1994 Annual Report

United States
Securities and Exchange Commission

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

The Honorable Albert Gore, Jr.
President of the Senate
Washington, D.C. 20515

The Honorable Newt Gingrich
Speaker of the House
Washington, D.C. 20510

Gentlemen:

I am pleased to transmit the annual report of the Securities and Exchange Commission for fiscal year 1994. During the year, the Commission:

- enhanced its commitment to protect investors with initiatives to improve public awareness and educate investors;

- completed a self-examination to create a more efficient reporting structure, improve resource utilization and streamline operations;

- obtained court orders requiring defendants to disgorge illicit profits of approximately $730 million;

- streamlined the regulatory process by eliminating the need for review of certain SRO rule filings;

- conducted several oversight inspections of self-regulatory organizations with a particular focus on sales practice abuses;

- released the report, *Market 2000: An Examination of Current Equity Market Developments,* which identified four areas where the markets could work better for investors and where competition could work better for the markets;

- adopted several initiatives to simplify and lower the cost of registration and reporting for domestic issuers and foreign companies accessing the United States public securities markets;

- focused on improving and simplifying communications to investment company shareholders, enhancing the integrity of participants in the investment management industry, and evaluating the use of derivatives by investment companies; and

- collected $588.2 million in fee revenue, more than twice as much as its annual funding level of $260.3 million.

The report has been prepared in accordance with the provisions of Section 23(b) of the Securities Exchange Act of 1934, as amended; Section 23 of the Public Utility Holding Company Act of 1935; Section 46(a) of the Investment Company Act of 1940; Section 216 of the Investment Advisers Act of 1940; Section 3 of the Act of June 29, 1949 amending the Bretton Woods Agreement Act; Section 11(b) of the Inter-American Development Bank Act; and Section 11(b) of the Asian Development Act.

Sincerely,

Arthur Levitt
Chairman

Table of Contents

Commission Members and Principal Staff Officers

(As of November 4, 1994)

Commissioners

Arthur Levitt, *Chairman*

Richard V. Roberts

J. Carter Beese, Jr.

Steven M. H. Wallman

(Commissioner Mary L. Schapiro resigned from the Commission on October 21,1994.)

Principal Staff Officers

Lori Richards, *Executive Assistant*

Linda C Quinn, *Director, Division of Corporation Finance*
- **Vacant.** *Deputy Director*
- **William E. Morley,** *Senior Associate Director*
- **Abigail Arms,** *Associate Director*
- **Meredith B. Cross,** *Associate Director*
- **Teresa E. lannaconi,** *Associate Director*
- **Howard F. Morin,** *Associate Director*
- **Mauri L. Osheroff,** *Associate Director*
- **Robert A. Bayless,** *Chief Accountant*
- **David A. Sirignano,** *Senior Legal Adviser*

William R. McLucas, *Director, Division of Enforcement*
- **Colleen P. Mahoney,** *Deputy Director*

Joseph I. Goldstein, *Associate Director*
Thomas C. Newkirk, *Associate Director*
Gary N. Sundick, *Associate Director*
Joan E. McKown, *Chief Counsel*
Barry R. Goldsmith, *Chief Litigation Counsel*
Stephen J. Crimmins, *Deputy Chief Litigation Counsel*
George H. Diacont, *Chief Accountant*
James A. Clarkson, III, *Director of Regional Office Operations*

Barry Barbash, *Director, Division of Investment Management*
Barbara J. Green, *Deputy Director*
Matthew A. Chambers, *Associate Director*
Gene A. Gohlke, *Associate Director*
C. Gladwyn Coins, *Associate Director*
William C. Weeden, *Associate Director*
Vacant, *Chief Counsel*

Brandon Becker, *Director, Division of Market Regulation*
Robert L.D. Colby, *Deputy Director*
Laity E. Bergmann, *Associate Director*
Mark D. Fitterman, *Associate Director*
Mary Ann Gadziala, *Associate Director*
Jonathan Kallman, *Associate Director*
Howard Kramer, *Associate Director*
Michael A. Macehiaroli, *Associate Director*
Catherine McGuire, *Associate Director/Chief Counsel*
Holly Smith, *Associate Director*

Simon M. Lome, *General Counsel, Office of General Counsel*
Paul Gonson, *Solicitor and Deputy General Counsel*
Phillip D. Parker, *Deputy General Counsel (Legal Policy)*
Anne E. Chafer, *Associate General Counsel*
Richard M. Humes, *Associate General Counsel*

