

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

**SECURITIES ACT OF 1933**

**Release No. 8556 / March 23, 2005**

**SECURITIES EXCHANGE ACT OF 1934**

**Release No. 51414 / March 23, 2005**

**ADMINISTRATIVE PROCEEDING**

**File No. 3-11867**

**In the Matter of**

**Capital Analysts Incorporated,**

**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 Capital Analysts, Incorporated (“CAI”).

**II.**

In anticipation of the institution of these proceedings, CAI 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, CAI 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 CAI’s Offer, the Commission finds that:

#### **Respondent**

1. Capital Analysts Incorporated has been registered with the Commission as a broker-dealer since 1968. CAI, a Delaware corporation, is headquartered in Radnor, Pennsylvania. All shares of CAI are held by CAI Holding Company, Inc.

#### **Overview**

2. From at least January 1, 2002 through December 31, 2003, CAI sold the funds of the mutual fund complexes participating in its revenue sharing program, called the Product Sponsor Tier Program (“Tier Program”), without fully disclosing material information to its customers regarding the program.

3. Under its Tier Program, CAI provided participating mutual fund complexes increased access to and visibility within CAI’s retail distribution network in exchange for compensation in the form of preferred marketing payments. However, CAI, in violation of Section 17(a)(2) of the Securities Act and Rule 10b-10 under the Exchange Act, failed to adequately disclose to its customers the existence of this program and the conflict of interest created by these payments.

#### **CAI’s Tier Program**

4. CAI charged each mutual fund complex participating in its Tier Program an annual fee, which increased for each Tier: \$10,000 for the Bronze Tier; \$20,000 for the Silver Tier, \$34,000 for the Gold Tier and \$45,000 for the Platinum Tier. In exchange for these fees, CAI provided the participants in each Tier with certain benefits.

5. In general, CAI provided those mutual fund complexes which paid the highest fees, as was the case for participants in the Platinum Tier, with the most benefits. These benefits, which were intended to increase a fund complex’s visibility or “shelf-space” within CAI’s retail network, included: increased access to branch offices; hyper-links and banner ads on CAI’s webpage; agenda space at CAI sales meetings and conference calls; publication in CAI’s newsletters; access to members of CAI’s “Circle of Excellence;”<sup>1</sup> and the opportunity to sponsor promotional/informational events and seminars for CAI’s registered representatives. CAI provided those participants in the Gold, Silver and Bronze Tiers with similar benefits, but reduced the number and level of those benefits in proportion to the reduced annual fees for each

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<sup>1</sup> The “Circle of Excellence” was composed of CAI’s top-producing registered representatives.

Tier. CAI did not provide any financial incentives to its sales force to promote the products of one mutual fund complex over another.

6. Although CAI had selling agreements with several hundred mutual fund complexes, only 11 to 15 complexes participated in the Tier Program each year. Based on various criteria, including past relationships or expressions of interest, CAI decided which mutual fund complexes were solicited and accepted into the program. Once CAI and the mutual fund complexes reached an agreement on the level of participation (Platinum, Gold, Silver or Bronze), CAI sent each mutual fund complex an invoice for the annual fee. The mutual fund complexes paid their fees almost exclusively by check or wire transfer. CAI accepted directed brokerage as payment in two instances, but has since terminated that practice.

### **CAI Failed Adequately to Disclose the Tier Program to its Customers**

7. From at least January 1, 2002 through December 31, 2003, CAI failed to adequately disclose to its mutual fund customers the existence of the Tier Program and the amounts of preferred marketing payments which CAI received from the mutual fund complexes whose products CAI, through its registered representatives, recommended and sold.

8. CAI disclosed information to its mutual fund customers through its registered representatives' direct contacts with customers and through the prospectuses and, if requested, statements of additional information ("SAIs") issued by the mutual fund complexes. However, CAI did not have any policies or procedures requiring its registered representatives to disclose to their customers the existence of the Tier Program and it was not the practice of the registered representatives to do so.

9. Instead, CAI relied on the disclosures in the mutual fund prospectuses and SAIs to satisfy its disclosure obligations regarding the Tier Program and the preferred marketing payments. While some of these documents contained various disclosures regarding payments to the broker-dealers distributing their funds, most of these disclosures were vague and lacked sufficient information to inform CAI's customers of the nature and scope of CAI's revenue sharing program. For example, these prospectuses and SAIs failed to disclose adequate information about the amounts of the preferred marketing payments or that certain fund complexes had greater access to, or increased visibility in, CAI's retail network. As a result, CAI customers were not provided with sufficient information to appreciate the dimension of the conflict of interest created by the revenue sharing program.

10. Based on the above-described conduct, CAI willfully violated:

a. Section 17(a)(2) of the Securities Act, which provides that it is "unlawful for any person in the offer or sale of any securities . . . by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly . . . to obtain money or property by means of any untrue statement of a material fact or any omission 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;” and

b. Rule 10b-10 under the Exchange Act, which provides in pertinent part that “it shall be unlawful for any broker or dealer to effect for or with an account of a customer any transaction in, or to induce the purchase or sale by such customer of, any security . . . unless such broker or dealer, at or before completion of such transaction, gives or sends to such customer written notification disclosing . . . the source and amount of any other remuneration received or to be received by the broker in connection with the transaction.”

