

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 61039A / November 20, 2009

Admin. Proc. File No. 3-12753

In the Matter of

JOSEPH JOHN VANCOOK

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and

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OPINION OF THE COMMISSION

BROKER-DEALER PROCEEDING

CEASE-AND-DESIST PROCEEDING

Grounds for Remedial Action

Fraud

Aiding and Abetting and Causing Recordkeeping Violations

Salesperson associated with registered broker-dealer willfully violated Section 10(b) of the Securities Exchange Act of 1934 and Exchange Act Rule 10b-5 by committing deceptive acts as part of a scheme to defraud and misrepresenting material facts in order to facilitate his clients' illegal trading activity in shares of certain registered investment companies; salesperson also aided and abetted and caused broker-dealer's failure to keep accurate books and records in violation of Section 17(a)(1) of the Exchange Act and Rule 17a-3(a)(6) thereunder. *Held*, it is in the public interest to bar Respondent from

associating with any broker or dealer, to impose a cease-and-desist order, to order disgorgement of \$533,234.01, plus prejudgment interest, and to assess a \$100,000 civil penalty.

APPEARANCES:

Lewis D. Lowenfels, Esq., of Law Offices of Tolins & Lowenfels, and *Michael J. Sullivan*, of Coughlin Duffy LLP, for Joseph John VanCook.

William P. Hicks, Robert K. Gordon, and Yolanda L. Ross, for the Division of Enforcement.

Appeal filed: July 21, 2008

Last brief received: December 3, 2008

Oral argument: July 20, 2009

I.

Joseph John VanCook, a former salesperson and partial owner of Pritchard Capital Partners, LLC ("Pritchard Capital" or the "Firm"), a registered broker-dealer, appeals an administrative law judge's decision.¹ The law judge found that VanCook willfully violated Section 10(b) of the Securities Exchange Act of 1934² and Exchange Act Rule 10b-5³ by orchestrating a fraudulent scheme involving material misrepresentations to permit his clients to late trade⁴ shares of certain registered investment companies. The law judge also found that VanCook aided and abetted and willfully caused the Firm's clearing broker to violate Rule 22c-1

¹ In connection with the conduct at issue in this proceeding, Pritchard Capital consented, without admitting or denying any findings, to the entry of our order finding that it willfully violated Section 17(a)(1) of the Securities Exchange Act of 1934 and Exchange Act Rule 17a-3(a)(6) for failing to make and keep current certain books and records, that it willfully aided and abetted and caused its clearing broker to violate Rule 22c-1 of the Investment Company Act of 1940, and that it failed reasonably to supervise VanCook with a view to preventing his willful violation of the federal securities laws. *Pritchard Capital Partners, LLC*, Securities Exchange Act Rel. No. 57704 (Apr. 23, 2008), 93 SEC Docket 5304, 5309-10.

² 15 U.S.C. § 78j(b).

³ 17 C.F.R. § 240.10b-5.

⁴ See *infra* Section II.A for a discussion of late trading.

of the Investment Company Act of 1940.⁵ The law judge further found that VanCook aided and abetted and willfully caused the Firm to violate Exchange Act Section 17(a)(1) and Exchange Act Rule 17a-3(a)(6) by failing to make and keep current certain books and records.⁶ The law judge barred VanCook from association with any broker or dealer or investment company, imposed a cease-and-desist order against him, ordered disgorgement of \$538,565.70, plus prejudgment interest, and assessed a \$100,000 third-tier civil money penalty. We base our findings on an independent review of the record, except with respect to those findings not challenged on appeal.

II.

A. Late Trading of Mutual Funds

Orders to buy and sell mutual fund shares can be submitted all day. The price of a mutual fund share is based on its net asset value ("NAV"). The NAV is the current market value of a mutual fund's total assets, minus its total liabilities, divided by the total number of shares outstanding. Mutual funds generally calculate the NAV once a day,⁷ usually at or as of when the major United States stock exchanges close at 4:00 p.m. Eastern time.⁸ Mutual funds typically disclose in their prospectuses the time when the NAV is computed. The prospectuses of mutual funds traded by Pritchard Capital's clients at issue disclosed that the funds calculated the NAV "at" or "as of" the close of regular trading on the New York Stock Exchange ("NYSE"), normally 4:00 p.m. Consistent with Investment Company Act Rule 22c-1, which requires a mutual fund

⁵ 17 C.F.R. § 270.22c-1.

⁶ 15 U.S.C. § 78q(a)(1); 17 C.F.R. § 240.17a-3(a)(6).

⁷ See 17 C.F.R. § 270.22c-1(b)(1) (generally requiring mutual funds to calculate their NAVs at least once daily, Monday through Friday, but providing for certain exceptions).

⁸ See, e.g., *DH2, Inc. v. SEC*, 422 F.3d 591, 592 (7th Cir. 2005) (stating that a mutual fund's NAV is "generally fixed by a fund when the major U.S. stock markets close at 4:00 p.m. eastern time"); *SEC v. Simpson Capital Mgmt., Inc.*, 586 F. Supp. 2d 196, 199 (S.D.N.Y. 2008) (stating that "[t]he prices of mutual fund shares are not continually reset over the course of the day, but are typically fixed for an entire day at a single price. Mutual funds . . . generally determine the NAV of mutual fund shares at the close of the major United States securities exchanges and markets – 4:00 p.m. [Eastern time]."); *Disclosure Regarding Market Timing and Selective Disclosure of Portfolio Holdings*, Securities Act Rel. No. 8343 (Dec. 11, 2003), 81 SEC Docket 2971, 2976 (stating that, "[t]ypically, mutual funds calculate their NAVs once each day at or near the close of the major U.S. securities exchanges and markets (usually 4:00 p.m., Eastern time)"). All times referenced in this opinion are Eastern time.

trading order to be priced at the "next computed" NAV,⁹ the prospectuses stated that orders had to be received by 4:00 p.m. in order to be executed at that day's NAV. The prospectuses further stated that the time of receipt of an order by a mutual fund intermediary, rather than by the mutual fund itself, was the time for determining the price that the order would receive.¹⁰

"Late trading" refers to the unlawful practice of permitting mutual fund orders received after the 4:00 p.m. pricing time to receive the NAV calculated at or as of 4:00 p.m. that day, instead of 4:00 p.m. the following trading day.¹¹ Late trading enables the trader to profit from

⁹ See 17 C.F.R. § 270.22c-1(a) (providing that "[n]o registered investment company issuing any redeemable security, no person designated in such issuer's prospectus as authorized to consummate transactions in any such security, and no principal underwriter of, or dealer in, any such security shall sell, redeem, or repurchase any such security except at a price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security").

¹⁰ See *Amendments to Rules Governing Pricing of Mutual Fund Shares*, Investment Company Act Rel. No. 26288 (Dec. 11, 2003), 81 SEC Docket 3177, 3179 (stating that under Investment Company Act Rule 22c-1 mutual fund orders must be submitted to dealers and other intermediaries by 4:00 p.m. in order to receive the current day's share price); *Staff Interpretive Positions Relating to Rule 22c-1*, Investment Co. Act Rel. No. 5569 (Jan. 9, 1969), 1969 WL 96373, at *1 (stating that Investment Company Act Rule 22c-1 "contemplates that the time of receipt of the order by the retail dealer is controlling" for determining the price that it receives).

The evidence as to when the mutual funds at issue calculated the NAV is based on a Division exhibit prepared by the Division's expert witness. The expert witness explained at the hearing that the exhibit is a summary of the relevant prospectus language for eighty percent of the funds at issue (the threshold for inclusion appears to have been prospectuses of non-money market funds with at least twenty-five transactions executed on behalf of the clients at issue) gathered from registration statements filed with the Commission. VanCook has not objected to the use of or reliance on this exhibit as representing the pricing practices of all the funds at issue in this proceeding.

¹¹ See, e.g., *SEC v. Pentagon Capital Mgmt. PLC*, 612 F. Supp. 2d 241, 248 (S.D.N.Y. 2009) (stating that late trading "refers to the practice of placing orders to buy, redeem or exchange U.S. mutual fund shares after the time as of which the funds calculate their NAV, but receiving the price based on the prior day's NAV"); *In re Mut. Funds Inv. Litig.*, 384 F. Supp. 2d 845, 852 n.1 (D. Md. 2005) (stating that late trading is the "practice of placing orders to buy or sell mutual fund shares after 4:00 p.m. ET [Eastern Time], but receiving the price based on the prior NAV already determined as of 4:00 p.m. that same day") & *id.* at 856 (holding that "[l]ate trading is itself illegal, and therefore, as alleged by plaintiffs, a scheme, practice, or course of business effectuating late trading is inherently fraudulent"); *Scott G. Monson*, Investment Co. Act (continued...)

market events, such as earnings announcements and futures trading, that occur after 4:00 p.m. but are not reflected in the current day's NAV.¹² The late trader obtains an advantage, at the expense of other shareholders of the mutual fund, when he learns of market-moving information and is able to buy, exchange, or sell mutual fund shares at NAVs set before the market-moving information is released.¹³ Late trading violates the "forward pricing rule" set forth in Investment Company Act Rule 22c-1,¹⁴ which requires the price of mutual fund shares to be set at the NAV

¹¹ (...continued)

Rel. No. 28323 (June 30, 2008), 93 SEC Docket 7517, 7518 n.2 (stating that "[t]he illegal practice of permitting a purchase or redemption order received after the fund calculates its NAV (typically 4:00 p.m. Eastern Time) to receive the same day's NAV is referred to as 'late trading'"); *Charles C. Fawcett*, Exchange Act Rel. No. 56770 (Nov. 8, 2007), 91 SEC Docket 3147, 3148-49 n.4 ("Late trading is the illegal practice of permitting a purchase or redemption order received after the 4:00 p.m. pricing time to receive the share price calculated as of 4:00 p.m. that day." (internal quotations and citation omitted)).

¹² See *Amendments to Rules Governing Pricing of Mutual Fund Shares*, 81 SEC Docket at 3177.

¹³ *Id.*

¹⁴ 17 C.F.R. § 270.22c-1(a). Rule 22c-1's primary purpose is to prevent dilution-based abuses related to "backward pricing," the practice of basing the price of a mutual fund share on the NAV determined as of the close of the markets on the previous day. See, e.g., *Adoption of Rule 22c-1 under the Investment Company Act of 1940 Prescribing the Time of Pricing Redeemable Securities for Distribution, Redemption, and Repurchase and Amendment of Rule 17a-3(a)(7) under the Securities Exchange Act of 1934 Requiring Dealers to Time-Stamp Orders*, Investment Co. Act Rel. No. 5519 (Oct. 16, 1968), 1968 WL 87057; see also, e.g., *United States v. NASD*, 422 U.S. 694, 707 (1975) (explaining that the "interim period" between the calculation of a mutual fund's closing price on the previous day and the next-day opening price based on the NAV at the current day's closing provides opportunities to engage in "riskless trading" by exploiting the price difference).