Diane Sanger, *Associate General Counsel*
Jacob H. Stillman, *Associate General Counsel*
William S. Stern, *Counselor for Adjudication*

Walter P. Schuetze, *Chief Accountant, Office of the Chief Accountant*
John P. Riley, *Deputy Chief Accountant*

Brenda Murray, *Chief Administrative Law Judge, Office of the Administrative law Judges*

Susan E. Woodward, *Chief Economist, Office of Economic Analysis*
Jeffry L. Davis, *Director, Economic and Policy Research*

Nancy M. Smith, *Director, Office of Consumer Affairs*

Vacant, *Director, Office of Equal Employment Opportunity*

James M. McConnell, *Executive Director, Office of the Executive Director*
Susan Baumann, *Deputy Executive Director*
Fernando L. Alegria, Jr., *Associate Executive Director*
Wilson A. Butler, Jr., *Associate Executive Director*
Lawrence H. Haynes, *Associate Executive Director*
Vacant, *Associate Executive Director*

Michael D. Mann, *Director, Office of International Affairs*

Kathryn Fulton, *Director, Office of Legislative Affairs*

Jennifer Kimball, *Director, Office of Public Affairs, Policy Evaluation and Research*

Jonathan G. Katz, *Secretary of the Commission*

Biographies of Commission Members

Arthur Leavitt, Jr., *Chairman*

Following his nomination by President Clinton and his confirmation by the Senate, Arthur Levitt, Jr. was sworn in as the 25th Chairman of the Securities and Exchange Commission on July 27, 1993.

Before being nominated to the Commission, Mr. Levitt served as the Chairman of the New York City Economic Development Corporation and, from 1978 to 1989, the Chairman of the American Stock Exchange (Amex).

Throughout his career, Mr., Levitt has been called upon to serve on many governmental task forces and boards of directors. At the federal level, he has served on four executive branch commissions, including chairing the White House Small Business Task Force from 1978 to 1980. Most recently, he was a member of the President's Base Closure and Realignment Commission and the Defense Department Task Force on the National Industrial Base. In addition to heading the New York City Economic Development Corporation, he chaired the Special Advisory Task Force on the Future Development of the West Side of Manhattan and the Committee on Incentives and Tax Policy of the New York City Mayor's Management Advisory Task Force.

Mr. Levitt has served on 10 corporate and philanthropic boards, including those of the Equitable Life Assurance Society of the United States, East New York Savings Bank, First Empire State Corporation,

the Revson Foundation, the Rockefeller Foundation, the Solomon R. Guggenheim Foundation and Williams College.

Mr. Levitt founded Levitt Media Company in 1990. Its primary holding was *Roll Call, the Newspaper of Congress*.

Prior to accepting the Amex chairmanship, Mr., Levitt worked for 16 years on Wall Street. From 1969 to 1978, he was President and Director of Shearson Hayden Stone, Inc. (today Smith Barney Shearson) whose predecessor firm he joined as a partner in 1962. It was during this period that Mr. Levitt first involved himself with Amex, becoming one of its governors in 1975 and in 1977 accepting the additional position of Vice Chairman,

From 1959 to 1962, Mr. Levitt worked at the Kansas-based agricultural management firm Oppenheimer Industries, where he rose to the position of Executive Vice President and Director. From 1954 to 1959, Mr. Levitt was assistant promotion director at Time, Inc.

Mr. Levitt, 63, graduated Phi Beta Kappa from Williams College in 1952 before serving two years in the Air Force. Married since 1955 to the former Marylin Blauner, Mr. Levitt has two children, Arthur III and Lauri.

Richard Roberts, *Commissioner*

Richard Roberts was nominated to the Commission by President Bush and confirmed by the Senate on September 27, 1990. He was sworn in as a Commissioner on October 1,1990 by the Honorable Stanley Sporkin, Judge for the United States District Court of the District of Columbia. His term expires in June 1995.

Before being nominated to the Commission, Mr. Roberts was in the private practice of law with the Washington office of Miller, Hamilton, Snider & Odorn. Before joining the law firm in April 1990, Mr. Roberts was administrative assistant and legislative director for Senator Richard Shelby (D., Ala.), a position he assumed in 1987. Prior to that, Mr. Roberts was, for four years, in the private practice of law in Alabama, From 1979 to 1982, Mr. Roberts was administrative assistant and legislative director for then-Congressman Shelby.

