not make an inquiry about the affiliate's products or services, the call does not constitute an inquiry and does not establish a pre-existing business relationship between the consumer and the affiliate. Also, the affiliate's capture of the consumer's telephone number does not constitute an inquiry and does not establish a pre-existing business relationship between the consumer and the affiliate.

(iii) If a consumer makes a telephone call to a broker-dealer in response to an advertisement offering a free promotional item to consumers who call a toll-free number, but the advertisement does not indicate that the broker-dealer's products or services will be marketed to consumers who call in response, the call does not create a pre-existing business relationship between the consumer and the broker-dealer because the consumer has not made an inquiry about a product or service offered by the institution, but has merely responded to an offer for a free promotional item.

(r) Transfer agent has the same meaning as in section 3(a)(25) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(25)).

(s) You means:

(1) Any broker or dealer other than a broker or dealer registered by notice with the Commission under section 15(b)(11) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)(11));

(2) Any investment company;

(3) Any investment adviser registered with the Commission under the Investment

Advisers Act of 1940 (15 U.S.C. 80b-1, et seq.); and

(4) Any transfer agent registered with the Commission under section 17A of the Securities Exchange Act of 1934 (15 U.S.C. 78q-1).

§ 248.121 Affiliate marketing opt out and exceptions.

(a) Initial notice and opt out requirement. (1) In general. You may not use eligibility information about a consumer that you receive from an affiliate to make a marketing solicitation to the consumer, unless:

(i) It is clearly and conspicuously disclosed to the consumer in writing or, if the consumer agrees, electronically, in a concise notice that you may use eligibility information about that consumer received from an affiliate to make marketing solicitations to the consumer;

(ii) The consumer is provided a reasonable opportunity and a reasonable and simple method to "opt out," or the consumer prohibits you from using eligibility information to make marketing solicitations to the consumer; and

(iii) The consumer has not opted out.

(2) Example. A consumer has a brokerage account with a broker-dealer. The broker-dealer furnishes eligibility information about the consumer to its affiliated investment adviser. Based on that eligibility information, the investment adviser wants to make a marketing solicitation to the consumer about its discretionary advisory accounts. The investment adviser does not have a pre-existing business relationship with the consumer and none of the other exceptions apply. The investment adviser is prohibited from using eligibility information received from its broker-dealer affiliate to make marketing solicitations to the consumer about its discretionary advisory accounts unless the consumer is given a notice and opportunity to opt out and the consumer does not opt out.

(3) Affiliates who may provide the notice. The notice required by this paragraph must be provided:

(i) By an affiliate that has or has previously had a pre-existing business relationship with the consumer; or

(ii) As part of a joint notice from two or more members of an affiliated group of companies, provided that at least one of the affiliates on the joint notice has or has previously had a pre-existing business relationship with the consumer.

(b) Making marketing solicitations. (1) In general. For purposes of this subpart, you make a marketing solicitation if:

(i) You receive eligibility information from an affiliate;

(ii) You use that eligibility information to do one or more of the following:

(A) Identify the consumer or type of consumer to receive a marketing solicitation;

(B) Establish criteria used to select the consumer to receive a marketing solicitation; or

(C) Decide which of your products or services to market to the consumer or tailor your marketing solicitation to that consumer; and

(iii) As a result of your use of the eligibility information, the consumer is provided a marketing solicitation.

(2) Receiving eligibility information from an affiliate, including through a common database. You may receive eligibility information from an affiliate in various ways, including when the affiliate places that information into a common database that you may access.

(3) Receipt or use of eligibility information by your service provider. Except as provided in paragraph (b)(5) of this section, you receive or use an affiliate's eligibility information if a service provider acting on your behalf (whether an affiliate or a nonaffiliated third party) receives

or uses that information in the manner described in paragraph (b)(1)(i) or (b)(1)(ii) of this section. All relevant facts and circumstances will determine whether a person is acting as your service provider when it receives or uses an affiliate's eligibility information in connection with marketing your products and services.

(4) Use by an affiliate of its own eligibility information. Unless you have used eligibility information that you receive from an affiliate in the manner described in paragraph (b)(1)(ii) of this section, you do not make a marketing solicitation subject to this subpart if your affiliate:

(i) Uses its own eligibility information that it obtained in connection with a pre-existing business relationship it has or had with the consumer to market your products or services to the affiliate's consumer; or

(ii) Directs its service provider to use the affiliate's own eligibility information that it obtained in connection with a pre-existing business relationship it has or had with the consumer to market your products or services to the consumer, and you do not communicate directly with the service provider regarding that use.

(5) Use of eligibility information by a service provider. (i) In general. You do not make a marketing solicitation subject to this subpart if a service provider (including an affiliated or third-party service provider that maintains or accesses a common database that you may access) receives eligibility information from your affiliate that your affiliate obtained in connection with a pre-existing business relationship it has or had with the consumer and uses that eligibility information to market your products or services to that affiliate's consumer, so long as:

(A) Your affiliate controls access to and use of its eligibility information by the service provider (including the right to establish the specific terms and conditions under which the service provider may use such information to market your products or services);

(B) Your affiliate establishes specific terms and conditions under which the service provider may access and use your affiliate's eligibility information to market your products and services (or those of affiliates generally) to your affiliate's consumers, such as the identity of the affiliated companies whose products or services may be marketed to the affiliate's consumers by the service provider, the types of products or services of affiliated companies that may be marketed, and the number of times your affiliate's consumers may receive marketing materials, and periodically evaluates the service provider's compliance with those terms and conditions;

(C) Your affiliate requires the service provider to implement reasonable policies and procedures designed to ensure that the service provider uses your affiliate's eligibility information in accordance with the terms and conditions established by your affiliate relating to the marketing of your products or services;

(D) Your affiliate is identified on or with the marketing materials provided to the consumer; and

(E) You do not directly use your affiliate's eligibility information in the manner described in paragraph (b)(1)(ii) of this section.

(ii) Writing requirements. (A) The requirements of paragraphs (b)(5)(i)(A) and (C) of this section must be set forth in a written agreement between your affiliate and the service provider; and

(B) The specific terms and conditions established by your affiliate as provided in paragraph (b)(5)(i)(B) of this section must be set forth in writing.

(6) Examples of making marketing solicitations. (i) A consumer has an investment advisory contract with a registered investment adviser that is affiliated with a broker-dealer. The broker-dealer receives eligibility information about the consumer from the investment adviser.

The broker-dealer uses that eligibility information to identify the consumer to receive a marketing solicitation about brokerage products and services, and, as a result, the broker-dealer provides a marketing solicitation to the consumer about its brokerage services. Pursuant to paragraph (b)(1) of this section, the broker-dealer has made a marketing solicitation to the consumer.

(ii) The same facts as in the example in paragraph (b)(6)(i) of this section, except that after using the eligibility information to identify the consumer to receive a marketing solicitation about brokerage products and services, the broker-dealer asks the registered investment adviser to send the marketing solicitation to the consumer and the investment adviser does so. Pursuant to paragraph (b)(1) of this section, the broker-dealer has made a marketing solicitation to the consumer because it used eligibility information about the consumer that it received from an affiliate to identify the consumer to receive a marketing solicitation about its products or services, and, as a result, a marketing solicitation was provided to the consumer about the broker-dealer's products and services.

(iii) The same facts as in the example in paragraph (b)(6)(i) of this section, except that eligibility information about consumers who have an investment advisory contract with a registered investment adviser is placed into a common database that all members of the affiliated group of companies may independently access and use. Without using the investment adviser's eligibility information, the broker-dealer develops selection criteria and provides those criteria, marketing materials, and related instructions to the investment adviser. The investment adviser reviews eligibility information about its own consumers using the selection criteria provided by the broker-dealer to determine which consumers should receive the broker-dealer's marketing materials and sends the broker-dealer's marketing materials to those consumers. Even though the broker-dealer has received eligibility information through the common database as provided in paragraph (b)(2) of this section, it did not use that information to identify consumers or establish selection criteria; instead, the investment adviser used its own eligibility information. Therefore, pursuant to paragraph (b)(4)(i) of this section, the broker-dealer has not made a marketing solicitation to the consumer.

(iv) The same facts as in the example in paragraph (b)(6)(iii) of this section, except that the registered investment adviser provides the broker-dealer's criteria to the investment adviser's service provider and directs the service provider to use the investment adviser's eligibility information to identify investment adviser consumers who meet the criteria and to send the broker-dealer's marketing materials to those consumers. The broker-dealer does not communicate directly with the service provider regarding the use of the investment adviser's information to market its products or services to the investment adviser's consumers. Pursuant to paragraph (b)(4)(ii) of this section, the broker-dealer has not made a marketing solicitation to the consumer.

(v) An affiliated group of companies includes an investment company, a principal underwriter for the investment company, a retail broker-dealer, and a transfer agent that also acts as a service provider. Each affiliate in the group places information about its consumers into a common database. The service provider has access to all information in the common database. The investment company controls access to and use of its eligibility information by the service provider. This control is set forth in a written agreement between the investment company and the service provider. The written agreement also requires the service provider to establish reasonable policies and procedures designed to ensure that the service provider uses the investment company's eligibility information in accordance with specific terms and conditions established by the investment company relating to the marketing of the products and services of all affiliates, including the principal underwriter and the retail broker-dealer. In a separate written communication, the investment company specifies the terms and conditions under which the service provider may use the investment company's eligibility information to market the retail broker-dealer's products and services to the investment company's consumers. The specific terms and conditions are: a list of affiliated companies (including the retail broker-dealer) whose products or services may be marketed to the investment company's consumers by the service provider; the specific products or services or types of products or services that may be marketed to the investment company's consumers by the service provider; the categories of eligibility information that may be used by the service provider in marketing products or services to the investment company's consumers; the types or categories of the investment company's consumers to whom the service provider may market products or services of investment company affiliates; the number and types of marketing communications that the service provider may send to the investment company's consumers; and the length of time during which the service provider may market the products or services of the investment company's affiliates to its consumers. The investment company periodically evaluates the service provider's compliance with these terms and conditions. The retail broker-dealer asks the service provider to market brokerage services to certain of the investment company's consumers. Without using the investment company's eligibility information, the retail broker-dealer develops selection criteria and provides those criteria, its marketing materials, and related instructions to the service provider. The service provider uses the investment company's eligibility information from the common database to identify the investment company's consumers to whom brokerage services will be marketed. When the retail broker-dealer's marketing materials are provided to the identified consumers, the name of the investment company is displayed on the retail broker-dealer's marketing materials, an introductory letter that accompanies the marketing materials, an account statement that accompanies the marketing materials, or the envelope containing the marketing materials. The requirements of paragraph (b)(5) of this section have been satisfied, and the retail broker-dealer has not made a marketing solicitation to the consumer.

(vi) The same facts as in the example in paragraph (b)(6)(v) of this section, except that the terms and conditions permit the service provider to use the investment company's eligibility information to market the products and services of other affiliates to the investment company's consumers whenever the service provider deems it appropriate to do so. The service provider uses the investment company's eligibility information in accordance with the discretion afforded to it by the terms and conditions. Because the terms and conditions are not specific, the requirements of paragraph (b)(5) of this section have not been satisfied.

(c) Exceptions. The provisions of this subpart do not apply to you if you use eligibility information that you receive from an affiliate:

(1) To make a marketing solicitation to a consumer with whom you have a pre-existing business relationship;

(2) To facilitate communications to an individual for whose benefit you provide employee benefit or other services pursuant to a contract with an employer related to and arising out of the current employment relationship or status of the individual as a participant or beneficiary of an employee benefit plan;

(3) To perform services on behalf of an affiliate, except that this paragraph shall not be construed as permitting you to send marketing solicitations on behalf of an affiliate if the affiliate would not be permitted to send the marketing solicitation as a result of the election of the

consumer to opt out under this subpart;

(4) In response to a communication about your products or services initiated by the consumer;

(5) In response to an authorization or request by the consumer to receive solicitations; or

(6) If your compliance with this subpart would prevent you from complying with any provision of State insurance laws pertaining to unfair discrimination in any State in which you are lawfully doing business.

(d) <u>Examples of exceptions</u>. (1) <u>Example of the pre-existing business relationship exception</u>. A consumer has a brokerage account with a broker-dealer. The consumer also has a deposit account with the broker-dealer's affiliated depository institution. The broker-dealer receives eligibility information about the consumer from its depository institution affiliate and uses that information to make a marketing solicitation to the consumer about the broker-dealer's college savings accounts. The broker-dealer may make this marketing solicitation even if the consumer has not been given a notice and opportunity to opt out because the broker-dealer has a pre-existing business relationship with the consumer.

(2) <u>Examples of service provider exception</u>. (i) A consumer has a brokerage account with a broker-dealer. The broker-dealer furnishes eligibility information about the consumer to its affiliate, a registered investment adviser. Based on that eligibility information, the investment adviser wants to make a marketing solicitation to the consumer about its advisory services. The investment adviser does not have a pre-existing business relationship with the consumer and none of the other exceptions in paragraph (c) of this section apply. The consumer has been given an opt out notice and has elected to opt out of receiving such marketing solicitations. The investment adviser asks a service provider to send the marketing solicitation to the consumer on

its behalf. The service provider may not send the marketing solicitation on behalf of the investment adviser because, as a result of the consumer's opt out election, the investment adviser is not permitted to make the marketing solicitation.

(ii) The same facts as in paragraph (d)(2)(i) of this section, except the consumer has been given an opt out notice, but has not elected to opt out. The investment adviser asks a service provider to send the solicitation to the consumer on its behalf. The service provider may send the marketing solicitation on behalf of the investment adviser because, as a result of the consumer's not opting out, the investment adviser is permitted to make the marketing solicitation.

(3) Examples of consumer-initiated communications. (i) A consumer who is the record owner of shares in an investment company initiates a communication with an affiliated registered investment adviser about advisory services. The affiliated investment adviser may use eligibility information about the consumer it obtains from the investment company or any other affiliate to make marketing solicitations regarding the affiliated investment adviser's services in response to the consumer-initiated communication.

(ii) A consumer who has a brokerage account with a broker-dealer contacts the broker-dealer to request information about how to save and invest for a child's college education without specifying the type of savings or investment vehicle in which the consumer may be interested. Information about a range of different products or services offered by the broker-dealer and one or more of its affiliates may be responsive to that communication. Such products, services, and investments may include the following: investments in affiliated investment companies; investments in section 529 plans offered by the broker-dealer; or trust services offered by a different financial institution in the affiliated group. Any affiliate offering products or services that would be responsive to the consumer's request for information about saving and investing for a child's college education may use eligibility information to make marketing solicitations to the consumer in response to this communication.

(iii) A registered investment adviser makes a marketing call to the consumer without using eligibility information received from an affiliate. The investment adviser leaves a voice-mail message that invites the consumer to call a toll-free number to receive information about services offered by the investment adviser. If the consumer calls the toll-free number to inquire about the investment advisory services, the call is a consumer-initiated communication about a product or service, and the investment adviser may now use eligibility information it receives from its affiliates to make marketing solicitations to the consumer.

(iv) A consumer calls a broker-dealer to ask about retail locations and hours, but does not request information about its products or services. The broker-dealer may not use eligibility information it receives from an affiliate to make marketing solicitations to the consumer because the consumer-initiated communication does not relate to the broker-dealer's products or services. Thus, the use of eligibility information received from an affiliate would not be responsive to the communication and the exception does not apply.

(v) A consumer calls a broker-dealer to ask about retail locations and hours. The customer service representative asks the consumer if there is a particular product or service about which the consumer is seeking information. The consumer responds that the consumer wants to stop in and find out about mutual funds (i.e., registered open-end investment companies). The customer service representative offers to provide that information by telephone and mail additional information to the consumer. The consumer agrees and provides or confirms contact information for receipt of the materials to be mailed. The broker-dealer may use eligibility information it receives from an affiliate to make marketing solicitations to the consumer about mutual funds because such marketing solicitations would respond to the consumer-initiated communication about mutual funds.

(4) Examples of consumer authorization or request for marketing solicitations. (i) A consumer who has a brokerage account with a broker-dealer authorizes or requests information about life insurance offered by the broker-dealer's insurance affiliate. The authorization or request, whether given to the broker-dealer or the insurance affiliate, would permit the insurance affiliate to use eligibility information about the consumer it obtains from the broker-dealer or any other affiliate to make marketing solicitations to the consumer about life insurance.

(ii) A consumer completes an online application to open an online brokerage account with a broker-dealer. The broker-dealer's online application contains a blank check box that the consumer may check to authorize or request information from the broker-dealer's affiliates. The consumer checks the box. The consumer has authorized or requested marketing solicitations from the broker-dealer's affiliates.

(iii) A consumer completes an online application to open an online brokerage account with a broker-dealer. The broker-dealer's online application contains a check box indicating that the consumer authorizes or requests information from the broker-dealer's affiliates. The consumer does not deselect the check box. The consumer has not authorized or requested marketing solicitations from the broker-dealer's affiliates.

(iv) The terms and conditions of a brokerage account agreement contain preprinted boilerplate language stating that by applying to open an account the consumer authorizes or requests to receive solicitations from the broker-dealer's affiliates. The consumer has not authorized or requested marketing solicitations from the broker-dealer's affiliates.

(e) Relation to affiliate-sharing notice and opt out. Nothing in this subpart limits the responsibility of a person to comply with the notice and opt out provisions of Section 603(d)(2)(A)(iii) of the FCRA (15 U.S.C. 1681a(d)(2)(A)(iii)) where applicable.

§ 248.122 Scope and duration of opt out.

(a) Scope of opt out. (1) In general. Except as otherwise provided in this section, the consumer's election to opt out prohibits any affiliate covered by the opt out notice from using eligibility information received from another affiliate as described in the notice to make marketing solicitations to the consumer.

(2) Continuing relationship. (i) In general. If the consumer establishes a continuing relationship with you or your affiliate, an opt out notice may apply to eligibility information obtained in connection with:

(A) A single continuing relationship or multiple continuing relationships that the consumer establishes with you or your affiliates, including continuing relationships established subsequent to delivery of the opt out notice, so long as the notice adequately describes the continuing relationships covered by the opt out; or

(B) Any other transaction between the consumer and you or your affiliates as described in the notice.

(ii) Examples of continuing relationships. A consumer has a continuing relationship with you or your affiliate if the consumer:

(A) Opens a brokerage account or enters into an advisory contract with you or your affiliate;

(B) Obtains a loan for which you or your affiliate owns the servicing rights;

(C) Purchases investment company shares in his or her own name;

(D) Holds an investment through you or your affiliate; such as when you act or your affiliate acts as a custodian for securities or for assets in an individual retirement arrangement;

(E) Enters into an agreement or understanding with you or your affiliate whereby you or your affiliate undertakes to arrange or broker a home mortgage loan for the consumer;

(F) Enters into a lease of personal property with you or your affiliate; or

(G) Obtains financial, investment, or economic advisory services from you or your affiliate for a fee.

(3) No continuing relationship. (i) In general. If there is no continuing relationship between a consumer and you or your affiliate, and you or your affiliate obtain eligibility information about a consumer in connection with a transaction with the consumer, such as an isolated transaction or an application that is denied, an opt out notice provided to the consumer only applies to eligibility information obtained in connection with that transaction.

(ii) Examples of isolated transactions. An isolated transaction occurs if:

(A) The consumer uses your or your affiliate's ATM to withdraw cash from an account at another financial institution; or

(B) A broker-dealer opens a brokerage account for the consumer solely for the purpose of liquidating or purchasing securities as an accommodation, i.e., on a one-time basis, without the expectation of engaging in other transactions.

(4) Menu of alternatives. A consumer may be given the opportunity to choose from a menu of alternatives when electing to prohibit solicitations, such as by electing to prohibit solicitations from certain types of affiliates covered by the opt out notice but not other types of affiliates covered by the notice, electing to prohibit marketing solicitations based on certain types of eligibility information but not other types of eligibility information, or electing to prohibit marketing solicitations by certain methods of delivery but not other methods of delivery. However, one of the alternatives must allow the consumer to prohibit all marketing solicitations from all of the affiliates that are covered by the notice.

(5) Special rule for a notice following termination of all continuing relationships. (i) In general. A consumer must be given a new opt out notice if, after all continuing relationships with you or your affiliate(s) are terminated, the consumer subsequently establishes another continuing relationship with you or your affiliate(s) and the consumer's eligibility information is to be used to make a marketing solicitation. The new opt out notice must apply, at a minimum, to eligibility information obtained in connection with the new continuing relationship. Consistent with paragraph (b) of this section, the consumer's decision not to opt out after receiving the new opt out notice would not override a prior opt out election by the consumer that applies to eligibility information obtained in connection with a terminated relationship, regardless of whether the new opt out notice applies to eligibility information obtained in connection with the terminated relationship.

(ii) Example. A consumer has an advisory contract with a company that is registered with the Commission as both a broker-dealer and an investment adviser, and that is part of an affiliated group. The consumer terminates the advisory contract. One year after terminating the advisory contract, the consumer opens a brokerage account with the same company. The consumer must be given a new notice and opportunity to opt out before the company's affiliates may make marketing solicitations to the consumer using eligibility information obtained by the company in connection with the new brokerage account relationship, regardless of whether the consumer opted out in connection with the advisory contract.

(b) Duration of opt out. The election of a consumer to opt out must be effective for a period of at least five years (the "opt out period") beginning when the consumer's opt out election is received and implemented, unless the consumer subsequently revokes the opt out in writing or, if the consumer agrees, electronically. An opt out period of more than five years may be established, including an opt out period that does not expire unless revoked by the consumer.

(c) Time of opt out. A consumer may opt out at any time.

§ 248.123 Contents of opt out notice; consolidated and equivalent notices.

(a) Contents of opt out notice. (1) In general. A notice must be clear, conspicuous, and concise, and must accurately disclose:

(i) The name of the affiliate(s) providing the notice. If the notice is provided jointly by multiple affiliates and each affiliate shares a common name, such as "ABC," then the notice may indicate that it is being provided by multiple companies with the ABC name or multiple companies in the ABC group or family of companies, for example, by stating that the notice is provided by "all of the ABC companies," "the ABC banking, credit card, insurance, and securities companies," or by listing the name of each affiliate providing the notice. But if the affiliates providing the joint notice do not all share a common name, then the notice must either separately identify each affiliate by name or identify each of the common names used by those affiliates, for example, by stating that the notice is provided by "all of the ABC and XYZ companies" or by "the ABC bank and securities companies and the XYZ insurance companies";

(ii) A list of the affiliates or types of affiliates whose use of eligibility information is covered by the notice, which may include companies that become affiliates after the notice is provided to the consumer. If each affiliate covered by the notice shares a common name, such as "ABC," then the notice may indicate that it applies to multiple companies with the ABC name or multiple companies in the ABC group or family of companies, for example, by stating that the notice is provided by "all of the ABC companies," "the ABC banking, credit card, insurance, and securities companies," or by listing the name of each affiliate providing the notice. But if the affiliates covered by the notice do not all share a common name, then the notice must either separately identify each covered affiliate by name or identify each of the common names used by those affiliates, for example, by stating that the notice applies to "all of the ABC and XYZ companies" or to "the ABC banking and securities companies and the XYZ insurance companies";

(iii) A general description of the types of eligibility information that may be used to make marketing solicitations to the consumer;

(iv) That the consumer may elect to limit the use of eligibility information to make marketing solicitations to the consumer;

(v) That the consumer's election will apply for the specified period of time stated in the notice and, if applicable, that the consumer will be allowed to renew the election once that period expires;

(vi) If the notice is provided to consumers who may have previously opted out, such as if a notice is provided to consumers annually, that the consumer who has chosen to limit marketing solicitations does not need to act again until the consumer receives a renewal notice; and

(vii) A reasonable and simple method for the consumer to opt out.

(2) Joint relationships. (i) If two or more consumers jointly obtain a product or service, a single opt out notice may be provided to the joint consumers. Any of the joint consumers may exercise the right to opt out.

(ii) The opt out notice must explain how an opt out direction by a joint consumer will be treated. An opt out direction by a joint consumer may be treated as applying to all of the associated joint consumers, or each joint consumer may be permitted to opt out separately. If each joint consumer is permitted to opt out separately, one of the joint consumers must be permitted to opt out on behalf of all of the joint consumers and the joint consumers must be permitted to exercise their separate rights to opt out in a single response.

(iii) It is impermissible to require all joint consumers to opt out before implementing any opt out direction.

(3) Alternative contents. If the consumer is afforded a broader right to opt out of receiving marketing than is required by this subpart, the requirements of this section may be satisfied by providing the consumer with a clear, conspicuous, and concise notice that accurately discloses the consumer's opt out rights.

(4) Model notices. Model notices are provided in the Appendix to this subpart.

(b) Coordinated and consolidated notices. A notice required by this subpart may be coordinated and consolidated with any other notice or disclosure required to be issued under any other provision of law by the entity providing the notice, including but not limited to the notice described in section 603(d)(2)(A)(iii) of the FCRA (15 U.S.C. 1681a(d)(2)(A)(iii)) and the GLBA privacy notice.

(c) Equivalent notices. A notice or other disclosure that is equivalent to the notice required by this subpart, and that is provided to a consumer together with disclosures required by any other provision of law, satisfies the requirements of this section.

§ 248.124 Reasonable opportunity to opt out.

(a) In general. You must not use eligibility information that you receive from an affiliate to make marketing solicitations to a consumer about your products or services unless the consumer is provided a reasonable opportunity to opt out, as required by § 248.121(a)(1)(ii).

(b) Examples of a reasonable opportunity to opt out. The consumer is given a reasonable opportunity to opt out if:

(1) By mail. The opt out notice is mailed to the consumer. The consumer is given 30

days from the date the notice is mailed to elect to opt out by any reasonable means.

(2) By electronic means. (i) The opt out notice is provided electronically to the consumer, such as by posting the notice at an Internet Web site at which the consumer has obtained a product or service. The consumer acknowledges receipt of the electronic notice. The consumer is given 30 days after the date the consumer acknowledges receipt to elect to opt out by any reasonable means.

(ii) The opt out notice is provided to the consumer by e-mail where the consumer has agreed to receive disclosures by e-mail from the person sending the notice. The consumer is given 30 days after the e-mail is sent to elect to opt out by any reasonable means.

(3) At the time of an electronic transaction. The opt out notice is provided to the consumer at the time of an electronic transaction, such as a transaction conducted on an Internet Web site. The consumer is required to decide, as a necessary part of proceeding with the transaction, whether to opt out before completing the transaction. There is a simple process that the consumer may use to opt out at that time using the same mechanism through which the transaction is conducted.

(4) At the time of an in-person transaction. The opt out notice is provided to the consumer in writing at the time of an in-person transaction. The consumer is required to decide, as a necessary part of proceeding with the transaction, whether to opt out before completing the transaction, and is not permitted to complete the transaction without making a choice. There is a simple process that the consumer may use during the course of the in-person transaction to opt out, such as completing a form that requires consumers to write a "yes" or "no" to indicate their opt out preference or that requires the consumer to check one of two blank check boxes—one that allows consumers to indicate that they want to opt out and one that allows consumers to

indicate that they do not want to opt out.

(5) By including in a privacy notice. The opt out notice is included in a GLBA privacy notice. The consumer is allowed to exercise the opt out within a reasonable period of time and in the same manner as the opt out under that privacy notice.

§ 248.125 Reasonable and simple methods of opting out.

(a) In general. You must not use eligibility information about a consumer that you receive from an affiliate to make a marketing solicitation to the consumer about your products or services, unless the consumer is provided a reasonable and simple method to opt out, as required by § 248.121(a)(1)(ii).

(b) Examples. (1) Reasonable and simple opt out methods. Reasonable and simple methods for exercising the opt out right include:

(i) Designating a check-off box in a prominent position on the opt out form;

(ii) Including a reply form and a self-addressed envelope together with the opt out notice;

(iii) Providing an electronic means to opt out, such as a form that can be electronically mailed or processed at an Internet Web site, if the consumer agrees to the electronic delivery of information;

(iv) Providing a toll-free telephone number that consumers may call to opt out; or

(v) Allowing consumers to exercise all of their opt out rights described in a consolidated opt out notice that includes the GLBA privacy, FCRA affiliate sharing, and FCRA affiliate marketing opt outs, by a single method, such as by calling a single toll-free telephone number.

(2) Opt out methods that are not reasonable and simple. Reasonable and simple methods for exercising an opt out right do not include:

(i) Requiring the consumer to write his or her own letter;

(ii) Requiring the consumer to call or write to obtain a form for opting out, rather than including the form with the opt out notice; or

(iii) Requiring the consumer who receives the opt out notice in electronic form only, such as through posting at an Internet Web site, to opt out solely by paper mail or by visiting a different Web site without providing a link to that site.

(c) Specific opt out means. Each consumer may be required to opt out through a specific means, as long as that means is reasonable and simple for that consumer.

§ 248.126 Delivery of opt out notices.

(a) In general. The opt out notice must be provided so that each consumer can reasonably be expected to receive actual notice. For opt out notices provided electronically, the notice may be provided in compliance with either the electronic disclosure provisions in this subpart or the provisions in section 101 of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001, et seq.

(b) Examples of reasonable expectation of actual notice. A consumer may reasonably be expected to receive actual notice if the affiliate providing the notice:

(1) Hand-delivers a printed copy of the notice to the consumer;

(2) Mails a printed copy of the notice to the last known mailing address of the consumer;

(3) Provides a notice by e-mail to a consumer who has agreed to receive electronic disclosures by e-mail from the affiliate providing the notice; or

(4) Posts the notice on the Internet Web site at which the consumer obtained a product or service electronically and requires the consumer to acknowledge receipt of the notice.

(c) Examples of no reasonable expectation of actual notice. A consumer may not reasonably be expected to receive actual notice if the affiliate providing the notice:

(1) Only posts the notice on a sign in a branch or office or generally publishes the notice in a newspaper;

(2) Sends the notice by e-mail to a consumer who has not agreed to receive electronic disclosures by e-mail from the affiliate providing the notice; or

(3) Posts the notice on an Internet Web site without requiring the consumer to acknowledge receipt of the notice.

§ 248.127 Renewal of opt out elections.

(a) Renewal notice and opt out requirement. (1) In general. After the opt out period expires, you may not make marketing solicitations to a consumer who previously opted out, unless:

(i) The consumer has been given a renewal notice that complies with the requirements of this section and §§ 248.124 through 248.126, and a reasonable opportunity and a reasonable and simple method to renew the opt out, and the consumer does not renew the opt out; or

(ii) An exception in § 248.121(c) applies.

(2) Renewal period. Each opt out renewal must be effective for a period of at least five years as provided in § 248.122(b).

(3) Affiliates who may provide the notice. The notice required by this paragraph must be provided:

(i) By the affiliate that provided the previous opt out notice, or its successor; or

(ii) As part of a joint renewal notice from two or more members of an affiliated group of companies, or their successors, that jointly provided the previous opt out notice.

(b) Contents of renewal notice. The renewal notice must be clear, conspicuous, and concise, and must accurately disclose:

(1) The name of the affiliate(s) providing the notice. If the notice is provided jointly by multiple affiliates and each affiliate shares a common name, such as "ABC," then the notice may indicate it is being provided by multiple companies with the ABC name or multiple companies in the ABC group or family of companies, for example, by stating that the notice is provided by "all of the ABC companies," "the ABC banking, credit card, insurance, and securities companies," or by listing the name of each affiliate providing the notice. But if the affiliates providing the joint notice do not all share a common name, then the notice must either separately identify each affiliate by name or identify each of the common names used by those affiliates, for example, by stating that the notice is provided by "all of the ABC and XYZ companies" or by "the ABC banking and securities companies and the XYZ insurance companies";

(2) A list of the affiliates or types of affiliates whose use of eligibility information is covered by the notice, which may include companies that become affiliates after the notice is provided to the consumer. If each affiliate covered by the notice shares a common name, such as "ABC," then the notice may indicate that it applies to multiple companies with the ABC name or multiple companies in the ABC group or family of companies, for example, by stating that the notice is provided by "all of the ABC companies," "the ABC banking, credit card, insurance, and securities companies," or by listing the name of each affiliate providing the notice. But if the affiliates covered by the notice do not all share a common name, then the notice must either separately identify each covered affiliate by name or identify each of the common names used by those affiliates, for example, by stating that the notice applies to "all of the ABC and XYZ companies" or to "the ABC banking and securities companies and the XYZ insurance companies";

(3) A general description of the types of eligibility information that may be used to make

marketing solicitations to the consumer;

(4) That the consumer previously elected to limit the use of certain information to make marketing solicitations to the consumer;

(5) That the consumer's election has expired or is about to expire;

(6) That the consumer may elect to renew the consumer's previous election;

(7) If applicable, that the consumer's election to renew will apply for the specified period of time stated in the notice and that the consumer will be allowed to renew the election once that period expires; and

(8) A reasonable and simple method for the consumer to opt out.

(c) Timing of the renewal notice. (1) In general. A renewal notice may be provided to the consumer either:

(i) A reasonable period of time before the expiration of the opt out period; or

(ii) Any time after the expiration of the opt out period but before marketing solicitations that would have been prohibited by the expired opt out are made to the consumer.

(2) Combination with annual privacy notice. If you provide an annual privacy notice under the GLBA, providing a renewal notice with the last annual privacy notice provided to the consumer before expiration of the opt out period is a reasonable period of time before expiration of the opt out in all cases.

(d) No effect on opt out period. An opt out period may not be shortened by sending a renewal notice to the consumer before expiration of the opt out period, even if the consumer does not renew the opt out.

§ 248.128 Effective date, compliance date, and prospective application.

(a) Effective date. This subpart is effective [Insert date 30 days after publication in the

Federal Register].

(b) Mandatory compliance date. Compliance with this subpart is required not later than January 1, 2010.

(c) Prospective application. The provisions of this subpart do not prohibit you from using eligibility information that you receive from an affiliate to make a marketing solicitation to a consumer if you receive such information prior to January 1, 2010. For purposes of this section, you are deemed to receive eligibility information when such information is placed into a common database and is accessible by you.

Appendix to Subpart B – Model Forms

a. Although you and your affiliates are not required to use the model forms in this Appendix, use of a model form (if applicable to each person that uses it) complies with the requirement in section 624 of the FCRA for clear, conspicuous, and concise notices.

b. Although you may need to change the language or format of a model form to reflect your actual policies and procedures, any such changes may not be so extensive as to affect the substance, clarity, or meaningful sequence of the language in the model forms. Acceptable changes include, for example:

1. Rearranging the order of the references to "your income," "your account history," and "your credit score."

2. Substituting other types of information for "income," "account history," or "credit score" for accuracy, such as "payment history," "credit history," "payoff status," or "claims history."

3. Substituting a clearer and more accurate description of the affiliates providing or covered by the notice for phrases such as "the [ABC] group of companies."

4. Substituting other types of affiliates covered by the notice for "credit card," "insurance," or "securities" affiliates.

5. Omitting items that are not accurate or applicable. For example, if a person does not limit the duration of the opt out period, the notice may omit information about the renewal notice.

6. Adding a statement informing the consumer how much time they have to opt out before shared eligibility information may be used to make solicitations to them.

7. Adding a statement that the consumer may exercise the right to opt out at any time.

8. Adding the following statement, if accurate: "If you previously opted out, you do not need to do so again."

9. Providing a place on the form for the consumer to fill in identifying information, such as his or her name and address.

10. Adding disclosures regarding the treatment of opt-outs by joint consumers to comply with § 248.123(a)(2), if applicable.

A-1 Model Form for Initial Opt Out Notice (Single-Affiliate Notice)

A-2 Model Form for Initial Opt Out Notice (Joint Notice)

A-3 Model Form for Renewal Notice (Single-Affiliate Notice)

A-4 Model Form for Renewal Notice (Joint Notice)

A-5 Model Form for Voluntary "No Marketing" Notice

A-1 – Model Form for Initial Opt Out Notice (Single-Affiliate Notice)--[Your Choice to Limit Marketing]/[Marketing Opt Out]

- [Name of Affiliate] is providing this notice.
- [Optional: Federal law gives you the right to limit some but not all marketing from our

affiliates. Federal law also requires us to give you this notice to tell you about your choice to limit marketing from our affiliates.]

- You may limit our affiliates in the [ABC] group of companies, such as our [investment adviser, broker, transfer agent, and investment company] affiliates, from marketing their products or services to you based on your personal information that we collect and share with them. This information includes your [income], your [account history with us], and your [credit score].
- Your choice to limit marketing offers from our affiliates will apply [until you tell us to change your choice]/[for x years from when you tell us your choice]/[for at least 5 years from when you tell us your choice]. [Include if the opt out period expires.] Once that period expires, you will receive a renewal notice that will allow you to continue to limit marketing offers from our affiliates for [another x years]/[at least another 5 years].
- [Include, if applicable, in a subsequent notice, including an annual notice, for consumers who may have previously opted out.] If you have already made a choice to limit marketing offers from our affiliates, you do not need to act again until you receive the renewal notice.

To limit marketing offers, contact us [include all that apply]:

- **By telephone:** 1-877-###-####
- **On the Web:** www.---.com
- **By mail:** check the box and complete the form below, and send the form to:

  [Company name]

  [Company address]

☐ Do not allow your affiliates to use my personal information to market to me.

A-2 – Model Form for Initial Opt Out Notice (Joint Notice)--[Your Choice to Limit Marketing]/[Marketing Opt Out]

- The [ABC group of companies] is providing this notice.
- [Optional: Federal law gives you the right to limit some but not all marketing from the [ABC] companies. Federal law also requires us to give you this notice to tell you about your choice to limit marketing from the [ABC] companies.]
- You may limit the [ABC] companies, such as the [ABC investment companies, investment advisers, transfer agents, and broker-dealers] affiliates, from marketing their products or services to you based on your personal information that they receive from other [ABC] companies. This information includes your [income], your [account history], and your [credit score].
- Your choice to limit marketing offers from the [ABC] companies will apply [until you tell us to change your choice]/[for x years from when you tell us your choice]/[for at least 5 years from when you tell us your choice]. [Include if the opt out period expires.] Once that period expires, you will receive a renewal notice that will allow you to continue to limit marketing offers from the [ABC] companies for [another x years]/[at least another 5 years].
- [Include, if applicable, in a subsequent notice, including an annual notice, for consumers who may have previously opted out.] If you have already made a choice to limit marketing offers from the [ABC] companies, you do not need to act again until you receive the renewal notice.

To limit marketing offers, contact us [include all that apply]:

- **By telephone:** 1-877-###-####

• **On the Web:** www.---.com

• **By mail:** check the box and complete the form below, and send the form to:

[Company name]

[Company address]

☐ Do not allow any company [in the ABC group of companies] to use my personal information to market to me.

A-3 – Model Form for Renewal Notice (Single-Affiliate Notice)--[Renewing Your Choice to Limit Marketing]/[Renewing Your Marketing Opt Out]

- [Name of Affiliate] is providing this notice.
- [Optional: Federal law gives you the right to limit some but not all marketing from our affiliates. Federal law also requires us to give you this notice to tell you about your choice to limit marketing from our affiliates.]
- You previously chose to limit our affiliates in the [ABC] group of companies, such as our [investment adviser, investment company, transfer agent, and broker-dealer] affiliates, from marketing their products or services to you based on your personal information that we share with them. This information includes your [income], your [account history with us], and your [credit score].
- Your choice has expired or is about to expire.

To renew your choice to limit marketing for [x] more years, contact us [include all that apply]:

• **By telephone:** 1-877-###-####

• **On the Web:** www.---.com

• **By mail:** check the box and complete the form below, and send the form to:

[Company name]

[Company address]

☐ Renew my choice to limit marketing for [x] more years.

A-4 – Model Form for Renewal Notice (Joint Notice)--[Renewing Your Choice to Limit Marketing]/[Renewing Your Marketing Opt Out]

- The [ABC group of companies] is providing this notice.
- [Optional: Federal law gives you the right to limit some but not all marketing from the [ABC] companies. Federal law also requires us to give you this notice to tell you about your choice to limit marketing from the [ABC] companies.]
- You previously chose to limit the [ABC] companies, such as the [ABC investment adviser, investment company, transfer agent, and broker-dealer] affiliates, from marketing their products or services to you based on your personal information that they receive from other ABC companies. This information includes your [income], your [account history], and your [credit score].
- Your choice has expired or is about to expire.

To renew your choice to limit marketing for [x] more years, contact us [include all that apply]:

- **By telephone:** 1-877-###-####
- **On the Web:** www.---.com
- **By mail:** check the box and complete the form below, and send the form to:

[Company name]

[Company address]

☐ Renew my choice to limit marketing for [x] more years.

A-5 – Model Form for Voluntary "No Marketing" Notice--Your Choice to Stop Marketing

- [Name of Affiliate] is providing this notice.
- You may choose to stop all marketing from us and our affiliates.
- [Your choice to stop marketing from us and our affiliates will apply until you tell us to change your choice.]

To stop all marketing, contact us [include all that apply]:

- **By telephone:** 1-877-###-####
- **On the Web:** www.---.com
- **By mail:** check the box and complete the form below, and send the form to:

  [Company name]

  [Company address]

❑ Do not send me marketing material.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Dated: August 4, 2009

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60450 / August 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13304

In the Matter of **CentreInvest, Inc.,** **OOO CentreInvest Securities,** **Vladimir Chekholko,** **William Herlyn,** **Dan Rapoport, and** **Svyatoslav Yenin,** **Respondents.**	**ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTION 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AS TO VLADIMIR CHEKHOLKO**

I.

On December 8, 2008, the Securities and Exchange Commission ("Commission") instituted public administrative and cease-and-desist proceedings pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against CentreInvest, Inc. ("CI-New York"), OOO CentreInvest Securities ("CI-Moscow"), Vladimir Chekholko ("Chekholko"), William Herlyn, Dan Rapoport and Svyatoslav Yenin.

II.

In connection with these proceedings, Respondent Chekholko 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, Chekholko consents to the entry of this Order Making Findings and Imposing Remedial Sanctions Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 as to Vladimir Chekholko ("Order"), as set forth below.

III.

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

SUMMARY

1. These proceedings arise out of violations of the broker-dealer registration, reporting, and record-keeping requirements of the Exchange Act by CI-Moscow, a Moscow-based unregistered broker-dealer, and its New York-based affiliate, CI-New York, a registered broker-dealer. From about 2003 through November 2007, CI-Moscow – directly and through CI-New York, Chekholko (its director of sales), and others – solicited institutional investors in the United States to purchase and sell thinly-traded stocks of Russian companies, without registering as a broker-dealer as required by Section 15(a) of the Exchange Act or meeting the requirements for the exemption from registration for foreign broker-dealers under Exchange Act Rule 15a-6(a).

SETTLING RESPONDENT

2. **Vladimir Chekholko**, age 47, is a resident of Brooklyn, New York, and holds Series 7 and 55 licenses. Chekholko was employed by CI-New York from May 2004 to March 2008, and he served as the firm's head of sales from July 24, 2004 through at least November 2007.

ENTITY RESPONDENTS

3. **OOO CentreInvest Securities** ("CI-Moscow") is a Moscow-based broker-dealer and limited liability company, specializing in the sale of second-tier Russian equities. During the relevant period, it was an affiliate of CI-New York. It was founded in 1992 under the laws of Russia and is regulated by the Russian Federal Financial Markets Service. CI-Moscow has never been registered with the Commission as a broker or dealer.

4. **CentreInvest, Inc.** ("CI-New York") is a registered broker-dealer organized under the laws of New York State with its principal place of business in New York, New York. During the relevant period, it was a subsidiary of Cyprus-based Intelsa Investments Limited. CI-New York first registered with the Commission on June 23, 1998, and during the relevant period, employed four to five full-time employees. On October 2, 2008, the Financial Industry Regulatory Authority, Inc. expelled CI-New York for failure to file a Financial and Operational Combined Uniform Single report.

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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.

CI-MOSCOW ACTED AS A BROKER-DEALER BUT FAILED TO REGISTER OR COMPLY WITH AN EXEMPTION FROM REGISTRATION

5. From about 2003 until at least November 2007, CI-Moscow directly and indirectly solicited investors in the United States to purchase and sell thinly-traded stocks of Russian companies – so-called "second-tier," or micro-cap, Russian companies – without registering as a broker-dealer, as required by Section 15(a) of the Exchange Act, or meeting the requirements for an exemption.

6. Under CI-Moscow's direction, employees of CI-New York, including Chekholko, its head of sales, regularly solicited U.S. institutional investors for the purchase and sale of Russian securities. Investors who expressed interest in a transaction were referred to CI-Moscow to complete the transaction.

7. At some or all relevant times, Chekholko knew that he was referring investors to representatives of CI-Moscow who were neither licensed and registered with the Commission or an appropriate U.S. self-regulatory organization, nor exempt from such licensing and registration requirements.

8. In some cases, employees of CI-Moscow, who were not licensed to sell securities under U.S. law or registered as brokers or dealers under U.S. law and were not exempt from such licensing and registration requirements, solicited U.S. investors directly.

9. CI-New York failed to maintain virtually any records concerning CI-Moscow's transactions with the U.S. investors.

10. Respondents benefited financially from CI-Moscow's transactions in securities with or on behalf of U.S. investors. For example, in 2006 alone, CI-Moscow received at least $928,000 in revenue as a result of its unlawful solicitation of U.S. institutional investors. Chekholko received compensation from CI-New York in the form of salary and bonus as a result of his role in CI-Moscow's unlawful solicitation of U.S. institutional investors.

VIOLATIONS

11. Rule 15a-6(a) of the Exchange Act permits unregistered foreign broker-dealers to effect transactions for U.S. institutional investors in certain limited circumstances, subject to reporting, record keeping and other requirements designed to ensure the protection of U.S. investors. Rule 15a-6(b)(3) defines a "foreign broker or dealer" as "any non-U.S. resident person (including any U.S. person engaged in business as a broker or dealer entirely outside the United States, except as otherwise permitted by this rule) that is not an office or branch of, or a natural person associated with, a registered broker-dealer, whose securities activities, if conducted in the U.S., would be described by the definition of "broker" or "dealer" in Sections 3(a)(4) or 3(a)(5) of the [Exchange Act]." Section 3(a)(4) of the Exchange Act defines a "broker" as any person, other than a bank, in certain circumstances, "engaged in the business of effecting transactions in securities for the account of others." A person "effects transactions in securities" if he or she participates in such transactions "at key points in the chain of distribution." Massachusetts Fin. Servs., Inc. v. Security Investor Protection Corp., 411 F. Sup. 411, 415 (D. Mass.), aff'd, 545 F. 2d 754 (1st Cir. 1976).

12. As a result of the conduct described above, CI-Moscow willfully violated Section 15(a) of the Exchange Act, which makes it illegal for a broker to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security unless the broker is registered with the Commission or, in the case of a natural person, is associated with a registered broker or dealer.

13. CI-Moscow failed to qualify for any exemption from registration.

14. As a result of the conduct described above, Chekholko willfully aided and abetted and caused CI-Moscow's violations of Section 15(a) of the Exchange Act.

UNDERTAKINGS

15. **Ongoing Cooperation:** Chekholko undertakes to cooperate fully with the Commission in any and all investigations, litigations or other proceedings brought by the Commission relating to or arising from the matters described in the Order and agrees:

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

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

(c) That in connection with any testimony of Chekholko to be conducted at deposition, hearing or trial pursuant to a notice or subpoena, Chekholko:

i. Agrees that any such notice or subpoena for his appearance and testimony may be served by regular mail, electronic mail, or facsimile on his counsel, Thomas J. McCabe, McCabe, Flynn & Arangio, LLP, One Whitehall Street, Suite 1825, New York, NY, 10004; and

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

16. **Affidavit of Compliance:** Chekholko shall provide to the Commission, within thirty days after the end of the six-month month suspension described in Section IV.2., below, an affidavit that he has fully complied with the sanctions described in Section IV., below.

In determining whether to accept Chekholko's Offer, the Commission has considered these undertakings.

IV.

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

Accordingly, pursuant to Section 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

1. Chekholko cease and desist from committing or causing violations and any future violations of Section 15(a) of the Exchange Act;

2. Chekholko be, and hereby is, suspended from association with any broker or dealer for a period of six months, effective on the second Monday following the entry of this Order; and

3. Chekholko shall comply with the undertaking enumerated in Section III.16., above.

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. 60440 / August 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13569

In the Matter of **TJM PROPRIETARY TRADING, LLC, MICHAEL R. BENSON, AND JOHN T. BURKE,** **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 TJM Proprietary Trading, LLC ("TJM") and Michael R. Benson, and pursuant to Section 15(b) of the Exchange Act against John T. Burke (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

These proceedings arise out of Respondent TJM's violations of Regulation SHO. Subject to certain exceptions, Regulation SHO requires market participants seeking to effect a short sale to borrow, arrange to borrow, or have reasonable grounds to believe that a security can be borrowed prior to effecting the short sale. This is also known as the "locate requirement." Market makers, who ensure liquidity in the market, are excepted from the locate requirement if they are engaged in bona-fide market making activities.

At the time, Regulation SHO also required "fail-to-deliver" positions[2] in certain securities that have lasted for thirteen consecutive settlement days to be immediately closed out.[3] In contrast to the locate requirement, market makers are not excepted from Regulation SHO's close-out requirement.

In this case, Respondent TJM engaged in certain transactions, known as "reverse conversions," which resulted in violations of Regulation SHO's locate and close-out requirements. A reverse conversion involves selling a put option and buying a call option – a transaction combination that creates what is known as a "synthetic" long position – while selling short the underlying stock. The short sale of the underlying stock serves as a hedge to the synthetic long position. By engaging in these transactions, Respondent TJM profited on the spread between the price of the put option and the price of the call option, while avoiding the cost of borrowing shares

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

2 "Fails-to-deliver" occur when a seller fails to deliver securities to the buyer when delivery is due. Generally, investors complete or settle their security transactions within three settlement days. This settlement cycle is known as T+3 (or "trade date plus three days"). T+3 means that when a trade occurs, the participants to the trade deliver and pay for the security at a clearing agency three settlement days after the trade is executed so the brokerage firm can exchange those funds for the securities on that third settlement day. The three-day settlement period applies to most security transactions, including stocks, bonds, municipal securities, mutual funds traded through a brokerage firm, and limited partnerships that trade on an exchange. Government securities and stock options settle on the next settlement day following the trade (or T+1).

3 A "close out" of a fail position involves the purchase of shares of like kind and quantity in the amount of the fail to deliver position.

of stock to sell short. As described below, because TJM failed to borrow securities to make delivery when delivery was due, the short sales were "naked" short sales.[4]

Specifically, from January 2007 through July 2007, Respondent TJM willfully[5] violated Rule 203(b)(1) of Regulation SHO as a result of Respondent Benson improperly utilizing the market-maker locate exception to avoid locating shares prior to effecting short sale transactions. In willful violation of Rule 203(b)(3) of Regulation SHO, TJM engaged in a series of transactions through Respondent Benson's use of short-term FLEX options that did not satisfy its close-out obligations in Regulation SHO threshold securities[6] that had been allocated to TJM by its clearing firm. Finally, Respondent John Burke, TJM's Chief Operating Officer, failed reasonably to supervise Respondent Benson with a view to preventing him from willfully aiding and abetting and causing TJM's violations of Rules 203(b)(1) and 203(b)(3) of Regulation SHO, within the meaning of Section 15(b)(4)(E) of the Exchange Act.

Respondents

1. TJM Proprietary Trading, LLC ("TJM"), an Illinois limited liability company located in Chicago, Illinois, is a market-maker registered with the Chicago Board Options Exchange, Inc. ("CBOE") since May 2003. TJM also is a broker-dealer registered with the Commission since May 2003. During the relevant time period, John T. Burke was associated with TJM as its Chief Operating Officer.

2. John T. Burke, age 48, is a resident of Glencoe, Illinois and served as a principal and the Chief Operating Officer of TJM during the relevant time period. As Chief Operating Officer, Burke was responsible for supervising TJM's traders. Burke holds the following securities licenses: Series 3, Series 4, Series 7, Series 24, Series 27, and Series 63.

3. Michael R. Benson, age 45, is a resident of Clarendon Hills, Illinois and worked as a trader at TJM Proprietary Trading, LLC during the relevant time period. He holds a Series 7 securities license.

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4 In a "naked" short sale, the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard three-day settlement period, and the seller fails to deliver the securities to the buyer when delivery is due.

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

6 A "threshold security" is a security for which there is an aggregate "fail-to-deliver" position exceeding the criteria set forth in Rule 203(c)(6) of Regulation SHO for a period of five consecutive settlement days.

Facts

A. Respondent TJM Failed to Locate Shares Prior to Effecting Short Sale Transactions

4. During the period January 2007 through July 2007, Respondent TJM engaged in transactions known as "reverse conversions" with purchasers of Regulation SHO threshold securities.

5. As part of these reverse conversions, Respondent Benson, on behalf of TJM, sold short shares of Regulation SHO threshold securities while simultaneously creating a synthetic long position by purchasing call options and selling put options (with the same strike price and expiration date) on the same threshold securities.[7] TJM purchased enough call options and sold enough put options so that the number of shares underlying the options equaled the number of shares it sold short. Through this set of transactions, Respondent TJM reduced its market risk because the short position was used to hedge the synthetic long position that had been created by purchasing call options and selling put options.

6. Respondent TJM profited from this set of transactions because the premium it received for the put options it sold was greater than the premium it paid to purchase the call options. As a general matter, this disparity in premiums for the put and call options (despite their same strike price and expiration date) on Regulation SHO threshold securities exists because of the additional cost that is incurred to hedge the sale of the put option. Specifically, the seller of the put option hedges that transaction by selling short the underlying security. Because these threshold securities were generally hard to borrow, they were more expensive to sell short. Consequently, the cost of hedging the sale of put options in Regulation SHO threshold securities causes the corresponding put options to trade at a higher price than that of the corresponding call options.