"next computed" by the fund after the receipt of an order to buy or sell shares.¹⁵ Late trading can harm innocent mutual fund shareholders by diluting the value of their investment.¹⁶

B. VanCook Joins Pritchard Capital

Joseph VanCook has been working in the securities industry since 1995. In 1996, he obtained his Series 7 and 63 licenses and became a registered representative. In early 2000, VanCook began to develop relationships with hedge funds that market timed mutual funds.¹⁷

¹⁵ Decisions interpreting Rule 22c-1 have read it to prohibit mutual fund investors from trading a fund's shares after the 4:00 p.m. pricing time while still receiving that day's NAV. *See Simpson Capital Mgmt.*, 586 F. Supp. 2d at 202 (holding that Rule 22c-1's requirement that the price of mutual fund shares be set at the NAV "next computed" by a mutual fund after the receipt of an order to buy or sell shares established that the time for setting NAV is the time "as of" which the NAV is calculated, generally 4:00 p.m., and not, as defendants argued, the time when the calculation is actually made) & *id.* at 203 (stating that defendants' interpretation of the Rule "would allow dealers to provide their customers with the same day's NAV on mutual fund trades submitted until the actual point of NAV calculation and would allow an end run around Congress's and the Commission's intent to prevent dilution of share value, speculative trading, and unfair treatment of investors"); *SEC v. JB Oxford Holdings, Inc.*, No. CV-04-7084 PA (C.D. Cal. Aug. 24, 2005) (unpublished minute order) (giving deference to Commission's interpretation of Rule 22c-1 setting the relevant "as of" time as the time that a mutual fund values its holdings for purposes of pricing mutual fund trades, rather than the time a fund actually performs its NAV calculation); *Paul A. Flynn*, Initial Decision No. 316 (Aug. 2, 2006), 88 SEC Docket 2146, 2173-74 (ALJ decision) (holding that the phrase "NAV that is next computed" means the NAV as of the time the mutual fund sets for its calculation, which is typically 4:00 p.m.), *declared final*, Exchange Act Rel. No. 54390 (Aug. 31, 2006), 88 SEC Docket 2649; *see also, e.g., Prusky v. Reliastar Life Ins. Co.*, 445 F.3d 695, 698 n.5 (3d Cir. 2006) (stating that "[t]he term 'late trading' is somewhat misleading because trading after the close of the market is entirely permissible so long as the trades are priced using the NAV set the next day. The Rule [Rule 22c-1]'s requirement that prices be based on the next computed NAV is referred to as 'forward pricing.' Thus, late trading may be more aptly described as violating the forward pricing rule.") (citations omitted); *Amendments to Rules Governing Pricing of Mutual Fund Shares*, 81 SEC Docket at 3178 (stating that "[l]ate trading not only violates [R]ule 22c-1, but managers who permit late trading also breach their fiduciary duties to the funds and fund shareholders").

¹⁶ *See Amendments to Rules Governing Pricing of Mutual Fund Shares*, 81 SEC Docket at 3181; *see also In re Mut. Funds Inv. Litig.*, 384 F. Supp. 2d at 852 n.1 (discussing plaintiffs' allegations of effects of late trading and market timing).

¹⁷ "Market timing" includes the frequent buying and selling of shares of the same mutual fund in order to exploit inefficiencies in mutual fund pricing. *Pentagon Capital Mgmt.*,
(continued...)

Pritchard Capital, a Louisiana-based broker-dealer, hired VanCook in March 2001 to open its New York branch office. Based on an understanding with Thomas Ward Pritchard,¹⁸ the Firm's majority owner, VanCook spent most of his time using his market-timing hedge fund relationships to open a new line of business for the Firm.¹⁹ Elizabeth McMahon, who was hired when the New York branch office opened in March 2001, assisted VanCook in servicing these clients and reported to him.²⁰

C. Van Cook Establishes an Order System for Late-Trading Clients

1. VanCook Changes the Firm's Clearing Broker, Enabling Him to Late Trade on Behalf of Clients

When VanCook joined Pritchard Capital, Bear Stearns was the Firm's clearing broker that transmitted orders placed by the Firm's clients to the mutual funds.²¹ Bear Stearns required that Pritchard Capital fax orders to its offices by 4:00 p.m. each day in order for the Firm's clients to

¹⁷ (...continued)

612 F. Supp. 2d at 253; *see also*, *SEC v. Ficken*, 546 F.3d 45, 48 (1st Cir. 2008) (stating that "[m]arket timing is a mutual fund share trading strategy that exploits brief discrepancies between the stock prices used to calculate the shares' value once a day, and the prices at which those stocks are actually trading" (internal quotations and citation omitted)).

¹⁸ In connection with the conduct at issue in this proceeding, Pritchard consented, without admitting or denying any findings, to the entry of our order finding that he failed reasonably to supervise VanCook with a view to preventing his willful violation of the federal securities laws. *Pritchard Capital Partners*, 93 SEC Docket at 5310.

¹⁹ VanCook eventually acquired a minority interest in the Firm. His association with Pritchard Capital ended in February 2004. Since leaving Pritchard Capital, VanCook was associated with registered broker-dealer Punk, Ziegel & Company, L.P. until May 2008, at which time he became associated with his current employer, registered broker-dealer Ladenburg Thalmann & Co., Inc.

²⁰ In connection with the conduct at issue in this proceeding, McMahon consented, without admitting or denying any findings, to the entry of our order finding that she willfully aided and abetted and caused Pritchard Capital's violation of Exchange Act Section 17(a)(1) and Exchange Act Rule 17a-3(a)(6) for failing to make and keep current certain books and records, and that she willfully aided and abetted and caused the Firm's clearing broker to violate Investment Company Act Rule 22c-1. *Pritchard Capital Partners*, 93 SEC Docket at 5310.

²¹ Pritchard Capital was an introducing broker; the Firm did not have dealer agreements with mutual funds and therefore could not directly submit its orders to the funds. Instead, the Firm contracted with a clearing broker, which had dealer agreements with mutual funds and submitted orders to the funds on the Firm's behalf.

receive that day's NAV. In late 2001, VanCook recommended that Pritchard Capital change its clearing broker from Bear Stearns to Banc of America Securities ("Banc of America"). Pritchard Capital placed client orders with Banc of America by entering them directly into a computer system called the Mutual Fund Routing System ("MFRS"). Unlike Bear Stearns' procedure that required orders to be faxed by 4:00 p.m., the Firm could enter mutual fund orders in MFRS until 5:30 p.m. and receive that day's NAV.²² VanCook acknowledged at the hearing that when he entered orders in MFRS, he expected to get the same day's NAV.

Page two of a May 2001 instructional manual on MFRS (the "Processing Guide") provided by Banc of America to the Firm stated:

All orders should be received and time stamped by the close of the NYSE 4 P.M. EST. The MFRS system allows orders that have been entered prior to 4 P.M. EST to be review [sic] until 5:15 P.M. EST.²³

Nothing in the Processing Guide stated that the review period provided additional time after the NYSE's regular trading session had closed for broker-dealers to submit new orders, or to confirm, modify, or cancel orders already submitted.

Van Cook testified that he "probably looked at the pictures and the pages that worked on order entry, but . . . never read [the Processing Guide] cover to cover." He also testified that "we never thought about [how the Processing Guide related to the time for receiving and placing orders]. This book to us was an instruction book of how to work MFRS and the system." VanCook further testified that he understood the statements in the Processing Guide to mean that he could enter orders until 5:30 p.m. regardless of whether he received an order before or after 4 p.m. Pritchard testified that he understood the statements in the Processing Guide to mean that entering orders into the MFRS until 5:30 p.m. served as the Firm's verification that it had received the order before 4:00 p.m.

VanCook did not create paper order tickets for his clients, but, upon receiving final instructions from a client, VanCook would enter the order information in MFRS and print out a snapshot of the computer screen that reflected that information. VanCook knew that MFRS provided no means for communicating to Banc of America or the relevant mutual fund the time at which a client order was actually received.

²² VanCook testified that he could not recall the "exact Bear Stearns rules," but, when asked if he would have been aware of the difference in the times by which he had to submit trades to his clearing brokers, VanCook responded, "Yeah, I guess so."

²³ Although the Processing Guide states that 5:15 p.m. was the cut-off time, the parties stipulated that it was 5:30 p.m.

2. VanCook Modifies Order System for Three Clients, Enabling Them to Late Trade

VanCook established an order system to accommodate and keep track of his market-timing clients' voluminous trading. VanCook's market-timing clients typically would e-mail or fax to VanCook a list of proposed orders, which VanCook referred to as a "trade sheet." VanCook instructed his clients to submit the proposed trade sheets, which he would time stamp upon receipt, to the Firm by 4:00 p.m. VanCook submitted an order to the relevant mutual fund company through the Firm's clearing broker only upon receiving final instructions via e-mail, fax, or telephone from a client about which trades to execute on the latest proposed trade sheet. VanCook required most of his clients to submit final instructions by 4:00 p.m.

However, VanCook does not dispute that he modified the proposed trade sheet order system for three clients by allowing them to finalize their proposed trade sheet instructions after 4:00 p.m. From November 2001 through July 2003, on behalf of these late-trading clients, VanCook, or others acting according to VanCook's instructions, executed 4,936 late trades²⁴ with approximately twenty-five mutual fund families.²⁵ As noted above, the funds' prospectuses stated that the NAV was determined at or as of 4:00 p.m. when regular trading on the NYSE closed, and that an order had to be received by the intermediary by the 4:00 p.m. close in order to obtain that day's NAV. McMahan testified that VanCook told her which clients were permitted to finalize their trading instructions after 4:00 p.m. It is undisputed that no one at the Firm time-stamped, or otherwise recorded, the time at which the Firm received these post-4:00 p.m. final trade instructions.

Goodwin Accounts. Andrew Goodwin ran numerous market-timing hedge funds over several years and learned about late-trading practices during 2000 while he was employed with Canary Capital, LLC as a vice president and senior portfolio manager. Goodwin understood the advantage of placing mutual fund orders after 4:00 p.m. and sought a trading platform that would allow him to engage in the practice.

²⁴ The number of late trades placed (4,936) does not include any proposed orders that the three hedge fund clients ultimately instructed Pritchard Capital to cancel. These canceled orders, the number of which has not been identified by the Division, was likely significant. One of VanCook's hedge fund clients testified, for example, that he cancelled seventy percent of the proposed trades he submitted to Pritchard Capital based on post-closing information.

²⁵ The record indicates that, at VanCook's direction, McMahan entered the majority (approximately one-half to two-thirds) of orders into the system, with VanCook entering approximately fifteen percent of the hedge fund clients' trades. Another Pritchard Capital employee named Keith Robinson entered the remainder, with the exception of a small number of corrections or other entries made by the staff of Banc of America for administrative ease.

