

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 63672 / January 7, 2011**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 3132 / January 7, 2011**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-14176**

**In the Matter of**

**FONTANA CAPITAL, LLC AND  
FORREST FONTANA**

**Respondents.**

**ORDER INSTITUTING  
ADMINISTRATIVE AND CEASE-AND-  
DESIST PROCEEDINGS PURSUANT TO  
SECTION 21C OF THE SECURITIES  
EXCHANGE ACT OF 1934, AND  
SECTIONS 203(e) AND 203(f) OF THE  
INVESTMENT ADVISERS ACT OF 1940**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), and Sections 203(e) and 203(f) of the Investment Advisers Act of 1940 (“Advisers Act”) against Fontana Capital, LLC (“Fontana Capital”) and Forrest Fontana (“Fontana”) (collectively, the “Respondents”).

**II.**

After an investigation, the Division of Enforcement alleges that:

**A. RESPONDENTS**

1. Fontana Capital is a limited liability company incorporated in Delaware in January 2005. At all relevant times, its principal place of business was in Boston, Massachusetts. Fontana Capital was registered with the Commission as an investment adviser from November 29, 2004 until it withdrew its registration effective April 28, 2010. During the

relevant times, Fontana Capital was, directly or indirectly, the investment adviser to Fontana Capital Long Short Fund L.P., Fontana Capital Enhanced Long Short Fund, L.P., Fontana Capital Fund QP, L.P., Fontana Capital Long Short Offshore Fund, Ltd. and Fontana Capital Enhanced Long Short Offshore Fund, Ltd.

2. Fontana is the sole owner of Fontana Capital. He served as the firm's Chief Investment Officer and portfolio manager from the firm's inception until April 2010. He is currently one of two remaining employees at Fontana Capital. At all relevant times, Fontana made all investment decisions for Fontana Capital.

#### B. OTHER RELEVANT ENTITIES

1. XL Group PLC ("XL Group") is a holding company domiciled in Ireland. XL Group's stock is registered pursuant to Section 12(b) of the Exchange Act and listed on the New York Stock Exchange and the Bermuda Stock Exchange. XL Group is a global insurance and reinsurance company. XL Group was at all relevant times known as XL Capital Ltd. ("XL Capital"). The company changed its name to XL Group effective July 1, 2010.

2. Merrill Lynch and Company ("Merrill Lynch") was at all relevant times a financial services company headquartered in New York, New York and registered with the Commission as a broker-dealer. Merrill Lynch's stock was at all relevant times registered pursuant to Section 12(b) of the Exchange Act and listed on the New York Stock Exchange. Merrill Lynch is now a wholly owned subsidiary of Bank of America Corporation.

3. Wells Fargo and Company ("Wells Fargo") is a financial services company headquartered in San Francisco, California. Wells Fargo's stock is registered pursuant to Section 12(b) of the Exchange Act and listed on the New York Stock Exchange.

#### C. RESPONDENTS' PARTICIPATION IN FOLLOW-ON OFFERINGS

1. Rule 105 of Regulation M of the Exchange Act provides, in pertinent part:

In connection with an offering of equity securities for cash pursuant to a registration statement . . . filed under the Securities Act of 1933 ("offered securities"), it shall be unlawful for any person to sell short . . . the security that is the subject of the offering and purchase the offered securities from an underwriter or broker or dealer participating in the offering if such short sale was effected during the period ("Rule 105 restricted period") that is the shorter of the period: (1) Beginning five business days before the pricing of the offered securities; or (2) Beginning with the initial filing of such registration statement . . . and ending with the pricing.

17 C.F.R. § 242.105(a)(1) and (a)(2) (effective October 9, 2007)

2. Rule 105 of Regulation M is designed to protect the independent pricing mechanism of the securities market shortly before follow-on or secondary offerings.<sup>1</sup>

3. During the relevant period, Respondents violated Rule 105 with respect to three follow-on offerings, involving XL Capital, Merrill Lynch and Wells Fargo, resulting in unlawful profits of approximately \$1,101,000.

4. On Friday, July 25, 2008, Fontana Capital, at Fontana's direction, sold short a total of 60,000 XL Capital shares at \$18.98 per share.