7. While engaging in these reverse conversions, Respondent TJM improperly availed itself of the market-maker exception in Rule 203(b)(2)(iii) of Regulation SHO and failed to locate, arrange to borrow, or borrow shares of the security in question prior to effecting the short sales.

B. Respondent TJM Failed to Close Out "Fail-to-Deliver" Positions in Regulation SHO Threshold Securities

8. Respondent TJM's short sales resulted in a "fail-to-deliver" position in the threshold security on the books and records of its clearing firm – i.e., TJM had not delivered the shares it sold short to its clearing firm so that the clearing firm could settle the trade.

9. Rule 203(b)(3) of Regulation SHO requires clearing firms immediately to close out any "fail-to-deliver" position in a threshold security that lasts for thirteen consecutive settlement days by purchasing securities of a like kind and quantity. In addition, pursuant to Rule 203(b)(3)(vi) of Regulation SHO, a clearing firm is permitted reasonably to allocate a "fail-to-

[7] In general, a call option purchaser pays a premium to buy the call option, and a put option seller (or writer) receives a premium for selling (or writing) the put option.

deliver" position to a broker or dealer whose sale resulted in the position. Once the clearing firm has allocated the "fail-to-deliver" position to another broker or dealer, the obligation for complying with the mandatory close-out shifts to that broker or dealer.

10. Respondent TJM's clearing firm, through electronic mail or other means, notified TJM that it was shifting the obligation to TJM to close out the "fail-to-deliver" positions and that it would close out those positions if TJM itself did not do so.

11. Respondent TJM did not want its "fail-to-deliver" position – which resulted from the short sale portion of the reverse conversion – to be closed out by the clearing firm because this would result in the clearing firm making large purchases of Regulation SHO threshold securities at a price determined by the market and allocating that cost to TJM. Additionally, the close-out would have exposed Respondent TJM to market risk on its initial reverse conversion transaction because it would eliminate the short position that had been used to hedge the synthetic long position created by purchasing call options and selling put options.

12. In order to avoid a close-out, Respondent Benson, on behalf of TJM, entered into a series of transactions that failed to satisfy TJM's obligation under Regulation SHO to close out its "fail-to-deliver" position. These complex transactions gave the appearance that TJM was closing out its "fail-to-deliver" position by purchasing securities of like kind and quantity.

13. Specifically, Respondent Benson, on behalf of TJM, effected short-term in-the-money FLEX option transactions in conjunction with stock-purchase transactions that did not satisfy the Regulation SHO close-out requirements.

14. A FLEX option allows the investor to customize the option's terms, such as strike price and expiration date. In this case, the FLEX options allowed Respondent TJM to reset the close-out date so that it would have an additional thirteen days to close out any "fail-to-deliver" position. Specifically, Respondent TJM "purchased" stock in the Regulation SHO threshold security from another market participant and simultaneously purchased a short-term, deep in-the-money FLEX put option for a corresponding number of shares from the same market participant. On the day that it "purchased" the stock, TJM's clearing firm received notice of the "purchase" and closed out the "fail-to-deliver" position. Respondent TJM, however, knew that the following day, or shortly thereafter, the FLEX put option would expire in-the-money, causing TJM to exercise the option and sell the stock.

15. Respondent TJM, however, did not actually receive any shares from the other market participant because that market participant was selling short the stock without having any shares to sell. Accordingly, Respondent TJM did not receive any shares and did not in fact close out the short position – as required by Regulation SHO – that was initially established during the reverse conversion transaction. In these instances, TJM knew, or should have known, that the combination of the purchase of securities and the purchase of the FLEX option would result in maintenance of the "fail-to-deliver" position.

16. TJM's clearing firm, however, reset TJM's Regulation SHO close-out obligation to day one (thus giving TJM a fresh thirteen days in which to close out the short position) based on the "purchase" of shares and the exercise of the FLEX option.

17. After receiving close-out notices from its clearing firm, TJM continued to engage in these and similar types of transactions until the initial options positions (call options purchase/put options sale) expired, at which point it no longer had a synthetic long position that needed to be hedged, and so closed out the short position. By engaging in this course of conduct, TJM impermissibly maintained "fail-to-deliver" positions in numerous Regulation SHO threshold securities.

18. During the relevant period, TJM engaged in a large volume of reverse conversions and reset transactions in numerous threshold securities, including, but not limited to, Medis Technologies Ltd., American Home Mortgage, and NutriSystem, Inc. As a result of TJM's repeated violation of Regulation SHO's locate and close-out requirements, it received ill-gotten gains of $541,000.

19. In addition, in a limited number of instances, Respondent TJM acted as the contraparty to other market participants engaging in the same trading activity involving FLEX options. Specifically, Respondent TJM (i) sold short shares of Regulation SHO threshold securities so that other market participants could close out their own "fail-to-deliver" positions, and (ii) simultaneously entered into deep in-the-money FLEX options, the combination of which allowed the other market participants to circumvent their own Regulation SHO close-out obligations.

C. Respondent Burke Failed Reasonably to Supervise

20. As Chief Operating Officer of TJM, Respondent Burke was responsible for oversight of all operations of the firm, including trading. The firm's traders, including Benson, reported directly to Burke.

21. A firm employee raised with Burke concerns regarding the propriety of Benson's use of FLEX options and informed Burke that there was a regulatory concern that such use of FLEX options may not satisfy the locate and close-out requirements of Regulation SHO.

22. Although Burke knew about Benson's use of FLEX options, he continued to allow Benson to engage in these transactions while failing to follow-up on the "red flags" indicating that such trading was improper.

23. By ignoring these "red flags" concerning the use of FLEX options, Burke failed reasonably to supervise Benson's trading with a view to preventing violations of Regulation SHO.

Legal Analysis

A. Rule 203(b)(1) of Regulation SHO

24. Pursuant to the locate requirement of Rule 203(b)(1) of Regulation SHO, a broker or dealer cannot effect a short sale in an equity security unless it has "(i) [b]orrowed the security, or entered into a bona-fide arrangement to borrow the security; or (ii) [r]easonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due; and (iii) [d]ocumented compliance with [these requirements]."

25. Rule 203(b)(2)(iii) contains an exception to this locate requirement for short sales made "by a market maker in connection with bona-fide market making activities in the security for which this exception is claimed."

26. At the time Respondent TJM placed orders to sell short certain Regulation SHO threshold securities, it failed to locate, arrange to borrow, or borrow the securities. Because the market-maker exception was not available to Respondent TJM, it willfully violated Rule 203(b)(1) of Regulation SHO by failing to locate, arrange to borrow, or borrow the securities before selling short.

27. As a result of his conduct, Benson willfully aided and abetted and caused TJM's violations of Rule 203(b)(1) of Regulation SHO.

B. Rule 203(b)(3) of Regulation SHO

28. At the time, Rule 203(b)(3) imposed an obligation on clearing firms to immediately close out any "fail-to-deliver" positions in a threshold security that lasts for thirteen consecutive settlement days by purchasing securities of like kind and quantity.[8] Pursuant to Rule 203(b)(3)(vi), however, a clearing firm is permitted reasonably to allocate a "fail-to-deliver" position to a broker or dealer whose short sale resulted in the position. Once the clearing firm has allocated the "fail-to-deliver" position to another broker or dealer, the obligation for complying with the mandatory close-out shifts to that broker or dealer.

29. Once the "fail-to-deliver" position is allocated to the broker or dealer, that broker or dealer, in order to satisfy the close-out requirement of Rule 203(b)(3) of Regulation SHO, must purchase securities of like kind and quantity. Borrowing securities, or otherwise entering into an arrangement that merely creates the appearance of a purchase, does not satisfy Regulation SHO's close-out requirement. Specifically, Rule 203(b)(3)(vii) provides that a clearing firm – or a broker

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8 Effective in September 2008, the Commission adopted Rule 204T, which amended Regulation SHO by, among other things, requiring that participants of a registered clearing agency close out fails resulting from short sales no later than the beginning of regular trading hours on the day immediately after the fail occurs. The rule also requires participants of a registered clearing agency to close out fails resulting from long sales or market making activity by no later than the beginning of regular trading hours on the third day after the fail occurs.

or dealer to which the clearing firm allocated a "fail-to-deliver" position – will be deemed not to have satisfied the close-out obligation if it knows, or has reasonable grounds to believe, that the close-out purchase will result in a "fail-to-deliver."

30. By purchasing deep in-the-money FLEX options while simultaneously purporting to "purchase" stock, Respondent TJM engaged in transactions that gave the appearance that it was closing out its "fail-to-deliver" position. As a result, TJM willfully violated Rule 203(b)(3) of Regulation SHO.

31. As a result of his conduct, Benson willfully aided and abetted and caused TJM's violations of Rule 203(b)(3) of Regulation SHO.

C. Failure to Supervise

32. Section 15(b)(4)(E) of the Exchange Act requires broker-dealers reasonably to supervise persons subject to their supervision, with a view toward preventing violations of the federal securities laws. See, e.g., Dean Witter Reynolds, Inc., Exchange Act Rel. No. 46578 (Oct. 1, 2002). The Commission has emphasized that the "responsibility of broker-dealers to supervise their employees by means of effective, established procedures is a critical component in the federal investor protection scheme regulating the securities markets." Id. Section 15(b)(4)(E) of the Exchange Act provides for the imposition of a sanction against a broker or dealer who "has failed reasonably to supervise, with a view to preventing violations of the securities laws, another person who commits such a violation, if such other person is subject to his supervision." Section 15(b)(6)(A)(i) incorporates by reference Section 15(b)(4)(E) and provides for the imposition of sanctions against persons associated with a broker or dealer.

33. Based on the foregoing, Respondent Burke failed reasonably to supervise Respondent Benson, with a view to preventing Benson's willful aiding and abetting and causing TJM's violations of Rules 203(b)(1) and 203(b)(3) of Regulation SHO, within the meaning of Section 15(b)(4)(E) of the Exchange Act.

Undertakings

34. Pursuant to the Chicago Board Options Exchange's ("CBOE") Decision Accepting Offer of Settlement (File No. 08-0049), Respondents shall pay, jointly and severally, a fine in the amount of $250,000 to the CBOE's Business Conduct Committee within fifteen (15) business days of the entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 08-0049).

35. Respondent Benson shall provide to the Commission, within thirty days after the end of the three-month suspension period described below, an affidavit confirming that he has complied fully with the sanctions described in Section IV below.

36. Respondent Burke shall provide to the Commission, within thirty days after the end of the nine-month supervisory suspension period described below, an affidavit confirming that he has complied fully with the sanctions described in Section IV below.

In determining whether to accept the Offers, the Commission has considered these undertakings.

IV.

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

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondent TJM cease and desist from committing or causing any violations and any future violations of Exchange Act Rules 203(b)(1) and 203(b)(3);

B. Respondent Benson cease and desist from causing any violations and any future violations of Exchange Act Rules 203(b)(1) and 203(b)(3);

C. Respondent TJM is censured;

D. Respondent Benson be, and hereby is, suspended from association with any broker or dealer for a period of three (3) months, effective on the second Monday following the entry of this Order;

E. Respondent Burke be, and hereby is, suspended from acting in a supervisory capacity with any broker or dealer for a period of nine (9) months, effective on the second Monday following the entry of this Order;

F. Respondent TJM shall pay disgorgement in the amount of $541,000, payment of which shall be deemed satisfied by the payment of $541,000 to the CBOE's Business Conduct Committee pursuant to the CBOE's Decision Accepting Offer of Settlement (File No. 08-0049) within fifteen (15) business days of the entry of the CBOE's issuance of its Decision Accepting Offer of Settlement (File No. 08-0049).

G. Respondent Benson shall comply with the undertakings enumerated in Section III, paragraph 35 above; and

H. Respondent Burke shall comply with the undertakings enumerated in Section III, paragraph 36 above.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 200

[Release No. 34-60448]

Delegation of Authority to Director of Division of Enforcement

Agency: Securities and Exchange Commission.

Action: Final rule.

SUMMARY: The Commission is amending its rules to delegate authority to the Director of the Division of Enforcement to issue formal orders of investigation. These orders designate the enforcement staff authorized to issue subpoenas in connection with investigations under the federal securities laws. This action is intended to expedite the investigative process by removing the need for enforcement staff to seek Commission approval prior to performing routine functions. The Commission is adopting this delegation for a one-year period, and at the end of the period will evaluate whether to extend the delegation (though any formal orders issued during this period will remain in effect).

EFFECTIVE DATE: [Insert date of publication in the Federal Register].

FOR FURTHER INFORMATION CONTACT: Kenneth H. Hall, 202-551-4936, Office of Chief Counsel, Division of Enforcement, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-6553.

SUPPLEMENTARY INFORMATION: The Commission is authorized to conduct investigations of possible violations of the federal securities laws, which provide that "any member of the Commission or any officer designated by it is empowered to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda, or other records which the

Commission deems relevant or material to the inquiry." Section 21(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(b). See also, Section 19(c) of the Securities Act of 1933, 15 U.S.C. 77s(c); Section 42(b) of the Investment Company Act of 1940, 15 U.S.C. 80a-41(b); and Section 209(b) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-9(b). The Commission issues formal orders of investigation that authorize specifically-designated enforcement staff to exercise the Commission's statutory power to subpoena witnesses and take the other actions authorized by the relevant cited provisions. The Commission is delegating the authority to issue formal orders of investigation to the Director of the Division of Enforcement. This delegation will expedite the investigative process by reducing the time and paperwork previously associated with obtaining Commission authorization prior to issuing subpoenas.

In any case the Division Director deems appropriate, the recommendation that a formal order be issued may be submitted to the Commission for review.

Administrative Law Matters:

The Commission finds, in accordance with the Administrative Procedure Act (APA) (5 U.S.C. 553(b)(3)(A)), that this amendment relates solely to agency organization, procedure, or practice. Accordingly, the provisions of the APA regarding notice of the proposed rulemaking and opportunities for public participation, 5 U.S.C. 553, are not applicable. For the same reason, and because this amendment does not substantively affect the rights or obligations of non-agency parties, the provisions of the Small Business Regulatory Enforcement Fairness Act, 5 U.S.C. 804(3)(C), are not applicable. Additionally, the provisions of the Regulatory Flexibility Act, which apply only when notice and comment are required by the APA or other law, 5 U.S.C. 603, are not applicable. Section 23(a)(2) of the Securities Exchange Act, 15 U.S.C. 78w, requires the Commission, in adopting rules under that Act, to consider the anticompetitive effects of any rules it adopts. Because the amendment imposes no new burdens on parties in investigations, the Commission does not believe it will have any impact on competition. Finally, this amendment does not contain any collection of information requirements as defined by the Paperwork Reduction Act of 1980, as amended. Accordingly, the amendment is effective [Insert date of publication in the Federal Register].

List of Subjects in 17 CFR Part 200

Administrative practice and procedure, Authority delegations (Government agencies).

Text of Amendment

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 200—ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS

1. The authority citation for part 200, subpart A, continues to read in part as follows:

Authority: 15 U.S.C. 77o, 77s, 77sss, 78d, 78d-1, 78d-2, 78w, 78ll(d), 78mm, 80a-37, 80b-11, and 7202, unless otherwise noted.

* * * * *

2. Section 200.30-4 is amended by adding paragraph (a)(13) to read as follows:

§ 200.30-4 Delegation of authority to Director of Division of Enforcement.

* * * * *

(a) * * *

(13) For the period from [insert date of publication in the Federal Register] through [insert date that is one year after date of publication in the Federal Register], to order the making of private investigations pursuant to section 19(b) of the Securities Act of 1933 (15 U.S.C.

77s(b)), section 21(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(b)), section 42(b) of the Investment Company Act of 1940 (15 U.S.C. 80a-41(b) and section 209(b) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-9(b)). Orders issued pursuant to this delegation during this period will continue to have effect after [insert date that is one year after date of publication in the Federal Register].

* * * * *

By the Commission

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Dated: August 5, 2009

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60441 / August 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13570

In the Matter of Hazan Capital Management, LLC and Steven M. Hazan, Respondents.	ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDSINGS 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 Respondent Hazan Capital Management, LLC ("HCM") and Respondent Steven M. Hazan ("Hazan") (collectively, "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have 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 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' Offer, the Commission finds[1] that:

Summary

1. These proceedings arise out of Respondent HCM's violations of Regulation SHO ("Reg SHO"). Subject to certain exceptions, Reg SHO requires market participants seeking to effect a short sale to borrow, arrange to borrow, or have reasonable grounds to believe that a security can be borrowed prior to effecting the short sale. This is known as the "locate requirement." Market makers, who ensure liquidity in the market, are excepted from the locate requirement if they are engaged in bona fide market making activities. At the time, Reg SHO also required fail-to-deliver positions[2] in certain securities that persisted for thirteen consecutive settlement days to be immediately closed out.[3] In contrast to the locate requirement, market makers are not excepted from Reg SHO's close-out requirement.

2. In this case, HCM improperly relied on the market marker exception from Reg SHO's locate requirement and engaged in certain transactions that violated the locate and close out requirements. The first type of transaction – known in the industry as a "reverse conversion" or "reversal" – involves selling a put option and buying a call option – a combination that creates what is known as a "synthetic" long position – while selling short the underlying stock. The counterparty on the components of the reverse conversion – which is engaging in a "conversion" – benefits from the transaction because it is able to acquire a long stock position that is perfectly hedged by the synthetic short options position. That party can then loan out the shares of stock

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

2 Fails to deliver occur when a seller fails to deliver securities to the buyer when delivery is due. Generally, investors complete or settle their security transactions within three settlement days. This settlement cycle is known as T+3 (or "trade date plus three days"). T+3 means that when a trade occurs, the participants to the trade deliver and pay for the security at a clearing agency three days after the trade is executed so the brokerage firm can exchange those funds for the securities on that third settlement day. The three-day settlement period applies to most securities transactions, including stocks, bonds, municipal securities, mutual funds traded through a brokerage firm, and limited partnerships that trade on an exchange. Government securities and stock options settle on the next settlement day following the trade (or T+1).

3 A "close out" of a fail position involves the purchase of shares of like kind and quantity in the amount of the fail-to-deliver position.

and receive fees from the borrowers. Those fees can be quite significant when the stock is a threshold security, because threshold securities are hard to borrow and therefore command large fees in the stock loan market. Consequently, prime brokers created the demand for the reverse conversion to create inventory for stock loans on hard to borrow securities, and options market makers like HCM fed this demand.

3. The second type of transaction – referred to herein as a "reset" – is a transaction in which a market participant who has a "fail-to-deliver" position in a threshold security buys shares of that security while simultaneously selling short-term, deep in-the-money[4] call options to – or buying short-term, deep in-the-money put options from – the counterparty to the share purchase. The purchase of shares creates the illusion that the market participant has satisfied the close out obligation of Reg SHO. However, the shares that are apparently purchased in the reset transactions are never actually delivered to the purchaser because on the day after executing the reset, the option is either exercised (if a call) or assigned (if a put), transferring the shares back to the party that apparently sold them the previous day. This paired transaction allows the market participant with the fail-to-deliver position to effectively borrow the stock for a day, in order to appear to have satisfied the close out requirement of Rule 203(b)(3).

4. By avoiding the cost of borrowing shares and engaging in these reverse conversion and reset transactions, HCM was able to earn a profit while subject to minimal risk. Because HCM improperly failed to borrow or arrange to borrow securities to make delivery when delivery was due, the short sales were "naked" short sales[5] that violated Reg SHO.

5. Specifically, from January 2005 through October 2007, Respondent HCM – a putative options market maker – willfully violated Rule 203(b)(1) of Reg SHO by improperly claiming the market maker exception to avoid locating shares before effecting short sale transactions in Reg SHO threshold securities. HCM also willfully violated Rule 203(b)(3) of Reg SHO by engaging in a series of sham reset transactions that employed short-term, paired stock and option positions, which enabled HCM to circumvent its close out obligations in Reg SHO threshold

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4 An "in-the-money" option is an option that entitles its holder to either buy securities below the current market price for that security (in the case of a call option), or to sell securities above the market price (in the case of a put option). An option that is "deep in-the-money" has a strike price that is far below (in the case of a call option) or far above (in the case of a put) the market price for the given security.

5 In a "naked" short sale, the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard three-day settlement period. As a result, the seller fails to deliver the securities to the buyer when delivery is due.

securities.[6] HCM also assisted other options market makers who were executing their own sham reset transactions by acting as a counterparty to the sham transactions and in doing so violated the locate requirement. Respondent Hazan, the principal trader at HCM and its majority owner, willfully aided and abetted and caused HCM's violations of Rules 203(b)(1) and 203(b)(3) of Reg SHO.

Respondents

6. **Hazan Capital Management, LLC**, a New York limited liability company, is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act. HCM was a Regular Member Organization of the AMEX[7] until terminating its membership effective December 24, 2007. From June 2006 until on or about October 20, 2007, HCM was an Options Trading Permit Holder and market maker on the ARCA.

7. **Steven Moses Hazan**, age 31, is a resident of New York, New York. At all relevant times, Hazan was the majority owner and managing member of HCM and controlled its trading activity. During the relevant period, Hazan was registered as Regular Member and a registered options trader on the AMEX, and was also an Options Trading Permit Holder and market maker with the ARCA. Hazan's membership on the AMEX was terminated effective August 3, 2006; his membership on the ARCA was terminated on or about October 20, 2007.

Facts

HCM Failed to Locate Shares Prior to Effecting Short Sales

8. From January 2005 through October 2007,[8] HCM engaged in reverse conversions with purchasers of Reg SHO threshold securities.

9. In these reverse conversions, Hazan, on behalf of HCM, sold short shares of Reg SHO threshold securities while simultaneously creating a synthetic long position in those same securities by purchasing call options from, and selling put options to, the same counterparty to

[6] A "threshold security" is a security for which there is an aggregate fail-to-deliver position exceeding the size criteria set forth in Rule 203(c)(6) of Regulation SHO for a period of five consecutive settlement days.

[7] On October 1, 2008, the AMEX was acquired by NYSE Euronext and renamed NYSE Alternext US, LLC. On March 6, 2009, NYSE Alternext US, LLC was renamed NYSE Amex, LLC.

[8] The trading at issue took place on the AMEX during the period January 3, 2005 through July 31, 2006, and on the ARCA during the period June 2006 through October 20, 2007.

whom HCM was selling short the shares of the threshold securities. These call and put options had the same strike price and expiration date, and were options to buy (or sell) the same threshold securities that HCM sold short in the reverse conversion transactions. HCM purchased enough call options and put options so that the number of shares underlying the options equaled the number of shares it sold short. Through this set of transactions, HCM eliminated its market risk because the short position was used to hedge the synthetic long position that had been created by purchasing call options and selling put options.

10. The reverse conversion transactions in Reg SHO securities were profitable for HCM because the prices of the three separate components of the transactions – the short sale, the sale of the put options, and the purchase of the call options -- were interdependent, and were set at levels that created an agreed-upon net profit per share for HCM. That per-share net profit was the effective price of the conversion, a price that HCM's counterparties were willing to pay in order to obtain shares of hard-to-borrow Reg SHO threshold securities for the length of time between the original execution of the conversion and the expiration of the option components of the conversion.

11. In executing these reverse conversions, HCM claimed the market maker exception in Rule 203(b)(1) of Reg SHO and did not locate, arrange to borrow, or borrow shares of the security in question prior to effecting the short sale. This failure to locate, arrange to borrow, or borrow shares was improper, however, because HCM was not engaged in bona fide market making activity in connection with effecting the short sale transactions.

HCM Failed to Close Out Fail-to-Deliver Positions in Reg SHO Threshold Securities

12. HCM's short sales resulted in a fail-to-deliver position in the threshold security on the books and records of its clearing firm -- i.e. HCM had not delivered the shares it sold short to its clearing firm so that the clearing firm could settle the trade.

13. During the relevant time, Rule 203(b)(3) of Reg SHO required clearing firms immediately to close out any fail-to-deliver position in a threshold security that persists for thirteen consecutive settlement days by purchasing securities of a like kind and quantity. Specifically, at the relevant time, Rule 203(b)(3) required a participant of a clearing agency registered with the Commission to take immediate action to close out a fail-to-deliver position in a threshold security in the Continuous Net Settlement system that has persisted for thirteen consecutive settlement days. However, pursuant to Rule 203(b)(3)(vi) of Reg SHO, a clearing firm is permitted reasonably to allocate a fail-to-deliver position to a broker or dealer whose short sale resulted in the position. Once the clearing firm has allocated the fail-to-deliver position to another broker or dealer, the obligation for complying with the close out requirement shifts to that broker or dealer.

14. On numerous occasions from January 2005 through October 2007, HCM's clearing firm notified HCM that the clearing firm had allocated to HCM the obligation to close out fail-to-deliver positions in threshold securities. These notifications informed HCM that if it did not purchase shares sufficient to satisfy its fail-to-deliver position, the clearing firm would purchase (or "buy-in") those shares for HCM's account.

15. HCM did not want its fail-to-deliver position – which resulted from the short sale portion of the reverse conversion – to be closed out by the clearing firm because this would result in the clearing firm making large purchases of Reg SHO threshold securities, at HCM's expense, at a price determined by the market. Additionally, the close out would have exposed Respondent HCM to market risk on its reverse conversion transaction because it would have eliminated the short position that had been used to hedge HCM's synthetic long position created by the options component of the reverse conversion.

16. To avoid a forced close out, Hazan, on behalf of HCM, entered into a series of sham reset transactions that circumvented HCM's obligation under Reg SHO to close out its fail-to-deliver position. These complex sham transactions gave the appearance that HCM was closing out its fail-to-deliver position by purchasing securities of like kind and quantity.

17. Specifically, on numerous occasions, Hazan, on behalf of HCM, effected short-term in-the-money option transactions in conjunction with stock purchases to circumvent the Reg SHO close out requirements. HCM "purchased" stock in the Reg SHO threshold security from another market maker and simultaneously sold a short-term call option to (or purchased a short-term put option from) the same market maker. These combined stock and option transactions were either "married puts" (the purchase of stock in conjunction with the purchase of a put option on the same security) or "buy-writes" (the purchase of stock in conjunction with the sale (or "writing") of call options on the same security).

18. Although married puts and buy-writes can be created using standard options, the option component of HCM's reset transactions were usually established using "FLEX" options. FLEX options are exchange traded options for which the parties can customize certain terms of the options, including the strike price, expiration date, and exercise type (*i.e.*, American or European). HCM used these FLEX options because it did not intend to actually purchase the shares required to satisfy its close out obligation. Rather, it simply wanted to appear to have satisfied that obligation through a purported purchase of shares. Thus, HCM structured the reset transactions so that the options component of the transaction would expire very soon after the purported "purchase" of shares had been reflected in HCM's account at its clearing firm. Indeed, most of the FLEX options were customized to expire one day after they were purchased.[9]

[9] The options exchanges prohibited the trading of FLEX options on certain days right before and right after the standard expiration date of any given month (*i.e.*, the third

19. By entering into these reset transactions, HCM created the false impression that it had satisfied its Reg SHO close out obligation. HCM, however, knew that the following day, or shortly thereafter, the option would expire in-the-money, causing the market maker that had purchased that call option to assign an exercise notice to HCM for HCM to sell the stock. (In the case of a put option, HCM itself would exercise the right to sell the stock back to its counterparty.)

20. Moreover, HCM never actually received the stock it "purchased" from the other market maker because that market maker was selling short the stock without actually having any shares to sell.[10] Accordingly, HCM never received any shares and so never in fact closed out the "fail-to-deliver" position – as required by Reg SHO – that was initially established during the reverse conversion transaction. HCM knew, or should have known, that the combination of the purchase of shares and the sale of the FLEX option would result in maintenance of the "fail-to-deliver" position.

21. HCM's clearing firm, however, reset HCM's Reg SHO close out obligation to day one – thus giving HCM another thirteen settlement days in which to close out the short position – based on HCM's purported "purchase" of shares and exercise of the option.

22. After receiving subsequent close out notices from its clearing firm, HCM continued to engage in these and other types of transactions until the initial options positions (call options purchase/put options sale) expired or were assigned, thus closing out the short position and eliminating the synthetic long position that the short position had hedged. By engaging in this course of conduct, Hazan, on behalf of HCM, impermissibly maintained fail-to-deliver positions in numerous Reg SHO threshold securities longer than thirteen settlement days. Indeed, on numerous occasions, HCM's repeated use of reset transactions allowed it to maintain a large fail-to-deliver position in a threshold security for several months.

23. During the relevant period, HCM engaged in a large volume of reverse conversions and reset transactions in numerous threshold securities. As a result of HCM's repeated violation of Reg SHO's locate and close out requirements, it received ill-gotten gains of at least $3 million.

Saturday after the first Friday of the month). Thus, for reset transactions executed on those days, HCM used standard options to create the married puts and buy-writes.

10 These market makers were themselves improperly relying on Reg SHO's locate exception related to bona fide market making activity because they were not engaged in bona fide market making activity in connection with these short sales.

24. In addition, on numerous occasions, HCM assisted other putative market makers in evading their close out obligations by acting as the counterparty to reset transactions. Specifically, HCM sold short shares of Reg SHO threshold securities so that other market makers could "purchase" the securities to close out their own fail-to-deliver positions, and simultaneously bought deep in-the-money call options, the combination of which allowed the other market makers to circumvent their own Reg SHO close out obligations. HCM did not borrow, arrange to borrow, or locate the shares of these threshold securities prior to entering into the short sale component of these reset transactions.

VIOLATIONS

HCM Willfully Violated Rule 203(b)(1) of Reg SHO and Hazan Willfully Aided and Abetted and Caused HCM's Violation

25. Pursuant to the locate requirement of Rule 203(b)(1) of Reg SHO, a broker or dealer may not effect a short sale in an equity security unless it has "(i) [b]orrowed the security, or entered into a bona-fide arrangement to borrow the security; or (ii) [r]easonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due; and (iii) [d]ocumented compliance with [these requirements]."

26. Rule 203(b)(2)(iii) contains an exception to this locate requirement for short sales effected "by a market maker in connection with bona-fide market making activities in the security for which this exception is claimed."

27. At the time Hazan, on behalf of HCM, placed orders to sell short certain Reg SHO threshold securities as part of the reverse conversion transactions and reset transactions described above, he failed to borrow, arrange to borrow, or locate the securities, claiming the market maker exception to the locate requirement. The market maker exception was not available to HCM, however, because it was not engaging in bona-fide market making activities in these securities.

28. As a result of this conduct, HCM willfully violated, and Hazan willfully aided and abetted and caused HCM's violations, of Rule 203(b)(1) of Reg SHO.

HCM Willfully Violated Rule 203(b)(3) of Reg SHO and Hazan Willfully Aided and Abetted and Caused HCM's Violation

29. At the relevant time, Rule 203(b)(3) imposed an obligation on clearing firms immediately to close out any fail-to-deliver positions in a threshold security that lasts for thirteen consecutive settlement days[11] by purchasing securities of like kind and quantity. Pursuant to

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[11] In October 2008, the Commission adopted Rule 204T (which was made permanent as Rule 204 on July 27, 2009). Under Rule 204, clearing firms must close out fails-to-

Rule 203(b)(3)(vi), however, a clearing firm is permitted reasonably to allocate a fail-to-deliver position to a broker or dealer whose short sale resulted in the position. Once the clearing firm has allocated the fail-to-deliver position to another broker or dealer, the obligation to comply with the mandatory close out requirement shifts to that broker or dealer.

30. Once the fail-to-deliver position is allocated to the broker or dealer, that broker or dealer, in order to satisfy the close out requirement of Rule 203(b)(3) of Reg SHO, must purchase securities of like kind and quantity. Borrowing securities, or otherwise entering into an arrangement that merely creates the appearance of a purchase, does not satisfy Reg SHO's close out requirement.

31. In addition, Rule 203 of Reg SHO specifically prohibits firms from satisfying their close out obligations through sham transactions that merely give the appearance of closing out a fail-to-deliver position. Specifically, Rule 203(b)(3)(vii) provides that a clearing firm – or a broker or dealer to which the clearing firm allocated a fail-to-deliver position – will be deemed not to have satisfied the close out obligation if it knows, or has reasonable grounds to believe, that the close out purchase will result in a fail-to-deliver.

32. By selling (or purchasing) deep in-the-money FLEX call (or put) options while simultaneously purporting to "purchase" stock, Respondent HCM engaged in sham transactions that gave the appearance that it was closing out its fail-to-deliver position when, in fact, Respondent HCM knew, or should have known, that these transactions would result in a fail-to-deliver position.

33. As a result of this conduct, HCM willfully violated, and Hazan willfully aided and abetted and caused HCM's violations of, Rule 203(b)(3) of Reg SHO.

Undertakings

34. Respondent Hazan and Respondent HCM have undertaken to pay, jointly and severally, a fine in the amount of $500,000 to NYSE Amex, LLC pursuant to the terms of the decision by the NYSE Amex, LLC Hearing Board accepting the Stipulation of Facts and Consent to Penalty entered into by Respondents and NYSE Amex, LLC on February 19, 2009.

35. Respondent Hazan and Respondent HCM have undertaken to pay, jointly and severally, a fine in the amount of $500,000 to NYSE Arca, Inc. pursuant to the terms of the

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deliver on all securities (not just threshold securities) and must do so earlier than under Rule 203(b)(3). Clearing firms must now close out fails-to-deliver by either borrowing or purchasing sufficient shares before the beginning of trading hours on the first settlement day after the settlement date. Fails relating to long sales or bona fide market making activity have two additional settlement days before they must be closed out.

decision by the NYSE Arca, Inc. Hearing Board accepting the Stipulation of Facts and Consent to Penalty entered into by Respondents and NYSE Arca, Inc. on February 19, 2009.

In determining whether to accept Respondents' Offer, the Commission has considered these undertakings.

IV.

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

Accordingly, pursuant to Section 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

1. Respondent HCM shall cease and desist from committing or causing, and Respondent Hazan shall cease and desist from causing, any violations and any future violations of Exchange Act Rules 203(b)(1) and 203(b)(3);

2. Respondent Hazan be, and hereby is barred from association with any broker, or dealer, with the right to reapply for association after five (5) years to the appropriate self-regulatory organization, or if there is none, to the Commission.

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

4. Respondent HCM is censured;

5. Respondent Hazan and Respondent HCM shall pay, jointly and severally, disgorgement in the amount of $3,000,000. This order to pay disgorgement shall be deemed satisfied by the orders of NYSE Amex, LLC directing Respondent Hazan and Respondent HCM to pay disgorgement in the amount of $1,500,000, and NYSE Arca, Inc. directing Respondent Hazan and Respondent HCM to pay disgorgement in the amount of $1,500,000, in related actions brought by those self-regulatory organizations, NYSE Amex Disciplinary Proceedings against

Steven M. Hazan and Hazan Capital Management, LLC and NYSE Arca Disciplinary Proceedings against Steven M. Hazan and Hazan Capital Management, LLC.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-60451; August 5, 2009]

Notice Regarding the Requirement to Use eXtensible Business Reporting Language Format to Make Publicly Available the Information Required Pursuant to Rule 17g-2(d) of the Exchange Act

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

ACTION: Notice.

SUMMARY: The Commission today is providing notice that an NRSRO subject to the disclosure provisions of paragraph (d) of Rule 17g-2 can satisfy the requirement to make publicly available ratings history information in an XBRL format by using an XBRL format or any other machine-readable format, until such time as the Commission provides further notice.

DATES: The compliance date for Rule 17g-2(d) is August 10, 2009.

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, at (202) 551-5525; Thomas K. McGowan, Deputy Associate Director, at (202) 551-5521; Randall W. Roy, Assistant Director, at (202) 551-5522; Joseph I. Levinson, Special Counsel, at (202) 551-5598; or Rebekah E. Goshorn, Attorney, at (202), 551-5514; Division of Trading and Markets, Securities and Exchange Commission; 100 F Street, NE, Washington, DC 20549-7010.

SUPPLEMENTARY INFORMATION:

I. BACKGROUND

The Credit Rating Agency Reform Act of 2006 ("Rating Agency Act")[1] defined the term "nationally recognized statistical rating organization" ("NRSRO") and provided authority for the Securities and Exchange Commission ("Commission") to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies. The regulations implemented by the Commission pursuant to this mandate include Securities

[1] Public Law 109-291 (2006).

Exchange Act of 1934 ("Exchange Act") Rule 17g-2,[2] which requires an NRSRO to make and retain certain records relating to its business and to retain certain other business records made in the normal course of business operations.

On February 2, 2009, the Commission adopted amendments to its NRSRO rules imposing additional requirements on NRSROs in order to address concerns about the integrity of their credit rating procedures and methodologies.[3] Among other things, the rule amendments added new paragraphs (a)(8) and (d) to Rule 17g-2. New paragraph (a)(8) of Rule 17g-2 requires an NRSRO to make and retain a record for each outstanding credit rating it maintains showing all rating actions (initial rating, upgrades, downgrades, placements on watch for upgrade or downgrade, and withdrawals) and the date of such actions identified by the name of the security or obligor rated and, if applicable, the CUSIP for the rated security or the Central Index Key (CIK) number for the rated obligor.[4] New paragraph (d) of Rule 17g-2 requires an NRSRO to make publicly available, on a six-month delayed basis, the ratings histories for a random sample of 10% of the credit ratings paid for by the obligor being rated or by the issuer, underwriter, or sponsor of the security being rated ("issuer-paid credit ratings") pursuant to paragraph (a)(8) of Rule 17g-2 for each class of credit rating for which the NRSRO is registered and has issued 500 or more issuer-paid credit ratings.[5]

Paragraph (d) of Rule 17g-2 further requires that this information be made public on the NRSRO's corporate Internet Web site in eXtensible Business Reporting Language ("XBRL") format.[6] The rule provides that in preparing the XBRL disclosure, an NRSRO must use the List

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2 17 CFR 240.17g-2.

3 See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 59342 (February 2, 2009), 74 FR 6456 ("February 2009 Adopting Release").

4 17 CFR 240.17g-2(a)(8).

5 17 CFR 240.17g-2(d).

6 Id.

of XBRL Tags for NRSROs as specified on the Commission's Web site.[7] The Commission established a compliance date of August 10, 2009 for this provision.

The Commission today is providing notice that an NRSRO subject to the disclosure provisions of paragraph (d) of Rule 17g-2 can satisfy the requirement to make publicly available ratings history information in an XBRL format by using an XBRL format or any other machine-readable format, until such time as the Commission provides further notice.

II. DISCUSSION

The Commission adopted Rule 17g-2 and the amendments thereto, in part, under authority to require NRSROs to make and keep for specified periods such records as the Commission prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.[8] In adopting new paragraph (d) to Rule 17g-2, the Commission noted that although NRSROs generally make their issuer-paid credit ratings publicly available for free, it can be difficult to compile the actions and compare them across NRSROs.[9] The Commission therefore adopted the new disclosure requirements of paragraph (d) with the expectation that making this information more accessible will advance the Commission's goal of fostering accountability and comparability among NRSROs with respect to their issuer-paid credit ratings.[10] Requiring NRSROs to publicly disclose rating action histories for a limited percentage of their outstanding issuer-paid credit ratings will allow market participants, academics and others to use the information to perform

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7 Id. The February 2009 Adopting Release specified a compliance date of 180 days after publication in the Federal Register.

8 See Section 17(a)(1) of the Exchange Act (15 U.S.C. 78q(a)(1)).

9 See February 2009 Adopting Release, 74 FR at 6461.

10 Id at 6460.

analysis comparing how the NRSROs subject to the disclosure rule perform in the classes of credit ratings for which they are registered.[11]

As noted above, Rule 17g-2(d) provides that the ratings histories required under the rule must be made public on the NRSRO's corporate Internet Web site using an XBRL format.[12] Further, the rule requires an NRSRO to use the List of XBRL Tags for NRSROs published on the Commission's Web page. The List of XBRL Tags currently is not available. Therefore, the Commission is providing notice to NRSROs that they can satisfy the requirement in Rule 17g-2(d) to make publicly available ratings history information in an XBRL format by using an XBRL format or any other machine readable format, until such time as the Commission provides further notice. The Commission has every intention of providing notice as soon as practicable, once the List of XBRL Tags for NRSROs is available, that an XBRL format is the sole means by which an NRSRO may satisfy this requirement. Examples of other types of machine-readable formats include pipe delimited text data ("PDTD") and eXtensible Markup Language ("XML"). Data that is provided in a machine-readable format must be easily downloadable into commercially available spreadsheets or database programs.

The Commission also notes that the requirement in Exhibit 1 to Form NRSRO which states that "If the Applicant/NRSRO is required to make and keep publicly available on its corporate Internet Web site in an XBRL (eXtensible Business Reporting Language) format a sample of ratings action information pursuant to the requirements of 17 CFR 240.17g-2(d), provide in this Exhibit the Web site address where this information is, or will be, made publicly available" can be satisfied by providing the Web site address where the information is made

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11 Id at 6461

12 17 CFR 240.17g-2(d).

publicly available in an XBRL format or any other machine readable format, until such time as the Commission provides further notice.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60447 / August 5, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-12720

In the Matter of GENERAL AMERICAN LIFE INSURANCE COMPANY AND WILLIAM C. THATER, Respondents.	ORDER DIRECTING DISBURSEMENT OF FAIR FUND

On May 23, 2008, the United States Securities and Exchange Commission ("Commission") published a plan of distribution ("Distribution Plan") and issued a Notice of Proposed Distribution Plan and Opportunity for Comment (Exchange Act Rel. No. 57863) pursuant to Rule 1103 of the Commission's Rules on Fair Funds and Disgorgement Plans, 17 C.F.R. §201.1103. The Notice advised parties they could obtain a copy of the Distribution Plan at www.sec.gov. The Notice also advised that all persons desiring to comment on the Distribution Plan could submit their comments, in writing, no later than June 23, 2008. No comments were received by the Commission in response to the Notice. On July 25, 2008, the Commission issued an Order Approving the Distribution Plan, Appointing a Plan Administrator and Waiving Bond. (Exchange Act Rel. No. 58225).

The Distribution Plan provides that the Commission will arrange for distribution of the Fair Fund when a validated electronic payment file listing the payees with the identification information required to make the distribution has been received and accepted. The validated electronic payment file has been received and accepted for the disbursement of $3,532,822.80.

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Accordingly, it is ORDERED that the Commission staff shall disburse the Fair Fund in the amount stated in the validated electronic payment file of $3,532,822.80, as provided for in the Distribution Plan.

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. 60453 / August 6, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13572

In the Matter of **FREEHAND SYSTEMS INTERNATIONAL, 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 FreeHand Systems International, Inc. ("FreeHand" 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, 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, as set forth below.

III.

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

A. FreeHand, a Delaware corporation based in Los Altos, California, produces hardware and software technology applications for the sheet music industry. The common stock of

FreeHand is registered under Section 12(g) of the Exchange Act. FreeHand common stock is quoted through the Pink Sheets managed by Pink OTC.

B. FreeHand has 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-K or Form 10-KSB, or periodic or quarterly reports on Form 10-Q or Form 10-QSB, for any fiscal period subsequent to its fiscal quarter ending December 31, 2007.

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

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 10, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13573

In the Matter of **Tops Appliance City, Inc.,** **Tower Global Ventures Corp.** **(n/k/a Coffeehouse.com, Inc.),** **Transact International, Inc.,** **Transderm Laboratories Corp.,** **Trizak Corp., and** **Tropic Air Cargo, 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 Tops Appliance City, Inc., Tower Global Ventures Corp. (n/k/a Coffeehouse.com, Inc.), Transact International, Inc., Transderm Laboratories Corp., Trizak Corp., and Tropic Air Cargo, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Tops Appliance City, Inc. (CIK No. 888470) is an inactive New Jersey corporation located in Edison, New Jersey with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tops Appliance 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 28, 1999, which reported a net loss of over $5.7 million for the prior nine months. On February 2, 2000, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of New Jersey. On April 17, 2000, the case was converted to Chapter 7 and is still pending. As of August 5, 2009, the company's stock (symbol "TAPLQ") was traded on the over-the-counter markets.

2. Tower Global Ventures Corp. (n/k/a Coffeehouse.com, Inc.) (CIK No. 1103580) is an inactive Delaware corporation located in New Britain, Connecticut with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tower Global 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.

3. Transact International, Inc. (CIK No. 102701) is a Connecticut corporation located in Darien, Connecticut with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Transact 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 April 30, 1999, which reported a net loss of $505,929 for the prior twelve months. As of August 5, 2009, the company's stock (symbol "TRAH") was traded on the over-the-counter markets.

4. Transderm Laboratories Corp. (CIK No. 948704) is a Delaware corporation located in Emigsville, Pennsylvania with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Transderm 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, 2007, which reported a net loss of over $1.9 million for the prior six months. As of August 5, 2009, the company's stock (symbol "TLCC") was traded on the over-the-counter markets.

5. Trizak Corp. (CIK No. 16760) is a revoked Georgia corporation located in Delray Beach, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Trizak 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 December 31, 1994. As of August 5, 2009, the company's stock (symbol "TIZK") was no longer publicaly quoted or traded.

6. Tropic Air Cargo, Inc. (CIK No. 791027) is a void Delaware corporation located in Miami, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tropic Air 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, 1998, which reported a net loss of over $1 million for the prior nine months. As of August 5, 2009, the company's stock (symbol "TRPC") 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 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 registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

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, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any 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
Tops Appliance City, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tops Appliance City, Inc.					
	10-KSB	12/28/99	03/27/00	Not filed	113
	10-QSB	03/28/00	05/12/00	Not filed	111
	10-QSB	06/27/00	08/11/00	Not filed	108
	10-QSB	09/26/00	11/10/00	Not filed	105
	10-KSB	12/26/00	03/26/01	Not filed	101
	10-QSB	03/27/01	05/11/01	Not filed	99
	10-QSB	06/26/01	08/10/01	Not filed	96
	10-QSB	09/25/01	11/09/01	Not filed	93
	10-KSB	12/26/01	03/26/02	Not filed	89
	10-QSB	03/26/02	05/10/02	Not filed	87
	10-QSB	06/25/02	08/09/02	Not filed	84
	10-QSB	09/24/02	11/08/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/25/03	05/09/03	Not filed	75
	10-QSB	06/24/03	08/08/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/30/03	03/29/04	Not filed	65
	10-QSB	03/30/04	05/14/04	Not filed	63
	10-QSB	06/29/04	08/13/04	Not filed	60
	10-QSB	09/28/04	11/12/04	Not filed	57
	10-KSB	12/28/04	03/28/05	Not filed	53
	10-QSB	03/29/05	05/13/05	Not filed	51
	10-QSB	06/28/05	08/12/05	Not filed	48
	10-QSB	09/27/05	11/11/05	Not filed	45
	10-KSB	12/27/05	03/27/06	Not filed	41
	10-QSB	03/28/06	05/12/06	Not filed	39
	10-QSB	06/27/06	08/11/06	Not filed	36
	10-QSB	09/26/06	11/10/06	Not filed	33
	10-KSB	12/26/06	03/26/07	Not filed	29
	10-QSB	03/27/07	05/11/07	Not filed	27
	10-QSB	06/26/07	08/10/07	Not filed	24
	10-QSB	09/25/07	11/09/07	Not filed	21

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tops Appliance City, Inc.					
	10-KSB	12/26/07	03/25/08	Not filed	17
	*10-Q**	03/25/08	05/09/08	Not filed	15
	*10-Q**	06/24/08	08/08/08	Not filed	12
	*10-Q**	09/23/08	11/07/08	Not filed	9
	*10-K**	12/30/08	03/30/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**38**				
Tower Global Ventures Corp. (n/k/a Coffeehouse.com, Inc.)					
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tower Global Ventures Corp. (n/k/a Coffeehouse.com, Inc.)					
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**33**				
Transact International, Inc.					
	10-QSB	07/31/99	09/14/99	Not filed	119
	10-QSB	10/31/99	12/15/99	Not filed	116
	10-QSB	01/31/00	03/16/00	Not filed	113
	10-KSB	04/30/00	07/31/00	Not filed	109
	10-QSB	07/31/00	09/14/00	Not filed	107
	10-QSB	10/31/00	12/15/00	Not filed	104
	10-QSB	01/31/01	03/19/01	Not filed	101
	10-KSB	04/30/01	07/30/01	Not filed	97
	10-QSB	07/31/01	09/14/01	Not filed	95
	10-QSB	10/31/01	12/17/01	Not filed	92
	10-QSB	01/31/02	03/18/02	Not filed	89
	10-KSB	04/30/02	07/29/02	Not filed	85
	10-QSB	07/31/02	09/16/02	Not filed	83
	10-QSB	10/31/02	12/16/02	Not filed	80
	10-QSB	01/31/03	03/17/03	Not filed	77
	10-KSB	04/30/03	07/29/03	Not filed	73
	10-QSB	07/31/03	09/15/03	Not filed	71
	10-QSB	10/31/03	12/15/03	Not filed	68
	10-QSB	01/31/04	03/16/04	Not filed	65

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Transact International, Inc.					
	10-KSB	04/30/04	07/29/04	Not filed	61
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-QSB	10/31/04	12/15/04	Not filed	56
	10-QSB	01/31/05	03/17/05	Not filed	53
	10-KSB	04/30/05	07/29/05	Not filed	49
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-QSB	10/31/05	12/15/05	Not filed	44
	10-QSB	01/31/06	03/17/06	Not filed	41
	10-KSB	04/30/06	07/31/06	Not filed	37
	10-QSB	07/31/06	09/14/06	Not filed	35
	10-QSB	10/31/06	12/15/06	Not filed	32
	10-QSB	01/31/07	03/19/07	Not filed	29
	10-KSB	04/30/07	07/30/07	Not filed	25
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-QSB	10/31/07	12/17/07	Not filed	20
	10-QSB	01/31/08	03/17/08	Not filed	17
	10-KSB	04/30/08	07/29/08	Not filed	13
	*10-Q**	07/31/08	09/15/08	Not filed	11
	*10-Q**	10/31/08	12/15/08	Not filed	8
	*10-Q**	01/31/09	03/17/09	Not filed	5
	*10-K**	04/30/09	07/29/09	Not filed	1
Total Filings Delinquent	**40**				
Transderm Laboratories Corp.					
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**7**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Trizak Corp.					
	10-KSB	03/31/95	06/29/95	Not filed	170
	10-QSB	06/30/95	08/14/95	Not filed	168
	10-QSB	09/30/95	11/14/95	Not filed	165
	10-QSB	12/31/95	02/14/96	Not filed	162
	10-KSB	03/31/96	07/01/96	Not filed	157
	10-QSB	06/30/96	08/14/96	Not filed	156
	10-QSB	09/30/96	11/14/96	Not filed	153
	10-QSB	12/31/96	02/14/97	Not filed	150
	10-KSB	03/31/97	06/30/97	Not filed	146
	10-QSB	06/30/97	08/14/97	Not filed	144
	10-QSB	09/30/97	11/14/97	Not filed	141
	10-QSB	12/31/97	02/17/98	Not filed	138
	10-KSB	03/31/98	06/29/98	Not filed	134
	10-QSB	06/30/98	08/14/98	Not filed	132
	10-QSB	09/30/98	11/16/98	Not filed	129
	10-QSB	12/31/98	02/16/99	Not filed	126
	10-KSB	03/31/99	06/29/99	Not filed	122
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-QSB	12/31/99	02/14/00	Not filed	114
	10-KSB	03/31/00	06/29/00	Not filed	110
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-QSB	12/31/00	02/14/01	Not filed	102
	10-KSB	03/31/01	06/29/01	Not filed	98
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-QSB	12/31/01	02/14/02	Not filed	90
	10-KSB	03/31/02	07/01/02	Not filed	85
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-QSB	12/31/02	02/14/03	Not filed	78
	10-KSB	03/31/03	06/30/03	Not filed	74
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-QSB	12/31/03	02/17/04	Not filed	66
	10-KSB	03/31/04	06/29/04	Not filed	62
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Trizak Corp.					
	10-QSB	12/31/04	02/14/05	Not filed	54
	10-KSB	03/31/05	06/29/05	Not filed	50
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-QSB	12/31/05	02/14/06	Not filed	42
	10-KSB	03/31/06	06/29/06	Not filed	38
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-QSB	12/31/06	02/14/07	Not filed	30
	10-KSB	03/31/07	06/29/07	Not filed	26
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-QSB	12/31/07	02/14/08	Not filed	18
	10-KSB	03/31/08	06/30/08	Not filed	14
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-Q**	12/31/08	02/17/09	Not filed	6
	*10-K**	03/31/09	06/29/09	Not filed	2
Total Filings Delinquent	**57**				
Tropic Air Cargo, Inc.					
	10-KSB	12/31/98	03/31/99	Not filed	125
	10-QSB	03/31/99	05/17/99	Not filed	123
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Tropic Air Cargo, Inc.					
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3

Total Filings Delinquent **42**

*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.

Commissioner Aguilar not participating

SECURITIES AND EXCHANGE COMMISSION
[Release No. 34-60473; August 10, 2009]

Order Providing NRSROs a Temporary Exemption from the Requirement in Rule 17g-2(d) (Incorporating the Provisions of Rule 17g-2(a)(8)) of the Securities Exchange Act of 1934 that CUSIP Numbers Be Displayed

I. BACKGROUND

The Credit Rating Agency Reform Act of 2006 ("Rating Agency Act")[1] defined the term "nationally recognized statistical rating organization" ("NRSRO") and provided authority for the Securities and Exchange Commission ("Commission") to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies. The regulations implemented by the Commission pursuant to this mandate include Securities Exchange Act of 1934 ("Exchange Act") Rule 17g-2,[2] which requires an NRSRO to make and retain certain records relating to its business and to retain certain other business records made in the normal course of business operations.