VanCook met Goodwin sometime in 2001. After joining Pritchard Capital, VanCook asked Goodwin, who at the time was independently operating market-timing hedge funds, if he would be interested in opening an account at Pritchard Capital. Goodwin testified that he and VanCook discussed the details of Goodwin submitting proposed trade sheets before 4:00 p.m. and confirming which of those trades to execute after 4:00 p.m. Goodwin also testified that, during this discussion, he learned that Banc of America, with whom he had worked before, was the Firm's clearing broker and he "knew that they could handle orders . . . after 4:00 p.m." Goodwin testified that the ability to late trade was one of the services that attracted him to Pritchard Capital. According to Goodwin, VanCook stated that he was "dumbfounded" by why another client, who declined an opportunity to late trade in a fund, "couldn't perceive a way to make money with the advantage."

Beginning in February 2002, Goodwin opened several late-trading accounts with VanCook ("Goodwin accounts"). VanCook's counsel stipulated at the hearing that Goodwin regularly finalized orders after 4:00 p.m. and that either VanCook or McMahon entered those orders in MFRS to effect the trade. Goodwin testified that he finalized "probably over ninety percent" of his proposed trade sheets after 4:00 p.m., and McMahon testified that the number was closer to ninety-eight percent, occurring "usually between 4:00 p.m. and 4:45 p.m."²⁶ The Firm placed 1,828 late-trading orders on behalf of the Goodwin accounts between February 2002 and July 2003. The prospectuses of those funds stated that the NAV was determined at or as of 4:00 p.m. when regular trading on the NYSE closed, and that an order had to be received by the 4:00 p.m. close in order to obtain that day's NAV. Goodwin closed the accounts in July 2003.

Millennium Accounts. Kovan Pillai was a portfolio manager at Millennium Capital Partners, L.P. ("Millennium"), a market-timing hedge fund, from April 2001 through December 2005.²⁷ Scott Murray, an assistant portfolio manager at Millennium from June 2001 until April 2006, helped Pillai place orders. Pillai met VanCook in the summer of 2002 and told him that he market timed international mutual funds. Pillai began to open international mutual fund market-timing accounts with VanCook in October 2002.

At first, Pillai and Murray regularly submitted and finalized proposed trade sheets with VanCook by 3:30 p.m. Pillai quickly concluded that the performance in his international mutual fund market-timing accounts with VanCook was inferior to market-timing accounts he held with other firms. Pillai testified that, when he informed VanCook that he intended to close the

²⁶ Goodwin testified that the Firm processed proposed trade sheets that he sometimes submitted to the Firm after 4:00 p.m.

²⁷ In connection with their market-timing activities conducted during the period at issue, Millennium and Pillai consented, without admitting or denying any findings, to the entry of our order finding that they willfully violated Securities Act Section 17(a), Exchange Act Section 10(b), and Exchange Act Rule 10b-5. *Millennium Capital Partners, L.P.*, Securities Act Rel. No. 8639 (Dec. 1, 2005), 86 SEC Docket 2412, 2420-21.

accounts, VanCook told him "about this other business that he was doing with some other clients that was extremely profitable." Pillai testified that VanCook:

told me that you submit the orders as you always do but before 5:00 or 5:05 at the latest, if you have a change of heart, if you see something happening in the business world that would change your opinion, then you were able to bust that trade.

Murray recalled at the hearing that VanCook told him that there was a way to:

allow trades to be canceled if they were no longer desirable based on information that came out between 4:00 and however late the trades could be canceled.

Pillai testified that VanCook suggested that using this order system for domestic mutual funds would be advantageous and "told us we would get the price that we normally would get from placing the order before 4:00." Pillai viewed VanCook's comments to be an attempt to retain his business. VanCook testified, "I don't deny it happened, I don't remember the conversation. . . . My main concern was trying to keep the account and continue to do business with Millennium."

In December 2002, Pillai and Murray began to use the late-trading system outlined by VanCook with two domestic mutual fund accounts ("Millennium accounts"). According to Pillai, "we would submit scenarios in the middle of the day as we had always done and then sometime around 5:00 we would make a decision whether we wanted to take the trade or not." Pillai or Murray finalized all proposed trade sheets with VanCook or McMahon after 4:00 p.m. and cancelled approximately seventy percent of the proposed trades.

In January 2003, Pillai became concerned about the legality of his late trading and consulted Millennium's attorney, Fred Stone. Stone advised Pillai to discontinue late trading, and Pillai immediately informed VanCook about his conversation with Stone. Pillai testified that VanCook stated in response:

Kovan, I promise you I never would have dropped you in something if it was legally questionable. I'm sure your in-house counsel is being overly cautious, I'm sure he's wrong about this

Pillai testified that, at a subsequent lunch meeting, VanCook "repeated more or less what he had said earlier" and reiterated his opinion that he believed that Stone was "wrong." VanCook testified that he did not recall that Pillai told him about the conversation with Stone or that he responded as Pillai stated.

From December 2002 through January 2003, the Firm placed twenty-three late-trading orders for the Millennium accounts. The prospectuses of those mutual funds stated that the NAV was determined at or as of 4:00 p.m., when regular trading on the NYSE closed, and that an order had to be received by the 4:00 p.m. close in order to obtain that day's NAV. Pillai stopped late trading in the Millennium accounts with Pritchard Capital in January 2003.

Simpson Accounts. Robert Simpson was the director and/or managing member of a number of market-timing hedge funds on whose behalf he opened accounts with VanCook in October 2001 ("Simpson accounts").²⁸ VanCook testified that he had told Simpson that Simpson could finalize his mutual fund orders with the Firm after 4:00 p.m. VanCook's counsel stipulated at the hearing that, "calls came in from Simpson regularly after 4:00 p.m. with final directives as to what to do and that either Mr. VanCook or Ms. McMahon put those orders through to the MFRS to effect the trade." McMahon testified that final instructions regarding the Simpson accounts were received "always" after 4:00 p.m. and "almost always after 5:00 p.m."

When asked at the hearing why Simpson account orders were finalized after 4:00 p.m., McMahon explained, "they just seemed to always know that you could put trades in at Banc of America up until 5:30, and Joe said it was acceptable." The Firm placed 3,085 late-trading orders on behalf of the Simpson accounts between November 2001 and July 2003 with mutual funds whose prospectuses stated that the NAV was determined at or as of 4:00 p.m., when regular trading on the NYSE closed, and that an order had to be received by the 4:00 p.m. close in order to obtain that day's NAV.²⁹ Simpson closed the accounts in September 2003.³⁰

D. VanCook Receives Legal Advice from Pritchard Capital's Attorney to Place Orders by 4:00 p.m.

In May 2003, VanCook told Pritchard that one of VanCook's customers wanted legal advice regarding Investment Company Act Rule 22c-1, a rule with which Pritchard was

²⁸ No one testified on behalf of the Simpson accounts at the hearing.

²⁹ The Firm placed orders on behalf of the Simpson accounts through September 2003. However, because the Order Instituting Proceedings charged VanCook with violations of the securities laws only through July 2003, we do not base findings of liability on the orders placed after that date.

³⁰ In connection with the conduct at issue in this proceeding, among other things, the Division filed a complaint in the United States District Court for the Southern District of New York alleging that Simpson, his hedge fund, and another respondent engaged in an illegal late-trading scheme in violation of Exchange Act Section 10(b) and Exchange Act Rule 10b-5. That matter is currently pending. *See Simpson Capital Mgmt.*, 586 F. Supp. 2d at 208 (denying Simpson's motion to dismiss complaint). Our findings here with respect to Simpson are made solely for the purpose of the proceeding before us.

unfamiliar. According to Pritchard, VanCook generally described the rule, and Pritchard agreed to participate in a conference call with Pritchard Capital's attorney, Jay Seale, VanCook, VanCook's client, and the client's business acquaintance, who ran a hedge fund. Pritchard testified that, during the call, he and VanCook mainly listened to the others, who discussed Rule 22c-1 in general, opined that the rule applied to mutual fund companies but not salespersons, and expressed concern that a salesperson could nonetheless be liable for "aiding and abetting a dealer" if orders were placed after 4:00 p.m.

Pritchard testified that Seale told him and VanCook to "stick to 4:00 p.m.," *i.e.*, do not permit orders received after 4:00 p.m. to be entered for execution at that day's NAV, a point that Pritchard re-emphasized to VanCook. At the hearing, the Division introduced Pritchard's handwritten notes taken during the call, which state, among other things, "tentative orders during day, take verbal confirm at end of day" and "not making trade after pricing." Pritchard also testified that, at the time, he thought that "Joe being a partner, and us paying for legal advice, and the legal advice saying stick to 4:00, that both partners, Joe VanCook and Tommy Pritchard, would know that 4:00 is what you stick to."

VanCook testified that he did not recall that Rule 22c-1 was discussed during the call. Instead, VanCook testified that a 4:00 p.m. order deadline "wasn't one of the important things to me in that conversation. This piece of particular business you're talking about was \$2 million a year commission to our Firm. That's the part that I really remember, and the fact that we weren't going to do it is another part that I really remember." VanCook also testified that, at the time, Rule 22c-1 was not his "issue," "job," or "concern." Following the call, VanCook continued to allow the Goodwin and Simpson accounts to late trade.

E. VanCook Assures Pritchard that He Is Placing Orders by 4:00 p.m.

In July 2003, Pritchard became aware of the New York Attorney General's investigation into mutual fund trading practices. Pritchard testified that, at that time, he explicitly asked VanCook numerous times whether VanCook had been "letting people put trades in after 4:00 p.m." Pritchard testified that VanCook replied that he had not been and had never done so.³¹ VanCook testified that he does not remember discussing late trading with Pritchard.

F. VanCook's Perspective About the Timing of Placing Client Orders

According to VanCook, he believed that receiving and time stamping proposed trade sheets by 4:00 p.m., despite the fact that clients confirmed which trades to execute on the proposed trade sheets after 4:00 p.m., "would have satisfied any '4:00 p.m. rule.'" He testified that "it was made very clear" to him only in August or September 2003 that Rule 22c-1 prescribed the time when orders had to be placed for purposes of calculating a fund's NAV. He

³¹ It is unclear whether VanCook had stopped late trading when he responded to Pritchard's inquiries.

also testified that he did not read any of the prospectuses of the mutual funds in which his clients traded, including the language regarding when NAVs were calculated, because he "thought the most important thing was to build relationships and talk to the people that work at those fund families." In response to being asked at the hearing whether he thought it was important for him to know when mutual funds set their prices, VanCook stated, "No, we never thought about it."

