

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 64839 / July 8, 2011

INVESTMENT ADVISERS ACT OF 1940
Release No. 3233 / July 8, 2011

ADMINISTRATIVE PROCEEDING
File No. 3-14176

In the Matter of

**FONTANA CAPITAL, LLC AND
FORREST FONTANA**

Respondents.

**ORDER MAKING FINDINGS AND
IMPOSING REMEDIAL SANCTIONS
AND A CEASE-AND-DESIST ORDER
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.

On January 7, 2011, the Securities and Exchange Commission (“Commission”) instituted administrative and cease-and-desist proceedings 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.

In response to these proceedings, Respondents have submitted Offers of Settlement (“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 Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order 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 as to Fontana Capital, LLC and Forrest Fontana (“Order”) as set forth below.

III.

On the basis of this Order and the Respondents' Offers, the Commission finds that:

Summary

These proceedings arise out of violations of Rule 105 of Regulation M of the Exchange Act by Fontana Capital and Fontana. Fontana Capital was at all relevant times, the investment adviser to as many as five hedge funds. On three occasions from July 2008 through November 2008, Fontana Capital and Fontana violated Rule 105 of Regulation M by participating in public offerings by XL Group PLC ("XL Group"), Merrill Lynch and Company ("Merrill Lynch") and Wells Fargo and Company ("Wells Fargo") after having shorted each of these securities during the five business days prior to the pricing of the offerings. By participating in these offerings, Fontana Capital obtained profits of \$816,184.

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. The firm does not presently have any revenues.

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 Fontana Capital's only employee. Fontana, 45 years old, is a resident of Winchester, Massachusetts.

Other Relevant Entities

3. 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.

4. 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.

5. 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.

Respondents' Participation in Follow-on Offerings

6. 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)

7. Rule 105 of Regulation M is designed to protect the independent pricing mechanism of the securities market shortly before follow-on or secondary offerings. Rule 105 is prophylactic and prohibits the conduct irrespective of the short seller’s intent. Pursuant to amendments that became effective in October 2007, it is not required that the shares purchased in the offering be used to “cover” the restricted period short sales. Short Selling in Connection with a Public Offering, Rel. No. 34-56206, 72 Fed. Reg. 45094 (August 10, 2007) (effective October 9, 2007).

8. On Friday, July 25, 2008, hedge funds advised by Fontana Capital, at Fontana’s direction, sold short a total of 60,000 XL Capital shares at \$18.98 per share.

9. 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.

10. On Tuesday, July 29, 2008, hedge funds advised by Fontana Capital, at Fontana’s direction, purchased 50,000 shares in the XL Capital Offering. Fontana Capital did not “cover” its short position in XL Capital’s stock with the shares bought in the offering. Fontana Capital realized a profit of \$149,000 by participating in the XL Capital Offering after having shorted XL Capital’s stock during the Rule 105 restricted period.

11. On Friday, July 25, 2008, hedge funds advised by Fontana Capital, at Fontana’s direction, sold short a total of 40,000 Merrill Lynch shares at \$27.30 per share.

12. 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.

13. On Tuesday, July 29, 2008, hedge funds advised by Fontana Capital, at Fontana's direction, purchased 200,000 Merrill Lynch shares in the Merrill Lynch Offering. Fontana Capital did not "cover" its short position in Merrill Lynch's stock with the shares bought in the offering. Fontana Capital realized a profit of \$507,184 by participating in the Merrill Lynch offering after having shorted Merrill Lynch's stock during the Rule 105 restricted period.

14. On Thursday, November 6, 2008, hedge funds advised by 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.

15. 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.

16. On Friday, November 7, 2008, hedge funds advised by Fontana Capital, at Fontana's direction, purchased 100,000 shares in the Wells Fargo Offering. Fontana Capital did not "cover" its short position in Wells Fargo's stock with the shares bought in the offering. Fontana Capital realized a profit of \$160,000 by participating in the Wells Fargo offering, after having shorted Wells Fargo's stock during the Rule 105 restricted period.

Violations

17. As a result of the conduct described above, Fontana Capital and Fontana willfully¹ committed violations of Rule 105 of Regulation M.

IV.

On the basis 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 Section 21C of the Exchange Act and Sections 203(e) and 203(f) of the Advisers Act, it is hereby ORDERED that:

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

A. Respondent Fontana Capital shall cease and desist from committing or causing any violations and any future violations of Rule 105 of Regulation M under the Exchange Act.

B. Respondent Fontana shall cease and desist from committing or causing any violations and any future violations of Rule 105 of Regulation M under the Exchange Act.

C. Respondent Fontana Capital is censured.

D. Respondent Fontana is censured.

E. Respondents shall, jointly and severally, pay disgorgement of \$816,184, prejudgment interest of \$3,606 and a civil penalty of \$165,000 to the United States Treasury. Payment shall be made in the following installments: \$196,958 within thirty (30) days of the entry of this Order and \$787,832 plus accrued post-judgment interest of \$1,590 or a total second payment of \$789,422 within one year of the entry of this Order. If payment is not made by the date the payment is required by this Order, the entire outstanding balance of disgorgement, prejudgment interest, and civil penalty, plus any additional interest accrued pursuant to SEC Rule of Practice 600 or pursuant to 31 U.S.C. § 3717, shall be due and payable immediately, without further application. Payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Securities and Exchange Commission, Office of Financial Management, 100 F. Street, NE, Stop 6042, Washington, DC 20549; and (D) submitted under cover letter that identifies Fontana Capital LLC and Forrest N. Fontana as Respondents in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to John T. Dugan, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, Boston Regional Office, 33 Arch Street, 23rd Floor, Boston, MA 02210.

By the Commission.

Elizabeth M. Murphy
Secretary