On February 2, 2009, the Commission adopted amendments to its NRSRO rules imposing additional requirements on NRSROs in order to address concerns about the integrity of their credit rating procedures and methodologies.[3] Among other things, the rule amendments added new paragraphs (a)(8) and (d) to Rule 17g-2. New paragraph (a)(8) of Rule 17g-2 requires an NRSRO to make and retain a record for each outstanding credit rating it maintains showing all rating actions (initial rating, upgrades, downgrades, placements on watch for upgrade or downgrade, and withdrawals) "identified by the

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1 Public Law 109-291 (2006).

2 17 CFR 240.17g-2.

3 See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 59342 (February 2, 2009), 74 FR 6456 ("February 2009 Adopting Release").

name of the rated security or obligor and, if applicable, the CUSIP of the rated security or the Central Index Key (CIK) number of the rated obligor."[4] New paragraph (d) of Rule 17g-2 requires an NRSRO to make publicly available, on a six-month delayed basis, the ratings histories for a random sample of 10% of the credit ratings paid for by the obligor being rated or by the issuer, underwriter, or sponsor of the security being rated ("issuer-paid credit ratings") pursuant to paragraph (a)(8) of Rule 17g-2 for each class of credit rating for which the NRSRO is registered and has issued 500 or more issuer-paid credit ratings.[5]

Paragraph (d) of Rule 17g-2 further requires that this information be made public on the NRSRO's corporate Internet Web site in eXtensible Business Reporting Language ("XBRL") format.[6] The rule provides that in preparing the XBRL disclosure, an NRSRO must use the List of XBRL Tags for NRSROs as specified on the Commission's Web site.[7] The Commission established a compliance date of August 10, 2009 for this provision.

The XBRL tags are not yet available. Therefore, the Commission issued a Notice on August 5, 2009 that an NRSRO subject to the disclosure provisions of Rule 17g-2(d) can satisfy the requirement to make publicly available ratings history information in an XBRL format by using an XBRL format or any other machine readable format until such time as the Commission provides further notice.[8]

4 17 CFR 240.17g-2(a)(8).
5 17 CFR 240.17g-2(d).
6 Id.
7 Id. The February 2009 Adopting Release specified a compliance date of 180 days after publication in the Federal Register.
8 Notice Regarding the Requirement to Use eXtensible Business Reporting Language Format to Make Publicly Available the Information Required Pursuant to Rule 17g-2(d) of the

As noted above, the required rating actions information includes, if applicable, the CUSIP of each rated security and the CIK number of each rated obligor. Although CIK numbers are available free of charge on the Commission's Web site, CUSIPs are owned and distributed by private parties.

Subsequent to the issuance of the August 5, 2009 Notice, several NRSROs have notified Commission staff that, despite their efforts, they have not been able to resolve certain issues with the managers of the CUSIP program. The Commission believes, however, that users of credit ratings would benefit from having ratings action information available by the August 10, 2009 implementation date for Rule 17g-2(d), even if CUSIP numbers are not included for a limited time. We note that identifying information, such as the name of the security, will be included.

For these reasons, the Commission finds that providing NRSROs a partial temporary exemption from Rule 17g-2(d) (incorporating the provisions of Rule 17g-2(a)(8)) is necessary and appropriate in the public interest and is consistent with the protection of investors.[9] Therefore, the Commission is providing NRSROs with a 30-day exemption from the requirement in Rule 17g-2(d) (incorporating the provisions of Rule 17g-2(a)(8)) that the CUSIP for each rated security be included with the ratings action information.

II. CONCLUSION

Accordingly, pursuant to Section 36 of the Exchange Act,

Exchange Act, Exchange Act Release No. 60451, August 5, 2009 ("August 5, 2009 Notice").

9 Section 36 of the Exchange Act authorizes the Commission, by rule, regulation, or order, to conditionally or unconditionally exempt any person from any rule under the Exchange Act, to the extent that the exemption is necessary or appropriate in the public interest and is consistent with the protection of investors. 15 U.S.C. 78mm.

IT IS HEREBY ORDERED that NRSROs are temporarily exempt from the requirement in Rule 17g-2(d) (incorporating the provisions of Rule 17g-2(a)(8)) that the CUSIP for each rated security be included with the ratings action information for thirty days, until September 9, 2009.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13575

In the Matter of **V-Twin Holdings, Inc.** **(n/k/a Tobacco One, Inc.),** **Valley Media, Inc.,** **Venturequest Group, Inc.** **(n/k/a Dex-Ray Resources, Inc.),** **Verex Laboratories, Inc.,** **Vibro-Tech Industries, Inc.,** **Video City, Inc., and** **Vidikron Technologies Group, 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 V-Twin Holdings, Inc. (n/k/a Tobacco One, Inc.), Valley Media, Inc., Venturequest Group, Inc. (n/k/a Dex-Ray Resources, Inc.), Verex Laboratories, Inc., Vibro-Tech Industries, Inc., Video City, Inc., and Vidikron Technologies Group, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. V-Twin Holdings, Inc. (n/k/a Tobacco One, Inc.) (CIK No. 1067597) is a District of Columbia corporation located in Las Vegas, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). V-Twin Holdings 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 $2,308,680 for the prior nine months. As of July 22, 2009, the company's stock (symbol "TBCO") 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).

2. Valley Media, Inc. (CIK No. 1074908) is a forfeited Delaware corporation located in Woodland, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Valley Media 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 29, 2001, which reported a net loss of $50,308,000 for the prior twenty-six weeks. On November 21, 2001, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Delaware, and the case was terminated on January 18, 2006. As of July 22, 2009, the company's stock (symbol "VMIXQ") 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).

3. Venturequest Group, Inc. (n/k/a Dex-Ray Resources, Inc.) (CIK No. 1017483) is a defaulted Nevada corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Venturequest Group 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 $335,552 for the prior nine months. As July 22, 2009, the company's stock (symbol "DXRY") 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. Verex Laboratories, Inc. (CIK No. 716861) is a non-compliant Colorado corporation located in Englewood, Colorado with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Verex Laboratories 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, 2002, which reported a net loss of $92,247 for the prior three months. As of July 22, 2009, the company's stock (symbol "VRXL") 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).

5. Vibro-Tech Industries, Inc. (CIK No. 1099386) is a void Delaware corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Vibro-Tech Industries is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-SB on January 5, 2000. As of July 22, 2009, the company's stock (symbol "VBTH") 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).

6. Video City, Inc. (CIK No. 773135) is a forfeited Delaware corporation located in Bakersfield, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Video City 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 31, 2003, which reported a net loss of $996,747 for the prior six months. On March 24, 2004, the company filed a Chapter 7 petition in the U.S.

Bankruptcy Court for the Eastern District of California, and the case was terminated on December 3, 2007. As of July 22, 2009, the company's stock (symbol "VDCY") was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

7. Vidikron Technologies Group, Inc. (CIK No. 848135) is a void Delaware corporation located in Jersey City, New Jersey with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Vidikron Technologies 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, 1999, which reported a net loss of $1,680,091 for the prior three months. On November 12, 1999, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the District of New Jersey, and the case was terminated on May 17, 2004. As of July 22, 2009, the company's stock (symbol "VIDI") 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).

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.

10. 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 V-Twin Holdings, Inc. (n/k/a Tobacco One, Inc.), et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
V-Twin Holdings, Inc. (n/k/a Tobacco One, Inc.)					
	10-KSB	06/30/01	9/28/01	Not filed	95
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-QSB	12/31/01	2/14/02	Not filed	90
	10-QSB	03/31/02	5/15/02	Not filed	87
	10-KSB	06/30/02	9/30/02	Not filed	83
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-QSB	12/31/02	2/14/03	Not filed	78
	10-QSB	03/31/03	5/15/03	Not filed	75
	10-KSB	06/30/03	9/29/03	Not filed	71
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-QSB	12/31/03	2/17/04	Not filed	66
	10-QSB	03/31/04	5/17/04	Not filed	63
	10-KSB	06/30/04	9/28/04	Not filed	59
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-QSB	12/31/04	2/14/05	Not filed	54
	10-QSB	03/31/05	5/16/05	Not filed	51
	10-KSB	06/30/05	9/28/05	Not filed	47
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-QSB	12/31/05	2/14/06	Not filed	42
	10-QSB	03/31/06	5/15/06	Not filed	39
	10-KSB	06/30/06	9/28/06	Not filed	35
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-QSB	12/31/06	2/14/07	Not filed	30
	10-QSB	03/31/07	5/15/07	Not filed	27
	10-KSB	06/30/07	9/28/07	Not filed	23
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-QSB	12/31/07	2/14/08	Not filed	18
	10-QSB	03/31/08	5/15/08	Not filed	15
	10-KSB	06/30/08	9/29/08	Not filed	11
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-Q**	12/31/08	2/17/09	Not filed	6
	*10-Q**	03/31/09	5/15/09	Not filed	3
Total Filings Delinquent	32				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Valley Media, Inc.					
	10-Q	12/29/01	02/12/02	Not filed	90
	10-K	03/30/02	06/28/02	Not filed	86
	10-Q	06/29/02	08/13/02	Not filed	84
	10-Q	09/28/02	11/12/02	Not filed	81
	10-Q	12/28/02	02/11/03	Not filed	78
	10-K	03/29/03	06/27/03	Not filed	74
	10-Q	06/28/03	08/12/03	Not filed	72
	10-Q	09/27/03	11/11/03	Not filed	69
	10-Q	01/03/04	02/17/04	Not filed	66
	10-K	04/03/04	07/02/04	Not filed	61
	10-Q	07/03/04	08/17/04	Not filed	60
	10-Q	10/02/04	11/16/04	Not filed	57
	10-Q	01/01/05	02/15/05	Not filed	54
	10-K	04/02/05	07/01/05	Not filed	49
	10-Q	07/02/05	08/16/05	Not filed	48
	10-Q	10/01/05	11/15/05	Not filed	45
	10-Q	12/31/05	02/14/06	Not filed	42
	10-K	04/01/06	06/30/06	Not filed	38
	10-Q	07/01/06	08/15/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-Q	12/30/06	02/13/07	Not filed	30
	10-K	03/31/07	06/29/07	Not filed	26
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/29/07	11/13/07	Not filed	21
	10-Q	12/29/07	02/12/08	Not filed	18
	10-K	03/29/08	06/27/08	Not filed	14
	10-Q	06/28/08	08/12/08	Not filed	12
	10-Q	09/27/08	11/11/08	Not filed	9
	10-Q	12/27/08	02/10/09	Not filed	6
	10-K	03/28/09	06/26/09	Not filed	2
Total Filings Delinquent	**30**				
Venturequest Group, Inc. (n/k/a Dex-Ray Resources, Inc.)					
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Venturequest Group, Inc. (n/k/a Dex-Ray Resources, Inc.) (continued)	*10-KSB*	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	5/15/09	Not filed	3
Total Filings Delinquent	**29**				
Verex Laboratories, Inc.					
	10-K	06/30/02	09/30/02	Not filed	83
	10-Q	09/30/02	11/14/02	Not filed	81
	10-Q	12/31/02	02/14/03	Not filed	78
	10-Q	03/31/03	05/15/03	Not filed	75
	10-K	06/30/03	09/29/03	Not filed	71
	10-Q	09/30/03	11/14/03	Not filed	69
	10-Q	12/31/03	02/17/04	Not filed	66
	10-Q	03/31/04	05/17/04	Not filed	63
	10-K	06/30/04	09/28/04	Not filed	59
	10-Q	09/30/04	11/15/04	Not filed	57

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Verex Laboratories, Inc.	*10-Q*	12/31/04	02/14/05	Not filed	54
(continued)	*10-Q*	03/31/05	05/16/05	Not filed	51
	10-K	06/30/05	09/28/05	Not filed	47
	10-Q	09/30/05	11/14/05	Not filed	45
	10-Q	12/31/05	02/14/06	Not filed	42
	10-Q	03/31/06	05/15/06	Not filed	39
	10-K	06/30/06	09/28/06	Not filed	35
	10-Q	09/30/06	11/14/06	Not filed	33
	10-Q	12/31/06	02/14/07	Not filed	30
	10-Q	03/31/07	05/15/07	Not filed	27
	10-K	06/30/07	09/28/07	Not filed	23
	10-Q	09/30/07	11/14/07	Not filed	21
	10-Q	12/31/07	02/14/08	Not filed	18
	10-Q	03/31/08	05/15/08	Not filed	15
	10-K	06/30/08	09/28/08	Not filed	11
	10-Q	09/30/08	11/14/08	Not filed	9
	10-Q	12/31/07	02/17/08	Not filed	18
	10-Q	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**27**				
Vibro-Tech Industries, Inc.					
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Vibro-Tech Industries, Inc.	*10-QSB*	09/30/04	11/15/04	Not filed	57
(continued)	*10-KSB*	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	37				
Video City, Inc.					
	10-QSB	10/31/03	12/15/03	Not filed	68
	10-KSB	01/31/04	04/30/04	Not filed	64
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-QSB	10/31/04	12/15/04	Not filed	56
	10-KSB	01/31/05	05/02/05	Not filed	51
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-QSB	10/31/05	12/15/05	Not filed	44
	10-KSB	01/31/06	05/01/06	Not filed	39
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-QSB	07/31/06	09/14/06	Not filed	35
	10-QSB	10/31/06	12/15/06	Not filed	32
	10-KSB	01/31/07	05/01/07	Not filed	27
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-QSB	10/31/07	12/17/07	Not filed	20

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Video City, Inc. (continued)	*10-KSB*	01/31/08	04/30/08	Not filed	16
	*10-Q**	04/30/08	06/16/08	Not filed	14
	*10-Q**	07/31/08	09/15/08	Not filed	11
	*10-Q**	10/31/08	12/17/08	Not filed	8
	*10-K**	01/31/09	05/01/09	Not filed	3
	*10-Q**	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	23				
Vidikron Technologies Group, Inc.					
	10-Q	06/30/99	08/16/99	Not filed	120
	10-Q	09/30/99	11/15/99	Not filed	117
	10-K	12/31/99	03/30/00	Not filed	113
	10-Q	03/31/00	05/15/00	Not filed	111
	10-Q	06/30/00	08/14/00	Not filed	108
	10-Q	09/30/00	11/14/00	Not filed	105
	10-K	12/31/00	04/02/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	99
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-K	12/31/01	04/01/02	Not filed	88
	10-Q	03/31/02	05/15/02	Not filed	87
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-K	12/31/02	03/31/03	Not filed	77
	10-Q	03/31/03	05/15/03	Not filed	75
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69
	10-K	12/31/03	03/30/04	Not filed	65
	10-Q	03/31/04	05/17/04	Not filed	63
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-K	12/31/04	03/31/05	Not filed	53
	10-Q	03/31/05	05/16/05	Not filed	51
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-K	12/31/05	03/31/06	Not filed	41
	10-Q	03/31/06	05/15/06	Not filed	39
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Vidikron Technologies Group, Inc.	*10-K*	12/31/06	04/02/07	Not filed	28
(continued)	*10-Q*	03/31/07	05/15/07	Not filed	27
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/30/07	11/14/07	Not filed	21
	10-K	12/31/07	03/31/08	Not filed	17
	10-Q	03/31/08	05/15/08	Not filed	15
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-K	12/31/08	03/31/09	Not filed	5
	10-Q	03/31/09	05/15/09	Not filed	3

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.

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

August 11, 2009

In the Matter of **V-Twin Holdings, Inc.** **(n/k/a Tobacco One, Inc.),** **Valley Media, Inc.,** **Venturequest Group, Inc.** **(n/k/a Dex-Ray Resources, Inc.),** **Verex Laboratories, Inc.,** **Vibro-Tech Industries, Inc.,** **Video City, Inc., and** **Vidikron Technologies 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 V-Twin Holdings, Inc. (n/k/a Tobacco One, Inc.) because it has not filed any periodic reports since the period ended March 31, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Valley Media, Inc. because it has not filed any periodic reports since the period ended September 29, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Venturequest Group, Inc. (n/k/a Dex-Ray Resources, Inc.), because it has not filed any periodic reports since the period ended September 30, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Verex Laboratories, Inc. because it has not filed any periodic reports since the period ended March 31, 2002.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Vibro-Tech Industries, Inc. because it has not filed any periodic reports since it filed a Form 10-SB on January 5, 2000.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Video City, Inc. because it has not filed any periodic reports since the period ended July 31, 2003.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Vidikron Technologies Group, Inc. because it has not filed any periodic reports since the period ended March 31, 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 August 11, 2009, through 11:59 p.m. EDT on August 24, 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
August 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13576

In the Matter of **What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.), Wherehouse Entertainment, Inc., Windpower Partners 1983-1, Windpower Partners 1984, World Financial Systems Co. Ltd., Wrap-N-Roll USA, Inc., and Wyrlis 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 What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.), Wherehouse Entertainment, Inc., Windpower Partners 1983-1, Windpower Partners 1984, World Financial Systems Co. Ltd., Wrap-N-Roll USA, Inc., and Wyrlis Corp.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.) (CIK No. 881460) is a revoked Nevada corporation located in Scottsdale, Arizona with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). What's For Free 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, 2000, which reported a net loss of over $20 million for the prior nine months. As of August 6, 2009, the company's stock (symbol "KFTG") was traded on the over-the-counter markets.

2. Wherehouse Entertainment, Inc. (CIK No. 1031754) is a delinquent Delaware corporation located in Torrance, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Wherehouse 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 31, 2002, which reported a net loss of over $20 million for the prior six months. On January 20, 2003, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Delaware, a reorganization plan was confirmed on March 15, 2004, and the case was terminated on December 27, 2006. As of August 6, 2009, the company's stock (symbol "WHENQ") was no longer publicly quoted or traded.

3. Windpower Partners 1983-1 (CIK No. 719934) is a cancelled California limited partnership located in San Francisco, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Windpower 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, 1995, which reported a net loss of over $6.3 million for the prior three months.

4. Windpower Partners 1984 (CIK No. 746059) is a cancelled California limited partnership located in San Francisco, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Windpower 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 16, 1994, which reported a net loss of over $3.7 million for the prior twelve months, and a cessation of operations as of December 16, 1994.

5. World Financial Systems Co. Ltd. (CIK No. 1174783) is a defaulted Nevada corporation located in Las Vegas, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). World Financial 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 23, 2002, which reported a net loss of $2,050 for the fiscal year ended July 15, 2002.

6. Wrap-N-Roll USA, Inc. (CIK No. 1105858) is a defaulted Nevada corporation located in Salt Lake City, Utah with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Wrap-N-Roll 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, 2006, which reported a net loss of $34,863 for the prior twenty-seven months.

7. Wyrlis Corp. (CIK No. 1175025) is a permanently revoked Nevada corporation located in Mesa, Arizona with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Wyrlis 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 June 18, 2002, which reported a net loss of $6,965 since inception on February 26, 2002.

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 issuers to file quarterly reports.

10. 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.

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

<u>*Appendix 1*</u>

Chart of Delinquent Filings

What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.), et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.)					
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
What's For Free Technologies, Inc. (n/k/a Krifter Holdings, Inc.)					
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**34**				
Wherehouse Entertainment, Inc.					
	10-QSB	10/31/02	12/16/02	Not filed	80
	10-KSB	01/31/03	05/01/03	Not filed	75
	10-QSB	04/30/03	06/16/03	Not filed	74
	10-QSB	07/31/03	09/15/03	Not filed	71
	10-QSB	10/31/03	12/15/03	Not filed	68
	10-KSB	01/31/04	04/30/04	Not filed	64
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-QSB	10/31/04	12/15/04	Not filed	56
	10-KSB	01/31/05	05/02/05	Not filed	51
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-QSB	10/31/05	12/15/05	Not filed	44
	10-KSB	01/31/06	05/01/06	Not filed	39
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-QSB	07/31/06	09/14/06	Not filed	35
	10-QSB	10/31/06	12/15/06	Not filed	32
	10-KSB	01/31/07	05/01/07	Not filed	27
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-QSB	10/31/07	12/17/07	Not filed	20

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Wherehouse Entertainment, Inc.					
	10-KSB	01/31/08	04/30/08	Not filed	16
	*10-Q**	04/30/08	06/16/08	Not filed	14
	*10-Q**	07/31/08	09/15/08	Not filed	11
	*10-Q**	10/31/08	12/15/08	Not filed	8
	*10-K**	01/31/09	05/01/09	Not filed	3
	*10-Q**	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	**27**				
Windpower Partners 1983-1					
	10-KSB	12/31/95	04/01/96	Not filed	160
	10-QSB	03/31/96	05/15/96	Not filed	159
	10-QSB	06/30/96	08/14/96	Not filed	156
	10-QSB	09/30/96	11/14/96	Not filed	153
	10-KSB	12/31/96	03/31/97	Not filed	149
	10-QSB	03/31/97	05/15/97	Not filed	147
	10-QSB	06/30/97	08/14/97	Not filed	144
	10-QSB	09/30/97	11/14/97	Not filed	141
	10-KSB	12/31/97	03/31/98	Not filed	137
	10-QSB	03/31/98	05/15/98	Not filed	135
	10-QSB	06/30/98	08/14/98	Not filed	132
	10-QSB	09/30/98	11/16/98	Not filed	129
	10-KSB	12/31/98	03/31/99	Not filed	125
	10-QSB	03/31/99	05/17/99	Not filed	123
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Windpower Partners 1983-1					
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3

Total Filings Delinquent **54**

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Windpower Partners 1984					
	10-QSB	03/31/95	05/15/95	Not filed	171
	10-QSB	06/30/95	08/14/95	Not filed	168
	10-QSB	09/30/95	11/14/95	Not filed	165
	10-KSB	12/31/95	04/01/96	Not filed	160
	10-QSB	03/31/96	05/15/96	Not filed	159
	10-QSB	06/30/96	08/14/96	Not filed	156
	10-QSB	09/30/96	11/14/96	Not filed	153
	10-KSB	12/31/96	03/31/97	Not filed	149
	10-QSB	03/31/97	05/15/97	Not filed	147
	10-QSB	06/30/97	08/14/97	Not filed	144
	10-QSB	09/30/97	11/14/97	Not filed	141
	10-KSB	12/31/97	03/31/98	Not filed	137
	10-QSB	03/31/98	05/15/98	Not filed	135
	10-QSB	06/30/98	08/14/98	Not filed	132
	10-QSB	09/30/98	11/16/98	Not filed	129
	10-KSB	12/31/98	03/31/99	Not filed	125
	10-QSB	03/31/99	05/17/99	Not filed	123
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Windpower Partners 1984					
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**57**				
World Financial Systems Co. Ltd.					
	10-QSB	10/15/02	12/6/02	Not filed	80
	10-QSB	01/13/03	2/27/03	Not filed	78
	10-QSB	04/13/03	5/28/03	Not filed	75
	10-KSB	07/15/03	10/14/03	Not filed	70
	10-QSB	10/14/03	11/28/03	Not filed	69
	10-QSB	01/13/04	2/27/04	Not filed	66
	10-QSB	04/13/04	5/28/04	Not filed	63
	10-KSB	07/15/04	10/14/04	Not filed	58
	10-QSB	10/14/04	11/29/04	Not filed	57

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
World Financial Systems Co. Ltd.					
	10-QSB	01/13/05	2/28/05	Not filed	54
	10-QSB	04/13/05	5/30/05	Not filed	51
	10-KSB	07/15/05	10/14/05	Not filed	46
	10-QSB	10/14/05	11/28/05	Not filed	45
	10-QSB	01/13/06	2/27/06	Not filed	42
	10-QSB	04/13/06	5/29/06	Not filed	39
	10-KSB	07/15/06	10/13/06	Not filed	34
	10-QSB	10/14/06	11/28/06	Not filed	33
	10-QSB	01/13/07	2/27/07	Not filed	30
	10-QSB	04/13/07	5/28/07	Not filed	27
	10-KSB	07/15/07	10/15/07	Not filed	22
	10-QSB	10/14/07	11/28/07	Not filed	21
	10-QSB	01/13/08	2/27/08	Not filed	18
	10-QSB	04/13/08	5/28/08	Not filed	15
	10-KSB	07/15/08	10/14/08	Not filed	10
	*10-Q**	10/14/08	11/28/08	Not filed	9
	*10-Q**	01/13/09	2/27/09	Not filed	6
	*10-Q**	04/13/09	05/28/09	Not filed	3
Total Filings Delinquent	**27**				
Wrap-N-Roll USA, Inc.					
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**9**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Wyrlis Corp.					
	10-QSB	06/30/02	10/01/02	Not filed	82
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3

Total Filings Delinquent **27**

*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.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60470 / August 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13574

In the Matter of **Atmospheric Glow Technologies, Inc.,** **Respondent.**	**ORDER INSTITUTING PROCEEDINGS, MAKING FINDINGS, AND REVOKING REGISTRATION OF SECURITIES 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 proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act"), against Atmospheric Glow Technologies, Inc. ("Atmospheric Glow Technologies" 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, 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:

A. Atmospheric Glow Technologies, a Delaware corporation based in Knoxville, Tennessee was a development stage company that conducted research and development activities to develop commercial applications for a patented process of non-thermal, atmospheric pressure processing for use in areas such as sterilization, decontamination, surface cleaning and etching. The common stock of Atmospheric Glow Technologies and its predecessors has been registered under Section 12 of the Exchange Act, 15 U.S.C. §78*l*, since 1997. Atmospheric Glow Technologies' stock is currently quoted by the Pink OTC Markets, Inc.

B. Atmospheric Glow Technologies has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder, 17 C.F.R. §§ 270.13a-1 and -13, while its common stock was registered with the Commission in that it has not filed an annual report on Form 10-K since its Form 10-K for the fiscal year ended March 31, 2007 or quarterly reports on Form 10-Q for any period subsequent to its quarter ending December 31, 2007.

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 deems it necessary and appropriate for the protection of investors to impose the sanction specified in Respondent's Offer.

---

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.

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

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. 60480 / August 11, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13577

In the Matter of **AXA Advisors, LLC,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b)(4) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b)(4) of the Securities Exchange Act of 1934 ("Exchange Act") against AXA Advisors, LLC ("AXA" or "Respondent").

II.

In anticipation of the institution of these proceedings, AXA has submitted an Offer of Settlement which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b)(4) of the Securities Exchange Act of 1934 ("Order"), as set forth below.

III.

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

[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.

Summary

1. Respondent failed reasonably to supervise Gordon R. Moore ("Moore") with a view to preventing and detecting his violations of the federal securities laws during the period July 2004 through June 2007. During at least this time period, Moore fraudulently induced investors, the majority of whom were current teachers in Colorado public schools, to consent to roll over their retirement investments from their Colorado Public Employees' Association ("PERA") 401(k) accounts into existing 403(b) investment products offered by Respondent.

Respondent

2. Respondent is a New York corporation with its main office in New York, New York and has been registered with the Commission as a broker-dealer since 1974 and as an investment adviser since 1978.

Other Relevant Persons

3. Moore was a registered representative and investment adviser with AXA from June 1, 2001 through July 23, 2007 until he resigned in connection with an investigation by the Colorado Attorney General's office into his conduct. Moore operated out of an office in Longmont, Colorado and was supervised by an AXA branch office in Denver, Colorado.

Criminal Action Against Moore

4. On August 24, 2007, in the District Court for the City and County of Denver, Moore was charged with forty-five felony counts of securities fraud, theft, computer crime, criminal impersonation, forgery, and attempt to influence a public official. On January 8, 2008, Moore pled guilty to one count each of three class three felonies: securities fraud, theft, and computer crime. On February 26, 2008, Moore was sentenced to two years probation and ordered to pay criminal restitution in an amount based on the commissions he earned from his fraudulent activities.

Commission's Civil Action Against Moore

5. On August 1, 2008, the Commission instituted and simultaneously accepted Moore's offer to settle an administrative proceeding which barred Moore from association with any broker, dealer, or investment adviser pursuant to Section 15(b)(6) of the Exchange Act and Section 203(f) of the Investment Advisers of 1940.

Moore's Misconduct

6. Moore fraudulently induced investors, the majority of whom were current teachers in Colorado public schools, to consent to roll over their retirement investments in securities from their PERA 401(k) accounts into the customers' existing 403(b) products offered by Respondent during the period July 2004 through June 2007. PERA's rules, among other things, restrict withdrawals to participants who have terminated their PERA-eligible employment or reached the age of 59-1/2. The participants did not satisfy either requirement and thus were ineligible for rollovers. Moore misrepresented the PERA rollover rules to the participants and

induced them to sign documents which he later falsified. Moore fraudulently induced at least $1.6 million worth of direct participant rollovers into Respondent's 403(b) products using this scheme. As a result, Moore violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

AXA's Failure to Supervise

7. Respondent failed to establish adequate procedures relating to rollover transactions. Respondent knew that Moore was rolling over participants' PERA 401(k) accounts into 403(b) accounts with Respondent, transferring participants from mutual fund investments into annuity investments. Moore was actively soliciting participants to transfer investments resulting in a commission for Moore. Respondent had inadequate supervisory procedures in place to review rollover transactions into customers' existing accounts because supervisors were only required to review rollovers into new annuity accounts, not existing annuity accounts. Moore completed over 130 fraudulent rollovers by exploiting this gap in Respondent's supervisory system. If AXA had established a procedure for reviewing Moore's rollover transactions into existing accounts, Moore's fraud likely would have been detected and prevented.

8. The lack of procedures relating to review of rollovers led supervisors to miss information that could have signaled Moore's violations. Documents in the customer files indicated that Moore was completing rollovers for participants that were still employed by their respective school districts and thus were ineligible for rollovers unless they had reached the age of 59-1/2. Specifically, certain files contained copies of the PERA 401(k) rollover checks dated closely in time to forms authorizing continued automatic school system payroll deductions payable to their 403(b) annuity accounts with Respondent. Respondent's lack of procedures for reviewing rollover transactions into existing accounts allowed these red flags and Moore's fraudulent activity to go undetected.

Conclusions

9. Under Section 15(b)(4)(E) of the Exchange Act, broker-dealers are responsible for reasonably supervising, with a view to preventing violations of the federal securities laws, persons subject to their supervision. Respondent was responsible for supervising Moore.

10. The Commission has repeatedly emphasized that the "responsibility of broker-dealers to supervise their employees by means of effective, established procedures is a critical component in the federal investor protection scheme regulating the securities markets." *Dean Witter Reynolds, Inc.*, Exchange Act. Rel. 46578 (October 1, 2002). Section 15(b)(4)(E) provides that a broker-dealer may discharge this responsibility by having "established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect" such violations. "Where there has been an underlying violation of the federal securities laws, the failure to have or follow compliance procedures has frequently been found to evidence a failure reasonably to supervise the primary violator." *In the Matter of William V. Giordano*, Exchange Act Rel. No. 36742 (January 19, 1996). In addition to adopting effective procedures for supervision, broker-dealers "must provide effective staffing, sufficient resources, and a system of follow up and review to determine that any responsibility to supervise

delegated to compliance officers, branch managers, and other personnel is being diligently exercised." *In the Matter of Mabon, Nugent & Co.*, Exchange Act Rel. No. 19424 (January 13, 1983).

11. Because Moore violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder and Respondent failed to establish adequate procedures that would reasonably be expected to prevent and detect such violations, Respondent failed reasonably to supervise Moore for purposes of Section 15(b)(4)(E) of the Exchange Act.

AXA's Remedial Efforts

12. In determining to accept Respondent's Offer, the Commission considered the remedial acts promptly undertaken by Respondent to make significant improvements to its supervisory system, and the cooperation afforded the Commission staff.

13. Due in part to Respondent's remedial acts, the participants ultimately incurred no monetary harm.

Undertakings

14. Respondent has represented to the staff of the Denver Regional Office that, following the discovery of Moore's violations, Respondent hired an outside consultant to recommend improvements to its supervisory and compliance practices for sales made by its retirement benefits group. Respondent has already put into place procedures to ensure that all 401(k) rollovers into 403(b) accounts are appropriate and is in the process of implementing additional improvements recommended by the outside consultant. Among the improvements, Respondent has implemented procedures to confirm that all 401(k) rollover transactions into 403(b) accounts, including rollovers into accounts that have been previously established, are reviewed for eligibility and suitability. In addition, Respondent is in the process of developing an automated system for reviewing the suitability of all subsequent contributions not originating from ordinary payroll deductions and, once fully implemented, Respondent will provide written certification of that fact to the Commission staff.

IV.

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

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 15(b)(4) of the Exchange Act, AXA Advisors is hereby censured;

B. AXA Advisors shall, within ten days of the entry of this Order, pay a civil money penalty in the amount of $50,000 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 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 AXA 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 Donald Hoerl, Regional Director, Securities and Exchange Commission, 1801 California Street., Suite 1500, Denver, CO 80202.

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

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Walter not participating

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC-28845; File No. 812-13680]

GE Asset Management Incorporated and GE Investment Distributors, Inc.; Notice of Application and Temporary Order

August 11, 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 General Electric Company ("GE") on August 11, 2009 by the United States District Court for the District of Connecticut ("Injunction"), until the Commission takes final action on an application for a permanent order. Applicants also have applied for a permanent order.

Applicants: GE Asset Management Incorporated ("GEAM") and GE Investment Distributors, Inc. ("GEID", collectively with GEAM, the "Applicants").[1]

Filing Date: The application was filed on August 4, 2009, and amended on August 11, 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 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 GE is or may become an affiliated person (together with the Applicants, the "Covered Persons").

September 8, 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: 3001 Summer Street, Stamford, CT 06904-7900.

For Further Information Contact: Courtney S. Thornton, at (202) 551-6812, or Mary Kay Frech, 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 website 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. GE is a large diversified technology, media, and financial services company. GEAM, a Delaware corporation, is a direct, wholly-owned subsidiary of GE. GEAM is registered as an investment adviser under the Investment Advisers Act of 1940 and serves as investment adviser to a number of registered investment companies ("Funds"), including employees' securities companies ("ESCs").[2] GEID is, through GEAM, an indirect, wholly-owned subsidiary of GE. GEID is registered as a broker-

[2] The ESCs, as defined in section 2(a)(13) of the Act, are open-end management investment companies registered under the Act and provide investment opportunities for certain employees, officers, and directors of GEAM and its affiliates, and other eligible participants.

dealer under the Securities Exchange Act of 1934 and is a member of the Financial Industry Regulatory Authority, Inc. GEID serves as principal underwriter to a number of Funds.

2. On August 11, 2009, the United States District Court for the District of Connecticut entered a final judgment, which included the Injunction, against GE ("Judgment") in a matter brought by the Commission.[3] The Commission alleged in the complaint ("Complaint") that, in 2002 and 2003, high level GE accounting executives or other finance personnel approved accounting that was not in compliance with generally accepted accounting principles so as to increase earnings or revenues or to avoid reporting negative financial results. Without admitting or denying the allegations in the Complaint, except as to jurisdiction, GE consented to the entry of the Judgment that included, among other things, the entry of the Injunction, and a civil penalty of $50 million.

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

[3] Securities and Exchange Commission v. General Electric Company, Final Judgment as to General Electric Company, 3:09 CV 1235 (RNC) (D. Conn. Aug. 11, 2009).

"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 GE is an affiliated person of each of the 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 other 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 either of the Applicants acting in the capacity of investment adviser, subadviser or depositor for any Fund or as principal underwriter for any Fund, and no such Funds bought or held any securities issued by GE during the period of misconduct alleged in the Complaint, other than with respect to index funds. Applicants also state that none of

the current or former directors, officers, or employees of the Applicants had any responsibility for, or involvement in, the violative conduct alleged in the Complaint. Applicants further state that the personnel at GE who had any responsibility for, or involvement in, the violations alleged in the Complaint have had no, and will not have any future, involvement in providing investment advisory, subadvisory, or underwriting services to the Funds.

5. Applicants state that their inability to continue to provide investment advisory, subadvisory and underwriting services to the 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 Judgment 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 the Funds, the effect on their businesses and employees would be severe. Applicants state that they have committed substantial resources to establishing 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 about 500 employees who are involved in those activities.

7. A predecessor of one of the Applicants previously received an exemption 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 GEAM and GEID 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 August 11, 2009, until the Commission takes final action on their application for a permanent order.

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. 60485 / August 12, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13304

In the Matter of **CentreInvest, Inc.,** **OOO CentreInvest Securities,** **Vladimir Chekholko,** **William Herlyn,** **Dan Rapoport, and** **Svyatoslav Yenin,** **Respondents.**	**ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AS TO WILLIAM HERLYN**

I.

On December 8, 2008, the Securities and Exchange Commission ("Commission") instituted public administrative and cease-and-desist proceedings pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against CentreInvest, Inc. ("CI-New York"), OOO CentreInvest Securities ("CI-Moscow"), William Herlyn ("Herlyn"), Vladimir Chekholko, Dan Rapoport and Svyatoslav Yenin.

II.

In connection with these proceedings, Respondent Herlyn 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, Herlyn consents to the entry of this Order Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 as to William Herlyn ("Order"), as set forth below.

III.

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

SUMMARY

1. These proceedings arise out of violations of the broker-dealer registration, reporting, and record-keeping requirements of the Exchange Act by CI-Moscow, a Moscow-based unregistered broker-dealer, and its New York-based affiliate, CI-New York, a registered broker-dealer. From about 2003 through November 2007, CI-Moscow – directly and through CI-New York, Herlyn (its chief compliance officer), and others – solicited institutional investors in the United States to purchase and sell thinly-traded stocks of Russian companies, without registering as a broker-dealer as required by Section 15(a) of the Exchange Act or meeting the requirements for the exemption from registration for foreign broker-dealers under Exchange Act Rule 15a-6(a). In addition, Herlyn was responsible for CI-New York's filing of Forms BD that failed to disclose CI-Moscow's and its executive director's control of CI-New York, or that the license of the CI-New York's parent company had been revoked by the Cyprus SEC.

SETTLING RESPONDENT

2. **William Herlyn**, age 40, is a resident of Westport, Connecticut, and holds Series 7, 24 and 63 licenses. He was employed by CI-New York from 2003 until October 2008. From June 2006 until October 2008, Herlyn held the title of chief compliance officer. For most of his tenure, Herlyn was also responsible for marketing CI-New York's fee-based research and soliciting U.S. institutional investors.

ENTITY RESPONDENTS

3. **OOO CentreInvest Securities** ("CI-Moscow") is a Moscow-based broker-dealer and limited liability company, specializing in the sale of second-tier Russian equities. During the relevant period, it was an affiliate of CI-New York. It was founded in 1992 under the laws of Russia and is regulated by the Russian Federal Financial Markets Service. CI-Moscow has never been registered with the Commission as a broker or dealer.

4. **CentreInvest, Inc.** ("CI-New York") is a registered broker-dealer organized under the laws of New York State with its principal place of business in New York, New York. During the relevant period, it was a subsidiary of Cyprus-based Intelsa Investments Limited. CI-New York first registered with the Commission on June 23, 1998, and during the relevant period, employed four to five full-time employees. On October 2, 2008, the Financial Industry Regulatory Authority, Inc. ("FINRA") expelled CI-New York for failure to file a Financial and Operational Combined Uniform Single ("FOCUS") report.

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

CI-MOSCOW ACTED AS A BROKER-DEALER BUT FAILED TO REGISTER OR COMPLY WITH AN EXEMPTION FROM REGISTRATION

5. From about 2003 until at least November 2007, CI-Moscow directly and indirectly, solicited investors in the United States to purchase and sell thinly-traded stocks of Russian companies – so-called "second-tier," or micro-cap, Russian companies – without registering as a broker-dealer, as required by Section 15(a) of the Exchange Act, or meeting the requirements for an exemption.

6. Under CI-Moscow's direction, employees of CI-New York, including Herlyn, its chief compliance officer, regularly solicited U.S. institutional investors for the purchase and sale of Russian securities. Investors who expressed interest in a transaction were referred to CI-Moscow to complete the transaction.

7. In some cases, employees of CI-Moscow, who were not licensed to sell securities under U.S. law or registered as brokers or dealers under U.S. law and were not exempt from such licensing and registration requirements, solicited U.S. investors directly.

8. CI-New York failed to maintain virtually any records concerning CI-Moscow's transactions with the U.S. investors.

CI-NEW YORK FAILED TO DISCLOSE CI-MOSCOW'S AND ITS EXECUTIVE DIRECTOR'S CONTROL

9. Throughout the relevant period, CI-New York was under the control of CI-Moscow and, in at least 2006 and 2007, its executive director. CI-Moscow and its executive director controlled CI-New York by, among other things, supervising and directing the staff of CI-New York and controlling its budget and finances. Indeed, CI-New York employees sometimes referred to CI-Moscow's executive director as their "boss" and to CI-Moscow as CI-New York's "parent broker-dealer."

10. CI-New York filed its initial Form BD on July 5, 1999 and subsequently filed numerous amendments. Form BD amendments, signed and filed by Herlyn on behalf of CI-New York during the period June 29, 2006 to December 6, 2007, failed to disclose CI-Moscow's and its executive director's control of CI-New York.

11. At the time Herlyn signed these Form BD amendments, he knew that CI-Moscow and its executive director controlled CI-New York by, among other things, supervising and directing the staff of CI-New York and controlling its budget and finances.

CI-NEW YORK FAILED TO DISCLOSE THE DISCIPLINARY ACTIONS AGAINST CI-NEW YORK'S PARENT

12. In Form BD amendments, signed and filed by Herlyn on behalf of CI-New York, the firm inaccurately responded "No" to the question: "Has any other regulatory agency, any state regulatory agency or foreign financial regulatory authority: . . . ever denied, suspended, or revoked the applicant's or a control affiliate's registration or license or otherwise, by order, prevented it from associating with an investment-related business or restricted its activities?"

13. CI-New York should have answered that question "Yes" because the Cyprus Securities and Exchange Commission suspended the license of CI-New York's Cyprus-based parent on January 11, 2006 and revoked its license on May 26, 2006.

14. At the time that Herlyn signed at least some of the Form BD amendments that failed to disclose the regulatory action against CI-New York's Cyprus-based parent by the Cyprus Securities and Exchange Commission, he knew, or at a minimum should have known, of that regulatory action and that CI-New York's Cyprus-based parent was a control affiliate.

VIOLATIONS

15. Rule 15a-6(a) of the Exchange Act permits unregistered foreign broker-dealers to effect transactions for U.S. institutional investors in certain limited circumstances, subject to reporting, record keeping and other requirements designed to ensure the protection of U.S. investors. Rule 15a-6(b)(3) defines a "foreign broker or dealer" as "any non-U.S. resident person (including any U.S. person engaged in business as a broker or dealer entirely outside the United States, except as otherwise permitted by this rule) that is not an office or branch of, or a natural person associated with, a registered broker-dealer, whose securities activities, if conducted in the U.S., would be described by the definition of "broker" or "dealer" in Sections 3(a)(4) or 3(a)(5) of the [Exchange Act]." Section 3(a)(4) of the Exchange Act defines a "broker" as any person, other than a bank, in certain circumstances, "engaged in the business of effecting transactions in securities for the account of others." A person "effects transactions in securities" if he or she participates in such transactions "at key points in the chain of distribution." Massachusetts Fin. Servs., Inc. v. Security Investor Protection Corp., 411 F. Sup. 411, 415 (D. Mass.), aff'd, 545 F. 2d 754 (1st Cir. 1976).

16. As a result of the conduct described above, Herlyn caused CI-Moscow's violations of Section 15(a) of the Exchange Act, which makes it illegal for a broker to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security unless the broker is registered with the Commission or, in the case of a natural person, is associated with a registered broker or dealer.

17. CI-Moscow failed to qualify for any exemption from registration.

18. Section 15(b)(1) of the Exchange Act and Rule 15b3-1 require all brokers or dealers applying for registration with the Commission to file a Form BD with the Commission and to correct any information in the Form BD if it is or becomes inaccurate for any reason. Section 17(a) of the Exchange Act requires registered brokers or dealers, among other things, "to make and disseminate such reports as the Commission, by rule, prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of [the Exchange Act]." Among other things, Form BD requires registered brokers and dealers to disclose whether any person not identified as an owner or officer of the broker-dealer "directly or indirectly [has] control [over] the management or policies of the [broker-dealer] through agreement or otherwise." See, e.g., Alderman v. SEC, 104 F.3d 285, 287 n.1 (9th Cir. 1997). "[T]he correct disclosure of the . . . controlling persons of an applicant is more than a 'minor' point, indeed it is most important to the proper administration of the [Exchange] Act." Capital Funds, Inc. v. SEC, 348 F.2d 582, 588 (8th Cir. 1968). Form BD also requires registered broker-dealers to disclose whether any foreign financial regulatory authority has "ever denied, suspended, or revoked the applicant's or a control affiliate's registration or license or otherwise, by order, prevented it from associating with an investment-related business or restricted its activities."

19. As a result of the conduct described above, Herlyn willfully aided and abetted and caused CI-New York's violation of Section 17(a) of the Exchange Act and Rule 15b3-1 thereunder.

UNDERTAKINGS

20. **Ongoing Cooperation:** Herlyn undertakes to cooperate fully with the Commission in any and all investigations, litigations or other proceedings brought by the Commission relating to or arising from the matters described in the Order and agrees:

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

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

(c) That in connection with any testimony of Herlyn to be conducted at deposition, hearing or trial pursuant to a notice or subpoena, Herlyn:

i. Agrees that any such notice or subpoena for his appearance and testimony may be served by regular mail, electronic mail, or facsimile on his counsel, George Brunelle, Brunelle & Hadjikow, P.C, 120 Broadway, Suite, 1010, New York, NY, 10271.; and

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

21. **Affidavit of Compliance:** Herlyn shall provide to the Commission, within thirty days after the end of the three month suspension described in Section IV.2., below, an affidavit that he has fully complied with the sanctions described in Section IV.2 below.

In determining whether to accept Herlyn's Offer, the Commission has considered these undertakings.

IV.

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

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

1. Herlyn cease and desist from committing or causing violations and any future violations of Section 15(a) of the Exchange Act, and causing violations and any future violations of Section 17(a) of the Exchange Act and Rule 15b3-1 thereunder;

2. Herlyn be, and hereby is, suspended from association with any broker or dealer for a period of three months, effective on the second Monday following the entry of this Order;

3. Herlyn shall, within thirty (30) days of the entry of this Order, pay a civil penalty in the amount of $10,000 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 Herlyn 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 Andrew M. Calamari, Associate Regional Director, Securities and Exchange Commission, 3 World Financial Center, Suite 400, New York, NY, 10281; and

4. Herlyn shall comply with the undertakings enumerated in Section III.21., above.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9059 / August 12, 2009

In the Matter of **General Electric Company,** **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.

General Electric Company ("GE" or "Respondent") has submitted a letter, dated July 24, 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 GE's settlement of an injunctive action commenced by the Commission.

II.

On August 11, 2009, the Federal District Court for the District of Connecticut entered a final judgment permanently enjoining GE from violating Section 17(a) of the Securities Act of 1933 ("Securities Act") and Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Securities Exchange Act of 1934 ("Exchange Act") and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 thereunder. The complaint alleges that starting in at least 2002 and continuing through 2003, GE, acting primarily through senior corporate accountants, made a series of improper accounting decisions which resulted in its reporting materially false or misleading results in its financial statements and earnings reports through at least 2006.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if such issuer or any of its affiliates is subject to a court order entered within the past five years "permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities," 17 C.F.R. § 230.602(b)(4), or if any of the issuer's directors, officers or principal security holders, any investment adviser or underwriter of the securities to be offered, or any partner, director or officer of any such 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." 17 C.F.R. § 230.602(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 GE'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(c)(2) and 602(b)(4) under the Securities Act resulting from the entry of the Judgment is hereby granted.

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. 60484 / August 12, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3034 / August 12, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13578

In the Matter of **DOUGLAS K. HUTCHINS,** **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 Douglas K. Hutchins ("Hutchins" or "Respondent").[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, 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.

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[1] This matter is related to a civil action, Securities and Exchange Commission v. Douglas K. Hutchins, Civ. Action No. 1:03-cv-328, filed on July 9, 2009, in which Hutchins has consented to pay a $25,000 civil penalty.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[2] that:

1. Douglas K. Hutchins, age 37, of Denver, Colorado, was the director of finance for Qwest Communications International's Global Business Markets ("Global Business") unit and reported to the chief financial officer ("CFO") of Global Business from January 2001 until February 2002 when Hutchins was promoted to senior director of quality. Hutchins resigned from Qwest on October 12, 2002.

2. Qwest, based in Denver, Colorado, is one of the largest telecommunications and Internet services companies in the United States. Qwest's common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act, and the company is obligated to file reports on Forms 10-K and 10-Q. Qwest's common stock is traded on the New York Stock Exchange.

3. In January 2001, the Arizona School Facilities Board ("ASFB") and Qwest entered into agreements providing that Qwest would design and implement a statewide network and provide internet and local area network services for Arizona schools using equipment provided by Qwest.

4. The CFO of Global Business told Hutchins that Global Business needed to be aggressive in recognizing revenue on the ASFB transaction. The CFO of Global Business consulted with the assistant controller of Qwest and Hutchins and they inappropriately decided to separate the equipment sale from the other elements of the ASFB contract and then to improperly characterize the sale as a bill and hold transaction to ensure immediate revenue recognition.

5. Hutchins prepared the memorandum incorrectly concluding that Qwest met each requirement for a bill and hold transaction and that revenue could be recognized immediately on the equipment sale. The assistant controller of Qwest reviewed and edited the memorandum.

6. Hutchins drafted letter agreements for an ASFB official to sign to fulfill the bill and hold requirements, knowing they included terms contrary to the official's oral agreements with Qwest. The senior vice president ("SVP") and vice president of sales for the Government and Educational Services unit ("GES") and the assistant controller of Qwest reviewed and edited letter agreements, and the SVP of GES signed them.

7. As a result of the scheme, Qwest improperly recognized approximately $34 million in revenue on the sale of the equipment in its second quarter ended June 30, 2001. Accordingly, Qwest's June 30, 2001 quarterly report, September 30, 2001 quarterly report, and December 31, 2001 annual report were materially false and misleading.

8. As a result of the conduct described above, Qwest violated, and Hutchins was a cause of Qwest's violations of, Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, and

[2] 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.

13a-13 thereunder, which require every issuer of a security registered pursuant to Section 12 of the Exchange Act to 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.

9. As a result of the conduct described above, Qwest violated, and Hutchins was a cause of Qwest's violations of, Section 13(b)(2)(A) of the Exchange Act, which 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, and Section 13(b)(2)(B), which 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 conformity with generally accepted accounting principles.

10. Lastly, as a result of the conduct described above, Hutchins violated Section 13(b)(5) of the Exchange Act, which prohibits persons from knowingly circumventing or knowingly failing to implement a system of internal accounting controls, or knowingly falsifying any book, record or account, and Exchange Act Rule 13b2-1, which prohibits persons from directly or indirectly falsifying or causing to be falsified any book, record, or account subject to Section 13(b)(2)(A) of the Exchange Act.

Undertakings

In connection with this action and any related judicial or administrative proceeding or investigation commenced by the Commission or to which the Commission is a party, Respondent undertakes to cooperate with the Commission staff and: (i) agrees to appear and be interviewed by Commission staff at such times and places as the staff requests upon reasonable notice; (ii) will accept service by mail or facsimile transmission of notices or subpoenas issued by the Commission for documents or testimony at depositions, hearings, or trials, or in connection with any related investigation by Commission staff; (iii) appoints Respondent's attorney as agent to receive service of such notices and subpoenas; (iv) with respect to such notices and subpoenas, waives the territorial limits on service contained in Rule 45 of the Federal Rules of Civil Procedure and any applicable local rules, provided that the party requesting the testimony reimburses Respondent's travel, lodging, and subsistence expenses at the then-prevailing U.S. Government per diem rates; and (v) consents to personal jurisdiction over Respondent in any United States District Court for purposes of enforcing any such subpoena.

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

IV.

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

Accordingly, it is hereby ORDERED that:

A. Respondent Hutchins cease and desist from committing or causing any violations and any future violations of Section 13(b)(5) of the Exchange Act and Rule 13b2-1 thereunder, and from 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

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9060 / August 12, 2009

SECURITIES EXCHANGE ACT OF 1934
Release No. 60490 / August 12, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13581

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

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Robert J. Zannotti ("Zannotti" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Section 8A of the Securities Act of 1933 and Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Order"), as set forth below.

III.

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

Summary

1. From approximately June 2001 through March 2005 (the "Relevant Period"), Zannotti and two individuals who advised, and were the sole principals of, an unregistered fund (the "Fund") perpetrated a fraud on customers of the Fund, which lost millions of dollars due to misappropriation and undisclosed trading losses. As a part of the scheme, Zannotti, who was employed as a registered representative of broker-dealer Kimball & Cross Investment Management Corp. ("K&C"), agreed to kickback to the Fund's principals ninety percent of the brokerage commissions Zannotti earned on trades executed by K&C for the Fund, and, at the request of the Fund's principals, moved certain profitable trades from the Fund's account to other K&C customer accounts belonging to friends and family members of the Fund's principals and of Zannotti. In addition, Zannotti also solicited potential investors to invest in the Fund and knowingly distributed materially false and misleading information concerning the Fund's assets under management to these investors.

Respondent

2. **Robert J. Zannotti**, age 40, of Mashpee, Massachusetts, was a registered representative of K&C in its Boston branch office from June 2001 until K&C terminated his employment in October 2005. Zannotti was the registered representative for the Fund's account at K&C. During that period, Zannotti also worked full-time as a client service manager at a large financial services company unrelated to K&C. Zannotti conducted business for K&C from his office at the financial services company, an off-site location away from any established K&C office.