The law judge found that VanCook's testimony about his lack of knowledge of late trading and Investment Company Act Rule 22c-1 was "deliberately vague" and "evasive."³² The law judge noted that testimony from Goodwin, Pillai, Murray, and Pritchard was quite specific regarding discussions with VanCook about the mechanics of late trading and the fact that it violated Rule 22c-1 and was illegal. The law judge noted further that the testimony of these witnesses was consistent, either with each other or with documentary evidence.³³ Based on the law judge's observation that VanCook's testimony was deliberately vague and evasive, and on VanCook's general experience in the securities industry, his expertise with mutual funds, his spearheading the switch to a clearing broker that accommodated post-4:00 p.m. trading decisions, and the availability of prospectuses that contained pricing deadlines, the law judge determined that it was "simply incredible that [VanCook] did not know when the mutual funds' NAVs were calculated or that he did not fully understand the application of . . . Rule 22c-1 pricing requirements to mutual fund trades."³⁴

III.

The Order Instituting Proceedings ("OIP") alleged that VanCook willfully violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5 by permitting certain of the Firm's clients to late trade mutual fund shares from November 2001 through July 2003. Exchange Act Section 10(b) and Exchange Act Rule 10b-5 "prohibit the employing of fraudulent schemes or the making of material misrepresentations and omissions in . . . purchases or sales of securities."³⁵ To establish liability under Exchange Act Section 10(b) and Exchange Act

³² See *Joseph John VanCook*, Initial Decision Rel. No. 350 (July 10, 2008), 93 SEC Docket 7686, 7699.

³³ The law judge explicitly credited the testimony of Goodwin, Pillai, and Murray. Although the law judge did not explicitly credit Pritchard's testimony, he relied upon such testimony over that of VanCook's.

³⁴ See *Joseph John VanCook*, 93 SEC Docket at 7700.

³⁵ *SEC v. Brooks*, No. Civ. A. 3:99-CV-1326-D, 1999 WL 493052, at *2 (N.D. Tex. July 12, 1999); see also 15 U.S.C. § 78j(b), 17 C.F.R. § 240.10b-5; *SEC v. Dain Rauscher, Inc.*, 254 F.3d 852, 855-56 (9th Cir. 2001) (noting that the antifraud provisions "prohibit fraudulent conduct or practices" and "forbid making a material misstatement or omission" in connection with the offer or sale of securities).

Rule 10b-5, the Division must show by a preponderance of the evidence that VanCook (1) committed a deceptive or manipulative act as part of a scheme to defraud, made an untrue statement of material fact,³⁶ or omitted to state a fact that made a prior statement misleading; (2) engaged in such conduct in connection with the purchase or sale of a security;³⁷ and (3) acted with scienter.³⁸

A. VanCook's Conduct

Deceptive Acts as Part of a Scheme to Defraud. Courts have recognized that, as a general matter, late trading of mutual fund shares can constitute a scheme to defraud.³⁹ Here, VanCook engaged in numerous deceptive acts in furtherance of the deceptive late-trading scheme. VanCook made misrepresentations in furtherance of the late-trading scheme when he, or McMahan at his direction, submitted mutual fund orders after 4:00 p.m. on behalf of the Goodwin, Millennium, and Simpson accounts for execution at that day's NAV. The submission of orders to mutual funds after the 4:00 p.m. close for execution at the current day's NAV constitutes a misrepresentation that final orders were received before the funds' 4:00 p.m. pricing time, as reflected in the applicable prospectus language.⁴⁰ The submissions created the false impression that the orders were received before 4:00 p.m. when, in fact, the trading decisions

³⁶ A fact is material if there is a substantial likelihood that a reasonable investor would have considered the misstated or omitted fact important in making an investment decision, and if disclosure of the misstated or omitted fact would have significantly altered the total mix of information available to the investor. *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988); *TSC Indus. Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *see also Wheat v. Hall*, 535 F.2d 874, 876 (5th Cir. 1976) ("[T]he test of materiality is whether a reasonable man would attach importance to the fact misrepresented [or omitted] in determining his course of action.").

³⁷ The United States Supreme Court has embraced an expansive interpretation of Exchange Act Section 10(b)'s "in connection with" language. *See, e.g., Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 85 (2006); *SEC v. Zandford*, 535 U.S. 813, 819 (2002); *United States v. Naftalin*, 441 U.S. 768, 773 (1979). VanCook does not dispute that those requirements have been met.

³⁸ *See SEC v. U.S. Env'tl., Inc.*, 155 F.3d 107, 111 (2d Cir. 1998); *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1467 (2d Cir. 1996); *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 201.

³⁹ *See Pentagon Capital Mgmt.*, 612 F. Supp. 2d at 261; *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 204-05; *In re Mut. Funds Inv. Litig.*, 384 F. Supp. 2d at 856 & n.10.

⁴⁰ *See Paul A. Flynn*, Initial Decision No. 316 (Aug. 2, 2006) (ALJ opinion) (stating that "[s]ubmitting orders to mutual funds for execution at that day's NAV is a representation that the orders were received by the intermediary prior to the fund's NAV calculation"), 88 SEC Docket 2146, 2174, *declared final*, Exchange Act Rel. No. 54390 (Aug. 31, 2006), 88 SEC Docket 2649.

were made after 4:00 p.m.⁴¹ The mutual funds therefore were deceived into thinking that the trades were made before 4:00 p.m. and into giving the trades that day's NAV.⁴²

To effectuate his clients' late trades, VanCook secured a new clearing broker for the Firm knowing that its order entry system, MFRS, provided an opportunity to place orders after 4:00 p.m. and still receive that day's NAV, unlike the Firm's previous clearing broker. VanCook also knew that MFRS provided no means for communicating to the clearing broker or the relevant mutual fund the time at which a client order was received, thereby allowing late trades to sidestep detection.

VanCook's order submissions were contrary to provisions in mutual fund prospectuses that required broker-dealers to receive trade orders "at" or "as of" 4:00 p.m. and stated that orders had to be received by 4:00 p.m. in order to be executed at that day's NAV. Although the Processing Guide provided a review period until 5:30 p.m., this was not intended to provide additional time to submit new orders, or to confirm, modify, or cancel orders already submitted, after the NYSE's regular trading session had closed. Nonetheless, VanCook permitted the Goodwin, Millennium, and Simpson accounts to finalize their proposed trade sheets after 4:00 p.m. There is no dispute that VanCook and McMahon, at his direction, placed almost 5,000 orders on behalf of these clients, who consistently finalized their proposed trade sheets after 4:00 p.m.

⁴¹ See *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 204-05 (denying motion to dismiss complaint alleging illegal late trading scheme in violation of Exchange Act Section 10(b) and Exchange Act Rule 10b-5; complaint sufficiently alleged that defendants engaged in "deceptive conduct" where their acts communicated the "false impression" to mutual funds that trades were submitted before 4:00 p.m., when in fact they were submitted with the benefit of market news after 4:00 p.m.).

⁴² *Id.* At oral argument, VanCook's counsel asserted that there was no basis to conclude that mutual funds were deceived given the lack of testimony from any mutual fund. As discussed above, we find the record amply supports a conclusion that the mutual funds were deceived based on the false impression VanCook created that the orders were received before 4:00 p.m. when in fact they were received after 4:00 p.m. As the Second Circuit Court of Appeals stated recently, "[i]n its ordinary meaning, 'deceptive' covers a wide spectrum of conduct involving cheating or trading in falsehoods." *SEC v. Dorozhko*, 574 F.3d 42, 50 (2d Cir. 2009) (citing Webster's International Dictionary, 679 (2d ed. 1934), as "defining 'deceptive' as 'tending to deceive,' and defining 'deceive' as '[t]o cause to believe the false, or to disbelieve the true' or '[t]o impose upon; to deal treacherously with; cheat"). Noting the holding of the Fifth Circuit in *Regents of the Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 389 (5th Cir. 2007), the Court concluded that "[i]n light of this ordinary meaning, it is not at all surprising that Rule 10b-5 equates 'deceit' with 'fraud.'" *Id.*

VanCook's use of proposed trade sheets was another deceptive act in furtherance of the fraudulent late-trading scheme. VanCook instructed his clients to submit the proposed trade sheets to the Firm by 4:00 p.m. so that the sheets could be time stamped before the close of trading. However, VanCook allowed these clients to finalize their proposed trades after 4:00 p.m. without creating new order tickets or otherwise documenting the confirmations and cancellations. Thus, VanCook used the time-stamped trade sheets to disguise the fact that VanCook's customers made trading decisions after the close of trading. VanCook also falsely reassured Pritchard that VanCook had not been allowing customers to place orders after 4:00 p.m. and had never done so.

Through these numerous deceptive acts, VanCook created the false impression that final orders associated with the Goodwin, Millennium, and Simpson accounts were placed before 4:00 p.m. and were therefore entitled to that day's NAV when in fact they were not.⁴³ As a result, VanCook's late-trading clients obtained an undisclosed advantage, at the expense of other shareholders of the relevant mutual funds, when they learned of market-moving information and were able to buy, exchange, or sell mutual fund shares at NAVs set before the market-moving information was released. The mutual funds at issue were deceived into providing improper prices for those orders contrary to their prospectus language and transmitting and effecting orders contrary to their published policies and procedures, as well as applicable rules and regulations, thereby harming or causing the risk of harm to shareholders who made investment decisions premised upon improper prices and suffered dilution to the value of their shares.

Materiality. The late-trading scheme in which VanCook participated was material because mutual funds and their shareholders would have wanted to know that some investors were able to benefit from trading on post-4:00 p.m. information, thereby potentially diluting the value of shareholder investments. VanCook's submission of late trades also was material because the mutual funds at issue would have wanted to know that they were transmitting and effecting orders contrary to their published policies and procedures, as well as applicable rules and regulations, such as Investment Company Act Rule 22c-1.

VanCook's Arguments. VanCook argues that he cannot be held liable under Exchange Act Rule 10b-5(a) because "the Supreme Court ended so-called 'scheme liability' as a viable Rule 10b-5 theory" with its decision in *Stoneridge Investment Partners LLC v. Scientific-Atlantic, Inc.*⁴⁴ VanCook contends that the "*Stoneridge* case makes clear that a putative violator of Rule 10b-5 must himself or herself actually trigger each element of the rule. Merely being associated with a scheme is not enough."

⁴³ See *Pentagon Capital Mgmt.*, 612 F. Supp. 2d at 261 (observing that "deceptive conduct" within the meaning of Exchange Act Section 10(b) and Exchange Act Rule 10b-5 "irreducibly entails some act that gives the victim a false impression") (citation omitted).

⁴⁴ 552 U.S. 148 (2008).