Mr. Roberts is a 1973 graduate of Auburn University and a 1976 graduate of the University of Alabama School of Law. He also received a Master of Laws in taxation from the George Washington University National Law Center in 1981. He is admitted to the bar in the District of Columbia and Alabama. Mr. Roberts is a member of the Alabama State Bar Association and the District of Columbia Bar Association.

He and his wife, the former Peggy Frew, make their home in Fairfax, Virginia with their son and two daughters.

Mr. Roberts was born in Birmingham, Alabama on July 3, 1951.

J. Carter Beese, Jr., *Commissioner*

J. Carter Beese, Jr. was nominated to the U.S. Securities and Exchange Commission in October 1991 by President George Bush and confirmed by the U.S. Senate on February 27,1992. Mr. Beese was sworn in as the 71st member of the Commission in a private ceremony held on March 10, 1992, by the Honorable Stanley Sporkin, Judge for the U.S. District Court for the District of Columbia. On April 20,1992, Mr. Beese was formally sworn in at the White House by Vice President Dan Quayle.

During his tenure at the Commission, Commissioner Beese has been particularly active in the areas of investment management, the derivatives markets and cross-border capital flows. Commissioner Beese's focus on these areas is centered on his belief that the transformation of savers into investors through mutual funds, the development of new financial instruments to reallocate risk, and the globalization of the world's capital markets are fundamentally remaking our markets. Commissioner Beese is committed to maintaining the competitiveness of U.S. capital markets and is committed to a reassessment of the growing legal and regulatory burdens imposed on the capital formation process.

Before joining the Commission, Mr. Beese was a partner of Alex. Brown & Sons, the oldest investment banking firm in the United States. Mr. Beese's corporate responsibilities included business development in the areas of corporate finance, investment management, and institutional brokerage. Mr. Beese joined Alex. Brown in 1978, became an officer in 1984, and was named partner in 1987. Mr. Beese was also active in the founding of the Carlyle Group, a Washington based merchant bank, and served as an advisory director from 1986–1989.

Mr. Beese has also served in other capacities in government, each related to enhancing the competitiveness of U.S. industries and markets. In 1990, Mr. Beese was appointed by President Bush, and confirmed by the U.S. Senate, as a Director of the Overseas Private Investment Corporation (OPIC). OPIC is a U.S. government agency that assists American private business investment in over 120 countries by financing direct loans and loan guarantees and by insuring investments against a broad range of political risks. OPIC plays a vital role in the effort to gain access to new markets for U.S. products and businesses.

Mr. Beese also served as a member of the Securities and Exchange Commission's Emerging Markets Advisory Committee. As part of his responsibilities, Mr. Beese provided technical assistance on the formation and regulatory oversight of financial markets. Further, during 1991 Mr. Beese also served as a member of the Committee on Financing Technology in the U.S., a joint project between the Treasury and Commerce Departments initiated to study the adequacy of investment in the technology needed by U.S. companies to meet the challenges of global competition.

In addition, Mr. Beese has been involved in public and private sector initiatives to enhance the economic development of the Asia-Pacific region. He is a member of the United States National Committee for Pacific Economic Cooperation (US-PEC), which advises the U.S. government on ways to improve economic cooperation with countries in the Asia-Pacific region. Mr. Beese also serves as co-chairman with former U.S. Senator Adlai Stevenson of the US-PEC's Financial Markets Development project committee. This committee will develop policy recommendations to spur financial market development in the Pacific economies.

Mr. Beese is active in a number of civic organizations, including the American Center for International Leadership (ACIL), of which he is a director. ACIL brings young American leaders together with their counterparts in various foreign countries. Mr. Beese participated in ACIL missions to the Peoples Republic of China in 1988 and to the former Soviet Union in 1990. He serves on the boards of Preservation Maryland and the National Foundation for Teaching Entrepreneurship. He is also active in the Order of St. John. Mr. Beese resides in Baltimore, Maryland with his wife, Natalie, and three children, Courtney, John Carter and Wilson.

Steven M.H. Wallman, *Commissioner*

Steven M.H. Wallman was nominated to the Securities and Exchange Commission by President Bill Clinton and confirmed by the Senate on June *29,*1994. He was sworn in as a Commissioner on July 5,1994. His term expires in June 1997.