Other Relevant Entity

3. **Kimball & Cross Investment Management Corp.**, is a Massachusetts corporation that was registered as a broker-dealer with the Commission from April 12, 1982, to February 22, 2009. K&C has its principal place of business in Boston, Massachusetts. In November 2007, K&C registered as an investment adviser with the Commonwealth of Massachusetts. On December 23, 2008, K&C received notice from FINRA that K&C failed to meet minimum net capital requirements. On December 24, 2008, K&C filed with the Commission a Form BDW to withdraw its registration as a broker dealer, which became effective February 22, 2009.

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

Background

4. From October 2000 through at least March 2005, the Fund's principals raised almost $16 million from approximately twenty investors and dissipated nearly all of their clients' assets through undisclosed trading losses in the Fund's brokerage accounts, unauthorized use of investor funds, and misappropriation of client funds for personal use. During the Relevant Period, the Fund was a brokerage customer of K&C and had a brokerage account at K&C in which assets of the Fund were held.

5. Zannotti was the K&C registered representative for the Fund's account. He conducted his K&C business entirely at an off-site location -- his office at his full-time employer, a large financial services firm unrelated to K&C.

Zannotti Participated in a Scheme to Defraud the Fund and Its Clients

6. During the Relevant Period, and despite the fact that Zannotti became aware that his actions were improper, Zannotti provided the Fund's principals with Zannotti's K&C employee secure log-in information to enable the Fund's principals to effect trades directly on K&C's trading platform on behalf of the Fund and other K&C customers the Fund's principals had referred to K&C. Zannotti attempted to conceal the fact that the Fund's principals and not Zannotti himself were making the trades. Specifically, one of the Fund's principals regularly prepared a daily trade blotter and emailed it to Zannotti's e-mail address at the unrelated financial services firm where he worked. Rather than simply forwarding to his supervisor at K&C the emails sent to Zannotti by the Fund's principals, Zannotti typically composed a separate email to his supervisor to which he attached the daily trade blotters obtained from the Fund's principals to make it appear Zannotti had effected the trades.

7. During the Relevant Period, at the request of the Fund's principals and after the trades had proven profitable, Zannotti diverted approximately $56,000 in profitable trades from the Fund's account to other K&C customer accounts held in the names of Zannotti's sister and brother in-law and family members of one of the Fund's principals. Zannotti was aware that the profits from these trades would benefit relatives of Zannotti and one of the Fund's principals. Zannotti came to realize that this activity was wrong and advised one of the Fund's principals by email that he should space out the occasions in which he requested such diversions of profitable trades in order to avoid detection.

8. During the Relevant Period, Zannotti agreed to kick back to the Fund's principals ninety percent of commissions Zannotti earned from the Fund's trading activity. By at least 2003, Zannotti became aware that his conduct was improper and came to believe it violated NASD rules, yet continued to kick back commissions to the Fund's principals because the arrangement benefited him personally at a time that he was under financial strain. Zannotti earned approximately $1.5 million in commissions from the Fund's account activity. As a part of the kickback scheme, Zannotti made payments totaling approximately $1.2 million to the Fund's principals, including making payments to satisfy one Fund principal's personal expenditures.

9. During the Relevant Period, Zannotti solicited potential investors in the Fund using false and misleading sales materials concerning the Fund's assets under management. For example, in July 2004, Zannotti sent an email containing sales material that claimed the Fund's principals managed over $105 million in customer assets. At the time he sent the email, Zannotti knew that the Fund's total assets were no more than $33-34 million. This information overstating assets under management by nearly 200% was material to potential investors. Zannotti would have benefited if the persons he had solicited had invested additional assets in the Fund because he would have earned additional commissions from a resulting increase in trading by the Fund's principals.

10. While engaging in the conduct described above, Zannotti acted with scienter, as reflected by his attempt to conceal the fact that the Fund's principals and not Zannotti himself were effecting trades using Zannotti's password on the K&C order entry system, his diversion of profitable trades from the Fund's account to benefit his family members, his involvement in and failure to disclose the kickback scheme, his knowledge that the kickback scheme was improper, and his solicitation of potential investors using email containing information he knew to be false.

Zannotti's Violations

11. Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder generally prohibit any person from employing any device, scheme or artifice to defraud; obtaining money or property by means of any untrue statement of a material fact, or omitting to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or engaging in any transaction, act, practice or course of business which operates or would operate as a fraud or deceit upon any person in the offer or sale, or, for Section 10(b), in connection with the purchase or sale, of any security. Violations of Section 17(a)(1) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder require the respondent to have acted with scienter. Aaron v. SEC, 446 U.S. 680, 691 (1980).

12. Based on the conduct described above, Zannotti willfully violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Disgorgement and Civil Penalties

13. Zannotti has submitted a sworn Statement of Financial Condition dated May 10, 2008, and updated April 14, 2009, and other evidence submitted to the staff, and has asserted his inability to pay a civil penalty and an inability to pay complete disgorgement.

IV.

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

Accordingly, pursuant to Section 8A of the Securities Act and Sections 15(b)(6) and 21C of the Exchange Act, it is hereby ORDERED that:

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

B. Zannotti be, and hereby is, barred from association with any broker or dealer;

C. Any reapplication for association by 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.

D. Zannotti shall pay disgorgement of $182,721.20 and prejudgment interest of $54,451.16, but payment of such amount except $171,800, is waived based on Zannotti's sworn representations in his Statement of Financial Condition dated May 10, 2008, and updated April 14, 2009, and other documents submitted to the Commission. The payment required by this Order shall be made in the following installments:

a. within 10 days of the entry of this Order, a payment of $89,000;
b. on or before August 31, 2009, a payment of $6,900;
c. on or before November 30, 2009, a payment of $6,900;
d. on or before February 28, 2010, a payment of $6,900;
e. on or before May 31, 2010, a payment of $6,900;
f. on or before August 31, 2010, a payment of $6,900;
g. on or before November 30, 2010, a payment of $6,900;
h. on or before February 28, 2011, a payment of $6,900;
i. on or before May 31, 2011, a payment of $6,900;
j. on or before August 31, 2011, a payment of $6,900;
k. on or before November 30, 2011, a payment of $6,900;
l. on or before February 20, 2012, a payment of $6,900; and
m. on or before May 31, 2012, a payment of $6,900.

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, 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 Court Clerk, United States District Court for the District of Massachusetts; (C) hand-delivered or mailed to the

Clerk of Court, United States District Court for the District of Massachusetts, One Courthouse Way, Boston MA 02210; and (D) submitted under cover letter that identifies Robert Zannotti as a Respondent in these proceedings and the file number of these proceedings and states that the payment is to be applied to the obligation to pay restitution of the defendant in the criminal action United States v. Amit Mathur, 4:06-cr-40034-FDS, a copy of which cover letter and money order or check shall be sent to John T. Dugan, Division of Enforcement, Securities and Exchange Commission, 33 Arch Street, 23rd Floor, Boston, MA 02110.

E. Based upon Zannotti's sworn representations in his Statement of Financial Condition dated May 10, 2008, and updated April 14, 2009, and other documents submitted to the Commission, the Commission is not imposing a penalty against Zannotti.

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

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 12, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13580

In the Matter of **Action Auto Rental, Inc.,** **Addisson Industries, Inc.,** **Advanced Promotion Technologies, Inc.,** **Advantexcel Com Communications Corp.,** **Aeire Corp.,** **All American Food Group, Inc., and** **Allerion, 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 Action Auto Rental, Inc., Addisson Industries, Inc., Advanced Promotion Technologies, Inc., Advantexcel Com Communications Corp., Aeire Corp., All American Food Group, Inc., and Allerion, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Action Auto Rental, Inc. (CIK No. 810309) is a dissolved Delaware corporation located in Solon, Ohio with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Action Auto 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, 1993.

2. Addisson Industries, Inc. (CIK No. 1038492) is a void Delaware corporation located in Ottawa, Ontario, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Addisson 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 October 31, 1998.

3. Advanced Promotion Technologies, Inc. (CIK No. 874979) is a void Delaware corporation located in Pompano Beach, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Advanced Promotion 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 May 25, 1996, which reported a net loss of over $124 million since inception on December 4, 1987. As of March 4, 2009, the company's stock (symbol "APTV") was traded on the over-the-counter markets.

4. Advantexcel Com Communications Corp. (CIK No. 1094035) is an Ontario corporation located in Toronto, Ontario, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Advantexcel 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 June 30, 2000, which reported a net loss of over $2.1 million for the year ended June 30, 2000.

5. Aeire Corp. (CIK No. 3398) is a dissolved Massachusetts corporation located in Sunrise, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Aeire 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 December 31, 1996, which reported a net loss of over $2.2 million for the prior nine months.

6. All American Food Group, Inc. (CIK No. 1013627) is a New Jersey corporation located in South Plainfield, New Jersey with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). All American 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 31, 1998, which reported a net loss of over $2.8 million for the prior nine months. On November 30, 1998, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the District of New Jersey which terminated on October 11, 2002.

7. Allerion, Inc. (CIK No. 350874) is a New Jersey corporation located in Pine Brook, New Jersey with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Allerion 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 January 31, 1995, which reported a net loss of over $6.3 million for the prior nine months. On December 7, 1994, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of New Jersey, which terminated on January 31, 2000. As of March 4, 2009, the company's stock (symbol "AERI") was traded on the over-the-counter markets.

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

Chart of Delinquent Filings
Action Auto Rental, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Action Auto Rental, Inc.					
	10-Q	09/30/93	11/15/93	Not filed	189
	10-K	12/31/93	03/31/94	Not filed	185
	10-Q	03/31/94	05/16/94	Not filed	183
	10-Q	06/30/94	08/15/94	Not filed	180
	10-Q	09/30/94	11/14/94	Not filed	177
	10-K	12/31/94	03/31/95	Not filed	173
	10-Q	03/31/95	05/15/95	Not filed	171
	10-Q	06/30/95	08/14/95	Not filed	168
	10-Q	09/30/95	11/14/95	Not filed	165
	10-K	12/31/95	04/01/96	Not filed	160
	10-Q	03/31/96	05/15/96	Not filed	159
	10-Q	06/30/96	08/14/96	Not filed	156
	10-Q	09/30/96	11/14/96	Not filed	153
	10-K	12/31/96	03/31/97	Not filed	149
	10-Q	03/31/97	05/15/97	Not filed	147
	10-Q	06/30/97	08/14/97	Not filed	144
	10-Q	09/30/97	11/14/97	Not filed	141
	10-K	12/31/97	03/31/98	Not filed	137
	10-Q	03/31/98	05/15/98	Not filed	135
	10-Q	06/30/98	08/14/98	Not filed	132
	10-Q	09/30/98	11/16/98	Not filed	129
	10-K	12/31/98	03/31/99	Not filed	125
	10-Q	03/31/99	05/17/99	Not filed	123
	10-Q	06/30/99	08/16/99	Not filed	120
	10-Q	09/30/99	11/15/99	Not filed	117
	10-K	12/31/99	03/30/00	Not filed	113
	10-Q	03/31/00	05/15/00	Not filed	111
	10-Q	06/30/00	08/14/00	Not filed	108
	10-Q	09/30/00	11/14/00	Not filed	105
	10-K	12/31/00	04/02/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	99
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-K	12/31/01	04/01/02	Not filed	88
	10-Q	03/31/02	05/15/02	Not filed	87

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-K	12/31/02	03/31/03	Not filed	77
	10-Q	03/31/03	05/15/03	Not filed	75
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69
	10-K	12/31/03	03/30/04	Not filed	65
	10-Q	03/31/04	05/17/04	Not filed	63
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-K	12/31/04	03/31/05	Not filed	53
	10-Q	03/31/05	05/16/05	Not filed	51
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-K	12/31/05	03/31/06	Not filed	41
	10-Q	03/31/06	05/15/06	Not filed	39
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-K	12/31/06	04/02/07	Not filed	28
	10-Q	03/31/07	05/15/07	Not filed	27
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/30/07	11/14/07	Not filed	21
	10-K	12/31/07	03/31/08	Not filed	17
	10-Q	03/31/08	05/15/08	Not filed	15
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-K	12/31/08	03/31/09	Not filed	5
	10-Q	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	**63**				
Addisson Industries, Inc.					
	10-K	01/31/99	05/03/99	Not filed	123
	10-Q	04/30/99	06/14/99	Not filed	122
	10-Q	07/31/99	09/14/99	Not filed	119
	10-Q	10/31/99	12/15/99	Not filed	116
	10-K	01/31/00	05/01/00	Not filed	111
	10-Q	04/30/00	06/14/00	Not filed	110

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	07/31/00	09/14/00	Not filed	107
	10-Q	10/31/00	12/15/00	Not filed	104
	10-K	01/31/01	05/01/01	Not filed	99
	10-Q	04/30/01	06/14/01	Not filed	98
	10-Q	07/31/01	09/14/01	Not filed	95
	10-Q	10/31/01	12/17/01	Not filed	92
	10-K	01/31/02	05/01/02	Not filed	87
	10-Q	04/30/02	06/14/02	Not filed	86
	10-Q	07/31/02	09/16/02	Not filed	83
	10-Q	10/31/02	12/16/02	Not filed	80
	10-K	01/31/03	05/01/03	Not filed	75
	10-Q	04/30/03	06/16/03	Not filed	74
	10-Q	07/31/03	09/15/03	Not filed	71
	10-Q	10/31/03	12/15/03	Not filed	68
	10-K	01/31/04	04/30/04	Not filed	64
	10-Q	04/30/04	06/14/04	Not filed	62
	10-Q	07/31/04	09/14/04	Not filed	59
	10-Q	10/31/04	12/15/04	Not filed	56
	10-K	01/31/05	05/02/05	Not filed	51
	10-Q	04/30/05	06/14/05	Not filed	50
	10-Q	07/31/05	09/14/05	Not filed	47
	10-Q	10/31/05	12/15/05	Not filed	44
	10-K	01/31/06	05/01/06	Not filed	39
	10-Q	04/30/06	06/14/06	Not filed	38
	10-Q	07/31/06	09/14/06	Not filed	35
	10-Q	10/31/06	12/15/06	Not filed	32
	10-K	01/31/07	05/01/07	Not filed	27
	10-Q	04/30/07	06/14/07	Not filed	26
	10-Q	07/31/07	09/14/07	Not filed	23
	10-Q	10/31/07	12/17/07	Not filed	20
	10-K	01/31/08	04/30/08	Not filed	16
	10-Q	04/30/08	06/16/08	Not filed	14
	10-Q	07/31/08	09/15/08	Not filed	11
	10-Q	10/31/08	12/15/08	Not filed	8
	10-K	01/31/09	05/01/09	Not filed	3
	10-Q	04/30/09	06/15/09	Not filed	2

Total Filings Delinquent **42**

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Advanced Promotion Technologies, Inc.					
	10-Q	08/24/96	10/08/96	Not filed	154
	10-K	11/23/96	02/24/97	Not filed	150
	10-Q	02/22/97	04/08/97	Not filed	148
	10-Q	05/24/97	07/08/97	Not filed	145
	10-Q	08/23/97	10/07/97	Not filed	142
	10-K	11/22/97	02/23/98	Not filed	138
	10-Q	02/21/98	04/07/98	Not filed	136
	10-Q	05/23/98	07/07/98	Not filed	133
	10-Q	08/22/98	10/06/98	Not filed	130
	10-K	11/21/98	02/22/99	Not filed	126
	10-Q	02/20/99	04/06/99	Not filed	124
	10-Q	05/22/99	07/06/99	Not filed	121
	10-Q	08/28/99	10/12/99	Not filed	118
	10-K	11/27/99	02/28/00	Not filed	114
	10-Q	02/26/00	04/11/00	Not filed	112
	10-Q	05/27/00	07/11/00	Not filed	109
	10-Q	08/26/00	10/10/00	Not filed	106
	10-K	11/25/00	02/26/01	Not filed	102
	10-Q	02/24/01	04/10/01	Not filed	100
	10-Q	05/26/01	07/10/01	Not filed	97
	10-Q	08/25/01	10/09/01	Not filed	94
	10-K	11/24/01	02/25/02	Not filed	90
	10-Q	02/23/02	04/09/02	Not filed	88
	10-Q	05/25/02	07/09/02	Not filed	85
	10-Q	08/24/02	10/08/02	Not filed	82
	10-K	11/23/02	02/24/03	Not filed	78
	10-Q	02/22/03	04/08/03	Not filed	76
	10-Q	05/24/03	07/08/03	Not filed	73
	10-Q	08/23/03	10/07/03	Not filed	70
	10-K	11/22/03	02/23/04	Not filed	66
	10-Q	02/21/04	04/06/04	Not filed	64
	10-Q	05/22/04	07/06/04	Not filed	61
	10-Q	08/21/04	10/05/04	Not filed	58
	10-K	11/20/04	02/21/05	Not filed	54
	10-Q	02/19/05	04/05/05	Not filed	52
	10-Q	05/21/05	07/05/05	Not filed	49

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	08/20/05	10/04/05	Not filed	46
	10-K	11/19/05	02/20/06	Not filed	42
	10-Q	02/18/06	04/04/06	Not filed	40
	10-Q	05/20/06	07/04/06	Not filed	37
	10-Q	08/19/06	10/03/06	Not filed	34
	10-K	11/18/06	02/19/07	Not filed	30
	10-Q	02/17/07	04/03/07	Not filed	28
	10-Q	05/19/07	07/03/07	Not filed	25
	10-Q	08/18/07	10/02/07	Not filed	22
	10-K	11/17/07	02/19/08	Not filed	18
	10-Q	02/16/08	04/01/08	Not filed	16
	10-Q	05/17/08	07/01/08	Not filed	13
	10-Q	08/16/08	09/30/08	Not filed	11
	10-K	11/15/08	02/17/09	Not filed	6
	10-Q	02/14/09	03/31/09	Not filed	5
	10-Q	05/16/09	06/30/09	Not filed	2
Total Filings Delinquent	**52**				
Advantexcel Com Communications Corp.					
	20-F	06/30/01	9/28/01	Not filed	95
	20-F	06/30/02	9/30/02	Not filed	83
	20-F	06/30/03	9/29/03	Not filed	71
	20-F	06/30/04	9/28/04	Not filed	59
	20-F	06/30/05	9/28/05	Not filed	47
	20-F	06/30/06	9/28/06	Not filed	35
	20-F	06/30/07	9/28/07	Not filed	23
	20-F	06/30/08	9/29/08	Not filed	11
Total Filings Delinquent	**8**				
Aeire Corp.					
	10-K	03/31/97	06/30/97	Not filed	146
	10-Q	06/30/97	08/14/97	Not filed	144
	10-Q	09/30/97	11/14/97	Not filed	141
	10-Q	12/31/97	02/17/98	Not filed	138

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-K	03/31/98	06/29/98	Not filed	134
	10-Q	06/30/98	08/14/98	Not filed	132
	10-Q	09/30/98	11/16/98	Not filed	129
	10-Q	12/31/98	02/16/99	Not filed	126
	10-K	03/31/99	06/29/99	Not filed	122
	10-Q	06/30/99	08/16/99	Not filed	120
	10-Q	09/30/99	11/15/99	Not filed	117
	10-Q	12/31/99	02/14/00	Not filed	114
	10-K	03/31/00	06/29/00	Not filed	110
	10-Q	06/30/00	08/14/00	Not filed	108
	10-Q	09/30/00	11/14/00	Not filed	105
	10-Q	12/31/00	02/14/01	Not filed	102
	10-K	03/31/01	06/29/01	Not filed	98
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-Q	12/31/01	02/14/02	Not filed	90
	10-K	03/31/02	07/01/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-Q	12/31/02	02/14/03	Not filed	78
	10-K	03/31/03	06/30/03	Not filed	74
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69
	10-Q	12/31/03	02/17/04	Not filed	66
	10-K	03/31/04	06/29/04	Not filed	62
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-Q	12/31/04	02/14/05	Not filed	54
	10-K	03/31/05	06/29/05	Not filed	50
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-Q	12/31/05	02/14/06	Not filed	42
	10-K	03/31/06	06/29/06	Not filed	38
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-Q	12/31/06	02/14/07	Not filed	30
	10-K	03/31/07	06/29/07	Not filed	26
	10-Q	06/30/07	08/14/07	Not filed	24

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	09/30/07	11/14/07	Not filed	21
	10-Q	12/31/07	02/14/08	Not filed	18
	10-K	03/31/08	06/30/08	Not filed	14
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-Q	12/31/08	02/17/09	Not filed	6
	10-K	03/31/09	06/29/09	Not filed	2
Total Filings Delinquent	**49**				
All American Food Group, Inc.					
	10-KSB	10/31/98	01/29/99	Not filed	127
	10-QSB	01/31/99	03/17/99	Not filed	125
	10-QSB	04/30/99	06/14/99	Not filed	122
	10-QSB	07/31/99	09/14/99	Not filed	119
	10-KSB	10/31/99	01/31/00	Not filed	115
	10-QSB	01/31/00	03/16/00	Not filed	113
	10-QSB	04/30/00	06/14/00	Not filed	110
	10-QSB	07/31/00	09/14/00	Not filed	107
	10-KSB	10/31/00	01/29/01	Not filed	103
	10-QSB	01/31/01	03/19/01	Not filed	101
	10-QSB	04/30/01	06/14/01	Not filed	98
	10-QSB	07/31/01	09/14/01	Not filed	95
	10-KSB	10/31/01	01/29/02	Not filed	91
	10-QSB	01/31/02	03/18/02	Not filed	89
	10-QSB	04/30/02	06/14/02	Not filed	86
	10-QSB	07/31/02	09/16/02	Not filed	83
	10-KSB	10/31/02	01/29/03	Not filed	79
	10-QSB	01/31/03	03/17/03	Not filed	77
	10-QSB	04/30/03	06/16/03	Not filed	74
	10-QSB	07/31/03	09/15/03	Not filed	71
	10-KSB	10/31/03	01/29/04	Not filed	67
	10-QSB	01/31/04	03/16/04	Not filed	65
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-KSB	10/31/04	01/31/05	Not filed	55

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-QSB	01/31/05	03/17/05	Not filed	53
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-KSB	10/31/05	01/30/06	Not filed	43
	10-QSB	01/31/06	03/17/06	Not filed	41
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-QSB	07/31/06	09/14/06	Not filed	35
	10-KSB	10/31/06	01/29/07	Not filed	31
	10-QSB	01/31/07	03/19/07	Not filed	29
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-KSB	10/31/07	01/29/08	Not filed	19
	10-QSB	01/31/08	03/17/08	Not filed	17
	*10-Q**	04/30/08	06/16/08	Not filed	14
	*10-Q**	07/31/08	09/15/08	Not filed	11
	*10-K**	10/31/08	01/29/09	Not filed	7
	*10-Q**	01/31/09	03/17/09	Not filed	5
	*10-Q**	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	**43**				
Allerion, Inc.					
	10-K	04/30/95	07/29/95	Not filed	169
	10-Q	07/31/95	09/15/95	Not filed	167
	10-Q	10/31/95	12/15/95	Not filed	164
	10-Q	01/31/96	03/16/96	Not filed	161
	10-K	04/30/96	07/29/96	Not filed	157
	10-Q	07/31/96	09/14/96	Not filed	155
	10-Q	10/31/96	12/15/96	Not filed	152
	10-Q	01/31/97	03/17/97	Not filed	149
	10-K	04/30/97	07/29/97	Not filed	145
	10-Q	07/31/97	09/15/97	Not filed	143
	10-Q	10/31/97	12/15/97	Not filed	140
	10-Q	01/31/98	03/17/98	Not filed	137
	10-K	04/30/98	07/29/98	Not filed	133
	10-Q	07/31/98	09/14/98	Not filed	131
	10-Q	10/31/98	12/15/98	Not filed	128
	10-Q	01/31/99	03/17/99	Not filed	125

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-K	04/30/99	07/29/99	Not filed	121
	10-Q	07/31/99	09/14/99	Not filed	119
	10-Q	10/31/99	12/15/99	Not filed	116
	10-Q	01/31/00	03/16/00	Not filed	113
	10-K	04/30/00	07/31/00	Not filed	109
	10-Q	07/31/00	09/14/00	Not filed	107
	10-Q	10/31/00	12/15/00	Not filed	104
	10-Q	01/31/01	03/19/01	Not filed	101
	10-K	04/30/01	07/30/01	Not filed	97
	10-Q	07/31/01	09/14/01	Not filed	95
	10-Q	10/31/01	12/17/01	Not filed	92
	10-Q	01/31/02	03/18/02	Not filed	89
	10-K	04/30/02	07/29/02	Not filed	85
	10-Q	07/31/02	09/16/02	Not filed	83
	10-Q	10/31/02	12/16/02	Not filed	80
	10-Q	01/31/03	03/17/03	Not filed	77
	10-K	04/30/03	07/29/03	Not filed	73
	10-Q	07/31/03	09/15/03	Not filed	71
	10-Q	10/31/03	12/15/03	Not filed	68
	10-Q	01/31/04	03/16/04	Not filed	65
	10-K	04/30/04	07/29/04	Not filed	61
	10-Q	07/31/04	09/14/04	Not filed	59
	10-Q	10/31/04	12/15/04	Not filed	56
	10-Q	01/31/05	03/17/05	Not filed	53
	10-K	04/30/05	07/29/05	Not filed	49
	10-Q	07/31/05	09/14/05	Not filed	47
	10-Q	10/31/05	12/15/05	Not filed	44
	10-Q	01/31/06	03/17/06	Not filed	41
	10-K	04/30/06	07/31/06	Not filed	37
	10-Q	07/31/06	09/14/06	Not filed	35
	10-Q	10/31/06	12/15/06	Not filed	32
	10-Q	01/31/07	03/19/07	Not filed	29
	10-K	04/30/07	07/30/07	Not filed	25
	10-Q	07/31/07	09/14/07	Not filed	23
	10-Q	10/31/07	12/17/07	Not filed	20
	10-Q	01/31/08	03/17/08	Not filed	17
	10-K	04/30/08	07/29/08	Not filed	13
	10-Q	07/31/08	09/15/08	Not filed	11

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	10/31/08	12/15/08	Not filed	8
	10-Q	01/31/09	03/17/09	Not filed	5
	10-K	04/30/09	07/29/09	Not filed	1

Total Filings Delinquent **57**

* 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.

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60497; File No. PCAOB-2008-04)

August 13, 2009

Public Company Accounting Oversight Board; Order Approving Proposed Rules on Annual and Special Reporting by Registered Public Accounting Firms

I. Introduction

On June 10, 2008, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission" or "SEC") proposed rules (File No. PCAOB-2008-04) on annual and special reporting by registered public accounting firms, pursuant to Section 107 of the Sarbanes-Oxley Act of 2002 (the "Act"). Notice of the proposed rules was published in the Federal Register on June 18, 2009.[1] The Commission received four comment letters relating to this rule proposal. For the reasons discussed below, the Commission is granting approval of the proposed rules.

II. Description

On June 10, 2008, the Board adopted rules and submitted to the Commission a rule proposal 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 would establish the foundation of a reporting and disclosure system for registered public accounting firms pursuant to Section 102(d) of the Act, specify the details of certain reporting obligations, and provide forms for such reporting. To the extent that the Board identifies additional reporting requirements that

[1] See Release No. 34-60107 (June 12, 2009); 74 FR 29091 (June 18, 2009).

are necessary or appropriate in the public interest or for the protection of investors, the Board may propose and adopt them in the future.

According to the Board, 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 or a firm's awareness of a 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 effected through amendments to PCAOB Rule 2300 concerning the support that a firm must supply to support a confidential treatment request. 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 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.

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.

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.

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.

III. Discussion

A. Comments Received

The Commission received four comment letters relating to the rule proposal. All four of the comment letters came from registered public accounting firms.[2]
Each of the commenters expressed support for the overall purpose of the Board's rules. However, similar to the comments made to the PCAOB during its comment period, the commenters raised several main concerns related to: (1) provisions of proposed PCAOB Rule 2107 that relate to assertions of conflicts with non-U.S. laws; (2) Form 3 triggering events that depend on the firm's awareness; (3) the requirement that registered public accounting firms file with the PCAOB a Form 3 for withdrawn audit reports; (4) the reporting on Form 3 of the dates of registered public accounting firms' consents to the

[2] See comments of Deloitte and Touche LLP ("Deloitte"), Ernst & Young LLP ("E&Y"), KPMG International ("KPMG"), and PricewaterhouseCoopers LLP ("PwC").

use of previously issued audit reports; and (5) the Board's differing approach in Forms 2 and 3 for reporting the engagement of consultants or professionals subject to PCAOB/SEC discipline.

1. Assertions of Conflicts With Non-U.S. Laws

Some commenters expressed concerns about the proposed requirement for non-U.S. firms to gather and maintain certain information. Proposed Rule 2207(c)(1) would require non-U.S. firms to gather and maintain, for a period of seven years, the information required by Forms 2 and 3 that the non-U.S. firm asserts is unable to submit because of a conflicting local law. Some commenters observed that this requirement may cause problems for non-U.S. firms because in some jurisdictions there may be privacy or other laws that would preclude registered firms from gathering the information necessary to complete Form 3.[3]

All of the commenters expressed concerns about the discretion afforded the Board in proposed Rule 2207(e) that would allow the Board to request a non-U.S. firm to file information withheld under proposed Rule 2207(c)(1) based on an asserted conflict with non-U.S. law. Each commenter recognized that although the Board stated in its adopting release that it does not foresee invoking proposed Rule 2207(e) with any regularity, the commenters believe that where applied, it could be of significant concern to non-U.S. firms. According to the commenters, the concern rests on the fact that if the Board invoked Rule 2207(e), a non-U.S. firm could be put in an untenable situation where it would have to choose between breaching its reporting obligations under the PCAOB's rules and violating its home jurisdiction's laws.

[3] See comments of Deloitte, E&Y, and KPMG.

The Board addressed these concerns in its adopting release. In that release, the Board asserted that the requirement for a firm to have in its possession a version of Form 2 or Form 3 that includes the information that the firm would be required to report in absence of a legal conflict imposes no greater burden on a non-U.S. firm than on a U.S. firm that actually reports the information. The Board further stated that the opportunity to assert a legal conflict is an accommodation in light of the possibility that a firm may believe it is caught stuck between competing legal requirements.

The Board also stated that a firm should not assume that its mere assertion of a conflict resolves the matter, and that there is no reason for the Board to provide that a firm need not even have assembled the information, in the form in which any other firm would have to assemble it, before asserting that non-U.S. law precludes it from disclosing the particular information it is withholding. Lastly, and as one of the commenters pointed out, the Board specifically addressed this issue by adding a note to Rule 2207(c)(1) to provide that the materials maintained by the firm do not need to include 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.

As the commenters noted, the Board explained at length its purpose and intended administration of Rule 2207(e). The Board noted that its position is not dissimilar from the same situation it faces in the registration context. The Commission is not aware of any instances or concerns in the registration context in which the PCAOB has acted unreasonably with regard to conflicts with non-U.S. laws that were raised by non-U.S. firms.

The Commission believes the Board's responses to these comments are not unreasonable. The Commission presumes that the Board will continue to exercise reasonable judgment and discretion in considering conflicts with non-U.S. laws that are raised in connection with the completion of a Form 2 or Form 3 as it has for the past six years with respect to similar issues in the registration context.[4]

2. Firm Awareness of Form 3 Triggering Events

Certain items reported in Form 3 describe events that a firm must report to the Board within 30 days after the firm has become aware of certain facts. The Form provides 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.

All commenters expressed concern that triggering the reporting requirement based on the awareness of any one of the large number of people who fall into the definition provided by the Board, especially if they are not part of senior management, would be burdensome. Several of these commenters observed that, in response to the proposed rules, firms would put in place policies and procedures requiring reportable information be reported to the persons in the organization responsible for compliance with the rules. Because of their view that firms would put the necessary policies and procedures in place, these commenters recommended that the Commission encourage the PCAOB to consider issuing guidance providing that a registered firm will not be considered out of

[4] The Commission also notes that the Board has been willing to provide further implementation guidance where necessary to explain its administration of similar requirements. See http://www.pcaob.org/Registration/2004-03-11_FAQ.pdf.

compliance with a reporting obligation if there is an inadvertent failure to follow internal procedures that are designed in good faith to effectuate reporting.

Similar comments were originally raised to the Board in connection with the Board's original proposal of the annual and special reporting rules. After consideration of the comments received, the Board narrowed the Form 3 reporting requirements as to the reportable events and clarified the "deemed aware" standard as to which persons are covered. In addition, the Board stated it 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.

We agree. This matter is not dissimilar to the need for issuers to maintain appropriate disclosure and controls and procedures to meet their reporting obligations, including for current reporting on Form 8-K that is on a much shorter timeframe than Form 3 reporting. Those procedures include those to ensure that information is accumulated and communicated to the appropriate personnel to allow timely disclosure. This matter also is not dissimilar to a registered public accounting firm's existing obligations under the Commission's and the PCAOB's auditor independence requirements, which in many instances reaches down to obligations involving members of an engagement team below a partner level. Lastly, as to when it would be appropriate for the Board to take disciplinary action for reporting violations, the Commission assumes the Board will continue to exercise its discretion as to whether disciplinary action is warranted under the particular facts and circumstances.

3. <u>Disclosure of the Dates of Consents of Audit Reports</u>

Under the proposed rules, firms would be required to report on Form 2 the dates of any consent to an issuer's use of an audit report the firm previously issued to that issuer, if such consent constitutes the only instance of the firm issuing an audit report for that issuer during the reporting period. Three commenters expressed opposition to this proposed requirement on the basis that it would not be sufficiently meaningful to warrant the potential burden of gathering and reporting it,[5] with one noting that this information would in most, if not all, cases have already been listed in the previous year's public report on Form 2.[6]

We are not persuaded by the arguments raised by commenters that this requirement would be an undue burden, and we believe that it is not unreasonable for the Board to request firms to provide the dates of consents when such consent constitutes the only instance of the firm issuing an audit report for that issuer during the reporting period. We acknowledge that for the larger firms, they will likely need to institute additional controls to compile the information, but we do not believe the burden to be unreasonable.

4. Reporting of Withdrawn Audit Reports

The rules proposed by the Board include a requirement that a firm file a Form 3 when it withdraws an audit report and the related issuer has failed to comply with its requirement to file a Form 8-K regarding the event. Some commenters opposed this proposal and expressed the view that this matter fundamentally is about issuer conduct and, therefore, is more appropriately left to the Commission in the context of its

[5] See comments of E&Y, KPMG, and PwC.

[6] See comments of PwC.

disclosure framework and that such monitoring and reporting would create an unnecessary and duplicative burden on registered firms.[7]

Commenters expressed these same concerns during the Board's comment period and the Board responded to these comments by noting the following: (1) the point of this item is not have the firm draw the Board's attention to potential problems with an issuer's financial statements, but that 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; and (2) the Board has a regulatory interest in being aware of this information and possibly following up on that information for reasons directly related to its oversight of auditors.

The Commission agrees with the responses made by the PCAOB and believes that a requirement for registered firms to report this information is not unreasonable. In addition, we note the response of one commenter who indicated that registered firms already routinely track such instances.

5. <u>Differing Approach in Forms 2 and 3 to the Reporting of the Engagement of Consultants or Professionals Subject to PCAOB/SEC Discipline</u>

Form 2 requires registered firms to report information about certain types of relationships with individuals and entities who have specified disciplinary and other histories. One such reporting requirement under Part VII of Form 2 requires firms to report arrangements for services related to the firm's audit practice or related to services the firm provides to issuer audit clients. Section II of Form 3 includes a similar reporting

[7] See comments of Deloitte and PwC.

trigger, however that trigger is not limited to individuals who provide audit services. Two commenters raised concerns about these requirements.[8]

Both commenters acknowledged a statement made by the Board in its adopting release where the Board expressed its view that limiting the scope of the Form 3 reporting requirement would negate the purpose of the reporting requirement, "which is generally intended to gather information about new relationships with persons or entities that are effectively restricted from providing auditing services."[9] Both commenters disagreed with the Board's response.

The Commission believes the Board appropriately explained its rationale for the difference in the Form 2 and Form 3 reporting requirements and believes that it is not unreasonable for the Board to request this information in the current manner in which it is requested.

6. Requests for Additional Implementation Guidance

As noted in the above discussion, the Commission has considered the concerns and issues raised by commenters and appreciates the feedback. While the Commission believes the aforementioned matters are not unreasonable requirements, the Commission does encourage the Board to monitor implementation of its annual and special reporting rules and to be open to issuing timely implementation guidance as necessary as to these and the other comments raised, as was done with the Board's implementation of its registration rules.[10]

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[8] See comments of KPMG and Deloitte.

[9] See PCAOB Release No. 2008-004, June 10, 2008 [page 22].

[10] See, e.g., http://www.pcaob.org/Registration/Registration_FAQ.pdf; and http://www.pcaob.org/Registration/2004-03-11_FAQ.pdf.

B. Recommendation as to the Annual Fee

Section 102(f) of the Act requires the Board to "assess and collect a registration fee and an annual fee from each registered firm in amounts that are sufficient to recover the Board's costs of processing and reviewing applications and annual reports."[11] The PCAOB has collected registration fees from every firm that has registered with the Board since 2003. However, the Board has not assessed or collected annual fees from any registered firms.

In our order approving the PCAOB's budget and accounting support fee for 2008, the Commission directed the PCAOB to, among other things, analyze historical and planned expenditures related to the review and processing of registrations and annual reports of public accounting firms.[12] We understand from this analysis that there are unrecovered historical costs that need to be collected from registered firms. In addition, the Board needs to determine the amount of current and future costs of reviewing and processing registrations and annual reports and how and over what period to recover those costs. These matters also are impacted due to changes to the Board's registration profile that may occur as a result of the requirement for auditors of non-public broker dealers to be registered with the Board for fiscal periods ending on or after January 1, 2009.

The Commission recommends that, in setting its annual fee under PCAOB Rule 2202, Annual Fee, the Board recover all of the unrecovered historical costs associated with the Board's review and processing of registration applications in the first annual fee

[11] 15 U.S.C. 7212(f).

[12] See Release No. 34-56986 (December 18, 2007).

billed to registered public accounting firms and that these costs be recovered only from registered public accounting firms that were registered prior to January 1, 2009, and that such bill be separately itemized. In addition, for consistency and to aid transparency, the Commission recommends that future costs associated with reviewing and processing registration applications, processing annual and special reporting, and related system maintenance and development costs be recovered over a time period that is consistent with the time period the PCAOB uses for its financial statement purposes to depreciate long-lived assets similar to that used by the PCAOB in processing registration applications and annual and special reports.

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed PCAOB rules on annual and special reporting by registered public accounting firms are consistent with the requirements of the Act and the securities laws and are necessary or appropriate in the public interest or for the protection of investors.

IT IS THEREFORE ORDERED, pursuant to Section 107 of the Act and Section 19(b)(2) of the Exchange Act, that proposed PCAOB Rules on Annual and Special Reporting by Registered Public Accounting Firms (File No. PCAOB-2008-04) be and hereby are approved.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60496; File No. PCAOB-2008-05)

August 13, 2009

Public Company Accounting Oversight Board; Order Approving Proposed Rules on Succeeding to the Status of a Predecessor Firm

I. Introduction

On August 4, 2008, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission") proposed rules (File No. PCAOB-2008-05) on succeeding to the status of a predecessor firm, pursuant to Section 107 of the Sarbanes-Oxley Act of 2002 (the "Act"). Notice of the proposed rules was published in the Federal Register on June 18, 2009.[1] The Commission did not receive any comment letters relating to this rule proposal. For the reasons discussed below, the Commission is granting approval of the proposed rules.

II. Description

On July 28, 2008, the Board adopted rules and submitted to the Commission a rule proposal consisting of two new rules (PCAOB Rules 2108-2109) and a new form, Form 4, related to succeeding to the registration status of a predecessor firm. The proposed rules allow, in certain circumstances, a registered public accounting firm's registration status to continue with a firm that survives a merger or other change in the registered firm's legal form. If approved by the Commission, the rules on succession reporting would take effect 60 days after Commission approval. For firms that had a change in legal form, or that resulted from an acquisition or combination, in the period

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[1] See Release No. 34-60108 (June 12, 2009); 74 FR 29005 (June 18, 2009).

between the firm's registration and the effective date of the rules, those firms will be required to report the change on Form 4 within 14 days after the Commission's approval date.

The proposed rules provide the opportunity for continuity of a firm's registration in two categories: (1) changes related to a firm's legal form of organization or jurisdiction; 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 proposed 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 proposed rules set a deadline of 14 days for a firm to file a report on Form 4, 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 4 also build in safeguards to ensure that the Form 1 registration process is not circumvented in circumstances where that process is more appropriate than Form 4 succession.

III. Discussion

The Commission did not receive any comment letters relating to the rule proposal.

IV. Conclusion

The Commission finds that the proposed PCAOB rules on succeeding to the registration status of a predecessor firm are consistent with the requirements of the Act and the securities laws and are necessary or appropriate in the public interest or for the protection of investors.

IT IS THEREFORE ORDERED, pursuant to Section 107 of the Act and Section 19(b)(2) of the Exchange Act, that proposed PCAOB Rules on Succeeding to the Registration Status of a Predecessor Firm (File No. PCAOB-2008-05) be and hereby are approved.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Chairman Schapiro and Commissioner Aguilar not participating

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 60505 / August 14, 2009

Admin. Proc. File No. 3-13324

In the Matter of the Application of

NORTH WOODWARD FINANCIAL CORP.

and

DOUGLAS A. TROSZAK
690 East Maple
Birmingham, Michigan 48009-6353

For Review of Disciplinary Action Taken by

FINRA

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION -- REVIEW OF DISCIPLINARY PROCEEDINGS

Failure to Comply with Recordkeeping and Reporting Requirements

Conduct Inconsistent with Just and Equitable Principles of Trade

Where member firm of registered securities association maintained, and financial and operations principal caused member firm to maintain, deficient books and records, *held*, association's findings of violations and the sanctions it imposed are *sustained*.

APPEARANCES:

Douglas A. Troszak, pro se and for North Woodward Financial Corp.

Marc Menchel, Alan Lawhead, and *Jante C. Santos*, for FINRA.

Appeal filed: January 5, 2009
Last brief received: April 8, 2009

I.

North Woodward Financial Corp. ("North Woodward" or the "Firm"), a registered broker-dealer, and Douglas A. Troszak, its principal owner, president, and financial and operations principal ("FINOP"),[1] appeal from NASD disciplinary action.[2] NASD found that North Woodward, acting through Troszak, failed to prepare and maintain a current general ledger and trial balance for February and March 2005, in violation of Securities Exchange Act of 1934 Rules 17a-3(a)(2) and 17a-3(a)(11),[3] and NASD Rules 3110(a) and 2110.[4] NASD fined North

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[1] Troszak is also North Woodward's general securities representative and general securities principal.

[2] On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD's Restated Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority, Inc., or FINRA, in connection with the consolidation of NASD and the member-regulation, enforcement, and arbitration functions of the New York Stock Exchange. *See* Securities Exchange Act Rel. No. 56146 (July 26, 2007), 91 SEC Docket 517 (Aug. 1, 2007). Because NASD instituted the disciplinary action before that date, it is appropriate to continue to use the designation NASD.

[3] 17 C.F.R. §§ 240.17a-3(a)(2) and (11). Exchange Act Rules 17a-3(a)(2) and (11) require that broker-dealers "make and keep current . . . Ledgers (or other records) reflecting all assets and liabilities, income and expense and capital accounts," 17 C.F.R § 240.17a-3(a)(2), and "[a] record of the proof of money balances of all ledger accounts in the form of trial balances, and a record of the computation of aggregate indebtedness and net capital, as of the trial balance date," 17 C.F.R. § 240.17a-3(a)(11). Rule 17a-3(a)(11) further provides that "[s]uch trial balances and computations shall be prepared currently at least once a month."

[4] Conduct Rule 3110(a) requires, in pertinent part, that members "make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations and statements of policy promulgated [by NASD] . . . and as prescribed by SEC Rule 17a-3." Conduct Rule 2110 requires members to observe "high standards of commercial honor and just and equitable principles of trade." A violation of any NASD Conduct Rule, such as Conduct Rule 3110, also constitutes a violation of Rule 2110. *Ronald Pelligrino*, Exchange Act Rel. No. 59125 (Dec. 19, 2008), 94 SEC Docket 12628, 12629 n.2; *Robert E. Strong*, Exchange Act Rel. No. 57426 (Mar. 4, 2008), 92 SEC Docket 2875, 2887. NASD General Rule 115 extends the applicability of NASD rules governing members to their associated persons. *James W. Browne*, Exchange Act Rel. No. 58916 (Nov. 7, 2008), 94 SEC

(continued...)

Woodward and Troszak $2,500, jointly and severally.[5] We base our findings on an independent review of the record.

II.

This case concerns inadequacies in North Woodward's books and records that were identified during a routine examination conducted by NASD staff in May 2005. NASD notified the Applicants of the examination three days before it was set to begin and asked that Applicants make available to its staff North Woodward's financial records for the period from February 1, 2005 through April 30, 2005. In its notice, NASD specifically informed the Applicants that the Firm's "General Ledger" and "Trial Balance" would "be needed for review during the examination . . . ."

a. During the examination, Troszak gave the examiners a number of documents related to the Firm's finances, including bank and brokerage statements and check registers.[6] However, he failed to provide either a general ledger or a trial balance for February and March 2005. When NASD staff asked for North Woodward's general ledgers, Troszak responded that the documents that he had provided the examiners contained everything that would be included

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[4] (...continued)
Docket 11389, 11390 n.3; *Michael Frederick Siegel*, Exchange Act Rel. No. 58737 (Oct. 6, 2008), 94 SEC Docket 10501, 10509 n.13.

FINRA is in the process of revising and renumbering many of its rules as part of the process of developing a new consolidated rulebook. *See* FINRA Information Notice, Mar. 12, 2008 (Rulebook Consolidation Process). No substantive changes have been made to the rules at issue here.

[5] NASD also assessed $1,950.42 in costs.

[6] Troszak provided the examiners with the following North Woodward documents: (1) bank statements from January to March 2005, containing Troszak's handwritten notes of North Woodward's revenues, expenses, net capital, and profit computations; (2) a check register for March 2005; (3) cleared checks from February through April 2005; (4) the Financial and Operational Combined Uniform Single Report, Part IIA, for the period between January and March 2005 (the "FOCUS Report"); (5) a clearing statement from Sterne Agee Clearing, North Woodward's clearing firm, for March 2005; (6) a brokerage statement from Sterne, Agee & Leach, Inc. for the month of March 2005; (7) an invoice from the Securities Investor Protection Corporation ("SIPC") showing the assessment of $150 in January 2005 and the payment by check of the assessment on April 14, 2005; and (8) a copy of a bill from Blue Cross Blue Shield of Michigan for the coverage period from March 25, 2005 through April 25, 2005, which contains a handwritten notation stating that the bill was paid by North Woodward on February 8, 2005.

in a general ledger.[7] When the examiners asked Troszak to provide them with North Woodward's trial balances, Troszak told them that North Woodward's February bank account statement, along with some handwritten notes that he had made on that statement, was the same thing as the February trial balance and that North Woodward's statement of financial condition contained in its FOCUS Report was the same as the March trial balance.[8]

In the absence of North Woodward's general ledger and trial balance for February and March 2005, NASD staff used the Firm's bank statements, cleared checks, brokerage statement, clearing statement, and bills to check North Woodward's net capital calculation as of March 31, 2005. Based on these documents, the staff determined that North Woodward maintained an excess amount of net capital for the period (understating its net capital by $6,994) and, as a result, North Woodward's quarterly FOCUS Report for the period ending March 31, 2005 was inaccurate. The NASD examiner attributed the understatement primarily to Applicants' failure to use the accrual method of accounting.

b. Subsequent to the examination, NASD sent Applicants a written report summarizing the deficiencies identified in the Firm's books and records. In correspondence with NASD dated June 2, 2005 responding to this report, Troszak conceded that North Woodward's "general ledger and trial balance were not current as of March 31, 2005" but advised that, since the examination, "[t]hat deficiency [had been] corrected" and "both [the general ledger and trial

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7 Troszak conceded in his sworn, on-the-record testimony ("OTR Testimony") to NASD, that he had not provided the NASD examiners with the sort of general ledger that he had provided during earlier examinations but maintained that the documents he had provided "presented all records that clearly reflected the assets, liabilities, income and expense of the period." He also asserted that he had satisfied the requirement for maintaining a current trial balance since "[t]he checks and who the checks were written to is the same idea as a trial balance."

8 Although NASD initially sought North Woodward's general ledger and trial balance for the period from February 1 through April 30, 2005, during the on-site examination, the examiner only requested North Woodward's records for February and March 2005. The examiner testified that he did not request the April 2005 general ledger and trial balance because he "expected" Troszak to respond as he had for the February and March records, namely that Troszak "didn't have one for April." NASD's National Adjudicatory Council limited its review to just February and March 2005.

The NASD examiner testified that, during the exit interview, he again asked Troszak about his failure to furnish the examiners with a general ledger and trial balance. Troszak replied, according to the examiner, that he did not prepare a traditional general ledger and trial balance because it was Troszak's view "that the SEC and FINRA accounting requirements were archaic and don't reflect what actually happens in the true accounting world." Troszak confirmed at the NASD hearing that he told the examiner that the requirements were archaic.

balance were] accurate as of the end of the first quarter." In December 2005, the staff requested that North Woodward provide NASD with copies of several documents, including North Woodward's updated general ledger and trial balance as of March 31, 2005. Troszak provided NASD the requested documents in December 2005.[9]

III.

Applicants contend that they have "fully complied at all times" with regulatory requirements. They claim that the Firm "had a general ledger and trial balance," but that it was not presented in the format used by larger firms "which the examiner was used to examining." We disagree and find, as discussed below, that the Firm's books and records did not comply with regulatory requirements.

a. Source Documents Do Not Satisfy Substantive Requirements

Applicants assert that, notwithstanding the Firm's failure to maintain a traditional general ledger and trial balance, the records furnished to NASD's examiners satisfied the specific substantive requirements for what must be included in a broker-dealer's ledger and trial balance.[10] They claim that the Firm's bank statements, cancelled checks, various statements from North Woodward's clearing firm, some bills, and a check register were sufficient to comply with the requirement for maintaining a ledger. Applicants further contend that the statement of financial condition from the FOCUS filing for March of 2005 was the same thing as a trial balance and that North Woodward's statement of financial condition contained in its March 2005 FOCUS Report and the Firm's reconciled bank account statement, along with some handwritten notes that Troszak had made on the statement was the equivalent of the requested February 2005 trial balance.

Applicants note that the Firm only had seven transactions in March 2005 -- a clearing firm deposit and six checks that it wrote that month from its bank account -- and that it "does not have a payroll ledger, subsidiary ledgers, account receivable ledgers or inventory, land and buildings." They contend that NASD rules "allow[] small firms that deal mostly in mutual fund sales," such as North Woodward, "to have a simple recordkeeping system."

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9 On December 21, 2005, NASD issued North Woodward a Letter of Caution for, among other deficiencies, the inaccurate net capital computation and FOCUS Report filing during the preceding spring.

10 Applicants explained that North Woodward's general ledger was compiled by reconciling North Woodward's bank statement at the end of the month. The Firm's trial balance was compiled, Applicants state, by taking the unadjusted cash balance from the bank statement and adjusting it by adding any clearing firm deposits in order to derive North Woodward's "adjusted trial balance." From this amount, Applicants then determined whether the Firm was in compliance with its net capital requirement.

Applicants' records did not satisfy the applicable requirements. NASD Rule 3110(a) requires, in pertinent part, that members keep books and records as prescribed by Exchange Act Rule 17a-3. As relevant here, Rule 17a-3 requires that broker-dealers keep "[l]edgers (or other records) reflecting all assets and liabilities, income and expense and capital accounts"[11] and "[a] record of the proof of money balances of all ledger accounts in the form of trial balances, and a record of the computation of aggregate indebtedness and net capital, as of the trial balance date . . . [with] [s]uch trial balances [to] be prepared currently at least once a month."[12]

In a 1996 NASD Board of Governors Memorandum, the NASD noted that a general ledger should consist of "a record of all asset, liability and nominal accounts" and should be maintained in such a way that the broker-dealer's "trial balance can be abstracted in order to prepare financial statements showing the broker's or dealer's financial condition."[13] In addition, NASD declared in a 2004 release that a broker-dealer's general ledger should include all of its "asset account balances," "liability account balances," "income account balances," "expense account balances," and "capital account balances."[14] The NASD further noted in that release that a broker-dealer's trial balance should include the "account name," as well as the "open debit or credit balance" for the firm's various accounts.[15] These interpretations are consistent with those generally understood and applied in the accounting profession.[16]

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11 17 C.F.R. § 240.17a-3(a)(2). In a 1974 release, we clarified that the "ledgers" described in Rule 17a-3(a)(2) include a "general ledger" that is compiled from the "blotters and other records of original entry." *Statement Regarding the Maintenance of Current Books and Records by Brokers and Dealers*, Accounting Series Rel. No. 156 (Apr. 26, 1974), 4 SEC Docket 195, 196.

12 17 C.F.R. § 240.17a-3(a)(11).

13 *Memorandum of the NASD Board of Governors re: Rule 17a-3* (1996), NASD Manual (Nov. 2003 ed.).