VanCook's reliance on *Stoneridge* is misplaced. VanCook's liability is based not on "merely being associated with the scheme," but on engaging in acts that were directly linked to the deception practiced upon the mutual funds at issue. VanCook was intimately involved with the creation, marketing, and implementation of the system that enabled the three clients to late trade. VanCook communicated his deceptive acts to the mutual funds at issue by submitting late-trading orders to them through the Firm's clearing broker. Moreover, in *Stoneridge*, the Supreme Court held that the defendants were not liable under Exchange Act Section 10(b) and Exchange Act Rule 10b-5 because the investor plaintiffs had not relied on the defendants' acts or statements.⁴⁵ Unlike litigants in private causes of action, however, the Division is not required to prove reliance as an element of its claim against VanCook.⁴⁶ Accordingly, we reject VanCook's contention that his conduct does not fall within the scope of the antifraud provisions.

VanCook "challenges the finding that the mere submission of the trades can be a legally cognizable materially false representation sufficient to trigger Section 10(b) and Rule 10b-5 liability." He asserts that, "[a]s the Second Circuit recognized in [*United States v.*] *Finnerty*,⁴⁷ the mere execution of a trade (even if performed with an improper purpose and even if leading to an unfair windfall) cannot be converted into a materially false representation. A mere trade not accompanied by other communications, is not a representation."

In *Finnerty*, the Court of Appeals was presented with the question of whether interpositioning, the practice of a specialist declining to match public buy and sell orders and interposing itself between the matching orders in order to generate profits for the specialist's firm, constitutes deceptive conduct. The court determined that interpositioning did not amount to deceptive conduct under Exchange Act Section 10(b) or Exchange Act Rule 10b-5 because there was "no evidence that Finnerty conveyed an impression that was misleading."⁴⁸ Here, in contrast, VanCook communicated the false impression to mutual funds that the orders were

⁴⁵ *Id.* at 769-770.

⁴⁶ *SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1363-64 (9th Cir. 1993); *SEC v. Blavin*, 760 F.2d 706, 711 (6th Cir. 1985); *SEC v. North Am. Research & Dev. Corp.*, 424 F.2d 63, 84 (2d Cir. 1970); *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 201.

⁴⁷ 533 F.3d 143 (2d Cir. 2008).

⁴⁸ *Finnerty*, 533 F.3d at 149-50.

received before 4:00 p.m., when they were, in fact, received after 4:00 p.m.⁴⁹ We find that this constitutes deceptive conduct under Exchange Act Section 10(b) and Exchange Act Rule 10b-5.

B. VanCook's Scienter

Scienter is a mental state embracing an intent to deceive, manipulate, or defraud.⁵⁰ It includes recklessness, defined as conduct which is "'highly unreasonable' and . . . represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger [of misleading the individual or entity at issue] was either known to the defendants or so obvious that the defendant must have been aware of it.'"⁵¹

VanCook had substantial experience in the securities industry, held two securities licenses, was a partial owner of the Firm, and was responsible for opening the Firm's new branch office whose sole line of business initially involved the market-timing hedge fund customers that VanCook acquired and maintained based on his previous experience. VanCook knew that his success at developing and maintaining relationships with market-timing hedge funds was critical, given that it generated his primary source of income and was the basis for Pritchard's decision to hire him. The law judge found it "simply incredible that [VanCook] did not know when the

⁴⁹ See *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 204-05 (denying motion to dismiss complaint alleging illegal late-trading scheme in violation of Exchange Act Section 10(b) and Exchange Act Rule 10b-5).

Courts also have found that submitting an order containing misleading or inaccurate information to a mutual fund can constitute a misrepresentation. See *SEC v. Druffner*, 517 F. Supp. 2d 502, 508-09 (D. Mass. 2007) (finding that salesperson's submission of orders that included modified identifying client information constituted material misrepresentations), *aff'd sub nom. SEC v. Ficken*, 546 F.3d 45 (1st Cir. 2008); *SEC v. Gann*, 2008 WL 857633, at *10 (N.D. Tex. Mar. 31, 2008) (same), *aff'd*, 565 F.3d 932 (5th Cir. 2009). VanCook also asserts that he did not make misrepresentations because neither he nor the Firm "ever sent trade sheets to Banc of America." The Division has not alleged, and we have not found, that VanCook made misrepresentations on this basis.

⁵⁰ *Hochfelder*, 425 U.S. at 193 n.12.

⁵¹ *Rolf v. Blyth, Eastman, Dillion & Co.*, 570 F.2d 38, 47 (2d Cir. 1978) (quoting *Sanders v. John Nuveen & Co.*, 554 F.2d 790, 793 (7th Cir. 1977)), *cert. denied*, 439 U.S. 1039 (1978); see also, e.g., *SEC v. Steadman*, 967 F.2d 636, 641-42 (D.C. Cir. 1992) (quoting *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977), *cert. denied*, 434 U.S. 875). Proof of scienter may be demonstrated by circumstantial evidence. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390-91 n.30 (1983); *Valicenti Advisory Servs., Inc. v. SEC*, 198 F.3d 62, 65 (2d Cir. 1999).

mutual funds' NAVs were calculated or that he did not fully understand the application of . . . Rule 22c-1 pricing requirements to mutual fund trades."⁵²

Against that backdrop, VanCook knowingly manipulated the Firm's order system to facilitate late trading, a deceptive practice whose advantage he appreciated and that enabled him to acquire and/or maintain three clients. VanCook was responsible for Pritchard Capital's switch from a clearing broker who required trades to be submitted by 4:00 p.m. to one that allowed trades to be entered until 5:30 p.m. This enabled the late trading to occur. His "trade sheet" protocol required that all his clients submit their proposed trades by 4:00 p.m., but he allowed customers to make trading decisions after 4:00 p.m. The trade sheets permitted VanCook to create the false appearance that trades were placed prior to 4:00 p.m. That the trade sheets were used for this deceptive purpose is supported by the fact that the record contains no evidence that VanCook ever implemented procedures to record the times that orders on the trade sheets were modified or cancelled.

Testimony from clients who finalized trades after 4:00 p.m. consistently showed that VanCook knew of the advantage his scheme provided his clients and used the ability to late trade to attract and retain business. Goodwin testified that, before opening accounts with Pritchard, he discussed with VanCook the ability to finalize trades after 4:00 p.m. and recalled that VanCook appreciated the advantage that late trading offered. Pillai testified that VanCook offered him the ability trade after 4:00 p.m. to retain his business. Murray's testimony corroborates Pillai's testimony on this point. The law judge explicitly credited the testimony of Goodwin, Pillai, and Murray over that of VanCook, and we find no basis in the record to overturn the law judge's finding.⁵³

Moreover, VanCook persisted in encouraging his clients to late trade even after one expressed concern over the legality of post-4:00 p.m. trading in January 2003. The law judge found that Pillai credibly testified that VanCook argued that Pillai's attorney, who advised Pillai to stop late trading, was "wrong" and "overly cautious." A few months later, VanCook participated in a conference call with a different client about the same issue, *i.e.*, whether late trading was unlawful. Pritchard Capital's attorney told VanCook not to late trade. VanCook's claimed ignorance about the conference call is contradicted by Pritchard, whose testimony is supported by his handwritten notes. Unlike VanCook, Pritchard concluded, based on the statements of the Firm's attorney, that he and VanCook, as partners receiving clear legal advice, must abide by the 4:00 p.m. order deadline. However, VanCook continued late trading. When the New York Attorney General's investigations caused Pritchard concern over his Firm's compliance with securities laws and prompted him to ask VanCook whether he permitted clients

⁵² A law judge's credibility findings are entitled to considerable weight and deference. *See, e.g., Warwick Capital Mgmt., Inc.*, Investment Advisers Act Rel. No. 2694 (Jan. 16, 2008), 92 SEC Docket 1410, 1413-14 n.9.

⁵³ *Id.*

to trade after 4:00 p.m., VanCook lied to him, telling Pritchard that he had never accepted trades after 4:00 p.m.

The evidence is consistent in demonstrating that VanCook, despite his failure to recall many of the events and conversations that others remember with clarity and despite his assertions that he was unaware that his conduct was improper, knew or must have known that his scheme would deceive mutual funds into believing that his clients' late orders were received before 4:00 p.m. and that they were therefore entitled to receive that day's NAV. We find that VanCook acted with scienter.

VanCook's Arguments. VanCook argues that he lacked the requisite scienter. VanCook claims to have no awareness that 4:00 p.m. was a critical cut-off point for submitting mutual fund trades in order for his mutual fund clients to receive that day's NAV. For the reasons discussed above, the law judge did not credit VanCook's claim.⁵⁴ Moreover, VanCook would have been aware had he read the prospectuses of the dozens of mutual funds that his clients traded and the Processing Guide of the clearing broker that he helped to secure. The prospectuses consistently disclosed that shares were priced at or as of 4:00 p.m., and the Processing Guide contained explicit instructions to enter all trades by 4:00 p.m., excepting corrections and similar administrative tasks that could be entered until 5:30 p.m. VanCook nonetheless claims that he believed that he could enter orders until 5:30 p.m., a belief that his colleague, Pritchard, did not share. During this period he was warned that attorneys thought the practice was unlawful. VanCook's failure to comply with the requirements of the Processing Guide and mutual fund prospectuses was highly unreasonable and represented an extreme departure from the standards of ordinary care expected of a registered representative in his position to the extent that the danger of misleading the mutual funds and their shareholders was either known to VanCook or so obvious that he must have been aware of it.

VanCook contends that he did not engage in deceptive market timing or the use of deceptive devices typically used by market timers, such as altered account numbers, representative numbers, or tax identifications numbers. Assuming VanCook's assertions to be true, the fact that he did not use these deceptive devices as part of his market-timing trading is not evidence of lack of scienter with respect to the deceptive late-trading scheme.

VanCook also asserts that the fact that the "trade sheet protocol" was not invented by him and was used "throughout the market timing industry generally" refutes a finding that it was "somehow developed by [him] to facilitate late trading." Whether the trade sheet protocol VanCook used had innocuous origins is beside the point, given that VanCook ultimately used it on behalf of a subset of his clients to create the false appearance that trading decisions were made before 4:00 p.m., a feature that was central to the fraudulent scheme that he operated for almost two years.

⁵⁴

See supra Section II. F. discussing the law judge's credibility findings.