5. On Monday, July 28, 2008, XL Capital stock closed at \$18.37. On Tuesday, July 29, 2008, before the trading markets opened, XL Capital priced a follow-on offering of its securities at \$16 per share (the "XL Capital Offering"). The registered shares were offered to the public through an underwriter on a firm-commitment basis. Accordingly, the Rule 105 restricted period was from Tuesday, July 22, 2008 through Monday, July 28, 2008.

6. On Tuesday, July 29, 2008, Fontana Capital, at Fontana's direction, purchased 50,000 shares in the XL Capital Offering. Fontana Capital realized a profit of approximately \$149,000 by participating in the XL Capital Offering after having shorted XL Capital's stock during the Rule 105 restricted period.

7. On Friday, July 25, 2008, Fontana Capital, at Fontana's direction, sold short a total of 40,000 Merrill Lynch shares at \$27.30 per share.

8. On Monday, July 28, 2008, Merrill Lynch's stock closed at \$25.31. On Tuesday, July 29, 2008, before the trading markets opened, Merrill Lynch priced a follow-on offering of its securities at \$22.50 per share (the "Merrill Lynch Offering"). The registered shares were offered to the public through an underwriter on a firm-commitment basis. Accordingly, the Rule 105 restricted period was from Tuesday, July 22, 2008 through Monday, July 28, 2008.

9. On Tuesday, July 29, 2008, Fontana Capital, at Fontana's direction, purchased 200,000 Merrill Lynch shares in the Merrill Lynch Offering. Fontana Capital realized a profit of approximately \$792,000 by participating in the Merrill Lynch offering after having shorted Merrill Lynch's stock during the Rule 105 restricted period.

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<sup>1</sup> "The first time an issuer conducts a public offering of its securities, the offering is referred to as an initial public offering ("IPO"). Subsequent offerings by the issuer are referred to as follow-on offerings or repeat offerings. A secondary offering is an offering of securities held by security holders, for which there already exist trading markets for the same class of securities as those being offered." Short Selling in Connection With a Public Offering, 17 Fed. Reg. 75,002, 75,003 n. 12 (December 13, 2006).

10. On Thursday, November 6, 2008, Fontana Capital, at Fontana's direction, sold short a total of 100,000 Wells Fargo shares at \$28.60. That day, Wells Fargo stock closed at \$28.77.

11. After the close of the trading markets on Thursday, November 6, 2008, Wells Fargo priced a follow-on offering of its securities at \$27 per share (the Wells Fargo Offering"). The registered shares were offered to the public through an underwriter on a firm-commitment basis. Accordingly, the Rule 105 restricted period was from Friday October 31, 2008 through Thursday November 6, 2008.

12. On Friday, November 7, 2008, Fontana Capital, at Fontana's direction, purchased 100,000 shares in the Wells Fargo Offering. As a result, Fontana Capital realized a profit of approximately \$160,000 by participating in the Wells Fargo offering, after having shorted Wells Fargo's stock during the Rule 105 restricted period.

#### D. VIOLATIONS

As a result of the conduct described above, Fontana Capital and Fontana willfully committed violations of Rule 105 of Regulation M.

### III.

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

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

B. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Sections 203(e) and 203(f) of the Advisers Act including, but not limited to, disgorgement under Section 203(j) of the Advisers Act and penalties pursuant to Section 203(i) of the Advisers Act; and

C. Whether, pursuant to Section 21C of the Exchange Act Respondents should be ordered to cease and desist from committing or causing violations of and any future violations of Rule 105 of Regulation M of the Exchange Act and whether Respondents should be ordered to pay disgorgement pursuant to Section 21C(e) of the Exchange Act.

### IV.

IT IS ORDERED that a public hearing for the purposes of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge

to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

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

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

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

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

Service List

Rule 141 of the Commission's Rules of Practice provides that the Secretary, or another duly authorized officer of the Commission, shall serve a copy of the Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, and Sections 203(e) and 203(f) of the Investment Advisers Act of 1940 ("Order"), on the Respondents and their legal agent.

The attached Order has been sent to the following parties and other persons entitled to notice:

Honorable Brenda P. Murray  
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