14 *Suggested Formats for Books and Records* (Oct. 2004), *http://www.finra.org/web/groups/industry/@ip/@comp/@regis/documents/industry/p009847.pdf.*

15 *Id.* at 21.

16 *See, e.g.*, Patricia A. Woodbury, *Basics of Accounting for Lawyers: What Every Practicing Lawyer Needs to Know - Understanding Generally Accepted Accounting Principles (GAAP), Generally Accepted Auditing Standards (GAAS) and the Accounting Cycle*, 1613 PLI/Corp 9, 19, Practising Law Institute Corporate Law and Practice Course Handbook Series, PLI Order No. 11112, July-August, 2007 (noting that a general ledger is "the entire set of accounts for a company"), and at 20 (defining a "trial balance" as "a schedule that lists all the general ledger account balances at a given point in time"). *See also* Love, 1195 PLI/Corp at 137

(continued...)

The records provided to NASD's examiners did not satisfy the requirements of Rule 17a-3. The documents that Applicants submitted did not properly classify the Firm's transactions. As Edward Wegener, an NASD associate district director, explained, a general ledger, in contrast to the documents provided by North Woodward, "is meant to record not only that the event happened but how it was classified."[17] He observed that North Woodward's bank statements and other source documents merely recorded particular transactions but failed to classify them by type of transaction.

Moreover, many of the checks written by North Woodward during the examination period do not provide sufficient information to properly and fully classify the transaction. For example, the Firm wrote a check in the amount of $2,421.55 to the Bank of Northern Michigan on March 10, 2005. The note on this check indicated that it was for a "Loan #100032515." There is no indication on the check as to how much of this payment was for interest and how much was for principal repayment (or for other purposes). Similarly, a check in the amount of $752.56 made payable to the Birmingham Athletic Club has a notation "member #001307" but no indication as to whether this was, for example, a company expense, a reimbursable personal expense, or even a charitable contribution. And a number of checks were written to various payees where the only notation is an account number. Again, with this limited information, it is very difficult to properly classify these payments.

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[16] (...continued)
(describing a trial balance as "a listing of the net balances in all the accounts in the general ledger"); and *Accounting For Lawyers--A Satellite Program - Bookkeeping*, 622 PLI/Corp at 74 (explaining that a trial balance is prepared by, "not only aggregat[ing] the total of the related accounts into a single line item, but also includ[ing] certain adjustments that must be made under generally accepted accounting principles").

[17] As an example of how a general ledger should account for a transaction, Wegener explained that for a capital withdrawal, the ledger should show a credit to cash and a debit to the capital account. He noted that this accounting would permit an examiner to "review the general ledger and see that . . . there was a . . . credit to cash and a debit to capital withdrawal and review the supporting documentation to verify that that was . . . [r]ecorded correctly and classified correctly."

Broker-dealers are required to use the accrual method of accounting.[18] Applicants source documents, however, were not prepared using the accrual method of accounting. Under accrual accounting, a broker-dealer must recognize revenues when earned and liabilities when incurred.[19] Applicants admit that North Woodward "recognizes revenue when received, credit to bank statement, and expenses when checks are cut, 'debits' on a bank statement and a clearing deposit." In his OTR Testimony, Troszak seemed to confirm that the Firm's books examined by NASD were not kept regularly on an accrual basis.[20]

The NASD examiner determined from his review of North Woodward's records that, while North Woodward was in compliance with the net capital requirement, it had nevertheless understated its net capital by about $7,000, "primarily [due to its] . . . failure to accrue an account receivable from the clearing firm that was commissions and the failure to accrue a small account payable for a specific assessment." In addition, the examiner discovered after the examination that North Woodward had written a $500 check to NASD to pay a prior fine and that this had not been reflected in North Woodward's March 2005 net capital computation. The examiner explained that if North Woodward had had a proper general ledger, this amount should have been reflected in the March ledger as an accrual for the outstanding balance of the NASD fine and should have been recorded in the March trial balance as an account payable.

Applicants assert that, given North Woodward's small size and the limited number of transactions it engages in, the NASD examiners "could clearly ascertain the accuracy of [North Woodward's] net capital computation" by reviewing the books and records that Applicants

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18 *Joseph S. Barbera*, 54 S.E.C. 967, 969 (2000) (noting our long-standing position that "broker-dealers must . . . 'use the accrual method of accounting'" (citations omitted)); *James S. Pritula*, 53 S.E.C. 968, 973 (1998) (same); *Clinger & Co.*, 53 S.E.C. 358, 361 (1997) (same); *Troy A. Wetter*, 51 S.E.C. 763, 765 (1993) (same); s*ee also Net Capital Requirements for Brokers and Dealers*, Exchange Act Rel. No. 18737 (May 13, 1982), 25 SEC Docket 468, 468 & n.4 (noting that, in order for a broker-dealer to determine its net capital, it must first determine its net worth in accordance with generally accepted accounting principles, which requires, among other things, that it "us[e] the accrual method of accounting").

19 *Barbera*, 54 S.E.C. at 969 (explaining that "[u]nder accrual accounting, a broker-dealer 'must recognize revenues when earned and liabilities when incurred'" (citations omitted)); *Pritula*, 53 S.E.C. at 973-74 (same).

20 Troszak explained that North Woodward's books are kept on a cash basis until the end of a reporting or audit period, at which time they are adjusted and converted to an accrual basis. He conceded that the March 2005 documents, while providing "full disclosure" on a cash basis, were not complete on an accrual basis since they were "missing the work that happened during the month of March which is cash basis deposited in April."

furnished them.[21] According to Wegener, however, it would be difficult for an NASD examiner to determine a member firm's accrued but unpaid liabilities without a general ledger because the examiner would simply not know that these liabilities exist.[22]

We agree with the NASD staff testimony that the general ledger and the trial balance are "two key foundation documents" that allow examiners to verify the accuracy of the member firms' capital computation. Thus, we have previously rejected an applicant's claim that providing the underlying source documents was sufficient to comply with the requirement for maintaining a trial balance. In *Joseph S. Barbera,*[23] the applicant asserted that Rule 17a-3 was not violated, notwithstanding respondent's failure to prepare a trial balance, because NASD was provided with the "requisite information" for preparing the firm's trial balance, noting that the Exchange Act "is

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[21] Applicants assert that, in contrast to several of the largest investment banks which "have experienced severe liquidity problems," North Woodward has never had a problem with net capital. According to Applicants, NASD's contention that North Woodward had understated its net capital by $6,994 during the May 2005 examination was erroneous because North Woodward's net capital calculation was done in conformance with GAAP, "as opposed to FINRA examination rules." While Applicants acknowledge that NASD did not, in fact, charge North Woodward with violating the net capital rules, they assert that they are "compelled to bring it up" in this appeal "because it adds credence to the entire process which is designed to intentionally mislead the SEC."

However, the issue to be resolved here is not whether North Woodward's net capital computations were accurate or even whether these computations could be determined by reference to the source documents provided to the NASD examiners. Rather, the question for our determination is whether these source documents satisfied the requirements under Rule 17a-3 for a "ledger" and a "trial balance."

[22] Wegener explained that an examiner reviews a firm's trial balance and general ledger as part of the examination of the firm's net capital. This examination is done by "review[ing] the transactions as recorded on the general ledger, review[ing] those against what was posted to a trial balance and then follow[ing] those through to the financial statements to make sure all the transactions were recorded accurately, were transferred from the general ledger to the trial balance, to the ultimate financial statements to make sure that the net capital computation is correct." Wegener noted that, without the general ledger and a trial balance, an examiner would not know about a firm's accrued receivables and liabilities and, thus, would be hindered in determining the accuracy of the firm's net capital computation. He explained that an examiner will review the general ledger to make sure that the firm is correctly booking its receivables and liabilities and that the examiner will only know of the existence of these items if "it's reported in the firm's general ledger and then makes its way from the general ledger to the trial balance, etc."

[23] 54 S.E.C. 967 (2000).

silent on what constitutes a 'trial balance' for purposes of compliance" with the rules.[24] We noted that Exchange Act Rule 17a-3 (a)(11) expressly provides the requirements for the creation of trial balances, and emphasizing that "[a] principal purpose of the requirement for a trial balance is 'to assist in keeping members, brokers and dealers currently informed of their capital positions.'"[25]

Here, consistent with our analysis in *Barbera*, we conclude that the records required to be maintained under Rule 17a-3(a) are specific in their own right, not simply another name for a loose grouping of underlying source documents. We, thus, find that the underlying source documents North Woodward provided to examiners did not satisfy the applicable recordkeeping requirements.

b. Failure To Keep Ledger and Trial Balance Current

Rule 17a-3(a)(11) mandates that broker-dealers update their trial balances on at least a monthly basis, although the rule is silent as to the frequency for updating general ledgers beyond the general requirement that they be kept "current." In determining how frequently a broker-dealer must update its general ledger, we stated that a "broker-dealer is required to be in compliance with the net capital rule at all times and the general ledger must be posted as frequently as may be necessary to make that determination."[26] However, our release further specified that "[i]f a broker-dealer effects only a limited number of transactions during an accounting period and it is clear from the nature of the business conducted that such transactions would have no material adverse effect on the broker-dealer's financial and operational condition, net capital, and [customer] protection requirements during the period it may be appropriate to post the general ledger on a monthly basis."[27] In its 2004 release, NASD advised broker-dealers that their general ledgers "[s]hould be kept up-to-date and should be posted as frequently as activity warrants - daily, if necessary, but at least monthly in order to prepare financial statements."[28] Thus, in accordance with our and NASD's directives, even if a broker-dealer only has a limited amount of financial activity and that activity would not have a material adverse effect on the broker-dealer's financial and operational condition, net capital or customer

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24 *Id.* at 978.

25 *Id.* at 979 & n.35 (quoting Exchange Act Rel. No. 7550 (Mar. 10, 1965), 1965 SEC LEXIS 653, *1 (Proposal to Amend Rules 17a-3 and 17a-4), *adopted in* Exchange Act Rel. No. 8023 (Jan. 18, 1967), 1967 SEC LEXIS 446 (Adoption of Amendments)).

26 4 SEC Docket at 196.

27 *Id.*

28 *Suggested Formats for Books and Records* at 9 (Oct. 2004), *http://www.finra.org/web/groups/industry/@ip/@comp/@regis/documents/industry/p009847.pdf.*

protection requirements, as was the case with North Woodward, it must prepare and update its general ledger on at least a monthly basis.

Applicants failed to make these required monthly postings to North Woodward's records as required by Rule 17a-3(a)(2) and 17a-3(11). Indeed, Troszak conceded in his June 2005 letter to NASD staff that North Woodward's "general ledger and trial balance were not current as of March 31, 2005."[29]

* * *

Accordingly, we find that North Woodward violated Exchange Act Rule 17a-3 and NASD Conduct Rules 3110 and 2110 by failing to prepare and maintain a current general ledger and trial balance for February and March 2005. We further find that Troszak, who as North Woodward's principal and FINOP was responsible for North Woodward's violations, violated NASD Conduct Rules 3110 and 2110.[30]

IV.

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

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[29] Applicants complain that, during its settlement discussions, NASD staff threatened to increase the proposed fine if Applicants did not promptly settle the case. They further complain that NASD sought to "overwhelm" the Firm by bringing this proceeding and seek reimbursement of their associated costs. Applicants provide no evidence of improper conduct (during settlement negotiations or otherwise) and our review of the record indicates that the proceedings were fair, as required by the Exchange Act. *See* Exchange Act § 15A(b)(8), 15 U.S.C. § 78o-3(b)(8) (requiring that NASD "provide a fair procedure for the disciplining of members and persons associated with members").

We see no reason for awarding costs to Applicants since, as discussed herein, NASD was amply justified in bringing this proceeding. In any event, Applicants have cited to no basis for the awarding of costs to an NASD member firm (or associated persons of members) or for compensating a member for its "administrative costs," and we are unaware of any such provision.

[30] Exchange Act Rule 17a-3, by its terms, applies to broker-dealers, not to persons associated with broker-dealers. *See Davrey Fin. Servs., Inc.*, Exchange Act Rel. No. 51780 (June 2, 2005), 85 SEC Docket 2057, 2062 & n.13 (holding that, while member firm violated, among other rules, Exchange Act Rule 17a-3, the firm's principal and FINOP who caused the firm to commit the violation did not himself violate this rule as the rule only applies to broker-dealers). We therefore set aside NASD's finding that Troszak also violated Exchange Act Rule 17a-3. However, as discussed below, we do not believe that our decision to set aside this finding justifies a modification in the sanction imposed on Troszak.

excessive or oppressive or impose an unnecessary or inappropriate burden on competition.[31] The proper sanction depends on the unique facts and circumstances of each case, and it cannot be determined by comparison with other cases.[32] Applying this standard, we see no basis for reducing the sanctions.

Applicants do not address the sanctions in their briefs, and we believe, with consideration for the public interest and the protection of investors, that the fine that NASD imposed is remedial and not excessive or oppressive.[33] As an initial matter, we observe that the amount of the fine is at the lower end of the recommended range set out in NASD's Sanction Guidelines. The Sanction Guidelines recommend that, for non-egregious recordkeeping violations, NASD should consider suspending the firm and its FINOP or responsible party for up to 30 business days and imposing a fine of $1,000 to $10,000.[34]

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[31] Applicants do not assert, and the record does not show, that NASD's action imposes an undue burden on competition.

[32] *See, e.g.*, *Scott Epstein*, Exchange Act Rel. No. 59328 (Jan. 30, 2009), 95 SEC Docket 13833, 13865 n.75; *see also Butz v. Glover Livestock Comm'n Co.*, 411 U.S. 182, 187 (1973).

[33] *See PAZ Sec., Inc. v. SEC*, 566 F.3d 1172, 1176 (D.C. Cir. 2009) (noting that, while Exchange Act Section 19(e)(2) requires the Commission to "review[] NASD's sanction with 'due regard for the public interest and the protection of investors,'" it does "not limit the discretion of the Commission to choose an appropriate sanction so long as its choice meets the statutory requirements that a sanction be remedial and not 'excessive or oppressive'") (citations omitted)).

The NASD Hearing Panel had fined North Woodward and Troszak $10,000, jointly and severally, ordered Troszak to requalify as a FINOP, and imposed hearing costs of $1,950.42. NASD's National Adjudicatory Council affirmed the Hearing Panel's findings of violations and the imposition of hearing costs but reduced the fine to $2,500, joint and several, and eliminated Troszak's requalification requirement.

[34] Although the Commission is not bound by the Guidelines, we use them as a benchmark in conducting our review under Exchange Act Section 19(e)(2). *CMG Institutional Trading, LLC*, Exchange Act. Rel. No. 59325 (Jan. 30, 2009), 95 SEC Docket 13802, 13814 n.38; *see also Perpetual Sec., Inc.*, Exchange Act Rel. No. 56613 (Oct. 4, 2007), 91 SEC Docket 2489, 2506 n.56 (stating that NASD promulgated the Sanction Guidelines in an effort to achieve greater consistency, uniformity, and fairness in its sanctions). The Guidelines suggest that a principal consideration in determining the appropriate sanction should be the "[n]ature and materiality of [the] inaccurate or missing information." NASD Sanction Guidelines at 34 (2001 ed.).

A central purpose of the requirement for maintaining a general ledger and trial balance, as we explained in our 1974 release, is to "enable the broker-dealer to make the computations necessary to ascertain his compliance with the net capital rule and the customers' reserve requirement rule" and in order to facilitate the preparation of financial statements showing the broker's or dealer's financial condition.[35] As we have previously observed, the recordkeeping "rules are not technical but involve fundamental safeguards imposed for the protection of the investing public on those who wish to engage in the securities business."[36] The inadequacy of using these source documents to calculate North Woodward's net capital balance, in the absence of a properly prepared general ledger and trial balance, is illustrated by the inaccuracy of the Firm's net capital computation and by the difficulty the examiners had in verifying the Firm's actual net capital computation.[37]

Applicants argue that NASD staff was able to compute North Woodward's net capital from the documents provided. However, a broker-dealer is required to maintain current books and records in order to "demonstrate compliance to the Commission and the self-regulatory authorities without the burden of bringing books and records up-to-date being placed upon the regulatory authorities."[38] In this way, the requirement aids regulatory authorities in "conduct[ing] effective examinations of broker-dealers."[39] North Woodward's and Troszak's failure to maintain a general ledger and trial balance forced the NASD examiners to expend additional time reviewing the underlying documents in order to perform their verification of the Firm's net capital computation and thus undercut the rule's purpose in facilitating more effective examinations.

We note, in assessing the need for sanctions here, that this is not the first time Applicants have run afoul of regulatory requirements. They previously received an NASD Letter of Caution in connection with an inaccurate general ledger discovered during an earlier NASD examination. They also settled proceedings alleging the operation of their securities business without a FINOP for thirteen months and agreed to pay, as part of that settlement, a $5,000 fine.

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35 4 SEC Docket at 196.

36 *Lowell H. Listrom*, 50 S.E.C. 883, 888 (1992).

37 According to the NASD examiner, the absence of the ledger and trial ledger forced him to make a "best effort attempt . . . to verify the net capital position of the firm" by reviewing the various source documents.

38 4 SEC Docket at 195.

39 *Books and Records Requirements for Brokers and Dealers Under the Securities Exchange Act of 1934*, Exchange Act Rel. No. 44992 (Oct. 26, 2001), 76 SEC Docket 433, 433.

We further note that, in making its own sanction determination, NASD carefully considered certain circumstances that weighed against a significant sanction, including that North Woodward maintained excess net capital for the entire period at issue, that it was a small firm with few customers and limited operations (focused on the sale of mutual funds), and that Troszak was its only operating professional. We find that NASD properly considered the various applicable factors and that the relatively lenient sanction NASD imposed is appropriate in the public interest, remedial and neither excessive nor oppressive. The public interest requires that"appropriate sanctions be imposed to secure compliance with the rules, regulations, and policies of both NASD and SEC."[40] The fine that NASD imposed here protects investors and the public interest by encouraging the Applicants, who remain in the securities business, as well as others in the industry, to take their recordkeeping responsibilities seriously in the future.

An appropriate order will issue.[41]

By the Commission (Commissioners CASEY, WALTER and PAREDES); Chairman SCHAPIRO and Commissioner AGUILAR not participating.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

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[40] *Sisung Sec. Corp.*, Exchange Act Rel. No. 56741 (Nov. 5, 2007), 91 SEC Docket 3050, 3064 (quoting *Boruski v. SEC*, 289 F.2d 738, 740 (2d Cir. 1961)).

[41] We have considered all of the contentions advanced by the parties. We have rejected or sustained these contentions to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 60505 / August 14, 2009

Admin. Proc. File No. 3-13324

In the Matter of the Application of

NORTH WOODWARD FINANCIAL CORP.,

and

DOUGLAS A. TROSZAK
690 East Maple
Birmingham, Michigan 48009-6353

For Review of Disciplinary Action Taken by

FINRA

ORDER SUSTAINING DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES ASSOCIATION

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

ORDERED that the disciplinary action taken by FINRA against North Woodward Financial Corp. and Douglas A. Troszak, and the assessment of costs imposed, be, and they hereby are, sustained.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro and Commissioner Aguilar not participating

SECURITIES AND EXCHANGE COMMISSION
Washington D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 60506 / August 14, 2009

Admin. Proc. File No. 3-13243

In the Matter of the Application of

ANDREW P. GONCHAR
and
POLYVIOS T. POLYVIOU

c/o Martin H. Kaplan, Esq.
Gusrae, Kaplan, Bruno & Nusbaum PLLC
120 Wall Street
New York, New York 10005

For Review of Disciplinary Action by

NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION – REVIEW OF DISCIPLINARY PROCEEDINGS

Violations of Securities Laws and Conduct Rules

Unfair and Fraudulent Markups

Interpositioning

Registered representatives of member firm of registered securities association fraudulently interposed a third party between their member firm and their customers and charged their customers undisclosed and fraudulently excessive markups. *Held*, association's findings of violations and sanctions are *sustained*.

APPEARANCES:

Martin T. Kaplan, *Melvyn J. Falis* and *Brian D. Graifman*, of Gusrae, Kaplan, Bruno & Nusbaum PLLC, for Andrew P. Gonchar and Polyvios T. Polyviou.

Marc Menchel, Alan Lawhead and *Carla Carloni*, for Financial Industry Regulatory Authority, Inc.

Appeal filed: September 26, 2008
Last brief received: June 16, 2009

I.

Andrew P. Gonchar and Polyvios T. Polyviou, formerly general securities representatives associated with CIBC World Markets Corp. ("CIBC"), an NASD member firm, appeal from NASD disciplinary action.[1] NASD found that Applicants, in 142 sales to seventy-one customers over one and one-half years, fraudulently interposed a third party between CIBC and their customers and charged their customers undisclosed and fraudulently excessive markups in violation of Section 10(b) of the Securities Exchange Act of 1934,[2] Rule 10b-5 thereunder,[3] and

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[1] On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD's Restated Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority, Inc., or FINRA, in connection with the consolidation of NASD and the member-regulation, enforcement, and arbitration functions of the New York Stock Exchange. *See* Securities Exchange Act Rel. No. 56146 (July 26, 2007), 91 SEC Docket 517 (Aug. 1, 2007). Because NASD instituted the disciplinary action before that date, it is appropriate to continue to use the designation NASD.

[2] 15 U.S.C. § 78j(b).

[3] 17 C.F.R. § 240.10b-5.

NASD Conduct Rules 2110, 2120, 2320, and 2440.[4] NASD barred Applicants in all capacities and fined each $114,022.[5] We base our findings on an independent review of the record.

II.

Background

This case revolves around convertible bond trades that Applicants made at CIBC between August 2000 and January 2002. Convertible bonds, as with most bonds, provide a fixed return of principal. Unlike straight bonds, however, convertible bonds include a right to exchange the bonds for the common stock of the issuer at a predetermined price. The price of a convertible bond is thus directly related to the price of the underlying stock. The convertible bond price therefore tends to rise as the underlying stock price rises, and fall when the underlying stock price falls.[6]

The majority of Applicants' business at CIBC involved the sale of convertible bonds to retail customers, and the trades at issue here all involved bonds from one of five issuers: Juniper Networks, Inc. ("JNI"), Redback Networks, Inc. ("RNI"), Protein Design Labs, Inc. ("PDLI"),

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4 NASD Conduct Rule 2110 requires members to observe "high standards of commercial honor and just and equitable principles of trade," and a violation of any NASD rule constitutes a violation of Rule 2110. *Stephen H. Gluckman*, 54 S.E.C. 175, 185 (1999). NASD Conduct Rule 2120 prohibits members from effecting transactions, or inducing the purchase or sale of a security, by means of any manipulative, deceptive, or fraudulent device. NASD Conduct Rule 2320 generally prohibits members from interposing a third party between the member and the best available market. NASD Conduct Rule 2440 requires members to buy securities from and sell securities to customers at prices that are fair, taking into consideration all relevant circumstances.

5 NASD also assessed $21,558 in costs, jointly and severally, and $1,412 in appeal costs as to each Applicant.

6 *See United States. v. Regan*, 937 F.2d 823, 829 (2d Cir. 1991) ("[T]he higher the market value of the stock when the convertible bonds are offered for sale the more advantageous from the convertible standpoint the purchase of the bonds will appear to be."); *see also generally* William Bratton Jr., *The Economics and Jurisprudence of Convertible Bonds*, 1984 WIS. L. REV. 667, 673 ("[F]or investors, this [conversion feature] gives convertible bonds the advantage of combining desirable features of straight bonds, such as fixed income payments and principal repayment, with the upside potential of common stock.").

Enzon, Inc. ("EI") and Cell Therapeutics, Inc. ("CTI").[7] The prices of these bonds were not transparent, as none of these convertible bonds were listed on an exchange and transactions involving these bonds were not reported. The prices for these bonds were also very volatile. CIBC did not make a market in these bonds, and, like other participants in the convertible bond market, CIBC's traders used computerized models to determine their prices.

CIBC's Convertible Bond Trading Desk

Because Applicants were not traders, they had to contact CIBC's convertible bond trading desk whenever they wanted to obtain convertible bond prices. Applicants complained about this system, because they felt CIBC's traders were more responsive to CIBC's institutional clients. In an attempt to remedy the situation, CIBC created a retail liaison position in February 2000. Debora Frank, a former CIBC sales assistant, filled the newly created position.

Frank's primary role appears to have been providing Applicants and other retail salespeople with daily bond prices. Frank would first obtain prices from traders on CIBC's convertible bond desk. Frank would then update the prices during the trading day by either contacting a CIBC trader or using a computerized model available at Frank's desk. The computer system's ability to price convertible bonds, however, depended on the stock price that Frank entered into the system. If the price of the underlying stock put into the system was inaccurate, the resulting bond price would also be inaccurate.[8]

In addition to the computerized modeling system, CIBC also had an electronic trading and inventory system into which Frank would enter the name, price, and quantity of the security, the amount of markup or markdown, and the customer account number for each convertible bond trade. She was supposed to input this information at the time of the trade, but, at least with respect to the trades at issue here, did not. Frank instead maintained paper notes and generally

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[7] Applicants joined the securities industry in 1988 and, after moving to several different firms together, joined CIBC as a team in October 1996. Applicants left CIBC in February 2002, and neither is currently working in the securities industry.

[8] In 2004, NASD settled proceedings with Frank, alleging that she engaged in proprietary trades of convertible bonds, in violation of NASD rules, by purchasing bonds for CIBC from so-called "brokers' brokers" without being registered as a Series 55 equity trader. As part of that settlement, Frank consented to a censure and a $10,000 fine. That same year, NASD also settled proceedings with CIBC, alleging that CIBC (i) failed to register Frank as a Series 55 equity trader; (ii) failed to supervise Applicants' and the trading desk's trading of convertible bonds; and (iii) charged retail customers unfair and excessive markups on convertible bond sales as a result of Applicants' trading scheme. CIBC agreed, as part of that settlement, to a censure, a $75,000 fine and the payment of $154,700 in reimbursement, plus $50,600 in interest, to fifty-six retail customers affected by the interpositioning. Before settling with NASD, CIBC also paid $300,000 in partial restitution to the affected customers.

entered information into the electronic inventory system later in the day. Because of Frank's failure to enter information in "real time," it appears that no formal record exists of exactly when during the day Applicants' retail trades occurred.

The parties dispute whether Applicants also used paper tickets to record the time of their trades. Gonchar and Polyviou testified at their disciplinary hearing that, before the terrorist attacks of September 11, 2001, they used an older paper ticket system. Applicants claimed they sent these paper tickets to Frank by runner to enable her to enter the trades into CIBC's electronic system. According to Applicants, however, any paper tickets that Applicants used before September 11 were destroyed in the World Trade Center attacks. Applicants claim they continued to use paper tickets for a time after September 11, but it is unclear what happened to those subsequently created tickets.[9] As discussed below, however, the record does contain other evidence – primarily, transcripts from recorded telephone conversations – from which we can deduce the approximate time of certain trades.

Applicants' Cross Trades

The trades that led to this case involved a similar pattern. In the morning, Applicants would inform Frank that they intended to use a so-called "128 Account" to purchase bonds, but would not identify a purchaser until later in the day.[10] The 128 Account, which was owned by CIBC, was an account that did not maintain inventory, hold positions overnight, or take risk positions. The account's sole purpose was to facilitate order flow between CIBC and its retail customers in "riskless principal" transactions and to capture customers' fees from markups and markdowns.[11] The head of compliance for CIBC's convertible bond trading desk reviewed the

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[9] Polyviou testified that he had some of the relevant tickets in his possession after NASD launched its investigation, but he was unable to recall what had happened to those tickets. While Applicants produced some paper order tickets at the hearing, none was from the trades at issue.

[10] To acquire the bonds for the 128 Account, Frank appears to have either gone through CIBC's trading desk or purchased them herself from a non-CIBC broker. Although CIBC was not a market maker in the bonds at issue, CIBC apparently did hold some bonds in inventory in anticipation of customer demand. Therefore, if CIBC's trading desk had the bonds Frank was seeking in inventory, Frank would obtain the bonds from this inventory. If the bonds were not in inventory, however, CIBC's trading desk would obtain them from the market or, it appears, Frank would obtain the bonds herself from other dealers without going through CIBC's trading desk.

[11] *See P'ship Sec. Exch. Co.*, 51 S.E.C. 1198, 1204 (1994) ("[I]f the dealer is not a market maker, its markups have generally been computed based on the difference between a

(continued...)

128 Account at the end of each day to ensure that the account held no positions overnight, but he did not monitor the account's trading activity during the trading day.

In fact, CIBC's trading desk appeared to play little, if any, role in overseeing Applicants' cross trades. Frank testified at the hearing that, although the trading desk was not involved in setting prices for cross trades, CIBC's traders "instantly saw on their screen" any cross trade that she executed and, "if there had been a problem, they would have said something." The record, however, contains little evidence to corroborate that the trading desk played such an active role in monitoring cross trades.[12] Instead, one CIBC trader testified that, although he thought cross trades showed up on his computer screen and that he may have had to "accept" them, he would not have examined those trades closely enough to ensure that they were being executed at an appropriate price level. Two other CIBC traders testified more flatly that they played no role in approving cross trades between retail customers.

Regardless, once Applicants had identified a retail customer who would buy the bonds, Applicants would inform Frank they intended to execute a cross trade between a trading vehicle called Avalon Asset Management, Inc. ("Avalon") and the retail customer. Avalon was operated by a former colleague of Gonchar and Polyviou at CIBC, Anthony Coscio, and was one of Applicants' most active convertible bond customers. In each of the transactions at issue, Avalon

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[11] (...continued)
dealer's net contemporaneous cost of acquisition and the net amount it receives for a complained-of sales transaction.").

As we have explained,

> a riskless principal transaction is the economic equivalent of an agency trade. Like an agent, a firm engaging in such trades has no market making function, buys only to fill orders already in hand, and immediately 'books' the shares it buys to its customers. Essentially, the firm serves as an intermediary for others who have assumed the market risk. The firm in these circumstances provides no liquidity to the interdealer market.

Kevin B. Waide, 50 S.E.C. 932, 935-36 (1992) (footnotes omitted).

[12] In fact, the Hearing Panel expressly rejected Frank's testimony that traders had to approve her cross trades because, as discussed *infra*, CIBC traders testified that they played no such role. The Hearing Panel also "discount[ed] much of Frank's testimony due to her demeanor during the hearing, which was argumentative and overtly hostile . . . ." The panel noted further that Applicants helped Frank obtain another position after she left CIBC, and Applicants were apparently responsible for more than half her business at firms at which she worked after CIBC. "For all these reasons," the Hearing Panel found "that Frank's testimony was slanted in [Applicants'] favor and not entirely credible."

was the entity that Applicants interposed between CIBC and the retail customers. To execute the cross sale, Applicants would sell the bonds from the 128 Account to Avalon, which would, in turn, sell the bonds back to the 128 Account. On each leg of this round-trip transaction, Avalon would pay either a markup or markdown. Applicants would then sell the bonds out of the 128 Account to the retail customer, who would pay a markup. Applicants did not disclose to their retail customers, however, that these cross trades had occurred (as opposed to obtaining the bonds for the customers directly from the market or selling the bonds from CIBC's inventory) or the price at which Applicants had first acquired the bonds for Avalon. A more detailed look at some of Applicants' cross trades illustrates the pattern.

A. January 7, 2002 Trades

On January 7, 2002, PDLI's stock price opened the day's trading at $31.75 per share. According to transcripts of telephone conversations from that day between Applicants and Frank,[13] Gonchar directed Frank to buy 100 PDLI bonds through the 128 Account approximately forty minutes after trading opened, at 10:11 a.m., by which time the stock price had fallen to $30.50. Frank quoted Gonchar a price level of 107 $^{7}/_{16}$, 108 $^{7}/_{16}$ (traders would sometimes describe this as "a price level of 107 $^{7}/_{16}$, 108 $^{7}/_{16}$ versus 30.50") and, at 10:41 a.m., advised Gonchar that his order for PDLI bonds had been filled at 108 $^{5}/_{8}$ (*i.e.*, $108.625 per bond). Although Gonchar had not yet provided a customer account number for this bond purchase (nor had Frank asked for one), the purchase was later attributed to Avalon.

At 11:22 a.m., Gonchar advised Frank that he wanted to cross-sell the PDLI bonds. Frank asked Gonchar what stock price he wanted to use to calculate the bond price for the trade. Although the price of PDLI's stock had fallen to $29.75, Gonchar responded that a stock price of $31.75 was the "preference point," which was, as indicated above, the price that had occurred nearly two hours earlier, at 9:30 a.m., and, in fact, was the highest stock price PDLI achieved all day. Frank used this high stock price to calculate the bond level as 110, 111 versus $31.75 per share.

At 3:06 p.m., when PDLI's stock price was trading below the price upon which Applicants' purchase price for the bonds was based, Polyviou contacted Frank and gave her the customer account numbers, along with the following prices and markups for the PDLI bond trades:

- Avalon purchased 100 PDLI bonds from the 128 Account at 108 $^{5}/_{8}$ plus a three-point markup (for a total of $111 $^{5}/_{8}$ per bond).

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[13] CIBC recorded Frank's telephone conversations in the normal course of business, but recycled those tapes every fifteen days. As a result, the record contains transcripts of only the following dates: January 4, 7, 8, 14, 15, 16, 17 and 29, 2002.

- Avalon then sold 100 bonds to the 128 Account at $112 per bond (which included a $^3/_8$ of a point markdown).
- Applicants resold the bonds from the 128 Account to two retail customers (50 bonds each) for $112 per bond plus a 3-point markup (for a total of $115 per bond).

Applicants thus charged their retail customers a total purchase price of $115,000 for convertible bonds that Avalon purchased earlier in the day for only $108,625. As a result, the retail customers paid $6,375 more for the bonds than Applicants had paid to acquire the bonds. Of that difference, Avalon earned a net profit of $250 on the transaction, while Applicants earned nearly ten times as much – $2,311.26 – in charges to their customers.

B. January 8, 2002 Trades

A similar transaction occurred the following day. On the morning of January 8, 2002, Gonchar purchased 100 PDLI bonds at $104.75 versus a stock price of $28.628. Then, at 11:27 a.m., Gonchar asked Frank for a price quote versus a stock price of $30.50, which represented a stock price slightly above the highest price PDLI's stock achieved all day. (Moreover, the high price of the day, which was $30.45, occurred almost two hours earlier, at 9:32 a.m.). Frank calculated that a stock price of $30.50 would "equal like 107 ½ 108 ½." Approximately three hours later, at 2:28 p.m., Gonchar asked Frank to cross-sell the PDLI bonds at 109 ½, and, at 3:47 p.m., Polyviou called Frank to provide account numbers and prices for the transactions.

In other words, Applicants cross-sold the bonds at a price $1.00 more per bond than Frank's previous quote (which was based on a price above what the underlying stock had actually achieved) and $4.75 more per bond than Applicants had paid to acquire the bonds for Avalon. On top of this already inflated price, Applicants added an additional 2.7% markup, for a final cost to the customer of $112.50 per bond. The underlying PDLI stock, meanwhile, was headed in the other direction, having fallen below $28.50 per share by the time Gonchar asked to cross-sell the bonds. The retail customers thus paid $7,750 more for the bonds than Applicants had paid to acquire them. Of that amount, Avalon earned $500 in profit, while Applicants earned $2,755 in charges to their customers.

C. January 29, 2002 Trades

Another example of Applicants' cross-selling occurred later that month. On January 29, 2002, PDLI's stock price opened the day's trading at $22.93 per share, which turned out to be the high price of the day. Sometime that morning, Applicants purchased 100 PDLI bonds for $93.50 (which was based on a stock price of $22 ½). Then, at 1:56 p.m., when the underlying PDLI stock had fallen below $22 per share, the following conversation took place:

GONCHAR: How about PDLI? Can I do this cross, or do you want to do it later . . . . I think we got 93 ½ before . . .

FRANK: . . . we did, we bought 100 versus 22 ½ at 93 ½. I'll go back on my bond model. What price should I use here . . .

GONCHAR: 22.93 is the high, so . . .
FRANK: 22.93 would be ah 99, 93 $^{3}/_{8}$, 94 $^{3}/_{8}$.
GONCHAR: So I can use 95 ½, is that cool?

Thus, instead of using the actual stock price (which at the time was less than $22), Gonchar asked for a bond quote using the high stock price of the day ($22.93), which had occurred more than four hours earlier. After receiving a price range of 93 $^{3}/_{8}$, 94 $^{3}/_{8}$, which was based on a no-longer accurate stock price, Gonchar tacked on an additional dollar plus a 2.5 point markup (along with charging Avalon a 0.25 point markdown), for a final price of $98.00. The retail customer thus paid $4.50 (or 4.8%) more per bond than Applicants had paid to acquire the bonds. Avalon made $250 in profit, while Applicants earned seventeen times that much – $4,250 – in charges to their customers.

The above trading pattern was not unique to these three days. The same pattern took place on every day for which there is a recorded conversation between Applicants and Frank. Applicants would tell Frank they wanted to cross-sell the bonds and would ask her for a bond price based on the highest price of the day. By the time Applicants asked to price the bonds, however, that price would no longer be accurate because the market had moved lower. Applicants would also generally add at least one dollar to the price Frank quoted before executing the cross sale, in addition to which Applicants would also charge a markdown to Avalon and a markup to their customers.

D. January 3, 2001 Trades

Although most of Applicants' cross sales followed the pattern described above, a slight variation occurred on sixteen of the seventy-two days at issue. This variation involved Avalon trading the convertible bonds back and forth with itself through the 128 Account before Applicants cross-sold the bonds to their retail customers. In each of these round trip transactions, the bonds Avalon was buying and selling would go into the 128 Account, rather than back to CIBC's general inventory. For example, on January 3, 2001, Avalon made the following purchases and sales of 50 JNI bonds, in each case with the 128 Account:

- Purchased 50 JNI bonds at $89 per bond ($88.125 plus a $0.875 markup);
- Resold the bonds for $89.50 per bond ($92.25 minus a $2.75 markdown);
- Repurchased them at $95 per bond ($92.25 plus a $2.75 markup);
- Resold them for $95.25 per bond ($95.50 minus a $0.25 markdown);

- Repurchased them at $98.25 per bond ($95.50 plus a $2.75 markup);
- Resold them at $98.375 ($98.50 minus a $0.125 markdown);
- Repurchased them at $101.375 per bond ($98.50 plus a $2.875 markup);
- Resold them at $101.50 per bond ($102.50 minus a $1 markdown); and
- Repurchased them at $105.50 per bond ($102.50 plus a $3 markup).

After Avalon bought and sold the same bonds five times, Gonchar and Polyviou finally sold the bonds in a cross trade through the 128 Account to one of Polyviou's clients for $109.25. The total sale price to the retail customer of $5,462.50 represented $1,056.25 (nearly 25%) more than Applicants paid to acquire the bonds earlier in the day.[14] On this series of transactions, Avalon made a net profit of $750, while Applicants earned nearly six times that much – $3,728.78 – in charges to their customers.[15]

All told, Applicants interpositioned Avalon in 142 transactions between August 2000 and January 2002. Of these transactions, Avalon's total profit was approximately $30,000, while Applicants earned more than $228,000 in markups and markdowns charged to their customers. The retail customers, meanwhile, unknowingly paid between 3.5% and 23.97% more for the bonds at issue than what Applicants paid earlier in the day to acquire them for Avalon.

While most of the above examples involve conversations between Gonchar and Frank, Polyviou was also an active and knowing participant in the trading scheme. Telephone transcripts reveal that Polyviou and Gonchar interacted interchangeably with Frank. Polyviou obtained price levels from Frank, directed Frank to execute cross trades, set the price of those cross trades, and provided Frank with account information for both the buy side and sell side of the cross trades. In fact, Frank testified at the hearing that, when Polyviou called to provide markups and account numbers, he did not always have to identify the bond purchased or sold, because both he and Frank were already familiar with all of the trades that Gonchar had executed earlier in the day. Frank also testified that both Gonchar and Polyviou wanted to use the high stock price of the day to calculate bond prices for their trades, and a recorded conversation

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14 To calculate Applicants' cost of acquiring bonds, NASD used the lowest purchase price Avalon paid for a given convertible bond, not including any markup charged. As noted above, Avalon initially paid $88.125 per bond (not including markups) on January 3, 2001 to acquire the JNI bonds. Trading records from the 128 Account, however, suggest that Applicants may have only paid $85.63 per bond to first acquire the bonds for the 128 Account, which suggests that the retail customer on this trade may have paid an even larger 27.5% markup.

15 The record does not appear to contain any evidence, such as transcripts of conversations between Applicants and Frank, reflecting the times at which these trades occurred.

between Frank, Gonchar, and Polyviou indicates that the three discussed using the high stock price of the day as a basis for pricing Applicants' cross trades.

III.

NASD found that Applicants violated NASD rules and the federal securities laws by interpositioning Avalon between CIBC and their customers, charging excessive markups on the sales to Applicants' customers, and failing to disclose either the interpositioning or the excessive markups. Specifically, NASD found that Applicants violated Rule 2420, which requires members to sell securities to customers at a fair price, and NASD Rule 2320, which prohibits member firms and their associated persons from interpositioning a third party between the member and the best available market, except where the member can demonstrate the interpositioning resulted in the customer being charged a price lower than the prevailing market price.[16] NASD further found that Applicants violated Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and NASD Rule 2120, which prohibit the use of any manipulative or fraudulent device in connection with the purchase or sale of a security.[17] NASD finally found that Applicants' violations of the above rules also constituted a violation of NASD Rule 2110, which requires adherence to just and equitable principles of trade.

In their appeal to the Commission, Applicants do not deny that they placed Avalon between their original purchases of the convertible bonds and their sales to their retail customers or that they failed to disclose that fact to their customers. They instead argue that "[i]nterpositioning by itself is not fraudulent" and that NASD failed to establish that the prices at

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[16] As NASD Rule 2320(b) states, "[a] member's obligations to his customer are generally not fulfilled when he channels transactions through another broker/dealer or some person in a similar position, unless he can show that by so doing he reduced the costs of the transactions to the customer."

[17] Rule 10b-5(c), 17 CFR § 240.10b-5(c). One can establish violations of the antifraud provisions by showing that persons acting with scienter misrepresented material facts or engaged in deceit in connection with securities transactions. *Alvin W. Gebhart, Jr.*, Exchange Act Rel. No. 58951 (Nov. 14, 2008), 94 SEC Docket 11637, 11646 (citing *Basic Inc. v. Levinson*, 485 U.S. 224, 239 n.17 (1988) and *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976)).

which they sold the convertible bonds to their customers were excessive.[18] Applicants assert that NASD's decision should therefore be "vacated, remanded and/or modified." We disagree.

We have long held that interpositioning can result in fraud where, as here, it is done with scienter and results in the charging of excessive and undisclosed markups.[19] As the Second Circuit, among others, has stated, broker-dealers possess "an implied duty to disclose excessive markups."[20] Therefore, "[u]ndisclosed markups on sales of securities to retail customers can violate the antifraud provisions of the securities laws if they are not reasonably related to the baseline against which they are measured and if the responsible parties acted with scienter."[21]

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18 In support of their assertion that interpositioning does not amount to fraud, Applicants cite *United States v. Finnerty*, 533 F.3d 143 (2d Cir. 2008), in which the Second Circuit concluded that interpositioning by an NYSE specialist did not constitute securities fraud, because there was "no evidence that Finnerty conveyed an impression that was misleading." *Id.* at 149. In contrast, Applicants here failed to disclose the resulting excessive markups to their customers, and we and the Second Circuit have consistently held that, "[u]nder § 10(b) of the Exchange Act, a seller has a duty to disclose the details of a markup if the markup is 'excessive.'" *Ganino v. Citizens Utils. Co.*, 228 F.3d 154, 163 (2d Cir. 2000) (quoting *Press v. Chem. Inv. Servs. Corp.*, 166 F.3d 529, 534 (2d Cir. 1999)); *see also infra* notes 19 & 20 and accompanying text.

19 *See Donald T. Sheldon*, 51 S.E.C. 59, 78 (1992) (concluding that applicant's interpositioning resulted in fraudulent markups, "demonstrate[d] clear scienter and, in our view, was particularly egregious"), *aff'd*, 45 F.3d 1515 (11th Cir. 1995); *Del. Mgmt. Co.*, 43 S.E.C. 392, 396-98 (1967) (concluding that applicant's interpositioning violated the anti-fraud provisions of Section 10(b) of the Exchange Act).

20 *Starr ex rel. Estate of Sampson v. Georgeson S'holders, Inc.*, 412 F.3d 103, 111 (2d Cir. 2005) (quoting *Grandon v. Merrill Lynch & Co., Inc.*, 147 F.3d 184, 192 (2d Cir. 1998)); *see also SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1469 (2d Cir. 1996) (concluding that a failure to disclose excessive markups violated Rule 10b-5); *Ettinger v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 835 F.2d 1031, 1033 (3d Cir. 1987) ("The SEC has established through its enforcement actions the principle that charging undisclosed excessive commissions constitutes fraud.").

21 *Dennis Todd Lloyd Gordon*, Exchange Act Rel. No. 57655 (April 11, 2008), 93 SEC Docket 5055, 5111; *see also First Jersey*, 101 F.3d at 1469 (holding that "a broker-dealer who charges customers retail prices that include an undisclosed, excessive markup violates § 17(a) and § 10(b) of the securities laws").

We have also long held that a dealer that is not a market maker must base its prices on its own contemporaneous cost.[22] Moreover, where an applicant has interpositioned, "he has the burden of showing that the customer's total cost or proceeds of the transaction is the most favorable obtainable under the circumstances."[23]

Here, NASD used Applicants' contemporaneous cost of acquiring the bonds for the 128 Account as the basis for determining prevailing market price and, on that basis, found that Applicants' charged their customers markups ranging between 3.5% and 23.97%. Applicants do not dispute that NASD's calculations accurately reflect the spread between what the ultimate retail customers paid and what Applicants paid earlier in the day to acquire the bonds. Applicants instead argue that the spread between those two prices was not a "comparison of true contemporaneous price with any price the customer paid." As a result, Applicants contend that NASD failed to make a "showing or finding that the prices at which the customers purchased [the bonds] were unfair at the time purchased." Applicants add that NASD improperly shifted the burden of proof onto Applicants to show that the prices they charged were fair. We disagree and find NASD's methodology appropriate to the circumstances.

As noted above, firms that do not make a market in a security (such as CIBC with respect to the bonds at issue here) must calculate their markups based on the firm's contemporaneous cost of acquiring the security.[24] Therefore, once NASD presents evidence of contemporaneous cost, the burden shifts to Applicants to refute that evidence.[25] This is true even in cases involving

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22 *See Daniel R. Lehl*, 51 S.E.C. 1156, 1159 (1994) (holding that a firm that is not a market maker must base its prices on its own contemporaneous cost), *aff'd*, 90 F.3d 1483 (10th Cir. 1996); *see also F.B. Horner & Assocs., Inc. v. SEC*, 994 F.2d 61, 63 (2d Cir. 1993) (affirming contemporaneous cost of acquiring the bonds as an appropriate gauge of the market price for purposes of determining markups); *David Disner*, 52 S.E.C.1217, 1220 (1997) (using contemporaneous cost to conclude that applicant had charge fraudulently excessive markups) (citing *Alstead, Dempsey & Co.*, 47 S.E.C. 1034, 1035 (1984)); *George Salloum*, 52 S.E.C. 208, 215 (1995) (using contemporaneous cost to conclude that applicant had charged customers fraudulently excessive markups).

23 *Thomson & McKinnon*, 43 S.E.C. 785, 789 (1968) (concluding broker-dealers' interpositioning "constituted a fraud upon their customers" in violation of the antifraud provisions of the Exchange Act); *see also Milton M. Star*, 47 S.E.C. 58, 59 (1979) ("[W]here interpositioning has occurred, the burden is on the member to demonstrate that his action resulted in the customer being charged a lower price than that prevailing in the inter-dealer market.").

24 *See supra* note 22 and accompanying text.

25 *See Mark David Anderson*, 56 S.E.C. 840, 855 n.41 (2003) (noting that the applicant "had the burden of producing evidence to support his claim that his pricing was not

(continued...)

allegations of fraud.[26] Notably, however, the ultimate burden of proof for the violations does not, as Applicants assert, shift onto Applicants. NASD still retains the ultimate burden of persuasion.[27]

NASD's determination that Applicants' charged excessive markups is consistent with this precedent. While NASD has typically used a firm's contemporaneous cost as the basis for calculating markups, NASD here looked to Applicants' contemporaneous cost of acquiring the bonds into the 128 Account. Given the way Applicants used the 128 Account as an internal trading account for their transactions, we see no basis for rejecting that approach here.[28]

In those instances where Frank or the Firm's traders had to obtain bonds from the market because CIBC did not hold them in inventory, the 128 Accounts' costs were presumably the same as the Firm's costs. Furthermore, we have previously concluded that retail trades are an appropriate means for determining the prevailing market price, which is the approach NASD used here when looking to the cost Avalon paid to acquire the bonds from the 128 Account (not

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25 (...continued)
excessive"); *Steven P. Sanders*, 53 S.E.C. 889, 895 (1998) ("Once the NASD presented evidence that the Firm's markups exceeded 5% over its contemporaneous cost, the burden properly shifted to the applicants to show that the facts surrounding these transactions justified higher markups."); *First Honolulu Sec., Inc.*, 51 S.E.C. 695, 701 n.23 (1993) ("Once the NASD presented evidence of the markups, the burden shifted to Applicants to refute this evidence"); *Richard R. Perkins*, 51 S.E.C. 380, 383 n.16 (1993) ("Once the NASD presented its *prima facie* case, it was incumbent on Applicants to explain why, notwithstanding the evidence to the contrary, their pricing was fair.").

26 *See Anderson*, 56 S.E.C. at 855 n.41 (noting that respondent has the burden of refuting evidence of markups presented by the Division of Enforcement even where the respondent is charged with "federal securities fraud" (citing *Sheldon*, 51 S.E.C. at 77 (noting that burden shifted to respondent to refute evidence of markups in case involving allegations of fraud))).

27 *Id.* (stating that, even after burden to refute Division of Enforcement's evidence of excessive markups shifts to respondent, "the ultimate burden of persuasion remains with the Division").

28 *Cf. Bison Sec., Inc.*, 51 S.E.C. 327, 329, 333 (1993) (deeming retail account controlled by firm's holding company as *de facto* trading account and using its costs in determining fairness of markups).

including any markup that Avalon paid) to determine Applicants' contemporaneous cost.[29] Applicants assert that their trades with Avalon were legitimate, arm's-length transactions. Thus, those trades should provide a good indication of the prevailing market price at the time the transactions took place.

Perhaps the key fact, however, is that Applicants were aware of the prices Avalon paid to acquire the bonds, which Applicants failed to consider when later determining the retail prices at which they would sell the bonds to their retail customers. Applicants instead based the prices of the retail sales, in at least those instances where we have telephone transcripts, on the no-longer-accurate high stock price of the day and did so through entirely unnecessary cross sales between the 128 Account and Avalon, charging markups and markdowns on each leg of the transaction. We conclude, given these circumstances, that it was appropriate for NASD to limit Applicants' markups to a reasonable amount above Avalon's initial cost to acquire them.[30]

Moreover, Applicants still had the opportunity to show that their contemporaneous cost of acquiring the bonds did not accurately represent the prevailing market price at the time of the ultimate sale to the retail customers. Applicants, for example, could have provided countervailing evidence that showed a change in the market between when Applicants acquired the bonds and when they later sold the bonds to their customers (such as evidence of market trades occurring at the time of the ultimate retail trade). Applicants, however, wholly failed to do this. They instead offer a variety of reasons why they were unable to produce such evidence.[31] For example, Applicants argue that the September 11 terrorist attacks destroyed the paper tickets that allegedly would have established the time of Applicants' cross trades. Those tickets, in turn, allegedly would have established the prevailing market price at the time Applicants cross-sold the bonds at issue. That assertion, however, is undercut by the telephone conversations between Applicants and Frank indicating when several of Applicants' cross sales took place. Transcripts

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[29] *See G.K. Scott*, 51 S.E.C. at 965 (using applicant's purchases from retail customers to determine the prevailing market price for purposes of calculating markups).

[30] *Cf. Waide*, 50 S.E.C. at 936 (noting that the inquiry into whether prices are fair goes "beyond whether a broker-dealer charged prices that were reasonably related to the market price," that using a firm's contemporaneous cost to calculate markups appropriately addresses the other inquiry of "whether a firm employed a price-setting *process* that treated customers fairly," and that where "the firm serves as an intermediary for others who have assumed the market risk. . . . a firm is adequately compensated by a markup over its cost").

[31] In fact, on appeal, Applicants point to no evidence that conflicts with NASD's calculations. Applicants suggest that their pricing was fair by asserting that CIBC's trading desk would not have approved Applicants' trades if they could have been done at a more favorable price for the customer. This assertion, however, is undercut by testimony that CICB's traders played virtually no role in overseeing Applicants' cross trades. *See infra* note 35 and accompanying text.

of those conversation show that, instead of accurately pricing those sales, Applicants were basing the bond prices on the high stock price of the day, regardless of when that price occurred, underscoring the conclusion that Applicants' bond prices did not reflect the prevailing market.[32]

Applicants' contemporaneous cost therefore remains the best – and essentially only – evidence of the prevailing market price. This evidence shows that Applicants' markups ranged between 3.5% and 23.97%, with the majority of Applicants' markups at issue exceeding 5% – an amount we have consistently held, with respect to the sale of bonds, as "acceptable in only the most exceptional cases."[33] Applicants do not challenge that such markups are excessive nor do Applicants identify any special circumstances or otherwise try to justify the size of these markups.[34]

Applicants suggest only that, regardless of their actions, the prices they charged must have been consistent with the prevailing market prices because CIBC's trading desk would not have permitted such trades to be executed if Applicants could have done them at a more favorable price for the customer. As noted previously, however, testimony from CIBC's bond traders contradicts Applicants' assertion that CIBC was monitoring their trades, let alone that

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[32] Applicants similarly contend that NASD's refusal to allow them to subpoena certain witnesses prevented them from introducing certain exculpatory evidence. As discussed in the following section, however, none of that potential testimony would provide Applicants with evidence that they were pricing their cross sales fairly.