VanCook questions how it is "fair to say that [he] must have been aware that [his] practice was improper" when, he claims, no "red flags" existed. Specifically, VanCook claims that just about everyone else in the securities industry was unaware that late trading was improper, that his colleagues did not object to his order system, and that his clients were persons of "stature" whose account performance was relatively modest. VanCook repeatedly ignored numerous "red flags"—including the information contained in prospectuses and Banc of America's Processing Guide, the warnings issued by his client's attorney and his own Firm's attorney, and conversations with Pritchard regarding the importance of the 4:00 p.m. deadline—that indicated his conduct was not only improper but also deceptive.⁵⁵ Also, while the three clients at issue may have been sophisticated analysts who participated in the late-trading activity, VanCook was critical to its implementation and capitalized on its advantage to attract and retain customers and to generate significant commissions for himself. In the face of this evidence, we reject VanCook's claim that he acted without the requisite scienter.⁵⁶

* * *

⁵⁵ In this regard, we reject VanCook's claim that our finding that he must have been aware of the impropriety of his conduct "tramples on the fundamental notion of fair notice." "Due process requires . . . only that 'laws give the person of ordinary intelligence a reasonable opportunity to know what is prohibited.'" *Valicenti Advisory Servs.*, 198 F.3d at 66 (quoting *Upton v. SEC*, 75 F.3d 92, 98 (2d Cir. 1996)). VanCook, an experienced securities professional, cannot "credibly claim lack of fair notice of the proscription against defrauding investors." *Id.* As the First Circuit Court of Appeals stated in *SEC v. Tambone*, 550 F.3d 106, 148 (1st Cir. 2008), "[t]he Commission seeks with its action to enforce provisions of the securities laws that have been in existence for over half a century. Since their inception, it has been unlawful to offer or sell [] securities using a false or misleading statement. The Due Process Clause of the Constitution requires nothing more by way of notice."

⁵⁶ See *Joseph Abbondante*, Exchange Act Rel. No. 53066 (Jan. 6, 2006), 87 SEC Docket 203, 226 & n.76 (rejecting blame-shifting arguments); *Michael G. Keselica*, 52 S.E.C. 33, 37 (1994) (same); *B.R. Stickle & Co.*, 51 S.E.C. 1022, 1025 (1994) (same).

The purported failure of others to detect or object to the impropriety of VanCook's conduct does not relieve him of "responsibility for what he knew or was reckless in not knowing and for what he did." See *Jett*, 57 S.E.C. 350, 390 (2004) (finding that, even if management knew of respondent's fraudulent conduct, "indeed even if they ordered him to commit it – that would not relieve Jett of responsibility for what he knew or was reckless in not knowing and for what he did").

We conclude that VanCook willfully⁵⁷ violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5.⁵⁸

IV.

VanCook was also charged with aiding and abetting and causing Pritchard Capital's violations of certain provisions of the securities laws requiring firms to keep accurate books and records. Exchange Act Section 17(a)(1) and Rule 17a-3(a)(6) thereunder require that broker-dealers registered with the Commission make and keep current, for prescribed periods, certain books and records. Rule 17a-3(a)(6) requires that registered broker-dealers make and keep a

memorandum of each brokerage order, and of any other instruction, given or received for the purchase or sale of securities, whether executed or unexecuted. The memorandum shall show the terms and conditions of the order or instructions and of any modification or cancellation thereof; the account for which entered; the time the order was received; the time of entry; the price at which executed; the identity of each associated person, if any, responsible for the account; the identity of any other person who entered or accepted the order on behalf of the customer or, if a customer entered the order on an electronic system, a notation of that entry; and, to the extent feasible, the time of execution or cancellation.⁵⁹

⁵⁷ A willful violation of the securities laws means the intentional commission of an act that constitutes the violation; there is no requirement that the actor must be aware that he is violating any statutes or regulations. *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (internal quotation marks and citation omitted).

⁵⁸ In light of our conclusion that VanCook is liable as a primary violator of the antifraud provisions of Exchange Act Section 10(b) and Exchange Act Rule 10b-5, we do not address his secondary liability for aiding and abetting and causing Banc of America's violations of Investment Company Act Rule 22c-1, which, by its terms, does not apply to VanCook directly. 17 C.F.R. § 270.22c-1(a). As discussed, VanCook's liability here is premised on his commission of deceptive acts as part of a scheme to defraud that involved material misrepresentations. *See generally* 6 Thomas Lee Hazen, *Treatise on the Law of Securities Regulation*, § 20.5 (6th ed. 2009) (stating that "[e]ven in the absence of an express rule prohibiting late trading, the SEC has made clear that late trading is improper and violates the [antifraud provisions of the] securities laws").

⁵⁹ Rule 17a-3(a)(6) was amended, effective May 2, 2003, to add the requirement to record the time an order was received from a customer. *See* Books and Records Requirements for Brokers and Dealers Under the Securities Exchange Act of 1934, 66 Fed. Reg. 55,817 (Nov. 2, 2001).

To establish aiding and abetting liability, we must find that (1) Pritchard Capital violated those provisions, (2) VanCook substantially assisted the violations, and (3) VanCook provided that assistance with the requisite scienter.⁶⁰ The scienter requirement for aiding and abetting liability may be satisfied by showing that VanCook knew of, or recklessly disregarded, the wrongdoing and his role in furthering it.⁶¹

From May 2, 2003 through July 2003, Pritchard Capital time-stamped upon receipt proposed trade sheets from the three hedge fund clients.⁶² These trade sheets often did not represent the clients' final trading instructions. Instead, Pritchard Capital permitted these clients to confirm, cancel, or modify those trade instructions later in the day. It is undisputed that Pritchard did not record the time at which these confirmations or modifications were made. The Firm's failure to record the time at which customers submitted their final trading instructions constituted a primary violation of Exchange Act Section 17(a)(1) and Rule 17a-3(a)(6) thereunder. VanCook, who accepted order modifications from his hedge fund customers without noting the time he received these modifications, and who established the system by which McMahan also accepted "proposed trade sheets" and subsequent order modifications without documenting the time of receipt of these modifications, substantially assisted the violation.

We also find that VanCook provided that assistance with scienter. As explained above, VanCook engaged in a scheme to deceive mutual funds into believing that his late-trading clients were entitled to that day's NAV because their orders were received by 4:00 p.m. VanCook knew or must have known that time-stamping the clients' proposed trade sheets upon receipt but failing to record the time that his clients made their actual final trading decisions would help to conceal their late trading.⁶³ We conclude, therefore, that VanCook aided and abetted Pritchard Capital's violations of Exchange Act Section 17(a)(1) and Exchange Act Rule 17a-3(a)(6). Further,

⁶⁰ See *Robert J. Prager*, Exchange Act Rel. No. 51974 (July 6, 2005), 85 SEC Docket 3413, 3421 & n.17 (citing additional cases).

⁶¹ See, e.g., *Monetta Fin. Servs., Inc. v. SEC*, 390 F.3d 952, 956 (7th Cir. 2004); *Howard v. SEC*, 376 F.3d 1136, 1143, 1149 (D.C. Cir. 2004); *Graham v. SEC*, 222 F.3d 994, 1000 (D.C. Cir. 2000).

⁶² May 2, 2003 is the beginning of the violative conduct because that is the date Rule 17a-3(a)(6) was amended to add the requirement to show the time that an order was received from a customer. See *supra* note 59.

⁶³ See *Simpson Capital Mgmt.*, 586 F. Supp. 2d at 208 (finding that plaintiff's allegations, which included, among other things, that defendants "submitted proposed trades to the broker-dealers on 'scenario sheets' before 4:00 p.m. that allowed the defendants the opportunity to authorize those trades late in the day and incorporate after-market information into their decisions," were sufficient to defeat motion to dismiss complaint).

because one who aids and abets a primary violation is necessarily a cause of that violation,⁶⁴ we also find that VanCook was a cause of Pritchard Capital's violations of these provisions.⁶⁵

V.

A. Bar from Association

Exchange Act Section 15(b)(6) authorizes us to censure, place limitations on, suspend, or bar a person associated with a broker or dealer if we determine that the person has, among other things, willfully violated the federal securities laws and it is in the public interest to do so.⁶⁶ In determining what sanction is in the public interest, we consider the factors articulated in *Steadman v. SEC*.⁶⁷ Those factors include the egregiousness of a respondent's actions, the degree of scienter involved, the isolated or recurrent nature of the infraction, the recognition of the wrongful nature of the conduct, the sincerity of any assurances against future violations, and the likelihood that the respondent's occupation will present opportunities for future violations.⁶⁸ We have also stated that conduct that violates the antifraud provisions "is especially serious and subject to the severest sanctions."⁶⁹

We conclude that VanCook's conduct was egregious. He participated in a scheme that involved the placement of nearly 5,000 late mutual fund orders effecting the purchase and sale of

⁶⁴ *Sharon M. Graham*, 53 S.E.C. 1072, 1085 n.35 (1998), *aff'd*, 222 F.3d 994 (D.C. Cir. 2000).

⁶⁵ We have previously explained that "negligence is sufficient to establish 'causing' liability . . . , at least in cases in which a person is alleged to 'cause' a primary violation that does not require scienter." *KPMG Peat Marwick LLP*, 54 S.E.C. 1135, 1175 (2001), *petition denied*, 289 F.3d 109 (D.C. Cir. 2002). VanCook argues that, "b[y] placing no evidence into the record to establish the appropriate standard of care, the Division failed to prove negligence for its 'causing' charges." Here, we have found that VanCook was at least reckless in failing to record the time his clients submitted their final trade instructions, which "exceeds the statutory language of [Exchange Act] Section 21C." *Robert M. Fuller*, 56 S.E.C. 976, 989 n.29 (2003), *petition denied*, 95 Fed. Appx. 361 (D.C. Cir. 2004). The Division therefore need not have separately proven how VanCook's conduct was negligent.

⁶⁶ 15 U.S.C. § 78o(b)(6).

⁶⁷ 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981).

⁶⁸ *Id.*

⁶⁹ *Justin F. Ficken*, Advisers Act Rel. No. 2803 (Oct. 17, 2008), 94 SEC Docket 10887, 10891 & n.20 (citing cases).

billions of dollars' worth of mutual fund shares.⁷⁰ This volume of trading had the potential to cause substantial dilution in value of the mutual fund shares affected by the scheme.⁷¹ The scheme defrauded dozens of mutual funds and, ultimately, their shareholders, who—unlike VanCook's clients—did not have access to post-closing market information to inform their trading decisions and who were unaware of the effects VanCook's late trades were having on the value of their investments. VanCook's fraudulent scheme generated over \$500,000 in compensation for himself and another \$500,000 in account fees for Pritchard Capital.

As we explained above, VanCook's conduct demonstrated a high degree of scienter.⁷² The late-trading scheme was not an isolated incident, but a recurrent pattern that extended over a substantial period of time and stopped only after it was detected by regulators. VanCook has not offered assurances against future violations, nor has he recognized that he committed serious antifraud violations, instead characterizing himself as merely a "low level introducing broker who stumbled into late trading practices" conceived of by others. Further, VanCook fails to appreciate the duties and responsibilities attendant to being a securities professional, focusing on "trying to keep the account[s]" and the substantial commissions they represented while considering compliance with the securities laws to be outside the purview of his position—*i.e.*, not his "issue," "job," or "concern." We also consider that VanCook has remained in the securities industry and has been associated with two other registered broker-dealers since leaving Pritchard Capital, indicating a potential to commit future violations. These factors lead us to

⁷⁰ The Division did not calculate the precise monetary value represented by the late trade orders entered by VanCook; however, the vast majority of trades exceeded \$200,000 in value, and many trades were valued in the tens of millions of dollars.