### **Undertakings**

11. CAI undertakes the following:

a. CAI shall place and maintain on its website within 15 days from the date of entry of the Order disclosures regarding its Tier Program to include, if applicable: (i) the existence of the program; (ii) the fund complexes participating in the program; (iii) the estimated amount of payment that CAI is to receive from a fund complex in connection with the program; and (iv) the source of such payments. CAI shall make this information available via a hyperlink on the home page of its website.

b. CAI shall retain, within 45 days from the date of entry of the Order, the services of an Independent Consultant, who is not unacceptable to the Commission’s Staff. CAI shall require the Independent Consultant to perform all of the services and tasks described below. CAI shall exclusively bear all costs, including compensation and expenses, associated with the retention and performance of the Independent Consultant.

c. CAI shall retain and shall require the Independent Consultant to conduct a comprehensive review of: (i) the completeness of the disclosures regarding CAI’s Tier Program; and (ii) the policies and procedures relating to CAI’s recommendations to its customers of the mutual funds in its revenue sharing program. CAI shall retain the Independent Consultant to recommend policies and procedures that address deficiencies, if any, in these areas.

d. CAI shall further retain and shall require the Independent Consultant to prepare and, within 90 days from the date of entry of the Order, submit to CAI and the Commission’s Staff an Initial Report. The Initial Report shall address, at a minimum: (i) the adequacy of the disclosures regarding CAI’s Tier Program; and (ii) the adequacy of the policies and procedures regarding CAI’s recommendations and disclosures to its customers of the mutual funds in its Tier Program. The Initial Report must include a description of the review performed, the conclusions reached, and the Independent Consultant's recommendations for policies and

procedures to address any deficiencies identified, an effective system for implementing the recommended policies and procedures and an effective system for establishing and maintaining written records that evidence compliance with the recommended policies and procedures.

e. Within 100 days from the date of entry of the Order, CAI shall in writing advise the Independent Consultant and the Commission's Staff of the recommendations from the Initial Report that it is adopting and the recommendations that it considers to be unnecessary or inappropriate. With respect to any recommendation that CAI considers unnecessary or inappropriate, CAI shall explain why the objective or purpose of such recommendation is unnecessary or inappropriate and provide in writing an alternative policy, procedure or system designed to achieve the same objective or purpose.

f. With respect to any recommendation with which CAI and the Independent Consultant do not agree, CAI shall attempt in good faith to reach an agreement with the Independent Consultant within 120 days from the date of entry of the Order. In the event the Independent Consultant and CAI are unable to agree on an alternative proposal acceptable to the Commission's Staff, CAI shall abide by the recommendation of the Independent Consultant.

g. CAI shall further retain and shall require the Independent Consultant to complete the aforementioned review and submit a written Final Report to CAI and to the Commission's Staff within 140 days from the date of entry of the Order. The Final Report must recite the efforts the Independent Consultant undertook to review: (i) CAI's disclosures regarding its Tier Program; and (ii) the policies and procedures regarding CAI's recommendations and disclosures to its customers of the mutual funds in its Tier Program. The Final Report shall also set forth in detail the Independent Consultant's recommendations and a reasonable time period(s), not to exceed 180 days from the date of entry of the Order, for CAI to implement its recommendations. The Final Report must also describe how CAI proposes to implement those recommendations within the time period(s) set forth in the Final Report.

h. CAI shall take all necessary and appropriate steps to adopt and implement all recommendations and proposals contained in the Independent Consultant's Final Report.

i. To ensure the independence of the Independent Consultant, CAI : (i) shall not have the authority to terminate the Independent Consultant, without the prior written approval of the Commission's Staff; (ii) shall compensate the Independent Consultant, and persons engaged to assist the Independent Consultant, for services rendered pursuant to the Order at their reasonable and customary rates; and (iii) shall not be in and shall not have an attorney-client relationship with the Independent Consultant and shall not seek to invoke the attorney-client or any other

doctrine or privilege to prevent the Independent Consultant from transmitting any information, reports or documents to the Commission or the Commission's Staff.

j. To further ensure the independence of the Independent Consultant, for the period of the engagement and for a period of two years from completion of the engagement, CAI, its present or former affiliates, directors, officers, employees, and agents acting in their capacity shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Independent Consultant. Further, CAI, its present or former affiliates, directors, officers, employees, and agents acting in their capacity shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with any firm with which the Independent Consultant is affiliated in the performance of his or her duties under the Order, or agents acting in their capacity, for the period of the engagement and for a period of two years after the engagement without prior written consent of the Commission's Staff.

k. CAI shall cooperate fully with the Independent Consultant and shall provide the Independent Consultant with prompt access to CAI's files, books, records and personnel as the Independent Consultant reasonably deems necessary or appropriate in fulfilling any function or completing any task described in these undertakings.

l. For good cause shown, and upon receipt of a timely application from the Independent Consultant or CAI, the Commission's Staff may extend any of the procedural dates set forth above.

#### IV.

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

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

A. CAI shall cease and desist from committing or causing any violations and any future violations of Section 17(a)(2) of the Securities Act and Rule 10b-10 under the Exchange Act;

B. CAI is censured;

C. CAI shall, within 30 days from the date of entry of the Order, pay disgorgement and prejudgment interest in the total amount of \$350,000 to the United States Treasury. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Alexandria, Stop 0-3, VA 22312; and (D) submitted

under cover letter that identifies CAI 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 Arthur S. Gabinet, Securities and Exchange Commission, Mellon Independence Center, 701 Market St., Suite 2000, Philadelphia, PA 19106;

D. CAI shall, within 30 days from the date of entry of the Order, pay a civil money penalty in the amount of \$100,000 to the United States Treasury. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies CAI's 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 Arthur S. Gabinet, Securities and Exchange Commission, Mellon Independence Center, 701 Market St., Suite 2000, Philadelphia, PA 19106; and

E. CAI shall comply with the undertakings enumerated in Section III.11. above.

By the Commission.

Jonathan G. Katz  
Secretary