[33] *Inv. Planning, Inc.*, 51 S.E.C. 592, 594 (1993) (finding markups ranging from 4% to 7.26% on the sale of corporate bonds to be improper and noting "it has long been recognized that debt securities markups normally are lower than those for equities, and that, in appropriate circumstances, markups under [five percent] may be subject to sanction").

In fact, NASD's method of calculating markups may have underestimated some markups. In the example from January 29, 2002, the contemporaneous bond price NASD used for its calculations was $93.50, which was based on a stock price of $22.50. However, a transcript of Gonchar's telephone conversation with Frank reveals the exact time when Gonchar asked to price the cross sale. At that time, the underlying PDLI stock was trading at less than $22.00. This suggests that the fair market value of the bond was not only less than the price at which Applicants cross-sold the bonds ($98.00), but also less than the contemporaneous cost that NASD used to calculate the effective markup ($93.50).

[34] *See generally Press*, 166 F.3d at 535 (enumerating factors for determining excessiveness).

CIBC was ensuring Applicants were executing their cross trades at fair prices.[35] In fact, the above-mentioned transcripts indicate that Applicants made no effort to ensure that their customers were receiving the then-fair market price of the securities. Instead, Applicants' interpositioning essentially guaranteed that Applicants (and Avalon) would be buying low and selling high, as demonstrated by Avalon profiting on sixty-nine of the seventy-two days at issue, suffering a net loss of $125, on just one trade.

Moreover, the opaque and volatile nature of the convertible bond prices meant that Applicants' retail customers had no ready way to verify whether the price they were paying was fair. As a result, their customers were almost entirely reliant on Applicants to obtain a fair price. Instead of assisting their clients, however, Applicants exacerbated the lack of transparency by not disclosing to their customers that the bonds were coming from Avalon in a cross trade or that their clients were paying more than Avalon had paid earlier in the day.

As we have stated, "[p]ersons engaged in the securities business cannot be unaware of their obligation to serve the best interests of their customers, and that interpositioning is bound to result in increased prices or costs."[36] Here, instead of serving their customers' interests, Applicants showed a "reckless disregard for determining the actual prevailing market price," and, by using the highest stock price of the day to price the bonds and then adding a commission on top of that inflated price, Applicants displayed "not merely an insensitivity to the obligation of fair pricing, but an intent by Applicants to gouge their customers."[37]

We thus conclude that Applicants violated Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and NASD Conduct Rule 2120. By charging excessively high markups, Applicants also violated NASD Conduct Rule 2440, and, by interpositioning a third party between CIBC and their customers without demonstrating a benefit to those customers,

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35 An applicant also "cannot shift his responsibility to comply with NASD rules to his firm," and efforts to do so raises questions about the applicant's fitness to remain in the securities industry. *Jason A. Craig*, Exchange Act Rel. No. 59137 (Dec. 22, 2008), 94 SEC Docket 12694, 12700 (noting that an applicant cannot shift responsibility to his firm for complying with NASD rules); *see also Steven M. Muth*, Exchange Act Rel. No. 8622 (Oct. 5, 2005), 86 SEC Docket 1217, 1247 (concluding that applicant's attempt to shift responsibility to his supervisors for failing to object to certain of his transactions was a factor establishing that applicant "pose[d] a substantial, continuing risk of harm to investors").

36 *Del. Mgmt. Co.*, 43 S.E.C. at 400 (finding that applicant's interpositioning violated the antifraud provisions of the securities laws).

37 *Bison Sec.*, 51 S.E.C. at 332 ("Scienter is clearly evident here, as demonstrated by Applicants' reckless disregard for determining the actual prevailing market price.").

Applicants violated NASD Rule 2320.[38] Finally, Applicants' violation of the above rules constitutes a violation of NASD Rule 2110.[39]

IV.

Applicants contend that NASD's findings are flawed because of certain procedural defects related to (i) Applicants' efforts to use state law procedures to subpoena witnesses and (ii) the standard of proof NASD applied to the evidence. We discuss each in turn.

Subpoenas

Applicants' first procedural argument relates to their unsuccessful effort to subpoena certain witness not subject to NASD's jurisdiction, including Anthony Coscio, Avalon's owner, and Vincent Rusciano, a runner who Applicants claimed had delivered their handwritten trade tickets to Frank. The NASD Hearing Officer quashed Applicants' attempt to issue these

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[38] *See supra* note 23 and accompanying text. We also note that, on April 17, 2009, we solicited comments on a FINRA proposal to amend NASD Conduct Rule 2320 (the "Proposed Rule Change"), which would "replace the current [Rule 2320(b) (the "Interpositioning Rule")] with a more general statement that the factors enumerated in Rule 2320(a) apply to those situations contemplated by the Interpositioning Rule." Exchange Act Rel. No. 59788 (Apr. 17, 2009), 95 SEC Docket ____. The Proposed Rule Change would therefore require a broker-dealer to "use reasonable diligence to ascertain the best market for the subject security," as outlined in the present NASD Rule 2320(a), which lists the factors to be considered in determining "reasonable diligence" as "(1) the character of the market for the security, *e.g.*, price, volatility, relative liquidity, and pressure on available communications; (2) the size and type of transaction; (3) the number of markets checked; (4) accessability of the quotation; and (5) the terms and conditions of the order which result in the transaction, as communicated to the member and persons associated with the member." We asked the parties to provide supplemental briefing regarding the question of whether the Proposed Rule Change has any impact on the merits of this proceeding.

After considering the parties' supplemental briefs, we conclude that the Proposed Rule Change has no impact on the merits of this proceeding. Because the Proposed Rule Change has not taken effect as of the date of this opinion, we see no basis for applying it here. Moreover, even if the Proposed Rule Change were to take effect, Applicants, as discussed herein, failed to "use reasonable diligence" in determining the best market for the subject bonds by purposefully using their interpositioning scheme and artificially high bond quotations to charge retail customers excessively high markups.

[39] *Gluckman*, 54 S.E.C. at 185 (noting "our long-standing and judicially-recognized policy that a violation of another Commission or NASD rule or regulation . . . constitutes a violation of [NASD] Rule 2110").

subpoenas prior to the NASD disciplinary hearing, and Applicants now argue that this prevented them from bringing crucial evidence before the NASD Hearing Panel.

Because NASD rules do not provide for the use of subpoenas, Applicants relied on § 2302(a) of New York's Civil Practice Law and Rules ("C.P.L.R."), which allows subpoenas "to be issued without a court order by . . . an attorney of record for a party to . . . an administrative proceeding or an arbitration . . . in relation to which proof may be taken or the attendance of a person as a witness may be required."[40] In quashing Applicants' subpoenas, the Hearing Officer concluded that C.P.L.R. § 2302(a) did not apply because Applicants' disciplinary hearing was not an "administrative proceeding" for purposes of the New York rule. Applicants subsequently sought to enforce the subpoenas in state court, but the New York court agreed with the Hearing Officer's conclusion that C.P.L.R. § 2302 did not apply to NASD disciplinary proceedings.[41] This conclusion is consistent with prior New York precedent, which similarly held that NASD disciplinary proceedings are not administrative proceedings within the meaning of C.P.L.R. § 2302 and thus not subject to the New York rule.[42]

Under the law-of-the-case doctrine, "courts are understandably reluctant to reopen a ruling once made, especially when one judge or court is asked to consider the ruling of a different judge or court."[43] Applicants nevertheless ask us to discount the two above-mentioned New York decisions and instead rely on two other decisions: *Crimmins v. American Stock Exchange,*

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[40] N.Y. C.P.L.R. § 2302 (McKinney 2005).

[41] *Gonchar v. NASD*, Index No. 101445-2006, slip op. at 7 (N.Y. Sup. Ct. Feb. 7, 2006) ("Contrary to petitioners' contention, CPLR 2302 does not apply to the Disciplinary Proceeding herein brought by the NASD." (citation omitted)), *dismissed as moot*, 829 N.Y.S. 2d 900 (N.Y. App. Div. Feb. 27, 2007). Applicants characterize the New York court's holding regarding C.P.L.R. § 2302 as dictum because the court first held that it lacked jurisdiction to entertain Applicants' claims. Although the New York court did conclude that Applicants had "failed to exhaust the administrative remedies available under NASD rules," the court also went on to hold that, "[i]n any event, the Court rejects petitioners' alleged right to issue a subpoena in the Disciplinary Proceeding pursuant to CPLR § 2302(a)." *Id.* As the Supreme Court has stated, "where a decision rests on two or more grounds, none can be relegated to the category of obiter dictum." *Woods v. Interstate Realty Co.*, 337 U.S. 535, 537 (1949).

[42] *Application of NASD Regulation, Inc., Dep't of Enforcement v. Rosato*, Index No. 119971-1998, at 2 (N.Y. Sup. Ct. Nov. 5, 1998) (stating that an "NASD Regulation, Inc. hearing is not an administrative proceeding under [C.P.L.R. §]2302(a)").

[43] *Ali v. Mukasey*, 529 F.3d 478, 490 (2d Cir. 2008) (quoting *Lillbask ex rel. Mauclaire v. Conn. Dept. of Educ.*, 397 F.3d 77, 94 (2d Cir. 2005) (citation and internal quotation marks omitted)).

Inc.[44] and *Hessel v. Merrill Lynch, Pierce Fenner & Smith.*[45] Neither *Crimmins* nor *Hessel*, however, is on point. While both *Crimmins* and *Hessel* theorized that C.P.L.R. § 2302 may empower parties to subpoena witnesses in administrative proceedings, neither case involved NASD or its rules.[46] Moreover, neither case actually allowed the parties seeking the subpoenas to obtain them, and neither case addressed the question of enforcing subpoenas under C.P.L.R. § 2302 directly, instead addressing the New York statute only in dicta.[47]

Regardless, we need not decide whether a party is entitled to pursue subpoenas in NASD disciplinary proceedings.[48] As the *Crimmins* decision suggested, an applicant's inability to subpoena witnesses is not grounds for overturning a disciplinary action unless the applicant can show prejudice.[49] This is consistent with a myriad of other courts that have held that a party has

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[44] 368 F. Supp. 270, 277 (S.D.N.Y. 1973).

[45] Index No. 106285-2000 (N.Y. Sup. Ct. Aug. 9, 2000).

[46] *Crimmins*, 368 F. Supp. at 274 (involving disciplinary action by the American Stock Exchange ("AMEX")); *Hessel*, Index No. 106285-2000 (involving disciplinary action brought by the New York Stock Exchange).

[47] *Crimmins*, 368 F. Supp. at 277 (noting that C.P.L.R. § 2302 "seemed" to empower both administrative panels and attorneys of record with the ability to issue subpoenas without a court order, but concluding that applicant was not prejudiced by AMEX's refusal to subpoena certain witnesses); *Hessel*, Index No. 106285-2000, at 27 (concluding that applicant had waived his right to pursue a subpoena in state court, but stating that it "believe[d]" that C.P.L.R. § 2302 may have allowed applicant to pursue the subpoena in state court had he not waived that right).

[48] We also need not address NASD's contention that FINRA rules preempt C.P.L.R. § 2302.

[49] *See Crimmins*, 368 F. Supp. at 277 (rejecting plaintiff's attempt to vacate disciplinary action on grounds that plaintiff was not prejudiced by lack of subpoenas); *see also Thomas E. Warren, III*, 51 S.E.C. 1015, 1020 n.22 (1994) (dismissing allegation that applicant was disadvantages by inability to subpoena witnesses), *aff'd*, 69 F.3d 549 (10th Cir. 1995); *Gateway Stock & Bond, Inc.*, 43 S.E.C. 191, 195 (1966) (refusing to disturb NASD disciplinary sanctions where lack of subpoena did not cause prejudice).

no absolute right to subpoena witnesses in administrative hearings.[50] As one court relevantly explained,

> it makes perfect sense . . . to control the issuance of subpoenas . . . . For if it were otherwise, one can easily imagine the process becoming cumbersome and potentially unmanageable. For example, if the [applicants] were to have their own, absolute or independent subpoena power, they effectively could stop, or at the very least delay significantly, the entire . . . process by issuing subpoenas to potentially hundreds of individuals.[51]

Here, Applicants cannot point to any excluded testimony that would have been material. For example, Applicants contend Coscio was "the one witness who could have explained the rationale for his transactions underlying this matter," thus bolstering Applicants' argument that "they legitimately carried out Avalon's upright trading intentions." Avalon's trading intentions, however, are not the issue here. The issue is whether Applicants were interpositioning Avalon between their customers and the market – an issue Applicants do not dispute – and whether that interpositioning, along with the prices Applicants charged to their customers, constituted fraud. Avalon's reasons for trading bonds would not address these questions.[52]

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[50] *See, e.g., Foxy Lady, Inc. v. City of Atlanta, Ga.*, 347 F.3d 1232, 1237 (11th Cir. 2003) ("[N]o absolute or independent right to subpoena witnesses exists during administrative proceedings, and [we] now hold expressly that procedural due process also does not require an absolute or independent right to subpoena witnesses in administrative hearings."); *Travers v. Jones*, 323 F.3d 1294, 1297 (11th Cir. 2003) ("[A] party has no right to subpoena witnesses to state administrative hearings." (citations omitted)); *Amundsen v. Chicago Park Dist.*, 218 F.3d 712, 717 (7th Cir. 2000) ("Nonetheless, this court has held that in the administrative hearing context, the ability to subpoena witnesses is not an absolute right. . . . Indeed, in administrative matters, due process is satisfied when the party concerned is provided an opportunity to be heard in an orderly proceeding which is adapted to the nature and circumstances of the dispute." (quotation marks and citations omitted)).

[51] *Foxy Lady*, 347 F.3d at 1238.

[52] In fact, Avalon may well have had a legitimate reason for its pattern of buying and selling convertible bonds given Avalon's record of profiting on 69 out of the 72 trading days at issue and suffering a net loss only once. Regardless, Avalon's trading strategy – whatever it was – would provide no justification for Applicants' interpositioning scheme at issue here. At most, Coscio's testimony could have explained why Avalon occasionally bought and sold bonds with itself before Applicants' cross-sold the bonds to retail customers – a trading pattern that the NAC noted neither respondent was able to explain. Avalon's trades with itself, however, are not relevant with respect to Applicants' fraudulent conduct toward their customers.

Rusciano's testimony would have been similarly unhelpful. According to Applicants, Rusciano would have testified "that [Applicants] prepared time-stamped order tickets which reflected the exact time of each trade." Applicants contend that such testimony would have shown that NASD's method of calculating Applicants' markups was flawed. Because, by "[n]ot having the exact timing of the trades at issue, the [Hearing] Panel fell back on concluding that 'a dealer's 'contemporaneous cost' is the best evidence of the current market,' rather than the value of the convertible bonds on a myriad of factors including the then-current price of the underlying stock."

Contemporaneous costs, as discussed above, is not a "fall back" position. Rather, it is the primary method of calculating markups where a firm does not make a market in a security (such as CIBC with respect to the bonds at issue).[53] Applicants may challenge the resulting markups by introducing countervailing evidence, but they bear the burden of doing so.[54] Here, Rusciano's potential testimony would not have undermined the validity of NASD's calculations. Rusciano, at most, may have testified that time-stamped tickets existed, but there is no suggestion he would have produced the actual tickets. Moreover, the record does contain evidence of when several of Applicants' cross trades likely occurred (namely, from the transcripts of Applicants' conversations with Frank). As explained earlier, that evidence directly undercuts Applicants' assertion that they were pricing the bonds consistently with the then-current market price.

Standard of Proof

Applicants next contend NASD incorrectly applied the "preponderance of the evidence" standard of proof in reaching its decision, rather than the more demanding "clear and convincing" standard. Applicants argue that, because the evidence against them is only circumstantial and because their livelihood is at stake, the "clear and convincing" standard should apply. We have consistently rejected this argument when raised by other parties. For example, in *Sandra K. Simpson*, the respondent appealed an administrative law judge's use of the preponderance of the evidence standard in barring the applicant from the securities industry.[55] The *Simpson* applicant argued that, "because a decision against [her] would in all likelihood deprive her of her ability to make a living in the securities industry, a higher standard of proof should apply."[56] In rejecting this argument, we explained:

> To mandate that any misconduct for which the Division seeks a permanent bar must be proved by clear and convincing evidence would compromise the

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53 *See supra* note 22 and accompanying text.

54 *See supra* note 23 and accompanying text.

55 55 S.E.C. 766, 798 (2002).

56 *Id.* at 798.

> Commission's ability to protect public investors by, among other things, putting those respondents whose misconduct has been proven by a simple preponderance of the evidence beyond the reach of a permanent bar, however egregious the misconduct. This result would be inconsistent with our duty to protect the public.[57]

Despite our prior decisions, Applicants nevertheless argue that the "clear and convincing" standard should apply by pointing to *Collins Securities Corp. v. SEC*, in which the United States Court of Appeals for the District of Columbia held that the "clear and convincing" standard should govern cases involving a deprivation of livelihood.[58] As Applicants concede, however, the Supreme Court overruled *Collins* in *Steadman v. SEC*,[59] in which the Supreme Court rejected a petitioner's argument that the "clear and convincing" standard should apply "because of the potentially severe sanctions that the Commission was empowered to impose and because of the circumstantial and inferential nature of the evidence that might be used to prove intent to defraud, the Commission was required to weigh the evidence against a clear-and-convincing standard of proof."[60]

Applicants seek to get around *Steadman* by pointing to a district court decision from the Southern District of New York, *SEC v. Moran*.[61] Applicants quote *Moran*, which was decided after *Steadman*, for the proposition that "*Collins* remain[s] compelling post-*Steadman* because a member of the securities industry who is found liable of violations of § 10b or Rule 10b-5 will effectively be deprived of his livelihood."[62] In that quotation, however, the *Moran* court was not stating its own opinion, but rather reciting the *defendants'* position, which the court rejected as

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[57] *Id.* at 799. Although *Simpson* involved a bar imposed by the Commission, we have consistently applied the same preponderance of the evidence standard to bars imposed under NASD rules. *See, e.g.*, *John D. Audifferen*, Exchange Act Rel. No. 58230 (July 25, 2008), 93 SEC Docket 8129, 8134 n.9 (applying preponderance of the evidence standard when reviewing FINRA's decision to bar applicant in all capacities); *Kirk A. Knapp*, 51 S.E.C. 115, 116, 130 n.65 (1992) (stating that "[t]he correct standard is preponderance of the evidence" where NASD "barred [applicant] from association with any member in any capacity").

[58] 562 F.2d 820, 824 (D.C. Cir. 1977).

[59] 450 U.S. 91 (1981) (involving permanent bar against the petitioner for violating the antifraud provisions of the securities laws).

[60] *Id.* at 95 (overruling *Collins* and concluding that the proper standard of proof was preponderance of the evidence).

[61] 922 F. Supp. 867 (S.D.N.Y. 1996).

[62] Quoting *Moran*, 922 F. Supp. at 889.

inapplicable to the case before it.[63] Moreover, and contrary to Applicants' reading of the case, the court expressly rejected any contention that circumstantial evidence requires a "clear and convincing" standard, stating that "the fact that this is an action based on circumstantial evidence does not in any way necessitate a higher standard of proof [than preponderance of the evidence]."[64] Finally, because NASD introduced transcripts of Applicants' telephone conversations with Frank, NASD's case against Applicants was based on more than just circumstantial evidence.

For these reasons, we see no basis to reverse well-established precedent, regardless of whether both a deprivation of livelihood and circumstantial evidence are involved. We thus conclude that NASD correctly applied a preponderance of the evidence standard.

V.

Exchange Act Section 19(e)(2) directs us to sustain NASD's sanctions unless we find, having due regard for the public interest and the protection of investors, that the sanctions are excessive, oppressive, or impose an unnecessary or inappropriate burden on competition.[65] Here, Applicants contend NASD's sanctions were excessive because NASD failed to establish whether the alleged misconduct resulted in injury to others and, if so, "the nature and extent of that injury."[66] In making this argument, Applicants recycle their contention that, because the exact times of the trades are unknown, one cannot establish that the trades were unfairly priced. As we discussed above, however, NASD appropriately used Applicants' contemporaneous cost to establish that Applicants priced their trades unfairly. It was Applicants' burden to come forward with alternative evidence, and they failed to do so.

Applicants similarly argue that NASD failed to introduce any evidence "as to the ultimate impact to the customers on the liquidation of any of the transactions," which Applicants argue "could have been negligible in light of the ultimate price obtained by the customer." NASD did, however, establish that Applicants' interpositioning scheme deprived the customers of the best available market prices. Moreover, even assuming, *arguendo*, that some of Applicants'

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63 *Moran*, 922 F. Supp. at 889 (concluding that the penalties at issue would not, in fact, deprive defendants of their livelihood).

64 *Id.* at 890; *see also SEC v. Credit Bancorp, Ltd.*, 195 F. Supp. 2d 475, 491 (S.D.N.Y. 2002) ("[A]n action based upon circumstantial evidence is not any less sufficient than one based on direct evidence, and does not necessitate a higher standard of proof." (citations omitted)).

65 15 U.S.C. § 78s(e)(2). Applicants do not allege, and the record does not show, that NASD's sanctions imposed an undue burden on competition.

66 NASD Sanction Guidelines 6 ("Sanction Guidelines").

customers may have suffered only negligible losses when they ultimately sold their bonds,[67] that would not weigh in favor of reducing the sanctions.[68]

We also give no weight to Applicants' argument that the 142 trades at issue were out of 10,000-15,000 transactions Applicants executed while at CIBC. Because Applicants were registered with NASD, they were expected to follow its rules. That Applicants may have complied with those rules when executing other trades is not a mitigating factor.[69]

Applicants finally contend that Polyviou should not face the same sanctions as Gonchar, because, they assert, Polyviou performed principally administrative functions and is therefore not as culpable. We disagree. As noted earlier, Polyviou was more than a passive participant in Applicants' cross trading scheme. Among other things, he and Gonchar interacted with Frank interchangeably, he and Gonchar shared the commissions from the fraudulent cross trades equally, and many of the victims were Polyviou's customers. We thus see no basis for holding Polyviou less culpable than Gonchar.

We agree with NASD's characterization of Applicants' misconduct as egregious and, therefore, find the sanctions neither excessive nor oppressive. As we have stated, "[t]he charging of excessive markups [i]s a serious breach of [an applicant's] obligation to deal fairly with its customers."[70] Applicants' interpositioning of a favored account between the market and their retail customers, which resulted in excessive markups, showed a complete disregard for this obligation.[71] As such, Applicants' actions pose too great a risk to the markets and investors to

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67 The record does not contain evidence regarding this question. We note, however, that CIBC paid $300,000 in partial restitution. *See supra* note 8.

68 *Coastal Fin., Inc.*, 54 S.E.C. 388, 396 (1999) (affirming bar despite NASD presenting no evidence of customer harm); *cf. Chris Dinh Hartley*, 57 S.E.C. 767, 775 (2004) (concluding that applicant was not entitled to a reduction in his sanctions, which included a suspension, simply "because his clients may be able to recover some of their losses").

69 *Michael F. Siegel*, Exchange Act Rel. No. 58737 (Oct. 6, 2008), 94 SEC Docket 10501, 10519 ("[W]hen [applicant] registered with NASD, he agreed to abide by its rules, and compliance with this obligation is not a mitigating factor.").

70 *Nicholas A. Codispoti*, 48 S.E.C. 842, 845 (1987).

71 *See Sheldon*, 51 S.E.C. at 78 (finding applicant's conduct to be "particularly egregious" where "interpositioning of favored accounts between the dealer market and non-favored accounts resulted in fraudulent, effective markups of as much as 10 percent" and sustaining imposition of a bar); *see also Frank L. Palumbo*, 52 S.E.C. 467, 480 (1995) (stating that recklessly overcharging customers without justification demonstrates "a marked insensitivity

(continued...)

allow Applicants to remain in the securities industry. The sanctions are also consistent with NASD's Sanction Guidelines, which recommend fines of up to $100,000 plus the gross amount of any markups, along with a bar in egregious cases.[72] In addition, the sanctions will "have the salutary effect of deterring others from engaging in the same serious misconduct."[73]

For these reasons, we sustain NASD's findings of violation and imposition of sanctions. An appropriate order will issue.[74]

By the Commission (Commissioners CASEY, PAREDES, and WALTER); Chairman SHAPIRO and Commissioner AGUILAR not participating.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

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[71] (...continued)
to [the] obligation to deal fairly with customers"). As discussed above, however, we believe Applicants' actions went beyond recklessness and were done with an intent to defraud.

[72] Sanction Guidelines at 95. Although the Commission is not bound by the Sanction Guidelines, it uses them as a benchmark in conducting its review under Exchange Act Section 19(e)(2). *Wanda P. Sears*, Exchange Act Rel. No. 58075 (July 1, 2008), 93 SEC Docket 7395, 7403.

[73] *Gordon*, 93 SEC Docket at 5113 & n.75 ("[W]e are mindful that although 'general deterrence is not, by itself, sufficient justification for expulsion or suspension . . . it may be considered as part of the overall remedial inquiry.'" (quoting *PAZ Sec., Inc.*, 494 F.3d 1059, 1066 (D.C. Cir. 2007))); *see also Boruski v. SEC*, 289 F.2d 738, 740 (2d Cir. 1961) ("The public interest requires that appropriate sanctions be imposed to secure compliance with the rules, regulations and policies of both NASD and SEC . . . .").

[74] 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. 60506 / August 14, 2009

Admin. Proc. File No. 3-13243

In the Matter of the Application of

ANDREW P. GONCHAR
and
POLYVIOS T. POLYVIOU

c/o Martin H. Kaplan, Esq.
Gusrae, Kaplan, Bruno & Nusbaum PLLC
120 Wall Street
New York, New York 10005

For Review of Disciplinary Action by
NASD

ORDER SUSTAINING DISCIPLINARY ACTION

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

ORDERED that the disciplinary action taken by NASD against Andrew P. Gonchar and Polyvios T. Polyviou, and NASD's imposition of costs, be, and they hereby are, sustained.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

SECURITIES AND EXCHANGE COMMISSION

17 CFR PART 242

[Release No. 34-60509; File No. S7-08-09]

RIN 3235-AK35

Amendments to Regulation SHO

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; notice of re-opening of comment period and supplemental request for comment.

SUMMARY: The Securities and Exchange Commission is re-opening the comment period to the "Amendments to Regulation SHO" it proposed in Securities Exchange Act Release No. 59748 (Apr. 10, 2009), 74 FR 18042 (Apr. 20, 2009) (the "Proposal"). As a supplement to our request for comment on the Proposal, we are soliciting additional feedback regarding an alternative price test, on which we solicited comment in the Proposal, that would allow short selling only at a price above the current national best bid (the "alternative uptick rule"). We are publishing this supplemental request for comment and reopening the comment period to help ensure that the public has a full opportunity to provide comments on the alternative uptick rule.

DATES: Comments should be received on or before [insert date 30 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 S7-08-09 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 S7-08-09. 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. We will post all comments on the Commission's Internet Web site (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 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: Jo Anne Swindler, Acting Associate Director; Josephine J. Tao, Assistant Director; Victoria Crane, Branch Chief; or Katrina Wilson, Staff Attorney, Division of Trading and Markets, at (202) 551-5720, at the Commission, 100 F Street, NE, Washington, DC 20549-6628.

SUPPLEMENTARY INFORMATION: On April 8, 2009, we proposed to re-examine and seek comment on whether to impose price test restrictions or circuit breaker restrictions on short selling.[1] The Proposal was published for comment on April 20, 2009 and the comment period initially closed on June 19, 2009.[2]

I. INTRODUCTION

In the Proposal, we proposed two approaches to restrictions on short selling: one that would apply on a market-wide and permanent basis ("short sale price test" or "short sale price test restriction") and one that would apply only to a particular security during a severe market decline in the price of that security ("circuit breaker").[3] With respect to the first approach, we proposed two alternative short sale price tests: one based on the current national best bid (the "proposed modified uptick rule") and the second based on the last sale price (the "proposed uptick rule"). With respect to the second approach, we proposed two alternative circuit breaker tests: one that would temporarily prohibit short selling in a particular security when there is a severe decline in the price of that security; and one that would temporarily impose either the proposed modified uptick rule or the proposed uptick rule on short sales in a particular security when there is a severe decline in the price of that security. Although we sought comment on the alternative uptick rule, it was not one of the proposed approaches.

The Proposal sought comment on all aspects of the proposed approaches to restrictions on short selling. Among other things, the Proposal inquired whether the alternative uptick rule, which would permit short selling at a price above the current national best bid, would be preferable to the proposed modified uptick rule and the proposed uptick rule.[4] We sought comment regarding the application of the alternative uptick rule as a market-wide permanent

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1 See Proposal, 74 FR 18042.

2 See id.

3 See id.

4 See Proposal, 74 FR at 18072, 18081, 18082.

price test restriction or in conjunction with a circuit breaker.[5] We have received almost 4,000 unique comment letters in response to the Proposal, as well as over 250 copies of 4 different standard letter types, and a petition with 5,605 signatures.[6] We have received one comment letter that favored adoption of the alternative uptick rule on a market-wide permanent basis.[7] Six commenters who stated that there is not any need for the Commission to enact any further restrictions on short selling expressed support for applying the alternative uptick rule in combination with a circuit breaker if some form of a price test were to be instituted.[8] One commenter who stated that a price test could contribute to the goal of restoring investor confidence expressed support for the alternative uptick rule, but expressed a preference for the proposed modified uptick rule.[9] In addition, the Commission hosted a roundtable on May 5,

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5 See id.

6 The full text of comments to the Proposal, including the text of standard letter types and a petition, is publicly available at: http://www.sec.gov/comments/s7-08-09/s70809.shtml.

7 See letter from Glen Shipway, dated June 19, 2009.

8 See letter from Erik Swanson, SVP and General Counsel, BATS Exchange, Inc., dated May 14, 2009 ("BATS"); letter from Johnny Peters, ChFC, dated May 20, 2009; letter from Dan Mathisson, Managing Director, Credit Suisse Securities (USA), LLC, dated June 16, 2009 ("Credit Suisse"); letter from Ira D. Hammerman, Senior Managing Director and General Counsel, SIFMA, dated June 19, 2009 ("SIFMA"); letter from Paul M. Russo, Managing Director, Head of U.S. Equity Trading, Goldman, Sachs & Co., dated June 19, 2009 ("Goldman Sachs"); letter from Eric W. Hess, General Counsel, DirectEdge, dated June 23, 2009. In addition, we note that prior to the Commission issuing the Proposal, four exchanges, NYSE Euronext, The Nasdaq OMX Group, Inc., BATS Exchange, Inc., and National Stock Exchange (the "national securities exchanges"), submitted a comment letter recommending a circuit breaker combined with a price test that would allow short selling only at an increment above the current national best bid, like the alternative uptick rule. NYSE Euronext, in its subsequent comments, stated that it supported the proposed modified uptick rule rather than the position expressed in the earlier March 24, 2009 letter. See statement of Larry Leibowitz, Group Executive Vice President and Head of Global Technology and US Execution, NYSE Euronext, dated May 5, 2009 ("statement of NYSE Euronext"); letter from Janet M. Kissane, Senior Vice President, Legal and Corporate Secretary, NYSE Euronext, dated June 19, 2009 ("NYSE Euronext").

9 See statement of NYSE Euronext; letter from NYSE Euronext.

2009 to examine short sale price test and circuit breaker restrictions, at which several panelists expressed support for the alternative uptick rule.[10]

We want to further consider the alternative uptick rule and whether adopting it would achieve our objectives. Accordingly, we are publishing this supplemental request for comment and reopening the comment period to help ensure that the public has a full opportunity to provide comments on the Proposal, the alternative uptick rule, and any other matters that may have an effect on the Proposal and to assist the Commission in its consideration of the same.

II. DISCUSSION

A. The Alternative Uptick Rule

As noted in the Proposal, the alternative uptick rule would allow short selling only at a price above the current national best bid such that short selling would occur only at a higher price than the current national best bid.[11] The alternative uptick rule would be similar to the proposed modified uptick rule in that both would use the current national best bid as a reference point for short sale orders. Unlike the proposed modified uptick rule (and the proposed uptick rule), the alternative uptick rule would not allow short selling at the current national best bid (or last sale price). Instead, in an advancing or declining market, the alternative uptick rule would only permit short selling at an increment above the current national best bid, unless an applicable exception applies.[12]

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10 See Unofficial Copy of Roundtable Transcript available at http://www.sec.gov/spotlight/shortsales.htm. (the following individuals commented on the alternative uptick rule during the roundtable: Richard Ketchum, Chairman and CEO, FINRA; Dan Mathisson, Managing Director, Credit Suisse Securities (USA) LLC; Lawrence Leibowitz, Group Executive Vice President, Head of US Markets and Global Technology, NYSE Euronext; and Dr. Frank Hatheway, Chief Economist, Nasdaq OMX Group).

11 See Proposal, 74 FR at 18072, 18081, 18082.

12 See infra discussion in Section II.B., "Exceptions."

Because it would only permit short selling at an increment above the national best bid, the alternative uptick rule would not allow short sales to get immediate execution, even in an advancing market, and therefore the alternative uptick rule would restrict short selling to a greater extent than either the proposed modified uptick rule or the proposed uptick rule. We note, however, that because the alternative uptick rule would reference only the current national best bid in determining permissible short sales, it would not require monitoring of the sequence of bids or last sale prices (i.e., whether the current national best bid or last sale price is above or below the previous national best bid or last sale price). As a result, in the view of at least one commenter, the alternative uptick rule would likely be easier to monitor[13] and, in the view of several commenters, could likely be implemented more quickly than the proposed modified uptick rule or the proposed uptick rule.[14] For the same reason, at least two commenters stated that the alternative uptick rule could potentially be less costly to implement than the proposed modified uptick rule or the proposed uptick rule.[15] In addition, several commenters noted that the alternative uptick rule would be easier to program into trading and surveillance systems than the proposed modified uptick rule or the proposed uptick rule because it would not require bid sequencing.[16]

However, because the alternative uptick rule would restrict short selling to a greater extent than either the proposed modified uptick rule or the proposed uptick rule, it could also potentially lessen some of the benefits of legitimate short selling, including market liquidity and

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13 See, e.g., letter from SIFMA.

14 See, e.g., statement from NSYE Euronext; letter from Credit Suisse; letter from SIFMA; letter from Glen Shipway; letter from Goldman Sachs.

15 See, e.g., letter from BATS; letter from Glen Shipway.

16 See, e.g., letter from the national securities exchanges; letter from Glen Shipway; letter from Goldman Sachs.

pricing efficiency[17] to a greater extent. Thus, there may be potential costs associated with the alternative uptick rule in terms of potential impact of such a price test on quote depths, spread widths, market liquidity, execution and pricing inefficiencies.

In the Proposal, we proposed a policies and procedures approach with the proposed modified uptick rule, such that the rule would require trading centers[18] to have policies and procedures reasonably designed to prevent the execution or display of short sales at impermissible prices.[19] In contrast, we proposed a straight prohibition approach with the proposed uptick rule, such that the rule would prohibit any person from effecting short sales at impermissible prices.[20] We also discussed in the Proposal that in adopting a final rule, we could take several different approaches, or a combination of approaches.[21] Similarly, as discussed in the Proposal, the alternative uptick rule could ultimately be implemented through a policies and procedures approach or through a straight prohibition approach or some combination thereof.[22]

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[17] See, e.g., Securities Exchange Act Release No. 54891 (Dec. 7, 2006), 71 FR 75068, 75069 (Dec. 13, 2006); Securities Exchange Act Release No. 48709 (Oct. 28, 2003), 68 FR 62972, 62974 (Nov. 6, 2003); Securities Exchange Act Release No. 29278 (June 7, 1991), 56 FR 27280 (June 13, 1991); Securities Exchange Act Release No. 50103 (July 28, 2004), 69 FR 48009, n. 6 (Aug. 6, 2004); Boehmer, Ekkehart and Wu, Julie, Short Selling and the Informational Efficiency of Prices (Jan. 8, 2009).

[18] A "trading center" means a national securities exchange or national securities association that operates a self-regulatory organization trading facility, an alternative trading system, an exchange market maker, an over-the-counter market maker, or any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent. See 17 CFR 242.600(b)(78); see also Proposal, 74 FR at 18043, 18051.

[19] See Proposal, 74 FR at 18051 – 18052.

[20] See Proposal, 74 FR at 18052, 18062.

[21] See Proposal, 74 FR at 18049.

[22] See Proposal, 74 FR at 18072. For instance, the approaches could be combined so that persons are prohibited from selling short at or below the current national best bid and trading centers are also required to have reasonable policies and procedures to prevent the execution or display of a short sale at or below the current national best bid.

In addition, as was noted in the Proposal, the alternative uptick rule could be implemented in combination with a short selling circuit breaker.[23] Specifically, in the Proposal, we requested comment regarding whether a circuit breaker that would temporarily impose the alternative uptick rule on short sales in a particular security when there is a severe decline in the price of that security would be preferable to a circuit breaker that would impose either the proposed modified uptick rule or the proposed uptick rule.[24]

Similar to a circuit breaker that would impose either the proposed modified uptick rule or the proposed uptick rule, as discussed in the Proposal, a circuit breaker that would impose the alternative uptick rule would be triggered by an intraday decline in the price of an individual equity security by a set percentage (for example 10, 15 or 20 percent) from the prior day's closing price.[25] A circuit breaker that would impose the alternative uptick rule would include the same exceptions as discussed with respect to the market-wide permanent alternative uptick rule.[26] In addition, like the market-wide permanent alternative uptick rule, discussed above, a circuit breaker that would impose the alternative uptick rule would restrict short selling to a greater extent and would likely be easier to implement than a circuit breaker that would impose either the proposed modified uptick rule or the proposed uptick rule. However, a circuit breaker that would impose the alternative uptick rule would be less restrictive than a circuit breaker halt rule, which would temporarily prohibit short selling in a particular security if there is a severe decline in price in that security.[27]

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23 See Proposal, 74 FR at 18081, 18082.

24 See id.

25 See Proposal 74 FR at 18069.

26 See infra discussion in Section II.B., "Exceptions."

27 See Proposal, 74 FR at 18066.

B. Exceptions

In the Proposal, the proposed modified uptick rule and the proposed uptick rule included types of short sales that would not be subject to the requirements of the proposed rules.[28] For example, the proposed modified uptick rule would require that a trading center's policies and procedures be reasonably designed to permit the execution or display of a short sale order marked "short exempt" without regard to whether the order would otherwise be impermissible.[29] The proposed uptick rule included a number of exceptions to its price test restrictions on short sales that, for the most part, paralleled the provisions in the proposed modified uptick rule relating to short sale orders that could be marked "short exempt."[30]

We believe that, because the alternative uptick rule would be most similar to the proposed modified uptick rule, in that both approaches would use the current national best bid as their reference point, the rationale discussed in the Proposal for the "short exempt" marking provisions under the proposed modified uptick rule would be similarly applicable to the alternative uptick rule.[31] Whether requiring a policies and procedures approach, or a prohibition approach, the alternative uptick rule could also include "short exempt" provisions or exceptions for: (i) a seller's delay in delivery as set forth in Section III.A.2.b of the Proposal;[32] (ii) odd lots,

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28 See Proposal, 74 FR at 18054 – 18059, 18062 – 18064.

29 See Proposal, 74 FR at 18054 – 18059.

30 See Proposal, 74 FR at 18062 – 18064.

31 We have received comments noting that a more restrictive form of price test or circuit breaker would require additional exemptions. See e.g., Unofficial Copy of Roundtable Transcript, available at http://www.sec.gov/spotlight/shortsales.htm (statement by Lawrence Leibowitz, Group Executive Vice President, Head of US Markets and Global Technology, NYSE Euronext). See also letter from the Investment Company Institute, dated June 19, 2009.

32 74 FR at 18055.

as set forth in Section III.A.2.c. of the Proposal;[33] (iii) domestic arbitrage, as set forth in Section III.A.2.d. of the Proposal;[34] (iv) international arbitrage, as set forth in Section III.A.2.e. of the Proposal;[35] (v) over-allotments and lay-off sales, as set forth in Section III.A.2.f. of the Proposal;[36] (vi) transactions on a VWAP basis, as set forth in Section III. A.2.h. of the Proposal;[37] and (vii) riskless principal transactions as set forth in Section III.A.2.g. of the Proposal.[38] As we recognize that the alternative uptick rule would be more restrictive than the proposed modified uptick rule, we also renew our request for comment on the importance of a market maker exception. We ask for comment on the scope of any such exception and the conditions that should be imposed to ensure that it is used only for bona fide market making.

III. REQUEST FOR COMMENT

A. General Request for Comment

We renew our request for comment on all aspects of the alternative uptick rule. Commenters are requested to provide empirical data in support of any arguments and/or analyses. In addition to the questions posed above, commenters are welcome to offer their views on any other matter raised by the alternative uptick rule and the Proposal. With respect to any comments, we note that they are of the greatest assistance to our rulemaking initiative if

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33 Id.

34 74 FR at 18056.

35 Id.

36 74 FR at 18057.

37 74 FR at 18058.

38 74 FR at 18057. We note that the proposed uptick rule included exceptions that paralleled the "short exempt" marking provisions for the proposed modified uptick rule, as well as three exceptions specific to a price test based on last sale price. In addition, one exception (error in marking a short sale) was specific to a prohibition approach, rather than a policies and procedures approach, and would be applicable to the alternative uptick rule if it were adopted with a prohibition approach. See Proposal, 74 FR at 18063.

accompanied by supporting data and analysis of the issues addressed in those comments and by alternatives to our proposals where appropriate. We note that while there were questions in the Proposal that were specific to the alternative uptick rule, the Proposal also included discussion and solicited comment throughout that may be relevant to consideration of the alternative uptick rule and we refer commenters to the Proposal.

B. Specific Comment Request

We renew our request for comment in response to the following specific questions that were originally published in the Proposal.[39] We request comment on the questions set forth under the "Supplemental Comment Request" below.

Renewal of Comment Request

1. Would the alternative uptick rule be more effective at preventing short selling, including potentially manipulative or abusive short selling, from being used as a tool to drive down the market or from being used to accelerate a declining market than the approach set forth in the proposed modified uptick rule or proposed uptick rule? If so, how? If not, why not?[40]

2. What effect would the alternative uptick rule have on the benefits of short selling, such as providing price efficiency and liquidity?[41]

3. Would the alternative uptick rule be easier to program into trading and surveillance systems than the approach in the proposed modified uptick rule or proposed uptick rule? If so, why? If not, why not?[42]

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39 See Proposal, 74 FR at 18072, 18081.

40 See Proposal, 74 FR at 18072.

41 See id.

42 See id.

4. If adopted, should the alternative uptick rule be combined with a policies and procedures approach similar to that discussed under the proposed modified uptick rule or a prohibition approach similar to that discussed under the proposed uptick rule? What would be the advantages and disadvantages, including costs and benefits of each of these approaches as combined with the alternative uptick rule?[43]

5. If the Commission were to adopt a circuit breaker rule, should the circuit breaker, when triggered, result in the alternative uptick rule? If so, why? If not, why not?[44]

Supplemental Comment Request

1. How effective would the alternative uptick rule be at helping to prevent short selling, including potentially abusive or manipulative short selling, from being used as a tool for driving the market down or from being used to accelerate a declining market by exhausting all remaining bids at one price level? Please explain and provide empirical data in support of any arguments and/or analyses. Could the alternative uptick rule be modified to better meet these goals? If so, how? Please explain and provide empirical data in support of any arguments and/or analyses.

2. How would the alternative uptick rule affect short selling in an advancing market? How would the alternative uptick rule affect short selling in a declining market? Please explain and provide empirical data in support of any arguments and/or analyses.

3. To the extent that there are concerns regarding investor confidence based on the numerous requests for reinstatement of short sale price test restrictions, would adopting the alternative uptick rule help restore investor confidence? If so, why? If not, why not?

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[43] See id.

[44] See Proposal, 74 FR at 18081.

Please explain and provide empirical data or other specific information in support of any arguments and/or analyses.

4. In addition to investor confidence and market volatility, we have stated that we are concerned about potentially abusive short selling. Would the alternative uptick rule help address potentially abusive short selling? If so, how? If not, why not? Please explain and provide empirical data in support of any arguments and/or analyses.

5. In the Proposal, we also noted that short selling may be used to illegally manipulate stock prices.[45] What impact, if any, would the alternative uptick rule have on short selling used to illegally manipulate stock prices? Please explain and provide empirical data in support of any arguments and/or analyses.

6. What impact, if any, would the alternative uptick rule have on "bear raids"? Please explain and provide empirical data in support of any arguments and/or analyses.

7. Would the alternative uptick rule be an appropriate short sale price test in the current decimals environment? Would the alternative uptick rule be more suitable than the proposed modified uptick rule or the proposed uptick rule in a decimals environment with multiple trading centers? Please explain and provide empirical data in support of any arguments and/or analyses.

8. How would trading systems and strategies used in today's marketplace be affected by the alternative uptick rule? How might market participants alter their trading systems and strategies in response to the alternative uptick rule, if adopted?

9. What impact, if any, would the trading requirements of Regulation NMS have on implementing the alternative uptick rule?

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45 See id.

10. The proposed modified uptick rule and the proposed uptick rule have as their reference point for a permissible short sale the current national best bid, and the last sale price, respectively, in relation to the last differently priced national best bid, and the last differently priced sale price, respectively. In contrast, the alternative uptick rule would have as its reference point the current national best bid. Accordingly, the sequence of bids would not play a role in determining when short sales are permissible. How would removing bid or sale price sequencing from the requirements of a short sale price test restriction, if adopted, affect implementation costs, ongoing costs, the effectiveness of the restriction in achieving the Commission's goals, market liquidity, pricing efficiency, and investor confidence?

11. If we were to adopt the alternative uptick rule, would a two month implementation period following the effective date of the alternative uptick rule be appropriate? Would a shorter or longer implementation period be more appropriate for the alternative uptick rule? Please explain.

12. Because the alternative uptick rule would not require monitoring of the sequence of bids or last sale prices (i.e., whether the current national best bid or last sale price is above or below the previous national best bid or last sale price), could this type of rule be implemented more quickly than the proposed modified uptick rule or the proposed uptick rule?

13. What would be the impact of the alternative uptick rule on off-exchange trading? Specifically, would there be any special concerns with respect to off-exchange trading in connection with the alternative uptick rule, such as systems and/or implementation issues, or additional or alternative provisions that should be considered?

14. As discussed above, if adopted with a policies and procedures approach, similar to the proposed modified uptick rule, the following short sale orders could be marked as "short exempt" and could, therefore, be exempt from the requirements of the alternative uptick rule: (i) a seller's delay in delivery as set forth in Section III.A.2.b of the Proposal;[46] (ii) odd lots, as set forth in Section III.A.2.c. of the Proposal;[47] (iii) domestic arbitrage, as set forth in Section III.A.2.d. of the Proposal;[48] (iv) international arbitrage, as set forth in Section III.A.2.e. of the Proposal;[49] (v) over-allotments and lay-off sales, as set forth in Section III.A.2.f. of the Proposal;[50] (vi) transactions on a VWAP basis, as set forth in Section III. A.2.h. of the Proposal;[51] and (vii) riskless principal transactions as set forth in Section III.A.2.g. of the Proposal.[52] In addition, if adopted with a prohibition approach, the exception specific to the proposed uptick rule for error in marking a short sale, as set forth in Section III.B.2.a. of the Proposal,[53] would also apply to the alternative uptick rule. Are these "short exempt" provisions or exceptions necessary or appropriate? If so, why? If not, why not?

15. Are there other "short exempt" provisions or exceptions that should apply to the alternative uptick rule? If so, please explain. Should a general market maker exception

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[46] 74 FR at 18055.

[47] Id.

[48] 74 FR at 18056.

[49] Id.

[50] 74 FR at 18057.

[51] 74 FR at 18058.

[52] 74 FR at 18057.

[53] 74 FR at 18063.

apply to the alternative uptick rule? Should an options market maker exception apply? What should be the scope of any such exceptions? Should additional conditions apply to a market maker exception under the alternative uptick rule to ensure that only bona fide market making is captured by the exception?

16. The Proposal includes a discussion of estimated annual reporting and recordkeeping burdens with respect to provisions of the proposed rules that would require a new "collection of information" under the Paperwork Reduction Act of 1995.[54] We invite comment on these estimates with respect to the alternative uptick rule.[55]

17. The Proposal includes a discussion of estimated costs and benefits of the proposed rules.[56] We are sensitive to the costs and benefits of the alternative uptick rule, and encourage commenters to discuss any additional costs or benefits specific to the alternative uptick rule and/or beyond those discussed discussed in the Proposal, as well as any reduction in costs. What would be the costs and benefits of the alternative uptick rule versus the proposed modified uptick rule, the proposed uptick rule, the circuit breaker halt rule or a circuit breaker triggering either the proposed modified uptick rule or the proposed uptick rule? What would be the general costs and benefits of short sales being subject to the alternative uptick rule? Commenters should provide analysis and

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[54] 44 U.S.C. 3501 et seq. See Proposal, 74 FR at 18084 – 18090.

[55] Persons submitting comments on the collection of information requirements 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, Washington, DC 20503, and should also send a copy of their comments to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090, with reference to File No. S7-08-09. Requests for materials submitted to OMB by the Commission with regard to this collection of information should be in writing, with reference to File No. S7-08-09, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, 100 F Street, NE, Washington, DC 20549-0213. As OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

[56] See Proposal, 74 FR at 18090 – 18103.

data to support their views of the costs and benefits associated with the alternative uptick rule.

18. The Proposal includes a discussion of whether the proposed rules would promote efficiency, competition, and capital formation.[57] We request comment on whether the alternative uptick rule would likely promote efficiency, capital formation, and competition.

19. The Proposal includes an Initial Regulatory Flexibility Analysis ("IRFA"), in accordance with the provisions of the Regulatory Flexibility Act,[58] regarding the proposed rules.[59] We solicit written comments regarding our IRFA analysis. In particular, the Commission seeks comment on the number of small entities that would be affected by the alternative uptick rule. We request that commenters provide empirical data to quantify the number of small entities that could be affected by the proposed amendments. We request comment on whether the proposed amendments would have any effects that we have not discussed. We also request that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of the impact.

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[57] See Proposal, 74 FR at 18103 – 18104.

[58] 5 U.S.C. 603.

[59] See Proposal, 74 FR at 18105 – 18107.

20. A number of commenters stated that their first preference would be for the Commission not to adopt any of the short sale regulations set forth in the Proposal, and this option along with the alternative uptick rule and all other options discussed in the Proposal are under active consideration. We request comments on the position that the best result for investors and the markets would be for the Commission not to adopt any additional short selling regulations at this time. If the Commission determines that additional short selling regulations are necessary, what option, including the alternative uptick rule, would produce the best result for investors and the markets?

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Dated: August 17, 2009

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 18, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13582

In the Matter of **Magnum Resources, Inc.,** **Manakoa Services Corp.** **(n/k/a Teslavision Corp.),** **Maxus Technology Corp.,** **Med/Waste, Inc.,** **Medsearch Technologies, Inc., and** **Meisenheimer Capital, 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 Magnum Resources, Inc., Manakoa Services Corp. (n/k/a Teslavision Corp.), Maxus Technology Corp., Med/Waste, Inc., Medsearch Technologies, Inc., and Meisenheimer Capital, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Magnum Resources, Inc. (CIK No. 915637) is a delinquent Delaware corporation located in Phoenix, Arizona with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Magnum Resources 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 April 30, 1999, which reported a net loss of $1.66 million for the prior nine months. As of August 12, 2009, the company's stock (symbol "MGRI") was quoted on the Pink Sheets operated by Pink OTC Markets, Inc. ("Pink Sheets"), had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. Manakoa Services Corp. (n/k/a Teslavision Corp.) (CIK No. 1091967) is a Nevada corporation located in Kennewick, Washington with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Manakoa 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, 2006, which reported a net loss of over $11.5 million since the company's November 21, 2001 inception. As of August 12, 2009, the company's stock (symbol "TSLV") was traded on the over-the-counter markets, had eleven market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

3. Maxus Technology Corp. (CIK No. 1054709) is a forfeited Delaware corporation located in Milpitas, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Maxus 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 November 30, 2004, which reported a net loss of over $4.48 million for the prior twelve months. As of August 12, 2009, the company's stock (symbol "MXUS") was quoted on the Pink Sheets, had eight market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

4. Med/Waste, Inc. (CIK No. 885195) is a void Delaware corporation located in Miami Lakes, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Med/Waste 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, 2000, which reported a net loss of over $6.49 million for the prior nine months. On February 13, 2002, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Southern District of Florida, which was still pending as of August 12, 2009. As of August 12, 2009, the company's stock (symbol "MWDSQ") 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).

5. Medsearch Technologies, Inc. (CIK No. 1093759) is void Delaware corporation located in Chicago, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Medsearch 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. As of August 12, 2009, the company's stock (symbol "MDSX") was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

6. Meisenheimer Capital, Inc. (CIK No. 747574) is a void Delaware corporation located in Milford, Connecticut with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Meisenheimer 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 February 29, 2004, which reported a net loss of

$62,508 for the prior twelve months.[1] As of August 12, 2009, the company's stock (symbol "MEIS") 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).