⁷¹ The Division did not offer a calculation of the amount by which VanCook's trades diluted the value of the mutual fund shares affected; however, the substantial number and dollar volume of trades suggests the dilution was likely significant. *See In re Mut. Funds Litig.*, 437 F. Supp. 2d 439, 442 (D. Md. 2006) (discussing the potential dilutive effects of late trading on the net asset value of mutual fund shares); *Gen. Am. Life Ins. Co.*, Proposed Plan of Distribution, Admin. Proc. File No. 3-12720 (May 22, 2008), 2008 SEC LEXIS 1216, *7-8 (describing method of calculation of dilution of mutual fund shares caused by late trading as the product, per day, of the number of shares sold or purchased and the difference between the NAV on the transaction date and the NAV on the day after the transaction).

⁷² VanCook argues that "[e]ven if one were to accept, for the sake of argument, that Mr. VanCook's post-4:00 p.m. trading practices were illegal, the fact that he engaged in no deceptive market timing should have weighed heavily in determining appropriate sanctions," and therefore a bar is too strict a sanction. We have found that VanCook's post-4:00 p.m. trading practices were fraudulent; the fact that he did not also engage in other misconduct is not a mitigating circumstance. *Dane S. Faber*, 57 S.E.C. 297, 313 n.33 (2004) (finding that failure to engage in other violative conduct did not mitigate violations at issue).

conclude that a bar from association with any broker or dealer is necessary to protect the public interest and will serve a remedial purpose.

B. Cease-and-Desist Order

Securities Act Section 8A(a) and Exchange Act Section 21C authorize the Commission to impose a cease-and-desist order if it finds that any person has violated the federal securities laws or rules thereunder.⁷³ In determining whether a cease-and-desist order is appropriate, we look to whether there is some risk of future violations.⁷⁴ The risk of future violations required to support a cease-and-desist order is significantly less than that required for an injunction.⁷⁵ A single violation can be sufficient to indicate some risk of future violations.⁷⁶ Our finding that a violation is egregious "raises an inference that it will be repeated."⁷⁷ We also consider whether other factors demonstrate a risk of future violations, including the seriousness of the violation, the isolated or recurrent nature of the violation, whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, the respondent's state of mind, the sincerity of assurances against future violations, the recognition of the wrongfulness of the conduct, the opportunity to commit future violations, and the remedial function to be served by a cease-and-desist order in the context of any other sanctions sought in the proceeding.⁷⁸ This inquiry is flexible, and no single factor is dispositive.⁷⁹

We find that the risk of future violations is high. VanCook's conduct was serious and recurrent. He engaged in deceptive conduct that spanned at least twenty-one months. His violations were relatively recent and involved a high degree of scienter.⁸⁰ VanCook profited substantially from his deceptive conduct at the expense of mutual fund investors who did not

⁷³ 15 U.S.C. §§ 77A(a), 78u-3.

⁷⁴ *KPMG Peat Marwick, LLP*, 54 S.E.C. 1135, 1185 (2001), *reconsideration denied*, 55 S.E.C. 1 (2001), *petition denied*, 289 F.3d 109 (D.C. Cir. 2002).

⁷⁵ *KPMG Peat Marwick*, 54 S.E.C. at 1191.

⁷⁶ *See Geiger v. SEC*, 363 F.3d 481, 489 (D.C. Cir. 2004).

⁷⁷ *Id.*

⁷⁸ *KPMG Peat Marwick*, 54 S.E.C. at 1192.

⁷⁹ *Id.*

⁸⁰ *See Rita J. McConville*, Exchange Act Rel. No. 51950 (June 30, 2005) (imposing cease-and-desist order based on "relatively recent" conduct that occurred more than five years prior to issuance of Commission's opinion), 85 SEC Docket 3127, 3152, *petition denied*, 465 F.3d 780 (7th Cir. 2006), *cert. denied*, 552 U.S. 811 (2007).

have access to post-4:00 p.m. market information when they made their trading decisions. Although we have ordered that VanCook be barred from associating with any broker or dealer, the issuance of a cease-and-desist order will serve the remedial purpose of encouraging him to take his responsibilities more seriously in the future should he be allowed to re-enter the securities industry or should he act in a capacity that does not require registration. A cease-and-desist order will also serve to protect the investing public from possible future violations by VanCook should he become associated with an investment adviser or investment company. Therefore, we conclude that, in addition to a bar against associating with broker-dealers, it is in the public interest to impose a cease-and-desist order against VanCook.

C. Disgorgement

Securities Act Section 8A(e), Exchange Act Section 21B(e), and Exchange Act Section 21C(e) authorize disgorgement, including reasonable prejudgment interest, in a cease-and-desist proceeding and a proceeding in which a civil money penalty may be imposed.⁸¹ Disgorgement is an equitable remedy designed to deprive wrongdoers of their unjust enrichment and to deter others from similar misconduct.⁸² "[T]he amount of disgorgement should include all gains flowing from the illegal activities."⁸³

When calculating disgorgement, "separating legal from illegal profits exactly may at times be a near-impossible task."⁸⁴ As a result, disgorgement "need only be a reasonable approximation of profits causally connected to the violation."⁸⁵ Once the Division shows that its disgorgement figure is a reasonable approximation of the amount of unjust enrichment, the burden shifts to the respondent to demonstrate that the Division's estimate is not a reasonable approximation.⁸⁶

The Division requests that we order VanCook to disgorge \$538,565.70. The Division's expert arrived at this figure by adding the wrap fees (*i.e.*, fees based on the value of assets under management in the clients' accounts, not based on the number of trades the clients submitted)

⁸¹ 15 U.S.C. §§ 77h-1(a), 78u-2(e), 78u-3(e).

⁸² *SEC v. First City Fin. Corp., Ltd.*, 890 F.2d 1215, 1230 (D.C. Cir. 1989).

⁸³ *David Henry Disraeli*, Exchange Act Rel. No. 57027 (Dec. 21, 2007), 92 SEC Docket 852, 879, *aff'd*, 2009 WL 1791547 (D.C. Cir. 2009) (slip copy).

⁸⁴ *First City Fin. Corp.*, 890 F.2d at 1231.

⁸⁵ *Id.*

⁸⁶ *SEC v. Lorin*, 76 F.3d 458, 462 (2d Cir. 2006); *First City Fin. Corp.*, 890 F.2d at 1232.

paid monthly to Pritchard Capital by Simpson, Millennium, and Goodwin during certain time periods, and then dividing that figure in half.⁸⁷ As explained below, we conclude that this calculation reasonably approximates VanCook's ill-gotten gains from Simpson and Millennium but that the figure representing his improper gains from Goodwin is overstated.

Simpson. The Division's expert calculated that VanCook earned \$388,007.59 in fee-based commissions from the five accounts opened by Simpson. This figure includes commissions earned from these accounts only during the period charged in the OIP (*i.e.*, November 2001 through July 2003).⁸⁸ Simpson placed orders on behalf of all five of his accounts at Pritchard. The record establishes that essentially all of the trading decisions in these accounts were made after 4:00 p.m. but still received that day's NAV: VanCook's attorney stipulated at the hearing that Simpson "regularly" confirmed his orders after 4:00 p.m., and McMahon testified that final trade instructions from Simpson "always" came in after 4:00 p.m. We find that the record supports the conclusion that the figure of \$388,007.59, which represents the commissions VanCook earned from fees paid by Simpson for the maintenance of his late-trading accounts during the period charged, reasonably approximates the amount VanCook should disgorge for the fraud he perpetrated on mutual funds related to the Simpson accounts.

Millennium. The Division's expert calculated that VanCook earned \$97,241.23 in commissions from the seven accounts maintained by Millennium. Although Millennium had opened accounts with Pritchard as early as October 2002, the expert included in his disgorgement figure only those commissions earned from the Millennium accounts by VanCook beginning in December 2002—when Pillai first accepted VanCook's offer to submit trade confirmations after 4:00 p.m.—and continuing through July 2003. The record indicates that Millennium used only two of its seven accounts to late trade, and that the late trading in those two accounts occurred over only a two-month period; however, we find it is reasonable to characterize the commissions VanCook earned after November 2002 on all seven accounts as ill-gotten proceeds. As Pillai testified, Millennium intended to close its accounts with Pritchard—accounts that were underperforming compared to accounts Millennium maintained with other brokers—but decided to keep the accounts open when VanCook made an effort to keep Millennium's business by offering Pillai the ability to cancel or confirm trades after 4:00 p.m. VanCook himself testified that his "main concern was trying to keep the account and continue to do business with Millennium." Because the record evidence shows that VanCook retained all of the Millennium

⁸⁷ VanCook testified that he was paid as compensation half of the wrap fees paid to Pritchard Capital by his clients. The Division's expert included only those wrap fees paid by Simpson from November 2001 through July 2003, to conform to the period charged in the OIP. He also limited the fees paid by Millennium to include only those paid after December 2002, at which time Millennium began engaging in its late trading activity.

⁸⁸ The wrap fees were billed and collected monthly in arrears; for example, Pritchard collected the wrap fee for October 2001 by withdrawing funds from the client's account in November 2001. Not all of the Simpson accounts were open throughout this entire period.

accounts after November 2002 by virtue of his late-trading scheme and his offer to Pillai to take advantage of the benefits of that scheme, we conclude that \$97,241.23 reasonably approximates the ill-gotten proceeds VanCook earned from Millennium.

Goodwin. The Division's expert calculated that VanCook received \$53,316.89 in fee-based commissions from the fourteen Goodwin accounts that Pritchard serviced. This figure includes all of the commissions VanCook earned from all Goodwin accounts from their opening dates (which range from early 2002 through mid-2003) to their closing dates (as late as July 2003). The evidence suggests, however, that this figure is over-inclusive because not all of the trades that Goodwin submitted to Pritchard were confirmed after the close. Goodwin testified that he confirmed "probably over ninety percent" of his orders after 4:00 p.m., while McMahon estimated it to be "98 percent of the time." Moreover, in contrast to the Millennium accounts, it is not clear from the record that the ability to late trade was Goodwin's primary incentive for maintaining his accounts with Pritchard. Goodwin testified that the ability to trade after the close "was one of the reasons but not the only reason" he chose to do business with Pritchard. Therefore, we have determined to reduce the amount of disgorgement attributable to the Goodwin accounts by ten percent, to more closely align the figure with the approximate frequency of late trading in which Goodwin admittedly engaged. Accordingly, we find that \$47,985.20 reasonably approximates the ill-gotten proceeds VanCook earned from Goodwin.

Disgorgement total. VanCook has not demonstrated that the Division's estimate of the disgorgement amount is unreasonable. VanCook argues that, because the Division emphasizes the May 2003 telephone call with Pritchard and Seale as the time at which "VanCook should have known late trading was illegal," VanCook should have to disgorge only those fees he collected from his three hedge fund clients from May 2003 through July 2003. However, the Division has argued, and we have found, that VanCook acted with scienter throughout the entire period charged. Although the May 2003 telephone call represents particularly persuasive evidence of VanCook's deceptive state of mind, his role in Pritchard Capital's change of clearing brokers from Bear Stearns (which did not permit submission of orders after 4:00 p.m.) to Banc of America (which did permit it) as well as his use of this new capability to attract and retain hedge fund customers demonstrates that, from the origin of the scheme, VanCook acted with scienter. We therefore find that the estimate of disgorgement submitted by the Division (\$538,565.70), reduced by ten percent of the value of the fees received by VanCook from Goodwin (\$5,331.69), reasonably approximates his unjust enrichment.⁸⁹ We order VanCook to disgorge \$533,234.01, plus prejudgment interest.⁹⁰

⁸⁹ *First City Fin. Corp.*, 890 F.2d at 1231 (finding that disgorgement "need only be a reasonable approximation of profits causally connected to the violation").

⁹⁰ *See Terence Michael Coxon*, 56 S.E.C. 934, 971 (2003) ("[e]xcept in the most unique and compelling circumstances, prejudgment interest should be awarded on disgorgement, among other things, in order to deny a wrongdoer the equivalent of an interest free loan from the
(continued...)

D. Civil Penalty

Exchange Act Section 21B authorizes the Commission to impose a civil money penalty where a respondent has willfully violated any provision of the federal securities laws and a penalty is in the public interest.⁹¹ Exchange Act Section 21B establishes a three-tiered system of civil penalties, each with a larger maximum penalty amount applicable to increasingly serious misconduct.⁹² For each act or omission involving fraud that "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons or resulted in substantial pecuniary gain to the person who committed the act or omission," third-tier civil penalties may be warranted.⁹³ In determining whether a penalty is in the public interest, we may consider whether there was fraudulent misconduct, harm to others or unjust enrichment, whether the respondent had prior violations, and the need for deterrence, as well as such other matters as justice may require.⁹⁴

We find that a third-tier penalty is warranted here. As noted, VanCook engaged in fraud. He earned over half a million dollars in compensation from his late-trading hedge fund clients during the course of the scheme. Further, although the Division has not established the precise amount of losses suffered by the mutual fund shareholders who did not trade on post-closing information in this case, the risk of substantial loss through dilution of fund share values was significant given the number of trades (nearly 5,000 exclusive of cancelled orders) and the dollar amounts involved (most in excess of \$200,000 per trade). The Exchange Act permits a third-tier penalty of up to \$120,000 for each violation by a natural person committed during the relevant period.⁹⁵ However, in light of the other sanctions already imposed upon VanCook, we find that a penalty of \$100,000 for the entirety of VanCook's late-trading scheme is an amount necessary to

⁹⁰ (...continued)

wrongdoer's victims."); Commission Rule of Practice 600(a), 17 C.F.R. § 201.600(a) (noting that "[p]rejudgment interest shall be due on any sum required to be paid pursuant to an order of disgorgement" and describing method of calculation of prejudgment interest due on sums ordered to be disgorged).

⁹¹ 15 U.S.C. § 78u-2(a).

⁹² 15 U.S.C. § 78u-2(b).

⁹³ 15 U.S.C. § 78u-2(b)(3).

⁹⁴ 15 U.S.C. § 78u-2(c).

⁹⁵ Violations committed by a natural person after February 2, 2001, but before February 14, 2005, have a maximum penalty per occurrence of \$6,500 in the first tier; \$60,000 in the second tier; and \$120,000 in the third tier. *See* Debt Collection Improvement Act of 1996, Pub. L. No. 104-134, ch. 10, sec. 31001, § 3701(a)(1); 28 U.S.C. § 2461 (effective Mar. 9, 2006); 17 C.F.R. §§ 201.1001, 201.1002.

deter VanCook from future misconduct given his failure to appreciate his responsibilities as a securities professional, and will also have a remedial effect of deterring others from engaging in the same misconduct.⁹⁶

E. VanCook's Arguments Against Sanctions

VanCook claims that he cannot pay the disgorgement and prejudgment interest "together with the \$100,000 penalty." For the first time in these proceedings, he offers sworn financial statements purporting to document his financial situation. Under Rule of Practice 630(a), we may, in our discretion, consider evidence of ability to pay in determining whether a respondent should be required to pay disgorgement, interest, or civil penalties.⁹⁷ Ability to pay, however, is only one factor that informs our determination and is not dispositive.⁹⁸ In particular, "[e]ven when a respondent demonstrates an inability to pay, we have discretion not to waive the penalty, [disgorgement, or interest,] particularly when the misconduct is sufficiently egregious."⁹⁹

We have reviewed the financial statements submitted by VanCook. Those statements show that VanCook has a positive net worth of nearly \$400,000 and that he earned over \$200,000 working for broker-dealers in the twelve months prior to filing his financial statements. We are not persuaded, therefore, that VanCook is unable to pay the sanctions imposed. Moreover, VanCook's conduct was sufficiently egregious to outweigh any consideration of his inability to pay disgorgement, prejudgment interest, or penalties.¹⁰⁰ Ordering VanCook to pay disgorgement plus prejudgment interest and a third-tier penalty of \$100,000 is necessary to

⁹⁶ We note that the Division of Enforcement requested that the law judge impose a civil penalty equal to the amount of disgorgement (\$538,565.70). The law judge instead ordered a \$100,000 penalty, as do we. In its brief before us, the Division stated that it believed the penalty imposed by the law judge "is reasonable and in the public interest."

⁹⁷ 17 C.F.R. § 201.630(a).

⁹⁸ See, e.g., *Brian A. Schmidt*, 55 S.E.C. 576, 597-98 (2002) (noting that, under Exchange Act Section 21B, ability to pay a penalty is but one factor to consider in determining whether a penalty is in the public interest); see also, e.g., *SEC v. Warren*, 534 F.3d 1368, 1370 (11th Cir. 2008) (per curiam) (stating that "[a]t most" a defendant's ability to pay is one factor to be considered in imposing a civil money penalty or disgorgement for violations of the federal securities laws).

⁹⁹ *Philip A. Lehman*, Exchange Act Rel. No. 54660 (Oct. 27, 2006), 89 SEC Docket 536, 543.

¹⁰⁰ See, e.g., *Disraeli*, 92 SEC Docket at 883 (finding that respondent's misconduct was sufficiently egregious and outweighed any financial information submitted in support of his asserted inability to pay the disgorgement and penalty amounts) & n.125 (collecting cases).

prevent him from profiting from his misconduct and to deter him and others from defrauding mutual funds and their shareholders through illegal and deceptive trading practices.

VanCook also argues that the sanctions imposed against him are excessive compared to the sanctions imposed on other respondents involved in these proceedings. VanCook cites specifically to the sanctions to which Pillai, Pritchard, and McMahon consented in settling Commission proceedings against them.¹⁰¹ It is well-established that the determination of appropriate remedial action depends on the facts and circumstances of each case and cannot be determined by comparison with the actions taken in other proceedings.¹⁰² "Moreover, parties that settle disciplinary proceedings often receive less severe sanctions than those who do not."¹⁰³ VanCook argues that "a respondent who takes his case to a hearing should not be subject to a disproportionate and massive penalty for having the temerity to defend himself." However, the sanctions that are imposed in settled cases are the result of a myriad "pragmatic considerations such as the avoidance of time- and manpower-consuming adversarial litigation" that enter into decisions to accept offers of settlement from respondents.¹⁰⁴ For this reason they

¹⁰¹ See *supra* notes 18, 20 & 27. Pillai consented to a cease-and-desist order, twelve-month suspension from association with an investment adviser, \$1 disgorgement order, and \$150,000 civil penalty. *Millennium Capital Partners, L.P.*, 86 SEC Docket at 2421. Pritchard consented to a nine-month suspension from serving in a supervisory capacity and agreed to pay a \$50,000 civil penalty. *Pritchard Capital Partners*, 93 SEC Docket at 5310. McMahon consented to a censure and a cease-and-desist order. *Id.*

¹⁰² See *Butz v. Glover Livestock Comm'n Co.*, 411 U.S. 182, 187 (1973) (stating that "[t]he employment of a sanction within the authority of an administrative agency is thus not rendered invalid in a particular case because it is more severe than sanctions imposed in other cases"); *Geiger*, 363 F.3d at 488 (stating that "[t]he Commission is not obligated to make its sanctions uniform, so we will not compare this sanction to those imposed in previous cases").

¹⁰³ *Ficken*, 94 SEC Docket at 10893 & n.31 (citing cases).

¹⁰⁴ *Lehman*, 89 SEC Docket at 550.

cannot be meaningfully compared to the sanctions imposed in litigated cases, which are the result of fact-specific considerations of various factors designed to best protect the public interest. Accordingly, we reject VanCook's argument that we should reduce his sanctions based on those imposed in settlements with other individuals.

An appropriate order will issue.¹⁰⁵

By the Commission (Chairman SCHAPIRO and Commissioners CASEY, WALTER, and PAREDES; Commissioner AGUILAR not participating).

Elizabeth M. Murphy
Secretary

¹⁰⁵ 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. 61039A / November 20, 2009

Admin. Proc. File No. 3-12753

In the Matter of

JOSEPH JOHN VANCOOK

c/o Lewis D. Lowenfels, Esq.
Law Offices of Tolins & Lowenfels
747 Third Avenue
New York, NY 10017

and

Michael J. Sullivan, Esq.
Coughlin Duffy LLP
350 Mount Kemble Avenue
Morristown, NJ 07962

CORRECTED

ORDER IMPOSING REMEDIAL SANCTIONS

On the basis of the Commission's opinion issued this day, it is

ORDERED that Joseph VanCook be, and he hereby is, barred from association with any broker or dealer; and it is further

ORDERED that VanCook cease and desist from committing or causing any violations or future violations of Sections 10(b) and 17(a)(1) of the Exchange Act of 1934, and Exchange Act Rules 10b-5 and 17a-3(a)(6); and it is further

ORDERED that VanCook disgorge \$533,234.01, plus prejudgment interest of \$228,901.89, such prejudgment interest calculated beginning from August 1, 2003, in accordance with Commission Rule of Practice 600; and it is further

ORDERED that VanCook pay a civil money penalty in the amount of \$100,000.

Payment of the amount to be disgorged and the civil money penalty shall be: (i) made by United States postal money order, certified check, bank cashier's check, or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) mailed or delivered by hand to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Alexandria, VA 22312; and (iv) submitted under cover letter that identifies the respondent and the file number of this proceeding. A copy of the cover letter and check shall be sent to William P. Hicks, Division of Enforcement, Securities and Exchange Commission, Atlanta Regional Office, 3475 Lenox Road, Suite 1000, Atlanta, Georgia 30326.

By the Commission.

Elizabeth M. Murphy
Secretary