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

[1]Meisenheimer Capital, Inc. also has earlier gaps in its periodic reports: it never filed its Form 10-QSB for the period ended November 30, 1998, its reports between the Forms 10-KSB for the periods ended February 28, 1999 and February 29, 2000, or its reports between the Forms 10-KSB for the periods ended February 29, 2000 and February 29, 2004.

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

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Appendix 1

Chart of Delinquent Filings
In the Matter of Magnum Resources, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Magnum Resources, Inc.					
	10-KSB	07/31/99	10/29/99	Not filed	118
	10-QSB	10/31/99	12/15/99	Not filed	116
	10-QSB	01/31/00	03/16/00	Not filed	113
	10-QSB	04/30/00	06/14/00	Not filed	110
	10-KSB	07/31/00	10/30/00	Not filed	106
	10-QSB	10/31/00	12/15/00	Not filed	104
	10-QSB	01/31/01	03/19/01	Not filed	101
	10-QSB	04/30/01	06/14/01	Not filed	98
	10-KSB	07/31/01	10/29/01	Not filed	94
	10-QSB	10/31/01	12/17/01	Not filed	92
	10-QSB	01/31/02	03/18/02	Not filed	89
	10-QSB	04/30/02	06/14/02	Not filed	86
	10-KSB	07/31/02	10/29/02	Not filed	82
	10-QSB	10/31/02	12/16/02	Not filed	80
	10-QSB	01/31/03	03/17/03	Not filed	77
	10-QSB	04/30/03	06/16/03	Not filed	74
	10-KSB	07/31/03	10/29/03	Not filed	70
	10-QSB	10/31/03	12/15/03	Not filed	68
	10-QSB	01/31/04	03/16/04	Not filed	65
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-KSB	07/31/04	10/29/04	Not filed	58
	10-QSB	10/31/04	12/15/04	Not filed	56
	10-QSB	01/31/05	03/17/05	Not filed	53
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-KSB	07/31/05	10/31/05	Not filed	46
	10-QSB	10/31/05	12/15/05	Not filed	44
	10-QSB	01/31/06	03/17/06	Not filed	41
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-KSB	07/31/06	10/30/06	Not filed	34
	10-QSB	10/31/06	12/15/06	Not filed	32
	10-QSB	01/31/07	03/19/07	Not filed	29
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-KSB	07/31/07	10/29/07	Not filed	22
	10-QSB	10/31/07	12/17/07	Not filed	20
	10-QSB	01/31/08	03/17/08	Not filed	17

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Magnum Resources, Inc. (continued)	*10-QSB*	04/30/08	06/16/08	Not filed	14
	10-KSB	07/31/08	10/29/08	Not filed	10
	10-Q [1]	10/31/08	12/15/08	Not filed	8
	10-Q [1]	01/31/09	03/18/09	Not filed	5
	10-Q [1]	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	40				
Manakoa Services Corp. (n/k/a Teslavision Corp.)					
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	10-Q [1]	03/31/08	05/15/08	Not filed	15
	10-Q [1]	06/30/08	08/14/08	Not filed	12
	10-Q [1]	09/30/08	11/14/08	Not filed	9
	10-K [1]	12/31/08	03/31/09	Not filed	5
	10-Q [1]	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	9				
Maxus Technology Corp.					
	10-QSB	02/28/05	04/14/05	Not filed	52
	10-QSB	05/31/05	07/15/05	Not filed	49
	10-QSB	08/31/05	10/17/05	Not filed	46
	10-KSB	11/30/05	02/28/06	Not filed	42
	10-QSB	02/28/06	04/14/06	Not filed	40
	10-QSB	05/31/06	07/17/06	Not filed	37
	10-QSB	08/31/06	10/16/06	Not filed	34
	10-KSB	11/30/06	02/28/07	Not filed	30
	10-QSB	02/28/07	04/16/07	Not filed	28
	10-QSB	05/31/07	07/16/07	Not filed	25
	10-QSB	08/31/07	10/15/07	Not filed	22
	10-KSB	11/30/07	02/28/08	Not filed	18
	10-QSB	02/28/08	04/14/08	Not filed	16
	10-QSB	05/31/08	07/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Maxus Technology Corp. (continued)	*10-QSB*	08/31/08	10/15/08	Not filed	10
	10-KSB	11/30/08	03/02/09	Not filed	5
	10-Q [1]	02/28/09	04/14/09	Not filed	4
	10-Q [1]	05/31/09	07/15/09	Not filed	1
Total Filings Delinquent	18				
Med/Waste, Inc.					
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	10-Q [1]	03/31/08	05/15/08	Not filed	15
	10-Q [1]	06/30/08	08/14/08	Not filed	12

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Med/Waste, Inc. (continued)	*10-Q*[1]	09/30/08	11/14/08	Not filed	9
	10-K[1]	12/31/08	03/31/09	Not filed	5
	10-Q[1]	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	34				
Medsearch Technologies, Inc.					
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
Total Filings Delinquent	30				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Meisenheimer Capital, Inc.					
	10-QSB	11/30/98	01/14/99	Not filed	127
	10-QSB	05/31/99	07/15/99	Not filed	121
	10-QSB	08/31/99	10/15/99	Not filed	118
	10-QSB	11/30/99	01/14/00	Not filed	115
	10-QSB	05/31/00	07/17/00	Not filed	109
	10-QSB	08/31/00	10/16/00	Not filed	106
	10-QSB	11/30/00	01/16/01	Not filed	103
	10-KSB	02/28/01	05/29/01	Not filed	99
	10-QSB	05/31/01	07/16/01	Not filed	97
	10-QSB	08/31/01	10/15/01	Not filed	94
	10-QSB	11/30/01	01/14/02	Not filed	91
	10-KSB	02/28/02	05/29/02	Not filed	87
	10-QSB	05/31/02	07/15/02	Not filed	85
	10-QSB	08/31/02	10/15/02	Not filed	82
	10-QSB	11/30/02	01/14/03	Not filed	79
	10-KSB	02/28/03	05/29/03	Not filed	75
	10-QSB	05/31/03	07/15/03	Not filed	73
	10-QSB	08/31/03	10/15/03	Not filed	70
	10-QSB	11/30/03	01/14/04	Not filed	67
	10-QSB	05/31/04	07/15/04	Not filed	61
	10-QSB	08/31/04	10/15/04	Not filed	58
	10-QSB	11/30/04	01/14/05	Not filed	55
	10-KSB	02/28/05	05/31/05	Not filed	51
	10-QSB	05/31/05	07/15/05	Not filed	49
	10-QSB	08/31/05	10/17/05	Not filed	46
	10-QSB	11/30/05	01/17/06	Not filed	43
	10-KSB	02/28/06	05/30/06	Not filed	39
	10-QSB	05/31/06	07/17/06	Not filed	37
	10-QSB	08/31/06	10/16/06	Not filed	34
	10-QSB	11/30/06	01/16/07	Not filed	31
	10-KSB	02/28/07	05/29/07	Not filed	27
	10-QSB	05/31/07	07/16/07	Not filed	25
	10-QSB	08/31/07	10/15/07	Not filed	22
	10-QSB	11/30/07	01/14/08	Not filed	19
	10-KSB	02/29/08	05/29/08	Not filed	15
	10-Q[1]	05/31/08	07/15/08	Not filed	13

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Meisenheimer Capital, Inc.	*10-Q* [1]	08/31/08	10/15/08	Not filed	10
(continued)	*10-Q* [1]	11/30/08	01/14/09	Not filed	7
	10-K [1]	02/28/09	05/29/09	Not filed	3
	10-Q [1]	05/31/09	07/15/09	Not filed	1
Total Filings Delinquent	40				

[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 (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

August 18, 2009

In the Matter of **Magnum Resources, Inc.,** **Manakoa Services Corp.** **(n/k/a Teslavision Corp.),** **Maxus Technology Corp.,** **Med/Waste, Inc.,** **Medsearch Technologies, Inc., and** **Meisenheimer Capital, 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 Magnum Resources, 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 Manakoa Services Corp. (n/k/a Teslavision Corp.) because it has not filed any periodic reports since the period ended December 31, 2006.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Maxus Technology Corp. because it has not filed any periodic reports since the period ended November 30, 2004.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Med/Waste, Inc. because it has not filed any periodic reports since the period ended September 30, 2000.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Medsearch Technologies, Inc. because it has not filed any periodic reports since the period ended September 30, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Meisenheimer Capital, Inc. because it has not filed any periodic reports since the period ended February 29, 2004.

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 August 18, 2009, through 11:59 p.m. EDT on August 31, 2009.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 18, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13584

In the Matter of JAYCEE JAMES, Respondent.	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

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

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

James, 38 years old, is a resident of Victorville, California.

B. FALSE REPORTS ON FORMS 3 AND 4 AND SCHEDULES 13D AND 13D/A

1. From March 6, 2009 through May 6, 2009, James filed 83 Forms 3 and 4 and Schedules 13D and 13D/A reporting stock ownership in 29 different companies, as set forth in the Excel spreadsheet attached hereto as Exhibit 1.

2. For example, James reported that he was a 10% shareholder of APT Satellite Holdings Limited ("APT") in a Form 3 filed on March 24, 2009; a majority shareholder of APT in a Form 4 filed on March 30, 2009; and the sole owner of all outstanding shares in APT in a Schedule 13D/A filed on April 14, 2009. However, APT is not aware of any recent acquisitions of its stock; to the contrary, APT is in the process of exiting the U.S. trading market and the only recent activity is the surrender and cash settlement of American Depository Receipts in connection with that exit.

3. Similarly, on April 10, 2009, James filed Forms 3, 3/A, 4, and 4/A claiming stock ownership in CapitalSource Healthcare REIT ("CHR"). On April 17, 2009, he filed a Schedule 13D in which he claimed to have acquired all outstanding shares in CHR. However, in late 2008, CHR postponed its planned initial public offering due to adverse market conditions. As a result, most of its shares remain in the hands of the REIT's sponsor.

4. On May 5, 2009, the Division of Enforcement sent James a request for the voluntary production of documents supporting the claims he had made in his Edgar filings. The Division of Enforcement received no documents in response to that request. On May 8, 2009, the Division of Enforcement sent James a Wells notice, requesting that he provide documents supporting his stock ownership claims. On May 13, 2009, James made a Wells submission, which admitted that he has not traded any shares in the subject companies. James also submitted a spreadsheet entitled "Claimed Interest Record" in which he attempts to explain his interest in 18 of the companies by stating, for example, that they "dissolved," "went out of business," or their shares are no longer traded. The submission did not include any stock certificates or other evidence to substantiate his stock ownership claims.

5. Therefore, contrary to James' representations in his Forms 3 and 4 and Schedules 13D and 13D/A, he is not a shareholder of APT, CapitalSource, or the other 27 companies in which he claimed stock ownership.

C. VIOLATIONS

1. As a result of the conduct described above, James violated Section 13(d) of the Exchange Act and Rule 13d-1 thereunder, which require any person who acquires beneficial ownership of more than 5% of an issuer's common stock to file a Schedule 13D with the Commission, and Rule 13d-2, which requires an amendment to be filed on Schedule 13D/A if there is any material change in the facts set forth in a previously filed Schedule 13D.

2. As a result of the conduct described above, James violated Section 16(a) of the Exchange Act and Rule 16a-3 thereunder, which require officers and directors of reporting issuers, and beneficial owners of more than 10% of a class of securities registered under Section 12 of the Exchange Act, to file reports with the Commission disclosing his or her beneficial ownership of all equity securities of the issuer. Rule 16a-3 requires a report of initial beneficial ownership to be filed on Form 3, changes in such ownership to be filed on Form 4, and annual reports to be filed on Form 5.

III.

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

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

B. Whether, pursuant to Section 21C of the Exchange Act, Respondent should be ordered to cease and desist from committing or causing violations of and any future violations of Sections 13(d) and 16(a) of the Exchange Act and Rules 13d-1, 13d-2, and 16a-3 thereunder.

IV.

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

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

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

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

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

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

Exhibit - 1

Company Name	Sub Type	File Num	Filing Date	CIK	Login CIK	Accession Number	Subj Comp Name	Issuer Name
James JayCee	3	000-12169	3/6/09	1456907	1456907	0001456907-09-000004	(null)	SOLAR SATELLITE COMMUNICATION INC
James JayCee	3	033-07075-LA	3/6/09	1456907	1456907	0001456907-09-000005	(null)	FASHION HOUSE HOLDINGS INC
James JayCee	3	033-39271	3/6/09	1456907	1456907	0001456907-09-000006	(null)	SPORTS MEDIA INC
James JayCee	3	000-23897	3/6/09	1456907	1456907	0001456907-09-000007	(null)	EARTHFIRST TECHNOLOGIES INC
James JayCee	3	000-51918	3/9/09	1456907	1456907	0001456907-09-000008	(null)	IBROADBAND, INC.
James JayCee	3	000-02851	3/9/09	1456907	1456907	0001456907-09-000009	(null)	CORNET STORES
James JayCee	3	033-89520	3/9/09	1456907	1456907	0001456907-09-000010	(null)	GENERAL ACCEPTANCE CORP /IN/
James JayCee	3	033-03443-LA	3/9/09	1456907	1456907	0001456907-09-000011	(null)	CAPITAL MEDIA GROUP LTD
James JayCee	3	000-29217	3/10/09	1456907	1456907	0001456907-09-000014	(null)	ACCESSPOINT CORP /NV/
James JayCee	3	000-07501	3/10/09	1456907	1456907	0001456907-09-000015	(null)	ADMIRALTY HOLDING CO
James JayCee	3	000-50310	3/10/09	1456907	1456907	0001456907-09-000016	(null)	VISUAL FRONTIER, INC.
James JayCee	3	000-24265	3/10/09	1456907	1456907	0001456907-09-000017	(null)	NETWORK HOLDINGS INTERNATIONAL INC
James JayCee	3	000-12423	3/10/09	1456907	1456907	0001456907-09-000018	(null)	ALONG MOBILE TECHNOLOGIES INC
James JayCee	3	000-51464	3/10/09	1456907	1456907	0001456907-09-000019	(null)	AMERICAN BASKETBALL ASSOCIATION, INC.
James JayCee	3	000-25252	3/11/09	1456907	1456907	0001456907-09-000020	(null)	CINEMASTAR LUXURY THEATERS INC
James JayCee	3	000-17752	3/11/09	1456907	1456907	0001456907-09-000021	(null)	CHANNEL AMERICA TELEVISION NETWORK INC
James JayCee	3/A	000-07501	3/11/09	1456907	1456907	0001456907-09-000023	(null)	ADMIRALTY HOLDING CO
James JayCee	3	000-50769	3/11/09	1456907	1456907	0001456907-09-000024	(null)	ASIA BROADBAND INC
James JayCee	3	000-25668	3/11/09	1456907	1456907	0001456907-09-000025	(null)	GLOBAL TECHNOLOGIES LTD
James JayCee	3	000-33313	3/11/09	1456907	1456907	0001456907-09-000026	(null)	TNX TELEVISION HOLDINGS INC
James JayCee	3	333-140070	3/12/09	1456907	1456907	0001456907-09-000027	(null)	SOLAR NIGHT INDUSTRIES, INC.
James JayCee	3	000-50355	3/12/09	1456907	1456907	0001456907-09-000028	(null)	HYDROFLO INC
James JayCee	3	000-29424	3/12/09	1456907	1456907	0001456907-09-000029	(null)	ASIA ELECTRONICS HOLDING CO INC

James JayCee	3/A	000-12169	3/16/09	1456907	1456907	0001456907-09-000030	(null)	SOLAR SATELLITE COMMUNICATION INC
James JayCee	3/A	000-12169	3/23/09	1456907	1456907	0001456907-09-000031	(null)	SOLAR SATELLITE COMMUNICATION INC
James JayCee	3/A	000-51918	3/23/09	1456907	1456907	0001456907-09-000032	(null)	IBROADBAND, INC.
James JayCee	4	000-51918	3/23/09	1456907	1456907	0001456907-09-000034	(null)	IBROADBAND, INC.
James JayCee	3	001-14564	3/24/09	1456907	1456907	0001456907-09-000035	(null)	APT SATELLITE HOLDINGS LTD
James JayCee	4	000-29424	3/24/09	1456907	1456907	0001456907-09-000036	(null)	ASIA ELECTRONICS HOLDING CO INC
James JayCee	4/A	000-51918	3/24/09	1456907	1456907	0001456907-09-000038	(null)	IBROADBAND, INC.
James JayCee	3	333-149681	3/24/09	1456907	1456907	0001456907-09-000039	(null)	VOIP TALK INC
James JayCee	3/A	333-149681	3/24/09	1456907	1456907	0001456907-09-000040	(null)	VOIP TALK INC
James JayCee	4	333-149681	3/26/09	1456907	1456907	0001456907-09-000041	(null)	VOIP TALK INC
James JayCee	4/A	333-149681	3/26/09	1456907	1456907	0001456907-09-000042	(null)	VOIP TALK INC
James JayCee	3/A	001-14564	3/26/09	1456907	1456907	0001456907-09-000043	(null)	APT SATELLITE HOLDINGS LTD
James JayCee	4	000-02851	3/26/09	1456907	1456907	0001456907-09-000044	(null)	CORNET STORES
James JayCee	4/A	000-02851	3/26/09	1456907	1456907	0001456907-09-000045	(null)	CORNET STORES
James JayCee	4	000-12169	3/27/09	1456907	1456907	0001456907-09-000046	(null)	SOLAR SATELLITE COMMUNICATION INC
James JayCee	4	000-00000	3/27/09	1456907	1456907	0001456907-09-000047	(null)	WILLIAMS & ASSOCIATES
James JayCee	4/A	001-14564	3/30/09	1456907	1456907	0001456907-09-000048	(null)	APT SATELLITE HOLDINGS LTD
James JayCee	4/A	000-12169	3/30/09	1456907	1456907	0001456907-09-000049	(null)	SOLAR SATELLITE COMMUNICATION INC
James JayCee	3/A	033-89520	4/3/09	1456907	1456907	0001456907-09-000050	(null)	GENERAL ACCEPTANCE CORP /IN/
James JayCee	4	033-89520	4/3/09	1456907	1456907	0001456907-09-000051	(null)	GENERAL ACCEPTANCE CORP /IN/
James JayCee	4/A	033-89520	4/3/09	1456907	1456907	0001456907-09-000052	(null)	GENERAL ACCEPTANCE CORP /IN/
Voip Talk Inc	SC 13D	005-84807	4/6/09	1428779	1456907	0001456907-09-000056	VoipTalk, Inc.	(null)
CORNET STORES	SC 13D	005-33848	4/6/09	24734	1456907	0001456907-09-000057	Cornet Stores, Inc.	(null)
CORNET STORES	SC 13D	005-33848	4/6/09	24734	1456907	0001456907-09-000058	Cornet Stores, Inc.	(null)
GENERAL ACCEPTANCE CORP /IN/	SC 13D	005-51283	4/7/09	937965	1456907	0001456907-09-000059	General Acceptance Corporation	(null)

SOLAR SATELLITE COMMUNICATION INC	SC 13D	005-41605	4/7/09	729588	1456907	0001456907-09-000060	Solar Satellite Communications, Inc.	(null)
APT SATELLITE HOLDINGS LTD	SC 13D	005-50155	4/8/09	1027229	1456907	0001456907-09-000061	APT Satellite Holdings Limited	(null)
APT SATELLITE HOLDINGS LTD	SC 13D/A	005-50155	4/9/09	1027229	1456907	0001456907-09-000062	APT SATELLITE HOLDINGS LTD	(null)
APT SATELLITE HOLDINGS LTD	SC 13D/A	005-50155	4/9/09	1027229	1456907	0001456907-09-000063	APT SATELLITE HOLDINGS LTD	(null)
James JayCee	3/A	000-50355	4/8/09	1456907	1456907	0001456907-09-000064	(null)	HYDROFLO INC
James JayCee	4	000-50355	4/8/09	1456907	1456907	0001456907-09-000065	(null)	HYDROFLO INC
James JayCee	3	000-21302	4/10/09	1456907	1456907	0001456907-09-000066	(null)	TVSL S.A. IN LIQUIDATION
James JayCee	3/A	000-21302	4/10/09	1456907	1456907	0001456907-09-000067	(null)	TVSL S.A. IN LIQUIDATION
James JayCee	4	000-21302	4/10/09	1456907	1456907	0001456907-09-000068	(null)	TVSL S.A. IN LIQUIDATION
James JayCee	4/A	000-21302	4/10/09	1456907	1456907	0001456907-09-000069	(null)	TVSL S.A. IN LIQUIDATION
TVSL S.A. In Liquidation	SC 13D	005-44181	4/10/09	895649	1456907	0001456907-09-000070	TVSL In Liquidation	(null)
TVSL S.A. In Liquidation	SC 13D/A	005-44181	4/10/09	895649	1456907	0001456907-09-000071	TVSL SA In Liquidation	(null)
James JayCee	3	001-15268	4/10/09	1456907	1456907	0001456907-09-000072	(null)	SCOR HOLDING (SWITZERLAND) LTD
James JayCee	3/A	001-15268	4/10/09	1456907	1456907	0001456907-09-000073	(null)	SCOR HOLDING (SWITZERLAND) LTD
James JayCee	3	001-34194	4/10/09	1456907	1456907	0001456907-09-000074	(null)	CAPITALSOURCE HEALTHCARE REIT
James JayCee	3/A	001-34194	4/10/09	1456907	1456907	0001456907-09-000075	(null)	CAPITALSOURCE HEALTHCARE REIT
James JayCee	4	001-34194	4/10/09	1456907	1456907	0001456907-09-000076	(null)	CAPITALSOURCE HEALTHCARE REIT
James JayCee	4/A	001-34194	4/10/09	1456907	1456907	0001456907-09-000077	(null)	CAPITALSOURCE HEALTHCARE REIT
James JayCee	D	021-130171	4/13/09	1456907	1456907	0001456907-09-000082	(null)	(null)
James JayCee	3	000-51464	4/13/09	1456907	1456907	0001456907-09-000083	(null)	AMERICAN BASKETBALL ASSOCIATION, INC.
APT SATELLITE HOLDINGS LTD	SC 13D/A	005-50155	4/14/09	1027229	1456907	0001456907-09-000084	APT SATELLITE HOLDINGS LTD	(null)
James JayCee	3	333-06038	4/16/09	1456907	1456907	0001456907-09-000088	(null)	APT SATELLITE HOLDINGS LTD \ADR

CapitalSource Healthcare REIT	SC 13D	005-84821	4/17/09	1438355	1456907	0001456907-09-000090	Capital SourceHealthcare REIT	(null)
James JayCee	3/A	033-39271	4/20/09	1456907	1456907	0001456907-09-000092	(null)	SPORTS MEDIA INC
James JayCee	4	033-39271	4/20/09	1456907	1456907	0001456907-09-000093	(null)	SPORTS MEDIA INC
James JayCee	4/A	033-39271	4/20/09	1456907	1456907	0001456907-09-000094	(null)	SPORTS MEDIA INC
James JayCee	3/A	000-29217	4/20/09	1456907	1456907	0001456907-09-000095	(null)	ACCESSPOINT CORP /NV/
James JayCee	4	000-29217	4/20/09	1456907	1456907	0001456907-09-000096	(null)	ACCESSPOINT CORP /NV/
James JayCee	4/A	000-29217	4/21/09	1456907	1456907	0001456907-09-000099	(null)	ACCESSPOINT CORP /NV/
James JayCee	3/A	000-50310	4/21/09	1456907	1456907	0001456907-09-000100	(null)	VISUAL FRONTIER, INC.
James JayCee	3/A	000-24265	4/21/09	1456907	1456907	0001456907-09-000101	(null)	NETWORK HOLDINGS INTERNATIONAL INC
James JayCee	3/A	000-12423	4/21/09	1456907	1456907	0001456907-09-000102	(null)	ALONG MOBILE TECHNOLOGIES INC
James JayCee	3/A	000-12423	4/21/09	1456907	1456907	0001456907-09-000103	(null)	ALONG MOBILE TECHNOLOGIES INC
SPORTS MEDIA INC	SC TO-C	005-43412	4/28/09	873105	1456907	0001456907-09-000105	Sports Media, Inc.	(null)
James JayCee	4	000-23897	5/6/09	1456907	1456907	0001456907-09-000106	(null)	EARTHFIRST TECHNOLOGIES INC
iBroadband, Inc.	SC 13D	005-84844	5/6/09	1358700	1456907	0001456907-09-000107	iBroadband, Inc.	(null)

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60533 / August 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13587

In the Matter of **ENTRADE, 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 Entrade, Inc. ("Entrade" 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, 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.[1]

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[1] Concurrently with the entry of this Order, Entrade has consented to the entry of an 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, in which the Commission finds that Entrade violated Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 13a-1, 13a-13, 12b-20 thereunder and orders Entrade to cease and desist from committing or causing any violations and any future violations thereof. *In the Matter of Entrade, Inc.*, Admin. Proc. No. 3-

of March 31, 2009, the company's stock (symbol "XMSC") was quoted on the Pink Sheets, had eight market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. Xstream has violated Exchange Act Section 13(a), and Rules 13a-1 and 13a-13 thereunder, because it has not filed any periodic reports in a timely fashion since the period ended September 30, 2006.

IV.

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

Accordingly, it is hereby ORDERED that:

Xstream cease and desist from committing or causing any violations and any future violations of Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

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
Rel. No. 60524 / August 18, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13428

In the Matter of

Xino Corp. (n/k/a Asher Xino Corp.),
Xstream Mobile Solutions Corp.,
Yellowbubble.com, Inc.,
Yes! Entertainment Corp., and
Yifan Communications, Inc.,

Respondents.

ORDER DISMISSING PROCEEDINGS
WITH PREJUDICE AS TO XSTREAM MOBILE SOLUTIONS CORP.

For good cause shown,

IT IS HEREBY ORDERED THAT this proceeding is hereby DISMISSED as to Xstream Mobile Solutions Corp. with prejudice.

By the Commission.

Elizabeth M. Murphy
Secretary

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

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60532 / August 19, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3036 / August 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13586

In the Matter of **ENTRADE, 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 Entrade, Inc. ("Entrade" or "Respondent").

II.

In anticipation of the institution of these proceedings, Entrade 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, Entrade 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.[1]

[1] Concurrently with the entry of this Order, Entrade has consented to the entry of an order revoking the registration of its securities pursuant to Section 12(j) of the Securities Exchange Act of 1934. *In the Matter of Entrade, Inc.*, Securities Exchange Act Release No.

III.

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

FACTS

1. Entrade, Inc., a Pennsylvania corporation based in Chicago, Illinois, is a holding company whose principal asset is its wholly-owned subsidiary, Nationwide Auction Systems ("Nationwide"). Until late 2008, Nationwide provided public auction services for the disposal of surplus commercial property and operated a retail division selling used vehicles. The common stock of Entrade is registered under Section 12(g) of the Exchange Act. Until October 11, 2001, Entrade's common stock was listed and traded on the New York Stock Exchange. It is currently quoted on the "pink sheets" market under the symbol "ETAD."

2. On October 19, 1999, Entrade acquired Nationwide, which became Entrade's primary operating subsidiary. Owing to significant cash flow problems, Entrade was unable to service the liabilities stemming from this acquisition and the transaction was restructured several times. Entrade did not maintain adequate books and records of the liabilities arising from the various restructurings of the Nationwide acquisition. Entrade was also unable to pay its independent auditors regularly, and, on repeated occasions, the auditors suspended audit work for lengthy periods of time. Furthermore, Entrade lacked a system of internal accounting controls designed to provide reasonable assurances that its transactions were accurately and fairly recorded and executed. As a result of these failures, Entrade became seriously delinquent in its required periodic filings. Entrade did not file a Form 10-K after its 1999 Form 10-K (which it filed on March 30, 2000), and it did not file any Forms 10-Q since the third quarter of 2000.

3. In 2005, in an effort to address its reporting failures, Entrade hired new senior management for Nationwide and supplemented Nationwide's accounting staff. New management took steps to address Entrade's books and records problems and to implement new internal controls. These efforts resulted in the filing of a Form 10-K for the period ended December 31, 2006, which Entrade filed on June 28, 2008. The Form 10-K included audited balance sheets for 2005 and 2006 and audited statements of operations and cash flows for 2004, 2005, and 2006. However, after that filing, Entrade has failed to file the required Forms 10-K for 2007 and 2008. Further, Entrade has failed to file any of the required Forms 10-Q after the third quarter of 2000.

VIOLATIONS

4. As a result of the conduct described above, Entrade violated Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder, which require every issuer of a security registered pursuant to Section 12 of the Exchange Act to 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.

5. As a result of the conduct described above, Entrade also violated Section 13(b)(2)(A) of the Exchange Act, which 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.

6. Finally, as a result of the conduct described above, Entrade violated Section 13(b)(2)(B) of the Exchange Act, which 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 generally accepted accounting principles.

IV.

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

Accordingly, it is hereby ORDERED that:

Pursuant to Section 21C of the Exchange Act, Respondent Entrade 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 promulgated thereunder.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

III.

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

A. Entrade, Inc. (CIK No. 897265), a Pennsylvania corporation based in Chicago, Illinois, is a holding company whose principal asset is its wholly-owned subsidiary, Nationwide Auction Systems ("Nationwide"). Until late 2008, Nationwide provided public auction services for the disposal of surplus commercial property and operated a retail division selling used vehicles. The common stock of Entrade is registered under Section 12(g) of the Exchange Act. Until October 11, 2001, Entrade's common stock was listed and traded on the New York Stock Exchange. It is currently quoted on the "pink sheets" market under the symbol "ETAD."

B. Entrade has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1, 13a-13 and 12b-20 thereunder, while its common stock was registered with the Commission, in that: (i) it did not file an Annual Report on Form 10-K for its fiscal years 2000 through 2005 and 2007 through 2008;[2] and (ii) it has not filed any periodic or quarterly reports on Form 10-Q for any fiscal period after its fiscal quarter ending September 30, 2000.

C. Entrade has failed to comply with Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act by failing to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflected the transactions and disposition of its assets, and by failing to 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 conformity with generally accepted accounting principles.

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.

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[2] On June 26, 2008, Entrade filed an Annual Report on Form 10-K for its fiscal year 2006 which, in addition to audited balance sheets for 2005 and 2006, contained audited statements of operations and cash flows for 2004, 2005, and 2006.

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

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

17 CFR PARTS 211, 231, AND 241

Release Nos. 33-9062A; 34-60519A; FR-80A

Commission Guidance Regarding the Financial Accounting Standards Board's Accounting Standards Codification

AGENCY: Securities and Exchange Commission.

ACTION: Interpretation.

SUMMARY: The Securities and Exchange Commission (the "Commission") is publishing interpretive guidance regarding the release by the Financial Accounting Standards Board ("FASB") of its FASB Accounting Standards Codification™ ("FASB Codification").

EFFECTIVE DATE: [Insert date of publication in the Federal Register]

FOR FURTHER INFORMATION CONTACT: Questions about specific filings should be directed to staff members responsible for reviewing the documents the registrant files with the Commission. General questions about this release should be referred to Jenifer Minke-Girard, Senior Associate Chief Accountant, or Jeffrey S. Cohan, Senior Special Counsel, Office of the Chief Accountant, at (202) 551-5300, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-6628.

SUPPLEMENTARY INFORMATION:

I. Background

Section 108 of the Sarbanes-Oxley Act of 2002[1] amended Section 19(b) of the Securities Act of 1933[2] to provide that the Commission may recognize, as generally

[1] Pub. L. 107-204, 116 Stat. 745 (2002).

accepted for purposes of the securities laws, any accounting principles established by a standard setting body that meets specified criteria. On April 25, 2003, the Commission issued a policy statement concluding that the FASB and its parent organization, the Financial Accounting Foundation, satisfied the criteria for an accounting standard setting body under the Act, and recognizing the FASB's financial accounting and reporting standards as "generally accepted" for purposes of the federal securities laws.[3]

On June 30, 2009, the FASB issued FASB Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles – a replacement of FASB Statement No. 162 (Statement No. 168), to establish the FASB Codification as the source of authoritative non-Commission accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. generally accepted accounting principles ("U.S. GAAP"). Statement No. 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The FASB Codification reorganizes existing U.S. accounting and reporting standards issued by the FASB and other related private-sector standard setters, and all guidance contained in the FASB Codification carries an equal level of authority.[4]

The FASB Codification directly impacts certain of the Commission's rules, regulations, releases and staff bulletins (collectively referred to in this release as

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[2] 15 U.S.C. 77s(b).

[3] See Commission Statement of Policy Reaffirming the Status of the FASB as a Designated Private-Sector Standard Setter, Release Nos. 33-8221; 34-47743; IC-26028; FR-70 (April 25, 2003) [68 FR 23333 (May 1, 2003)].

[4] The FASB Codification is available at http://asc.fasb.org/home.

"Commission's rules and staff guidance"), which refer to specific FASB standards or other private sector standard-setter literature under U.S. GAAP, because such references are now superseded by the FASB Codification. The Commission is therefore issuing interpretive guidance to avoid confusion on the part of issuers, auditors, investors, and other users of financial statements and Commission rules and staff guidance.

II. Discussion

Many parts of the Commission's rules and staff guidance include direct references to specific standards under U.S. GAAP. For example, Regulation S-X, which, together with the Commission's Financial Reporting Releases, sets forth the form and content of and requirements for financial statements required to be filed with the Commission,[5] includes specific references to specific standards under U.S. GAAP.[6] In addition, some parts of the Commission's rules and staff guidance outside of the financial statement context include specific references to specific standards under U.S. GAAP, such as in Item 402 of Regulation S-K regarding disclosure of executive compensation.[7]

Given the possible confusion between the Commission's rules and staff guidance, on the one hand, and the FASB Codification, on the other hand, the Commission believes it is necessary to publish the guidance in this release. Concurrent with the effective date of the FASB Codification, references in the Commission's rules and staff guidance to specific standards under U.S. GAAP should be understood to mean the corresponding reference in the FASB Codification. We note that the FASB Codification includes a

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[5] 17 CFR 210.1-01.

[6] See, e.g., Rule 1-02(u) of Regulation S-X [17 CFR 210.1-02(u)], which defines the term "related parties" by reference to FASB Statement of Financial Accounting Standards No. 57, Related Party Disclosures.

[7] 17 CFR 229.402.

cross-reference finding tool that can assist users in identifying where previous accounting literature resides in the FASB Codification. The Commission and its staff also intend to embark on a longer term rulemaking and updating initiative to revise comprehensively specific references to specific standards under U.S. GAAP in the Commission's rules and staff guidance.

It should be noted that although the FASB has stated that the FASB Codification supersedes existing references in U.S. GAAP, the FASB Codification does not supersede Commission rules or regulations. We understand that the FASB Codification, as a service to users, includes references to some Commission rules and staff guidance. However, the FASB Codification is not the authoritative source for such content, nor does its inclusion in the FASB Codification affect how such content may be updated in the future.

III. Codification Update

The "Codification of Financial Reporting Policies" announced in Financial Reporting Release No. 1 (April 15, 1982) [47 FR 21028] is updated by adding at the end of Section 101, under the Financial Reporting Number (FR-80A) assigned to this interpretive release, the text in Sections I and II of this release.

The Codification is a separate publication of the Commission. It will not be published in the Federal Register/Code of Federal Regulations.

List of Subjects

17 CFR Part 211

Reporting and recordkeeping requirements, Securities.

17 CFR Parts 231 and 241

Securities.

Amendments to the Code of Federal Regulations

For the reasons set out in the preamble, the Commission is amending title 17, chapter II of the Code of Federal Regulations as set forth below:

PART 211 - INTERPRETATIONS RELATING TO FINANCIAL REPORTING MATTERS

Part 211, Subpart A, is amended by adding Release No. FR-80A and the release date of August 18, 2009 to the list of interpretive releases.

PART 231 - INTERPRETATIVE RELEASES RELATING TO THE SECURITIES ACT OF 1933 AND GENERAL RULES AND REGULATIONS THEREUNDER

Part 231 is amended by adding Release No. 33-9062A and the release date of August 18, 2009 to the list of interpretive releases.

PART 241 - INTERPRETATIVE RELEASES RELATING TO THE SECURITIES EXCHANGE ACT OF 1934 AND GENERAL RULES AND REGULATIONS THEREUNDER

Part 241 is amended by adding Release No. 34-60519A and the release date of August 18, 2009 to the list of interpretive releases.

By the Commission.

Florence E Harmon

Florence E. Harmon
Deputy Secretary

Dated: August 19, 2009

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13590

In the Matter of **National Tire Services, Inc.,** **TheNETdigest.com, Inc.,** **New Media, Inc. (n/k/a New Media Group, Inc.),** **New Tel, Ltd.,** **New York Film Works, Inc., and** **Newstar Resources, 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 National Tire Services, Inc., TheNETdigest.com, Inc., New Media, Inc. (n/k/a New Media Group, Inc.), New Tel, Ltd., New York Film Works, Inc., and Newstar Resources, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. National Tire Services, Inc. (CIK No. 891204) is an inactive Minnesota corporation located in South Chicago Heights, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). National Tire 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, 1994, which reported a net loss of $974,395 for the prior nine months. On January 25, 1996, National Tire filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Northern District of Illinois, which was converted to a Chapter 7 petition on June 30, 1997, and the case was terminated on September 6, 2007.

2. TheNETdigest.com, Inc. (CIK No. 945081) is a void Delaware corporation located in Ft. Lauderdale, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). TheNETdigest.com 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 February 28, 2002, which reported a net loss of $298,029 for the prior nine months. As of August 6, 2009, the company's stock (symbol "NTDGA") 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).

3. New Media, Inc. (n/k/a New Media Group, Inc.) (CIK No. 1176134) is a Delaware corporation located in Charlotte, North Carolina with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). New Media 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, 2004, which reported a net loss of $607,003 for the prior three months. New Media, Inc. changed its name to New Media Group, Inc. in November 2004, but failed to report this change in the Commission's EDGAR database as required by Commission rules.

4. New Tel, Ltd. (CIK No. 1022704) is an Australian corporation located in Herdsman, Australia with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). New Tel 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 June 30, 2001, which reported a net loss of over $28 million for the prior twelve months.

5. New York Film Works, Inc. (CIK No. 739279) is a New York corporation located in New York, New York with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). New York Film Works 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 31, 2003, which reported a net loss of $132,747 for the prior six months. As of August 6, 2009, the company's stock (symbol "NYFM") was traded on the over-the-counter markets.

6. Newstar Resources, Inc. (CIK No. 1032627) is an Ontario corporation located in Toronto, Ontario, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Newstar 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, 1997.

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 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.

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 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
National Tire Services, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
National Tire Services, Inc.					
	10-QSB	09/30/94	11/14/94	Not filed	177
	10-KSB	12/31/94	03/31/95	Not filed	173
	10-QSB	03/31/95	05/15/95	Not filed	171
	10-QSB	06/30/95	08/14/95	Not filed	168
	10-QSB	09/30/95	11/14/95	Not filed	165
	10-KSB	12/31/95	04/01/96	Not filed	160
	10-QSB	03/31/96	05/15/96	Not filed	159
	10-QSB	06/30/96	08/14/96	Not filed	156
	10-QSB	09/30/96	11/14/96	Not filed	153
	10-KSB	12/31/96	03/31/97	Not filed	149
	10-QSB	03/31/97	05/15/97	Not filed	147
	10-QSB	06/30/97	08/14/97	Not filed	144
	10-QSB	09/30/97	11/14/97	Not filed	141
	10-KSB	12/31/97	03/31/98	Not filed	137
	10-QSB	03/31/98	05/15/98	Not filed	135
	10-QSB	06/30/98	08/14/98	Not filed	132
	10-QSB	09/30/98	11/16/98	Not filed	129
	10-KSB	12/31/98	03/31/99	Not filed	125
	10-QSB	03/31/99	05/17/99	Not filed	123
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	
Total Filings Delinquent	**60**				
TheNETdigest.com, Inc.					
	10-KSB	05/31/02	08/29/02	Not filed	84
	10-QSB	08/31/02	10/15/02	Not filed	82
	10-QSB	11/30/02	01/14/03	Not filed	79
	10-QSB	02/28/03	04/14/03	Not filed	76
	10-KSB	05/31/03	08/29/03	Not filed	72
	10-QSB	08/31/03	10/15/03	Not filed	70

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-QSB	11/30/03	01/14/04	Not filed	67
	10-QSB	02/29/04	04/14/04	Not filed	64
	10-KSB	05/31/04	08/30/04	Not filed	60
	10-QSB	08/31/04	10/15/04	Not filed	58
	10-QSB	11/30/04	01/14/05	Not filed	55
	10-QSB	2/28/05	04/14/05	Not filed	52
	10-KSB	5/31/05	08/29/05	Not filed	48
	10-QSB	08/31/05	10/17/05	Not filed	46
	10-QSB	11/30/05	01/17/06	Not filed	43
	10-QSB	2/28/06	04/14/06	Not filed	40
	10-KSB	5/31/06	08/29/06	Not filed	36
	10-QSB	08/31/06	10/16/06	Not filed	34
	10-QSB	11/30/06	01/16/07	Not filed	31
	10-QSB	2/28/07	04/16/07	Not filed	28
	10-KSB	5/31/07	08/29/07	Not filed	24
	10-QSB	08/31/07	10/15/07	Not filed	22
	10-QSB	11/30/07	01/14/08	Not filed	19
	10-QSB	2/29/08	04/14/08	Not filed	16
	10-KSB	5/31/08	08/29/08	Not filed	12
	*10-Q**	08/31/08	10/15/08	Not filed	10
	*10-Q**	11/30/08	01/14/09	Not filed	7
	*10-Q**	2/28/09	04/14/09	Not filed	4
Total Filings Delinquent	**28**				
New Media, Inc. (n/k/a New Media Group, Inc.)					
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	
Total Filings Delinquent	**21**				
New Tel, Ltd.					
	20-F	06/30/02	12/31/02	Not filed	80
	20-F	06/30/03	12/31/03	Not filed	68
	20-F	06/30/04	12/31/04	Not filed	56
	20-F	06/30/05	01/02/06	Not filed	43
	20-F	06/30/06	01/02/07	Not filed	31
	20-F	06/30/07	01/02/08	Not filed	19
	20-F	06/30/08	12/31/08	Not filed	8
Total Filings Delinquent	**7**				
New York Film Works, Inc.					
	10-KSB	10/31/03	01/29/04	Not filed	67
	10-QSB	01/31/04	03/16/04	Not filed	65
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-KSB	10/31/04	01/31/05	Not filed	55
	10-QSB	01/31/05	03/17/05	Not filed	53
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-KSB	10/31/05	01/30/06	Not filed	43
	10-QSB	01/31/06	03/17/06	Not filed	41
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-QSB	07/31/06	09/14/06	Not filed	35

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-KSB	10/31/06	01/29/07	Not filed	31
	10-QSB	01/31/07	03/19/07	Not filed	29
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-KSB	10/31/07	01/29/08	Not filed	19
	10-QSB	01/31/08	03/17/08	Not filed	17
	10-QSB	04/30/08	06/16/08	Not filed	14
	10-QSB	07/31/08	09/15/08	Not filed	11
	10-KSB	10/31/08	01/29/09	Not filed	7
	10-QSB	01/31/09	03/18/09	Not filed	5
	*10-Q**	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	**23**				
Newstar Resources, Inc.					
	20-F	12/31/98	06/30/99	Not filed	122
	20-F	12/31/99	06/30/00	Not filed	110
	20-F	12/31/00	07/02/01	Not filed	97
	20-F	12/31/01	07/01/02	Not filed	85
	20-F	12/31/02	06/30/03	Not filed	74
	20-F	12/31/03	06/30/04	Not filed	62
	20-F	12/31/04	06/30/05	Not filed	50
	20-F	12/31/05	06/30/06	Not filed	38
	20-F	12/31/06	07/02/07	Not filed	25
	20-F	12/31/07	06/30/08	Not filed	14
	20-F	12/31/08	06/30/09	Not filed	2
Total Filings Delinquent	**11**				

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)

* 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 Walter and Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60540 / August 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13589

In the Matter of **LIGHTSPEED TRADING LLC,** **Respondent.**	**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 Lightspeed Trading LLC ("Lightspeed" 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) 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:[1]

Summary

1. From September 19 through September 29, 2008, Lightspeed, a registered broker-dealer, conducted several hundred short sales of financial institution securities, on behalf of customers, in contravention of the Commission's emergency order of September 18, 2008 (the "Emergency Order").[2] By acting in contravention of the Emergency Order, Lightspeed violated Section 12(k)(4) of the Exchange Act, which requires that brokers and dealers comply with Commission orders.

Respondent

2. Lightspeed is a New York limited liability company with its principal place of business in New York City. Lightspeed is an agency broker that provides trading technology and tools that provide its customers with self-directed access to multiple trade execution venues, particularly for active traders and small to mid-size hedge funds. Lightspeed is an introducing broker, who introduces its customer accounts to its clearing firms on a fully-disclosed basis. These clearing firms also provide Lightspeed with daily lists of stocks that are available to be borrowed by Lightspeed's customers in connection with short sales. During the period that the Emergency Order was effective, there were an average of approximately 230,000 daily executions by customers through Lightspeed's proprietary trading platform (the "Lightspeed Platform").

Background

3. The Commission issued the Emergency Order on the night of Thursday, September 18, 2008. The Emergency Order provided, among other things, that "all persons are prohibited from short selling any publicly traded securities of any Included Financial Firm." An appendix to the Emergency Order specifically identified 799 financial firms as "Included Financial Firms." The Emergency Order was effective immediately.

4. The Commission posted the Emergency Order and an accompanying press release on its website at 1:42 am EST on Friday, September 19. The Commission's Office of Public Affairs also circulated the press release to numerous media outlets via email at 5:56 am EST on September 19.

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

2 *See* Exchange Act Rel. No. 58592, which, as amended by Exchange Act Rel. No. 58611, was effective from September 18 through October 8, 2008.

5. On Sunday, September 21, 2008, the Commission amended the Emergency Order. The amendment required each exchange to designate which of their listed securities were subject to the short selling ban. The New York Stock Exchange ("NYSE") and Nasdaq Stock Market ("Nasdaq") published their "no short-sale lists" (*i.e.*, lists of financial firms covered by the short selling ban) by posting them on their websites and emailing them to interested parties beginning the morning of September 22.

Lightspeed Executes and Submits Customer Short Sell Orders
<u>in Securities Subject to the Emergency Order</u>

6. According to internal Lightspeed communications, by approximately 7:30 am EST on Friday, September 19, 2008, Lightspeed personnel had received the Included Financial Firms list, and knew the securities of the identified firms could not be sold short. After 7:30 am EST on September 19, Lightspeed executed short sales in Included Financial Firms and also submitted certain customer short sale orders to third-parties for execution.

7. At approximately 7:30 a.m. EST on the morning of Monday, September 22, 2008, Lightspeed received regulatory alerts, which were e-mailed to it by the NYSE and the Nasdaq, containing the updated no short-sale lists of financial firms. As the NYSE and Nasdaq added, and on limited occasions removed, financial firms from their no short-sale lists over the course of the Emergency Order period, Lightspeed was notified of the changes via email. After receiving regulatory alerts containing the updated no short-sale lists from the NYSE and Nasdaq, Lightspeed executed short sales in covered financial firms and also submitted certain customer short sale orders to third-parties for execution.

8. Lightspeed executed 690 short sales, on an agency basis, in securities covered by the Emergency Order from September 19, 2008 through September 24, 2008. Of the 690 sales, Lightspeed executed 554 on the Lightspeed Platform. These sales involved 29 issuers, and were executed on September 19, 22, 23 and 24.[3] Another 136 short sales were executed on the HUBB trading platform (the "HUBB Platform"), which is operated by Schonfeld Securities LLC, an entity under common control with Lightspeed. These short sales involved 18 issuers, and were executed on September 19, 22, and 24.

9. Lightspeed also submitted 34 customer short sale orders in securities covered by the Emergency Order to two third-parties for execution. Those orders resulted in 82 short sale executions, involved 12 issuers, and were executed on September 19, 22, 23, 24, 25, 26 and 29, with a substantial majority of these executions, like those on the Lightspeed Platform and the HUBB Platform, occurring on the first three trading days of the Emergency Order period.

[3] During this timeframe, in certain instances, Lightspeed received inaccurate or untimely information from its clearing firms regarding the availability of stocks to borrow for short selling.

10. Lightspeed received commissions of $2,222 upon the short sales in securities covered by the Emergency Order.

Violations

11. As a result of the conduct described above, Lightspeed willfully[4] violated Section 12(k)(4) of the Exchange Act.

Lightspeed's Remedial Efforts

12. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff. In particular, Lightspeed implemented enhanced procedures to update its systems to prevent short sales in existing and newly-added stocks, and required all customers to enter into buy transactions to cover short positions in prohibited securities the same day they were executed.

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) and 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondent Lightspeed cease and desist from committing or causing any violations and any future violations of Section 12(k)(4) of the Exchange Act resulting from Lightspeed's non-compliance with any Commission emergency order limiting, restricting, or prohibiting short selling in any security.

B. Respondent Lightspeed is censured.

C. Respondent Lightspeed shall, within 30 days of the entry of this Order, pay disgorgement of $2,222 and $38 in prejudgment interest to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the United States Treasury; (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 Lightspeed Trading LLC as a Respondent in these proceedings, the file number

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

of these proceedings, a copy of which cover letter and money order or check shall be sent to Stephen Korotash, Associate Regional Director (Enforcement), Fort Worth Regional Office, Securities and Exchange Commission, 801 Cherry Street, Suite 1900, Fort Worth, Texas 76109.

D. Respondent shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of $75,000 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 United States Treasury; (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 Lightspeed Trading LLC 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 Stephen Korotash, Associate Regional Director (Enforcement), Fort Worth Regional Office, Securities and Exchange Commission, 801 Cherry Street, Suite 1900, Fort Worth, Texas 76109.

By the Commission.

Elizabeth M. Murphy
Secretary

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

Commissioner Paredes
not participating

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-60539; File No. 4-588]

COMMODITY FUTURES TRADING COMMISSION

Joint meetings on Harmonization of Regulation

AGENCIES: Securities and Exchange Commission ("SEC") and Commodity Futures Trading Commission ("CFTC") (each, an "Agency," collectively, the "Agencies").

ACTION: Notice of joint meetings; request for comment.

SUMMARY:

On June 17, 2009, the Department of the Treasury released a White Paper on Financial Regulatory Reform ("White Paper") calling on the SEC and the CFTC to "make recommendations to Congress for changes to statutes and regulations that would harmonize regulation of futures and securities." Specifically, the White Paper recommended "that the CFTC and the SEC complete a report to Congress by September 30, 2009 that identifies all existing conflicts in statutes and regulations with respect to similar types of financial instruments and either explains why those differences are essential to achieve underlying policy objectives with respect to investor protection, market integrity, and price transparency or makes recommendations for changes to statutes and regulations that would eliminate the differences."

On September 2, 2009, from 9:00 a.m. until 5:00 p.m., and September 3, 2009, from 9:00 a.m. until 12:30 p.m., the SEC and the CFTC will hold joint meetings to discuss assessments of the current regulatory scheme, harmonization of the agencies' rules, and recommendations for changes to statutes and regulations.

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The meetings will consist of five panels. Topics to be discussed will include the regulation of exchanges and markets; the regulation of intermediaries; the regulation of clearance and settlement; enforcement; and the regulation of investment funds.

On September 2, 2009, a meeting will be held in Lobby Level Hearing Room (Room 1000) at the CFTC's headquarters at Three Lafayette Centre, 1155 21st Street, N.W., Washington, DC 20581. On September 3, 2009, a meeting will be held in the auditorium at the SEC's headquarters at 100 F Street, N.E., Washington, DC 20549. The meetings will be open to the public with seating on a first-come, first-served basis. The meetings also will be available via webcast on the SEC's Web site at http://www.sec.gov and at the CFTC's Web site at http://www.cftc.gov. A transcript of the meetings will be made and entered into the Agencies' public comment files, which will remain open for the receipt of written comments until September 14, 2009. The SEC and the CFTC welcome feedback regarding any of the topics to be addressed at the meetings.

DATES: Comments should be received on or before September 14, 2009.

Because the Agencies will jointly review all comments submitted, interested parties may send comments to either Agency and need not submit responses to both Agencies. Respondents are encouraged to use the title "Harmonization of Regulation" to facilitate the organization and distribution of comments between the Agencies. Interested parties are invited to submit responses to:

Securities and Exchange Commission: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the SEC's Internet comment form (http://www.sec.gov/rules/other.shtml); or

- Send an e-mail to rule-comments@sec.gov. Please include File Number 4-588 on the subject line.

Paper Comments:

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

All submissions should refer to File Number 4-588. 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 SEC staff will post all comments on the SEC's Internet Web site (http://www.sec.gov/rules/other.shtml). Comments also will be available for inspection and copying in the SEC's Public Reference Room, 100 F Street, N.E., 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.

Commodity Futures Trading Commission:

- Written comments may be mailed to the Commodity Futures Trading Commission, Three Lafayette Center, 1155 21st Street, N.W., Washington, DC 20581, attention Office of the Secretariat; transmitted by facsimile to the CFTC at (202) 418-5521; or transmitted electronically to secretary@cftc.gov. Reference should be made to "Harmonization of Regulation."

FOR FURTHER INFORMATION CONTACT: Sara Gillis Hawkins, Special Counsel, at (202) 551-5523, or Leigh W. Duffy, Attorney-Adviser, at (202) 551-5928, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549; or Sauntia Warfield, (202) 418-5084, at the CFTC.

By the Securities and Exchange Commission.

Florence E. Harmon

Deputy Secretary

August 19, 2009

By the Commodity Futures Trading Commission.

David A. Stawick

Secretary

August 19, 2009

[THIS SIGNATURE PAGE RELATES TO THE SECURITIES AND EXCHANGE COMMISSION'S PORTION OF THE JOINT MEETINGS ON HARMONIZATION OF REGULATION]

By the Securities and Exchange Commission.

Florence E. Harmon
Florence E. Harmon
Deputy Secretary

August 19, 2009

[THIS SIGNATURE PAGE RELATES TO THE COMMODITY FUTURES TRADING COMMISSION'S PORTION OF THE JOINT MEETINGS ON HARMONIZATION OF REGULATION]

By the Commodity Futures Trading Commission.

David A. Stawick

David Stawick
Secretary

August 19, 2009

SECURITIES AND EXCHANGE COMMISSION

17 CFR PARTS 211, 231, AND 241

Release Nos. 33-9062A; 34-60519A; FR-80A

Commission Guidance Regarding the Financial Accounting Standards Board's Accounting Standards Codification

AGENCY: Securities and Exchange Commission.

ACTION: Interpretation.

SUMMARY: The Securities and Exchange Commission (the "Commission") is publishing interpretive guidance regarding the release by the Financial Accounting Standards Board ("FASB") of its FASB Accounting Standards Codification^{TM} ("FASB Codification").

EFFECTIVE DATE: [Insert date of publication in the Federal Register]

FOR FURTHER INFORMATION CONTACT: Questions about specific filings should be directed to staff members responsible for reviewing the documents the registrant files with the Commission. General questions about this release should be referred to Jenifer Minke-Girard, Senior Associate Chief Accountant, or Jeffrey S. Cohan, Senior Special Counsel, Office of the Chief Accountant, at (202) 551-5300, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-6628.

SUPPLEMENTARY INFORMATION:

I. Background

Section 108 of the Sarbanes-Oxley Act of 2002[1] amended Section 19(b) of the Securities Act of 1933[2] to provide that the Commission may recognize, as generally

[1] Pub. L. 107-204, 116 Stat. 745 (2002).

accepted for purposes of the securities laws, any accounting principles established by a standard setting body that meets specified criteria. On April 25, 2003, the Commission issued a policy statement concluding that the FASB and its parent organization, the Financial Accounting Foundation, satisfied the criteria for an accounting standard setting body under the Act, and recognizing the FASB's financial accounting and reporting standards as "generally accepted" for purposes of the federal securities laws.[3]

On June 30, 2009, the FASB issued FASB Statement of Financial Accounting Standards No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles – a replacement of FASB Statement No. 162 (Statement No. 168), to establish the FASB Codification as the source of authoritative non-Commission accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. generally accepted accounting principles ("U.S. GAAP"). Statement No. 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The FASB Codification reorganizes existing U.S. accounting and reporting standards issued by the FASB and other related private-sector standard setters, and all guidance contained in the FASB Codification carries an equal level of authority.[4]

The FASB Codification directly impacts certain of the Commission's rules, regulations, releases and staff bulletins (collectively referred to in this release as

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[2] 15 U.S.C. 77s(b).

[3] See Commission Statement of Policy Reaffirming the Status of the FASB as a Designated Private-Sector Standard Setter, Release Nos. 33-8221; 34-47743; IC-26028; FR-70 (April 25, 2003) [68 FR 23333 (May 1, 2003)].

[4] The FASB Codification is available at http://asc.fasb.org/home.

"Commission's rules and staff guidance"), which refer to specific FASB standards or other private sector standard-setter literature under U.S. GAAP, because such references are now superseded by the FASB Codification. The Commission is therefore issuing interpretive guidance to avoid confusion on the part of issuers, auditors, investors, and other users of financial statements and Commission rules and staff guidance.

II. Discussion

Many parts of the Commission's rules and staff guidance include direct references to specific standards under U.S. GAAP. For example, Regulation S-X, which, together with the Commission's Financial Reporting Releases, sets forth the form and content of and requirements for financial statements required to be filed with the Commission,[5] includes specific references to specific standards under U.S. GAAP.[6] In addition, some parts of the Commission's rules and staff guidance outside of the financial statement context include specific references to specific standards under U.S. GAAP, such as in Item 402 of Regulation S-K regarding disclosure of executive compensation.[7]

Given the possible confusion between the Commission's rules and staff guidance, on the one hand, and the FASB Codification, on the other hand, the Commission believes it is necessary to publish the guidance in this release. Concurrent with the effective date of the FASB Codification, references in the Commission's rules and staff guidance to specific standards under U.S. GAAP should be understood to mean the corresponding reference in the FASB Codification. We note that the FASB Codification includes a

[5] 17 CFR 210.1-01.

[6] See, e.g., Rule 1-02(u) of Regulation S-X [17 CFR 210.1-02(u)], which defines the term "related parties" by reference to FASB Statement of Financial Accounting Standards No. 57, Related Party Disclosures.

[7] 17 CFR 229.402.

cross-reference finding tool that can assist users in identifying where previous accounting literature resides in the FASB Codification. The Commission and its staff also intend to embark on a longer term rulemaking and updating initiative to revise comprehensively specific references to specific standards under U.S. GAAP in the Commission's rules and staff guidance.

It should be noted that although the FASB has stated that the FASB Codification supersedes existing references in U.S. GAAP, the FASB Codification does not supersede Commission rules or regulations. We understand that the FASB Codification, as a service to users, includes references to some Commission rules and staff guidance. However, the FASB Codification is not the authoritative source for such content, nor does its inclusion in the FASB Codification affect how such content may be updated in the future.

III. Codification Update

The "Codification of Financial Reporting Policies" announced in Financial Reporting Release No. 1 (April 15, 1982) [47 FR 21028] is updated by adding at the end of Section 101, under the Financial Reporting Number (FR-80A) assigned to this interpretive release, the text in Sections I and II of this release.

The Codification is a separate publication of the Commission. It will not be published in the Federal Register/Code of Federal Regulations.

List of Subjects

17 CFR Part 211

Reporting and recordkeeping requirements, Securities.

17 CFR Parts 231 and 241

Securities.

Amendments to the Code of Federal Regulations

For the reasons set out in the preamble, the Commission is amending title 17, chapter II of the Code of Federal Regulations as set forth below:

PART 211 - INTERPRETATIONS RELATING TO FINANCIAL REPORTING MATTERS

Part 211, Subpart A, is amended by adding Release No. FR-80A and the release date of August 18, 2009 to the list of interpretive releases.

PART 231 - INTERPRETATIVE RELEASES RELATING TO THE SECURITIES ACT OF 1933 AND GENERAL RULES AND REGULATIONS THEREUNDER

Part 231 is amended by adding Release No. 33-9062A and the release date of August 18, 2009 to the list of interpretive releases.

PART 241 - INTERPRETATIVE RELEASES RELATING TO THE SECURITIES EXCHANGE ACT OF 1934 AND GENERAL RULES AND REGULATIONS THEREUNDER

Part 241 is amended by adding Release No. 34-60519A and the release date of August 18, 2009 to the list of interpretive releases.

By the Commission. Florence E. Harmon

Florence E. Harmon
Deputy Secretary

Dated: August 19, 2009

Commissioner Aguilar, and Commissioner Paredes not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60544 / August 19, 2009

INVESTMENT ADVISERS ACT OF 1940
Release No. 2919 / August 19, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13592

In the Matter of

MICHAEL A. ATKINS,

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 Michael A. Atkins ("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 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. Atkins was associated with LandOak Securities, LLC ("LandOak Securities"), an investment adviser registered with the Commission, from April 2000 until October 2006. LandOak Securities is also a broker-dealer registered with the Commission. From April 1996 until July 2007, Atkins was also a registered representative associated with LandOak Securities. Atkins, 47 years old, is a resident of Greensboro, Georgia.

2. On August 10, 2009, a final judgment was entered by consent against Atkins, permanently enjoining him from future violations of Sections 206(1) and 206(2) of the Advisers Act, in the civil action entitled Securities and Exchange Commission v. LandOak Securities, LLC, Patrick L. Martin, and Michael A. Atkins, Civil Action Number 3:08-cv-0209, in the United States District Court for the Eastern District of Tennessee.

3. The Commission's complaint alleged that in July 2002, Atkins and another person took $1,545,000 from LandOak Mortgage, a Tennessee limited liability company, and diverted or loaned it to Tice Technologies, Inc. ("Tice"). The complaint alleged that Atkins did not disclose to LandOak Mortgage's investors, several of whom were advisory clients of LandOak Securities, that Atkins had a conflict of interest because he was a director of Tice and owned a substantial stake in that company. The complaint alleged that this conduct operated as a fraud and deceit on investors.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Atkins'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 Atkins be, and hereby is barred from association with any broker, dealer, or investment adviser, with the right to reapply for association after three years to the appropriate self-regulatory organization, or if there is none, to the Commission;

Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

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. 60545 / August 20, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13593

In the Matter of **Samuel A. Fishman, Esq.** **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 Samuel A. Fishman pursuant to Rule 102(e)(2) of the Commission's Rules of Practice [17 C.F.R. 200.102(e)(2)].[1]

II.

The Commission finds that:

1. Fishman was an attorney admitted to practice law in New York.

2. On March 14, 2008, the United States Attorney for the Southern District of New York filed a criminal information against Fishman, alleging one count of mail fraud. The information alleged that between 1993 and 2005, Fishman engaged in a "fraudulent scheme" to charge his law firm and "its clients hundreds of thousands of dollars for personal and non-existent business expenses."

3. On March 28, 2008, Fishman entered a plea of guilty to one count of mail fraud.

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[1]Rule 102(e)(2) provides in pertinent part: "Any attorney who has been suspended or disbarred by a court of the United States or of any State" or "[a]ny person who has been convicted of a felony or misdemeanor involving moral turpitude shall be forthwith suspended from appearing or practicing before the Commission."

4. On June 29, 2009, a judgment was entered by the United States District Court for the Southern District of New York convicting Fishman of mail fraud and sentencing him to 15 months incarceration, a $10,000 fine, and three years of supervised release.

5. On February 26, 2009, the New York Supreme Court, Appellate Division, First Department ("New York Supreme Court"), ordered that Fishman be struck from New York's roll of attorneys and counselors-at-law.

III.

In view of the foregoing, the Commission finds that Fishman is an attorney who has been convicted of a felony involving moral turpitude, and has been disbarred by the New York Supreme Court, within the meaning of Rule 102(e)(2) of the Commission's Rules of Practice.

Accordingly, it is ORDERED, that Samuel A. Fishman 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

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 2920 / August 20, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13594

In the Matter of KNOX H. FUQUA,

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 Knox H. Fuqua ("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. Knox H. Fuqua ("Fuqua"), age 49, of Charleston, West Virginia, was an investment adviser and between 2003 and 2005 was the sole person in control of Commission-registered investment adviser KHF Advisors, LLC ("KHF Advisors"), his alter ego.

2. On August 14, 2009, a final judgment was entered by consent against Fuqua, permanently enjoining him from future violations of Section 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 Investment Advisers Act of 1940 ("Advisers Act"), in the civil action entitled Securities and Exchange Commission v. Knox H. Fuqua, et al., Civil Action Number 2:06-cv-0666, in the United States District Court for the Southern District of West Virginia.

3. The Commission's Complaint alleged, among other things, that Fuqua and his company were fiduciaries of their investment advisory clients. As such, they owed their clients a duty of honesty, undivided loyalty, fair-dealing and full disclosure. The Complaint further alleged that Fuqua and his company breached their fiduciary duties by: (1) misappropriating client funds, (2) materially misrepresenting the nature and risk of the investments made on behalf of the clients, and (3) investing client funds in a manner contrary to client instructions. Fuqua's clients gave him discretionary authority over their money, with the caveat that he not put their money in high-risk investments. Instead of investing his clients' funds according to their instructions, Fuqua used the funds to pay his personal and business expenses and repay money he had misappropriated from other investors.

IV.

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

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act that Respondent Fuqua 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
Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60558 / August 21, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13596

In the Matter of **KATHLEEN R. NOVINGER, 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 Kathleen R. Novinger, Esq. ("Respondent" or "Novinger") 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 her and the subject matter of these proceedings, and the findings contained in Section III, paragraph 2 below, which are admitted,

[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.

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. Novinger, age 38, is a resident of Cypress, California and has been an attorney licensed to practice in the State of California since 1999. From at least February 2007 through at least November 2007, Novinger issued legal opinions for the benefit of certain shareholders of Mobile Ready Entertainment Corp. ("Mobile Ready"), opining as to whether such shareholders could sell shares of Mobile Ready acquired in unregistered offerings and bearing restrictive legends into the public market, absent registration, pursuant to Rule 144 of the Securities Act of 1933 ("Securities Act").

2. On July 31, 2009, a final judgment was entered against Novinger, permanently enjoining her from future violations of 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, in the civil action entitled Securities and Exchange Commission v. Albert J. Rasch, Jr., et al., Civil Action Number 1:09-CV-1190, in the United States District Court for the Northern District of Georgia. Novinger was also: (a) ordered to pay a $10,000 civil monetary penalty; (b) ordered to pay post-judgment interest pursuant to 28 U.S.C. § 1961 on the civil penalty amount; and (c) barred Novinger for five years from participating in an offering of a penny stock. Novinger consented to the entry of the judgment without admitting or denying any of the allegations in the complaint.

3. The Commission's complaint alleged, among other things, that the legal opinions provided by Novinger to shareholders of Mobile Ready contained false and misleading statements of material fact, cited to nonexistent documents, and concluded without basis that more than 20 million shares acquired in unregistered offerings and bearing restrictive legends could be sold into the public market absent registration pursuant to Securities Act Rule 144.

IV.

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

Accordingly, it is hereby ORDERED, effective immediately, that Novinger is suspended from appearing or practicing before the Commission as an attorney for five years. Furthermore, after five years from the date of this Order, Novinger has the right to apply for reinstatement by submitting an affidavit to the Commission's Office of the General Counsel truthfully stating, under penalty of perjury, that she has complied with this Order, that she is not subject to any suspension or disbarment as an attorney by a court of the United States or of any state, territory, district, commonwealth, or possession, and that she has not been convicted of a felony or misdemeanor involving moral turpitude as set forth in 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. 60557 / August 21, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13595

In the Matter of **ALBERT J. RASCH, JR., ESQ.,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND 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 Albert J. Rasch, Jr., Esq. ("Respondent" or "Rasch") pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") and 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, paragraph 2 below, which are admitted,

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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 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.

Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and 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. Rasch, age 63, has been an attorney licensed to practice in the State of California since 1988. From at least February 2007 through at least November 2007, Rasch issued legal opinions for the benefit of certain shareholders of Mobile Ready Entertainment Corp. ("Mobile Ready"), opining as to whether such shareholders could sell shares of Mobile Ready acquired in unregistered offerings and bearing restrictive legends into the public market, absent registration, pursuant to Rule 144 of the Securities Act of 1933 ("Securities Act"). From January 1990 to the present, Rasch was also a registered representative associated with a broker-dealer registered with the Commission.

2. On July 31, 2009, a final judgment was entered against Rasch, permanently enjoining him from future violations of 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, in the civil action entitled Securities and Exchange Commission v. Albert J. Rasch, Jr., et al., Civil Action Number 1:09-CV-1190, in the United States District Court for the Northern District of Georgia. Rasch was also: (a) ordered to pay $1,080 in disgorgement, together with prejudgment interest thereon in the amount of $92.22; (b) ordered to pay a $20,000 civil monetary penalty; (c) ordered to pay post-judgment interest pursuant to 28 U.S.C. § 1961 on the disgorgement and civil penalty amounts; and (d) barred for five years from participating in an offering of a penny stock. Rasch consented to the entry of the judgment without admitting or denying any of the allegations in the complaint.

3. The Commission's complaint alleged, among other things, that the legal opinions provided by Rasch to shareholders of Mobile Ready contained false and misleading statements of material fact, cited to nonexistent documents, and concluded without basis that more than 20 million shares acquired in unregistered offerings and bearing restrictive legends could be sold into the public market absent registration pursuant to Securities Act Rule 144.

IV.

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

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

A. Pursuant to Section 15(b)(6) of the Exchange Act, that Respondent Rasch be, and hereby is barred from association with any broker or dealer, with the right to reapply for association after five years to the appropriate self-regulatory organization, or if there is none, to the Commission.

B. Any reapplication for association by Rasch 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.

C. Rasch is suspended from appearing or practicing before the Commission as an attorney for five years. Furthermore, after five years from the date of this Order, Rasch has the right to apply for reinstatement by submitting an affidavit to the Commission's Office of the General Counsel truthfully stating, under penalty of perjury, that he has complied with this Order, that he is not subject to any suspension or disbarment as an attorney by a court of the United States or of any state territory, district, commonwealth, or possession, and that he has not been convicted of a felony or misdemeanor involving moral turpitude as set forth in 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

ADMINISTRATIVE PROCEEDING
File No. 3-13597 / August 24, 2009

In the Matter of **Torque Engineering Corp., Transcoastal Marine Services, Inc., Transfinancial Holdings, Inc., Transwest Energy, Inc., Trend Vision Technologies, Inc., and Tricord Systems, 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 Torque Engineering Corp., Transcoastal Marine Services, Inc., Transfinancial Holdings, Inc., Transwest Energy, Inc., Trend Vision Technologies, Inc., and Tricord Systems, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Torque Engineering Corp. (CIK No. 1018675) is a dissolved Delaware corporation located in Elkhart, Indiana with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Torque Engineering 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 over $8.5 million for the prior twelve months.

2. Transcoastal Marine Services, Inc. (CIK No. 1043119) is a void Delaware corporation located in Houston, Texas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Transcoastal 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, 2000, which reported a net loss of over $9.8

million for the prior three months. On June 20, 2000, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Southern District of Texas, which was still pending as of August 21, 2009.

3. Transfinancial Holdings, Inc. (CIK No. 719271) is a dissolved Delaware corporation located in Lenexa, Kansas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Transfinancial 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, 2002, which reported a net loss of over $6.8 million for the prior twelve months.

4. Transwest Energy, Inc. (CIK No. 737837) 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). Transwest is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F for the year ended December 31, 1995, which reported a net loss of $590,000 for the prior twelve months.

5. Trend Vision Technologies, Inc. (CIK No. 784958) is a British Columbia corporation located in Scottsdale, Arizona with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Trend Vision is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F/A for the period ended September 30, 1993, which reported a deficit of over $14 million (Canadian) for the prior twelve months.

6. Tricord Systems, Inc. (CIK No. 837166) is a forfeited Delaware corporation located in Plymouth, Minnesota with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Tricord 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, 2002, which reported a net loss of $10,753 for the prior six months.

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 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.

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, 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

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60566 / August 25, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3037 / August 25, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13599

In the Matter of **HOWARD I. SMITH, 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 Howard I. Smith ("Respondent" or "Smith") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

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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.

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)(3)(i) 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. Smith, age 64, is a resident of Woodbury, New York. Smith is a certified public accountant licensed to practice in the State of New York, but his license is not currently active. He served as chief financial officer of American International Group, Inc. ("AIG") from 1996 until his termination in March 2005.

2. AIG was, at all relevant times, a Delaware corporation with its principal place of business in New York, NY. At all relevant times, AIG was a holding company that, through its subsidiaries was engaged in a broad range of insurance and insurance-related activities in the United States and abroad. AIG's common stock is registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and is listed on the New York Stock Exchange.

3. On August 7, 2009, a final judgment was entered against Smith, on consent, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933 and 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 controlling any person who violates 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 <u>Securities and Exchange Commission v. Maurice R. Greenberg, et al.</u>, Civil Action Number 09 Civ. 6939 (LAP), in the United States District Court for the Southern District of New York. Smith also was ordered to pay $750,000 in disgorgement and a $750,000 civil money penalty. He also was 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 three years from the date of entry of the judgment.

4. The Commission's complaint alleged, among other things, that Smith and AIG's former chairman and chief executive officer directed several different accounting transactions to materially affect AIG's reported financial results. The transactions

affected multiple reporting periods when Smith and the former chairman and chief executive officer were at the company. The complaint also alleges that Smith, as AIG's chief financial officer, was aware of transactions that enabled AIG to create the inaccurate impression that it met or exceeded expectations for certain key financial measures, and that he knew or recklessly disregarded that AIG's accounting for these transactions was not in conformity with generally accepted accounting principles. The complaint also alleges that during the period that AIG's financial results were misstated, AIG distributed its stock in connection with its acquisition of American General Corporation to that company's stockholders, and that Smith signed a registration statement for this distribution that incorporated by reference AIG financial statements containing misstated financial results that Smith also signed. The complaint also alleges that Smith falsified or caused to be falsified books, records, or accounts of AIG that were subject to Section 13(b)(2)(A) of the Exchange Act; that he made materially false or misleading statements or omissions to an accountant in connection with (i) audits, reviews, or examinations of the financial statements of AIG required to be made pursuant to Commission regulations, and (ii) the preparation or filing by AIG of documents and reports required to be filed with the Commission; and that he certified annual and quarterly reports of AIG that contained misstated financial results.

IV.

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

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

A. Smith 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.

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

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 25, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13598

In the Matter of **Pacific International Enterprises, Inc.,** **Paradise Holdings, Inc.,** **PC-EPhone, Inc.,** **Phoenix Laser Systems, Inc.,** **Phoenix Resources Technologies, Inc., and** **Pilot Network Services, 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 Pacific International Enterprises, Inc., Paradise Holdings, Inc., PC-EPhone, Inc., Phoenix Laser Systems, Inc., Phoenix Resources Technologies, Inc., and Pilot Network Services, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Pacific International Enterprises, Inc. (CIK No. 855359) is a permanently revoked Nevada corporation located in Los Alamitos, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Pacific International 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, 1997, which reported a net loss of over $5.7 million from the company's inception on February 28, 1995. On September 7, 1999, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Central District of California, which was converted to Chapter 7 on May 3, 2001, and the case was terminated on November 30, 2001. As of August 14, 2009, the company's stock (symbol "PCIEQ") was traded on the over-the-counter markets.

2. Paradise Holdings, Inc. (CIK No. 920528) is a void Delaware corporation located in Sacramento, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Paradise Holdings 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 March 31, 1998, which reported a net loss of $6.89 million for the prior twelve months. On August 21, 1998, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Eastern District of California, which was converted to Chapter 7 on July 5, 2000, and the case was terminated on August 26, 2004.

3. PC-EPhone, Inc. (CIK No. 1066651) is a permanently revoked Nevada corporation located in San Diego, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). PC-EPhone 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, 2002, which reported a net loss of over $8.27 million for the prior three months. As of August 14, 2009, the company's stock (symbol "PCPH") was traded on the over-the-counter markets.

4. Phoenix Laser Systems, Inc. (CIK No. 848102) is a void Delaware corporation located in San Jose, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phoenix Laser 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, 1994, which reported a net loss of over $113 million since its December 30, 1987 inception. On December 4, 1995, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the District of Delaware, and the case was terminated on October 30, 2008. As of August 14, 2009, the company's stock (symbol "PXSY") was traded on the over-the-counter markets.

5. Phoenix Resources Technologies, Inc. (CIK No. 808575) is a revoked Nevada corporation located in San Jose, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Phoenix Resources 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 31, 2000, which reported a net loss of over $4.8 million for the prior nine months. As of August 14, 2009, the company's stock (symbol "PRTI") was traded on the over-the-counter markets.

6. Pilot Network Services, Inc. (CIK No. 1063921) is a void Delaware corporation located in Alameda, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Pilot Network 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 December 31, 2000, which reported a net loss of over $24 million for the prior nine months. On May 1, 2001, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Northern District of California, which was still pending as of August 14, 2009. As of August 14, 2009, the company's stock (symbol "PILTQ"") 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 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 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
Pacific International Enterprises, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Pacific International Enterprises, Inc					
	10-KSB	12/31/97	03/31/98	Not filed	137
	10-QSB	03/31/98	05/15/98	Not filed	135
	10-QSB	06/30/98	08/14/98	Not filed	132
	10-QSB	09/30/98	11/16/98	Not filed	129
	10-KSB	12/31/98	03/31/99	Not filed	125
	10-QSB	03/31/99	05/17/99	Not filed	123
	10-QSB	06/30/99	08/16/99	Not filed	120
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	
Total Filings Delinquent	47				
Paradise Holdings, Inc.					
	10-Q	06/30/98	08/14/98	Not filed	132
	10-Q	09/30/98	11/16/98	Not filed	129
	10-Q	12/31/98	02/16/99	Not filed	126
	10-K	03/31/99	06/29/99	Not filed	122
	10-Q	06/30/99	08/16/99	Not filed	120
	10-Q	09/30/99	11/15/99	Not filed	117
	10-Q	12/31/99	02/14/00	Not filed	114
	10-K	03/31/00	06/29/00	Not filed	110
	10-Q	06/30/00	08/14/00	Not filed	108
	10-Q	09/30/00	11/14/00	Not filed	105
	10-Q	12/31/00	02/14/01	Not filed	102
	10-K	03/31/01	06/29/01	Not filed	98
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-Q	12/31/01	02/14/02	Not filed	90
	10-K	03/31/02	07/01/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-Q	12/31/02	02/14/03	Not filed	78
	10-K	03/31/03	06/30/03	Not filed	74
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	12/31/03	02/17/04	Not filed	66
	10-K	03/31/04	06/29/04	Not filed	62
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-Q	12/31/04	02/14/05	Not filed	54
	10-K	03/31/05	06/29/05	Not filed	50
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-Q	12/31/05	02/14/06	Not filed	42
	10-K	03/31/06	06/29/06	Not filed	38
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-Q	12/31/06	02/14/07	Not filed	30
	10-K	03/31/07	06/29/07	Not filed	26
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/30/07	11/14/07	Not filed	21
	10-Q	12/31/07	02/14/08	Not filed	18
	10-K	03/31/08	06/30/08	Not filed	14
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-Q	12/31/08	02/17/09	Not filed	6
	10-K	03/31/09	06/29/09	Not filed	2
	10-Q	06/30/09	08/14/09	Not filed	
Total Filings Delinquent	**45**				
PC-EPhone, Inc.					
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	
Total Filings Delinquent	**28**				
Phoenix Laser Systems, Inc.					
	10-K	12/31/94	03/31/95	Not filed	173
	10-Q	03/31/95	05/15/95	Not filed	171
	10-Q	06/30/95	08/14/95	Not filed	168
	10-Q	09/30/95	11/14/95	Not filed	165
	10-K	12/31/95	04/01/96	Not filed	160
	10-Q	03/31/96	05/15/96	Not filed	159
	10-Q	06/30/96	08/14/96	Not filed	156
	10-Q	09/30/96	11/14/96	Not filed	153
	10-K	12/31/96	03/31/97	Not filed	149
	10-Q	03/31/97	05/15/97	Not filed	147
	10-Q	06/30/97	08/14/97	Not filed	144
	10-Q	09/30/97	11/14/97	Not filed	141
	10-K	12/31/97	03/31/98	Not filed	137
	10-Q	03/31/98	05/15/98	Not filed	135
	10-Q	06/30/98	08/14/98	Not filed	132
	10-Q	09/30/98	11/16/98	Not filed	129
	10-K	12/31/98	03/31/99	Not filed	125
	10-Q	03/31/99	05/17/99	Not filed	123
	10-Q	06/30/99	08/16/99	Not filed	120

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-Q	09/30/99	11/15/99	Not filed	117
	10-K	12/31/99	03/30/00	Not filed	113
	10-Q	03/31/00	05/15/00	Not filed	111
	10-Q	06/30/00	08/14/00	Not filed	108
	10-Q	09/30/00	11/14/00	Not filed	105
	10-K	12/31/00	04/02/01	Not filed	100
	10-Q	03/31/01	05/15/01	Not filed	99
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-K	12/31/01	04/01/02	Not filed	88
	10-Q	03/31/02	05/15/02	Not filed	87
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-K	12/31/02	03/31/03	Not filed	77
	10-Q	03/31/03	05/15/03	Not filed	75
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69
	10-K	12/31/03	03/30/04	Not filed	65
	10-Q	03/31/04	05/17/04	Not filed	63
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-K	12/31/04	03/31/05	Not filed	53
	10-Q	03/31/05	05/16/05	Not filed	51
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-K	12/31/05	03/31/06	Not filed	41
	10-Q	03/31/06	05/15/06	Not filed	39
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-K	12/31/06	04/02/07	Not filed	28
	10-Q	03/31/07	05/15/07	Not filed	27
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/30/07	11/14/07	Not filed	21
	10-K	12/31/07	03/31/08	Not filed	17
	10-Q	03/31/08	05/15/08	Not filed	15
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-K	12/31/08	03/31/09	Not filed	5
	10-Q	03/31/09	05/15/09	Not filed	3
	10-Q	06/30/09	08/14/09	Not filed	

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Total Filings Delinquent	59				
Phoenix Resources Technologies, Inc.					
	10-KSB	10/31/00	01/29/01	Not filed	103
	10-QSB	01/31/01	03/19/01	Not filed	101
	10-QSB	04/30/01	06/14/01	Not filed	98
	10-QSB	07/31/01	09/14/01	Not filed	95
	10-KSB	10/31/01	01/29/02	Not filed	91
	10-QSB	01/31/02	03/18/02	Not filed	89
	10-QSB	04/30/02	06/14/02	Not filed	86
	10-QSB	07/31/02	09/16/02	Not filed	83
	10-KSB	10/31/02	01/29/03	Not filed	79
	10-QSB	01/31/03	03/17/03	Not filed	77
	10-QSB	04/30/03	06/16/03	Not filed	74
	10-QSB	07/31/03	09/15/03	Not filed	71
	10-KSB	10/31/03	01/29/04	Not filed	67
	10-QSB	01/31/04	03/16/04	Not filed	65
	10-QSB	04/30/04	06/14/04	Not filed	62
	10-QSB	07/31/04	09/14/04	Not filed	59
	10-KSB	10/31/04	01/31/05	Not filed	55
	10-QSB	01/31/05	03/17/05	Not filed	53
	10-QSB	04/30/05	06/14/05	Not filed	50
	10-QSB	07/31/05	09/14/05	Not filed	47
	10-KSB	10/31/05	01/30/06	Not filed	43
	10-QSB	01/31/06	03/17/06	Not filed	41
	10-QSB	04/30/06	06/14/06	Not filed	38
	10-QSB	07/31/06	09/14/06	Not filed	35
	10-KSB	10/31/06	01/29/07	Not filed	31
	10-QSB	01/31/07	03/19/07	Not filed	29
	10-QSB	04/30/07	06/14/07	Not filed	26
	10-QSB	07/31/07	09/14/07	Not filed	23
	10-KSB	10/31/07	01/29/08	Not filed	19
	10-QSB	01/31/08	03/17/08	Not filed	17
	10-QSB	04/30/08	06/16/08	Not filed	14
	10-QSB	07/31/08	09/15/08	Not filed	11
	10-KSB	10/31/08	01/29/09	Not filed	7
	*10-Q**	01/31/09	03/17/09	Not filed	5

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	*10-Q**	04/30/09	06/15/09	Not filed	2
Total Filings Delinquent	35				
Pilot Network Services, Inc.					
	10-K	03/31/01	06/29/01	Not filed	98
	10-Q	06/30/01	08/14/01	Not filed	96
	10-Q	09/30/01	11/14/01	Not filed	93
	10-Q	12/31/01	02/14/02	Not filed	90
	10-K	03/31/02	07/01/02	Not filed	85
	10-Q	06/30/02	08/14/02	Not filed	84
	10-Q	09/30/02	11/14/02	Not filed	81
	10-Q	12/31/02	02/14/03	Not filed	78
	10-K	03/31/03	06/30/03	Not filed	74
	10-Q	06/30/03	08/14/03	Not filed	72
	10-Q	09/30/03	11/14/03	Not filed	69
	10-Q	12/31/03	02/17/04	Not filed	66
	10-K	03/31/04	06/29/04	Not filed	62
	10-Q	06/30/04	08/16/04	Not filed	60
	10-Q	09/30/04	11/15/04	Not filed	57
	10-Q	12/31/04	02/14/05	Not filed	54
	10-K	03/31/05	06/29/05	Not filed	50
	10-Q	06/30/05	08/15/05	Not filed	48
	10-Q	09/30/05	11/14/05	Not filed	45
	10-Q	12/31/05	02/14/06	Not filed	42
	10-K	03/31/06	06/29/06	Not filed	38
	10-Q	06/30/06	08/14/06	Not filed	36
	10-Q	09/30/06	11/14/06	Not filed	33
	10-Q	12/31/06	02/14/07	Not filed	30
	10-K	03/31/07	06/29/07	Not filed	26
	10-Q	06/30/07	08/14/07	Not filed	24
	10-Q	09/30/07	11/14/07	Not filed	21
	10-Q	12/31/07	02/14/08	Not filed	18
	10-K	03/31/08	06/30/08	Not filed	14
	10-Q	06/30/08	08/14/08	Not filed	12
	10-Q	09/30/08	11/14/08	Not filed	9
	10-Q	12/31/08	02/17/09	Not filed	6

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
	10-K	03/31/09	06/29/09	Not filed	2
	10-Q	06/30/09	08/14/09	Not filed	

Total Filings Delinquent 34

*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 Paredes not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60567 / August 25, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-12631

In the Matter of	)	
	)	**ORDER APPOINTING A**
Morgan Stanley & Co.	)	**PLAN ADMINISTRATOR**
Incorporated,	)	**AND WAIVING BOND**
	)	
Respondent.	)	

On May 9, 2007, the Securities and Exchange Commission ("Commission") issued a settled Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 against Morgan Stanley & Co. Incorporated ("MS & Co.") for failing to seek to obtain best execution for certain orders for over-the-counter securities placed by retail customers of MS & Co., MS & Co.'s broker-dealer affiliate and third-party broker-dealers that routed orders to MS & Co. for execution. (See Exchange Act Rel. No. 34-55726). Pursuant to the Order, MS & Co., among other things, paid a total of $6,457,200 in disgorgement and prejudgment interest to the Commission and selected Elizabeth Coley, President and Chief Executive Officer of ComplianceRx LLC, as an Independent Distribution Consultant ("IDC"), to develop a distribution plan for the distribution of disgorgement and interest (the "Disgorgement Fund"). Since then, the IDC has developed a proposed distribution plan (the "Distribution Plan") in consultation with the staff and MS & Co.

In accordance with the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1100, *et seq.*, the Distribution Plan proposes a Plan Administrator and sets forth, among other things, procedures for the distribution of proceeds to funds or shareholders of funds; procedures for the administration of Disgorgement Fund, including provisions for filing tax returns; and a proposed timeframe for the termination of the Distribution Plan.

Rust Consulting, Inc., proposed in the Plan as the Plan Administrator, has not posted the bond generally required of third parties under Fair Fund Rule 1105(c). Rather, the Plan incorporates several layers of protection for the Disgorgement Fund. Among other things, under the Plan: (1) the Plan Administrator will have no custody, and only limited control, of the Disgorgement Fund; (2) the Disgorgement Fund will be held by the U.S. Treasury Bureau of Public Debt until the funds are transferred to the Escrow Bank[1] immediately before transmittal of checks or electronic transfers to eligible investors; (3) upon transfer from the U.S. Treasury, funds will be held in an escrow account, separate from the Escrow Bank's assets until presentation of a check or electronic transfer, at which time funds will be transferred to a controlled distribution account; (4) presented checks or electronic transfers will be subject to "positive pay" controls before being honored by the Escrow Bank; and (5) both the Escrow Bank and the Plan Administrator will maintain, throughout this process, insurance and/or a financial institution bond that covers errors and omissions, misfeasance and fraud.

Accordingly, IT IS HEREBY ORDERED that:

A. Pursuant to the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1105(a), Rust Consulting, Inc. is appointed as Plan Administrator; and

B. The bond requirement of Rule 1105(c) of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1105(c), is waived for good cause shown.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

[1] The "Escrow Bank" refers to Deutsche Bank as defined in paragraph 16 and described in paragraph 20 of the Distribution Plan.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60575 / August 26, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3038 / August 26, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13600

In the Matter of **L. Daniel Ferrer, 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 L. Daniel Ferrer ("Respondent" or "Ferrer") 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 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.

II.

In anticipation of the institution of these proceedings, Ferrer 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, Ferrer 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 Ferrer's Offer, the Commission finds that:

1. L. Daniel Ferrer ("Respondent" or "Ferrer") is an attorney licensed to practice law in the State of Florida. Ferrer was outside counsel for Weida Communications, Inc. during all times relevant to this Complaint. He lives in Fort Lauderdale, Florida where his practice has included, among other things, representing clients in securities-related matters before the SEC and the NASD.

2. Weida Communications, Inc. ("Weida" or "company") was a New Jersey corporation which was headquartered in Fort Lauderdale, Florida at all times relevant to this Complaint. Weida marketed itself as providing ground-based transmitters and receivers that purportedly allowed corporate and government customers to use satellite communications in China. During the relevant period, Weida's common stock was registered with the Commission under Section 12(g) of the Exchange Act and traded on the Over-the-Counter Bulletin Board (OTC Bulletin Board) under the symbol WDAC. On December 30, 2005, Weida announced that it had no effective interest in the China operations it had previously claimed to control. On March 29, 2006, Weida filed a voluntary petition for relief under Chapter 7 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Northern District of Ohio.

3. On August 3, 2009, a final judgment was entered against Ferrer, permanently enjoining him from future violations of Sections 10(b) of the Exchange Act and Rule 10b-5 thereunder in the civil action entitled Securities and Exchange Commission v. L. Daniel Ferrer, Civil Action Number 09-CV-61154, in the United States District Court for the Southern District of Florida. Ferrer was also barred from participating in an offering of penny stock.

4. As alleged in the complaint, from at least June 2004 through April 2005, two stock promoters who controlled Weida, and closely affiliated stock brokers acting at their direction, engaged in a scheme to defraud which included manipulating and supporting the market price for Weida common stock at artificially high levels. During this period, the stock price, as a consequence of the manipulation, allegedly did not accurately reflect the legitimate forces of supply and demand in a free and open market for the stock. As further alleged in the complaint, two of the goals of the promoters of the manipulative scheme were facilitating the sale of Weida

stock in private transactions at prices higher than the stock was actually worth, and attempting to satisfy the NASDAQ National Market's (now known as NASDAQ Global Market) listing requirements, which mandated that the stock must trade at $5 per share over a given time period to be eligible for listing. Approximately 165 investors — many elderly and unsophisticated — allegedly paid approximately $9.2 million to Weida for near-worthless unregistered securities during the manipulation period as part of private offerings orchestrated by the promoters.

5. As further alleged in the complaint, in furtherance of this scheme, Ferrer and one of the promoters used two brokerage accounts which Ferrer established in his own name and that of his law firm to execute transactions in Weida common stock on the open market. These transactions in Weida stock executed in Ferrer's accounts were alleged to have fraudulently supported the price of Weida stock at artificially inflated levels and given the false appearance of liquidity in the market for Weida stock.

IV.

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

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

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60576 / August 27, 2009

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3039/ August 27, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13601

In the Matter of **JERRY F. WELLS, JR.,** **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 Jerry F. Wells, Jr. ("Respondent" or "Wells") 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. Wells, age 46, is a certified public accountant licensed to practice in the State of South Carolina. Wells worked as a Senior Manager and consultant for PricewaterhouseCoopers LLP from 1985 until he was hired by UCI Medical Affiliates, Inc. ("UCI" or the "Company") in February 1995 as Executive Vice President and Chief Financial Officer. Wells worked in those capacities until he was terminated by the Company in December 2008.

2. UCI was, at all relevant times, a Delaware corporation with its principal place of business in Columbia, South Carolina. The Company was engaged in the business of providing nonmedical management and administrative services for a network of freestanding medical centers located in South Carolina and Tennessee. At all relevant times, UCI'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 OTC Bulletin Board.

3. On July 6, 2009, the Commission filed a complaint against Wells in SEC v. Jerry F. Wells, Jr. (Civil Action No. 3:09-CV-01792-MJP). On July 7, 2009, the court entered an order permanently enjoining Wells, by consent, from future violations of Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5, 13b2-1, 13b2-2 and 13a-14 thereunder, and from aiding and abetting any violation 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. Wells was also ordered, on consent, to be prohibited 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 complaint alleged, among other things, that between approximately 2003 and 2008, Wells fraudulently obtained more than $2.9 million from the Company by misusing UCI's expense reimbursement process and corporate credit card to pay his personal expenses and otherwise orchestrating unapproved, improper payments by the Company for his personal benefit. In addition, the complaint alleged that, in an effort to conceal

his misconduct, Wells also knowingly caused the Company to record these illicit payments as legitimate business expenses and asset purchases and thereby materially misrepresented its financial performance. As a result of his actions, UCI filed materially false and misleading financial information for its quarterly and annual reports during the period in question.

IV.

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

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

August 28, 2009

IN THE MATTER OF	:	
BROOKE CORPORATION	:	ORDER OF SUSPENSION
	:	OF TRADING
File No. 500-1	:	

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Brooke Corporation because it has not filed any periodic reports with the Commission since the period ended June 30, 2008.

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 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, August 28, 2009 through 11:59 p.m. EDT, on September 11, 2009.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 28, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13603

In the Matter of **BROOKE CORPORATION and BROOKE CAPITAL CORPORATION,** **Respondents.**	**ORDER INSTITUTING 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 Brooke Corporation and Brooke Capital Corporation.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Brooke Corporation ("Brooke"), a Kansas corporation with its principal place of business in Overland Park, Kansas, is a holding company for entities that franchise insurance agencies, provide franchisees with financing, and repackage and sell franchisee loans to third party financial institutions. Brooke filed a petition for Chapter 11 bankruptcy on October 28, 2008, and has ceased almost all of its business operations. Brooke's common stock is registered with the Commission pursuant to Section 12(g) of the Exchange Act. Brooke's stock was quoted through the National Association of Securities Dealers Automated Quotation System until October 23, 2008. Brooke's stock is currently quoted through the Pink Sheets operated by Pink OTC Markets Inc.

2. Brooke Capital Corporation ("Brooke Capital"), a Kansas corporation with its principal place of business in Overland Park, Kansas, franchises insurance agencies. Brooke Capital filed a petition for Chapter 11 bankruptcy on October 28, 2008, and has ceased almost all of its business operations. Brooke Capital's common stock is registered with the Commission pursuant to Section 12(g) of the Exchange Act. Brooke Capital's stock traded on the American Stock Exchange until October 23, 2008. Brooke Capital's stock is currently traded through the inter-dealer market, also known as the grey market.

B. DELINQUENT PERIODIC FILINGS

3. Brooke is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed its Form 10-Q for the quarter ended June 30, 2008. Brooke has not filed an Annual Report on Form 10-K for its fiscal year ending December 31, 2008, or periodic or quarterly reports on Form 10-Q for any fiscal period subsequent to its fiscal quarter ending June 30, 2008.

4. Brooke Capital is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed its Form 10-Q for the quarter ended June 30, 2008. Brooke Capital has not filed an Annual Report on Form 10-K for its fiscal year ending December 31, 2008, or periodic or quarterly reports on Form 10-Q for any fiscal period subsequent to its fiscal quarter ending June 30, 2008.

5. 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. Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

6. 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 hereof 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 to revoke the registration of each class of securities of the Respondents identified in Section II hereof 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 twenty (20) 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 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

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60580 / August 28, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13602

In the Matter of **ALERITAS CAPITAL CORP.,** **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 Aleritas Capital Corp. ("Aleritas" 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 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. Aleritas, a Delaware corporation with its principal place of business in Overland Park, Kansas, provides insurance franchisees with financing, and repackages and sells franchisee loans to third party financial institutions. Aleritas has ceased almost all of its business operations. Aleritas' units (consisting of one share of common stock and two warrants to purchase shares of common stock), common stock, and warrants to purchase shares of common stock are registered with the Commission pursuant to Section 12(g) of the Exchange Act. Aleritas' units, common stock, and warrants are currently quoted on the Pink Sheets managed by Pink OTC Markets Inc.

B. Aleritas has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder, while its securities were registered with the Commission, in that it has not filed an Annual Report on Form 10-K for its fiscal year ending December 31, 2008, or periodic or quarterly reports on Form 10-Q for any fiscal period subsequent to its fiscal quarter ending June 30, 2008.

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.

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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.

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
Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 28, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13605

In the Matter of **Value Merchants, Inc.,** **Varner Technologies, Inc.** **(f/k/a Peppermill Capital Corp.),** **Veronex Technologies, Inc.,** **ViaGrafix Corp., and** **Viapay Limited** **(f/k/a Interface e.com, 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 Value Merchants, Inc., Varner Technologies, Inc. (f/k/a Peppermill Capital Corp.), Veronex Technologies, Inc., ViaGrafix Corp., and Viapay Limited (f/k/a Interface e.com, Inc.).

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Value Merchants, Inc. (CIK No. 814228) is a delinquent Wisconsin corporation located in Milwaukee, Wisconsin with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Value Merchants 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 October 28, 1995, which reported a net loss of $6,570,000 for the prior seventeen weeks. On December 13, 1993, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Eastern District of Wisconsin, and the case was terminated on July 9, 2002.

2. Varner Technologies, Inc. (f/k/a Peppermill Capital Corp.) (CIK No. 1063653) is a revoked Nevada corporation located in Chesterfield, Missouri with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g).

Varner 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 September 30, 2001, which reported a net loss of $1,447,861 for the prior nine months.

3. Veronex Technologies, Inc. (CIK No. 781894) is a British Columbia corporation located in Vancouver, British Columbia, Canada with a class of equity securities registered with the Commission pursuant to Exchange Act Section 12(g). Veronex Technologies is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F/A for the period ended February 28, 1999.

4. ViaGrafix Corp. (CIK No. 1051556) is a dissolved Oklahoma corporation located in Pryor, Oklahoma with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). ViaGrafix 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, 1999, which reported a net loss of $1,261,000 for the prior six months. On July 23, 2003, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Delaware, and the case was terminated on September 7, 2004.

5. Viapay Limited (f/k/a Interface e.com, Inc.) (CIK No. 1084373) is a permanently revoked Nevada corporation located in Longford, Heathrow, Great Britain with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Viapay 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 March 31, 2001, which reported a net loss of $2,187,835 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 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

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Attachment

Appendix 1

Chart of Delinquent Filings
Value Merchants, Inc., et al.

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Value Merchants, Inc.					
	10-K	02/03/96	5/3/96	Not filed	159
	10-Q	04/27/96	6/11/96	Not filed	158
	10-Q	08/03/96	9/17/96	Not filed	155
	10-Q	11/02/96	12/17/96	Not filed	152
	10-K	02/01/97	5/2/97	Not filed	147
	10-Q	05/03/97	6/17/97	Not filed	146
	10-Q	08/02/97	9/16/97	Not filed	143
	10-Q	11/01/97	12/16/97	Not filed	140
	10-K	01/31/98	5/1/98	Not filed	135
	10-Q	05/02/98	6/16/98	Not filed	134
	10-Q	08/01/98	9/15/98	Not filed	131
	10-Q	10/31/98	12/15/98	Not filed	128
	10-K	01/30/99	4/30/99	Not filed	124
	10-Q	05/01/99	6/15/99	Not filed	122
	10-Q	07/31/99	9/14/99	Not filed	119
	10-Q	10/30/99	12/14/99	Not filed	116
	10-K	01/29/00	4/28/00	Not filed	112
	10-Q	04/29/00	6/13/00	Not filed	110
	10-Q	07/29/00	9/12/00	Not filed	107
	10-Q	10/28/00	12/12/00	Not filed	104
	10-K	02/03/01	5/4/01	Not filed	99
	10-Q	04/28/01	6/12/01	Not filed	98
	10-Q	07/28/01	9/11/01	Not filed	95
	10-Q	11/03/01	12/18/01	Not filed	92
	10-K	02/02/02	5/3/02	Not filed	87
	10-Q	04/27/02	6/11/02	Not filed	86
	10-Q	08/03/02	9/17/02	Not filed	83
	10-Q	11/02/02	12/17/02	Not filed	80
	10-K	02/01/03	5/2/03	Not filed	75
	10-Q	05/03/03	6/17/03	Not filed	74
	10-Q	08/02/03	9/16/03	Not filed	71
	10-Q	11/01/03	12/16/03	Not filed	68
	10-K	01/31/04	4/30/04	Not filed	64

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Value Merchants, Inc.					
	10-Q	05/01/04	6/15/04	Not filed	62
	10-Q	07/31/04	9/14/04	Not filed	59
	10-Q	10/30/04	12/14/04	Not filed	56
	10-K	01/29/05	4/29/05	Not filed	52
	10-Q	04/30/05	6/14/05	Not filed	50
	10-Q	07/30/05	9/13/05	Not filed	47
	10-Q	10/29/05	12/13/05	Not filed	44
	10-K	01/28/06	4/28/06	Not filed	40
	10-Q	04/29/06	6/13/06	Not filed	38
	10-Q	07/29/06	9/12/06	Not filed	35
	10-Q	10/28/06	12/12/06	Not filed	32
	10-K	02/03/07	5/4/07	Not filed	27
	10-Q	04/28/07	6/12/07	Not filed	26
	10-Q	07/28/07	9/11/07	Not filed	23
	10-Q	11/03/07	12/18/07	Not filed	20
	10-K	02/02/08	5/2/08	Not filed	15
	10-Q	05/03/08	6/17/08	Not filed	14
	10-Q	08/02/08	9/16/08	Not filed	11
	10-Q	11/03/08	12/18/08	Not filed	8
	10-K	01/31/09	3/17/09	Not filed	5
	10-Q	05/02/09	6/16/09	Not filed	2
Total Filings Delinquent	**54**				
Varner Technologies, Inc. (f/k/a Peppermill Capital Corp.)					
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Varner Technologies, Inc. (f/k/a Peppermill Capital Corp.)					
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	0
Total Filings Delinquent	**31**				
Veronex Technologies, Inc.					
	20-F	02/28/00	08/28/00	Not filed	108
	20-F	02/28/01	8/28/01	Not filed	96
	20-F	02/28/02	8/28/02	Not filed	84
	20-F	02/28/03	8/28/03	Not filed	72
	20-F	02/28/04	8/30/04	Not filed	60
	20-F	02/28/05	8/29/05	Not filed	48
	20-F	02/28/06	8/28/06	Not filed	36

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Veronex Technologies, Inc.					
	20-F	02/28/07	8/28/07	Not filed	24
	20-F	02/28/08	8/28/08	Not filed	12
Total Filings Delinquent	**9**				
ViaGrafix Corp.					
	10-QSB	09/30/99	11/15/99	Not filed	117
	10-KSB	12/31/99	03/30/00	Not filed	113
	10-QSB	03/31/00	05/15/00	Not filed	111
	10-QSB	06/30/00	08/14/00	Not filed	108
	10-QSB	09/30/00	11/14/00	Not filed	105
	10-KSB	12/31/00	04/02/01	Not filed	100
	10-QSB	03/31/01	05/15/01	Not filed	99
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
ViaGrafix Corp.					
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	0
Total Filings Delinquent	**40**				
Viapay Limited (f/k/a Interface e.com, Inc.)					
	10-QSB	06/30/01	08/14/01	Not filed	96
	10-QSB	09/30/01	11/14/01	Not filed	93
	10-KSB	12/31/01	04/01/02	Not filed	88
	10-QSB	03/31/02	05/15/02	Not filed	87
	10-QSB	06/30/02	08/14/02	Not filed	84
	10-QSB	09/30/02	11/14/02	Not filed	81
	10-KSB	12/31/02	03/31/03	Not filed	77
	10-QSB	03/31/03	05/15/03	Not filed	75
	10-QSB	06/30/03	08/14/03	Not filed	72
	10-QSB	09/30/03	11/14/03	Not filed	69
	10-KSB	12/31/03	03/30/04	Not filed	65
	10-QSB	03/31/04	05/17/04	Not filed	63
	10-QSB	06/30/04	08/16/04	Not filed	60
	10-QSB	09/30/04	11/15/04	Not filed	57
	10-KSB	12/31/04	03/31/05	Not filed	53
	10-QSB	03/31/05	05/16/05	Not filed	51
	10-QSB	06/30/05	08/15/05	Not filed	48
	10-QSB	09/30/05	11/14/05	Not filed	45
	10-KSB	12/31/05	03/31/06	Not filed	41
	10-QSB	03/31/06	05/15/06	Not filed	39
	10-QSB	06/30/06	08/14/06	Not filed	36
	10-QSB	09/30/06	11/14/06	Not filed	33
	10-KSB	12/31/06	04/02/07	Not filed	28

Company Name	Form Type	Period Ended	Due Date	Date Received	Months Delinquent (rounded up)
Viapay Limited (f/k/a Interface e.com, Inc.)					
	10-QSB	03/31/07	05/15/07	Not filed	27
	10-QSB	06/30/07	08/14/07	Not filed	24
	10-QSB	09/30/07	11/14/07	Not filed	21
	10-KSB	12/31/07	03/31/08	Not filed	17
	*10-Q**	03/31/08	05/15/08	Not filed	15
	*10-Q**	06/30/08	08/14/08	Not filed	12
	*10-Q**	09/30/08	11/14/08	Not filed	9
	*10-K**	12/31/08	03/31/09	Not filed	5
	*10-Q**	03/31/09	05/15/09	Not filed	3
	*10-Q**	06/30/09	08/14/09	Not filed	0

Total Filings Delinquent **33**

* 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.