Before being nominated to the Commission, Mr. Wallman was in private practice with the Washington law office of Covington and Burling. He joined the firm in 1978 as an Associate/ becoming a Partner in 1986. While at Covington & Burling, Mr. Wallman specialized in general corporate, securities, contract and business law. Mr. Wallman also worked for the Boston Consulting Group in 1978. He is a member of the American Law Institute and the American Bar Association.

Mr. Wallman received his J.D. from the Columbia University School of Law in 1978. In 1976, he earned an S.M. from the Sloan School of Management at the Massachusetts Institute of Technology and an S.B. from M.I.T. in 1975.

He and his wife live in Great Falls, Virginia. Mr. Wallman was born on November 14, 1953.

Regional Offices

Central Regional Office
Robert H. Davenport, Regional Director
1801 California St., Suite 4800
Denver, CO 80202-2648
(303) 391-6800

Fort Worth District Office
T. Christopher Browne, District Administrator
801 Cherry Street, 19th Floor
Fort Worth, TX 76102
(817) 334-3821

Salt Lake District Office
Kenneth D. Israel, District Administrator
500 Key Bank Tower
50 S. Main Street, Suite 500
Box 79
Salt Lake City, UT 84144-0402
(801) 524-5796

Midwest Regional Office
Mary Keefe, Regional Director
Citicorp Center
500 W. Madison St., Suite 1400
Chicago, IL 60661-2511
(312) 353-7390

Pacific Regional Office
Elaine M. Cacheris, Regional Director
5670 Wilshire Blvd., 11th Blvd.
Los Angeles, CA, 90036-3648
(213) 965-3998

San Francisco District Office
David B. Bayless, District Administrator
44 Montgomery Street, Suite 1100 San Francisco, CA
90036-3648
(415) 705-2500

Southeast Regional Office
Charles V. Senatore, Regional Director
1401 Brickell Avenue, Suite 200
Miami, FL 33131
(305) 536-5765

Atlanta District Office
Richard P. Wessel, District Administrator
3475 Lenox Road, N.E. Suite 1000
Atlanta, GA 30326-1232
(404) 842-7600

Northeast Regional Office
Richard H. Walker, Regional Director
7 World Trade Center, Suite 1300
New York, NY 10048
(212) 748-8000

Boston District Office
Juan M. Marcelino, District Administrator
73 Tremont Street
Sixth Floor, Suite 600
Boston, MA 02108
(617) 424-5900

Philadelphia District Office
Donald M. Hoerl, District Administrator
The Curtis Center, Suite 1005
E. 601 Walnut Street
Philadelphia, PA 19106-3322
(215) 597-3100

Enforcement

The Commission's enforcement program is designed to protect investors and foster confidence by preserving the integrity and efficiency of the securities markets. The enforcement program's principal legislative mandates contain explicit authority for the agency to conduct investigations and prosecute violations of the securities laws by bringing enforcement actions in federal court or instituting administrative proceedings before the Commission. Last year, as in prior years, the Commission maintained a strong presence in all areas within its jurisdiction.

Key 1994 Results

In 1994, the Commission instituted a significant number of enforcement actions in response to a wide range of securities law violations. In its administrative and judicial proceedings, the Commission sought and obtained relief from a broad and flexible array of remedies designed to protect investors and the public interest.

The Commission obtained court orders requiring defendants to disgorge illicit profits of approximately $730 million. Civil penalties authorized by the Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (Remedies Act), the Insider Trading Sanctions Act of 1984 (ITSA), and the Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA) totalled over $34 million. In some instances, the payment of disgorgement pursuant to a court order was waived based upon the defendant's demonstrated inability to pay. Courts have noted also in some cases that civil penalties

were appropriate but were not imposed because of the demonstrated inability to pay.

In Commission-related cases, criminal authorities obtained 48 criminal indictments or informations, and 53 convictions during 1994. The Commission granted access to its files to domestic and foreign prosecutorial authorities in 451 instances.

[table deleted]

Enforcement Authority

The Commission has broad authority to investigate possible violations of the federal securities laws, Informal investigations are conducted on a voluntary basis, with the Commission requesting persons with relevant information to cooperate by providing documents and testifying before SEC staff. The federal securities laws also empower the Commission to conduct formal investigations in which the Commission has the authority to issue subpoenas that compel the production of books and records and the appearance of witnesses to testify. Generally, both types of investigations are conducted on a confidential, non-public basis.

Traditionally, the Commission's primary enforcement mechanism for addressing violative conduct has been the federal court injunction, which prohibits future violations. In civil actions for injunctive relief, the Commission is authorized to seek temporary restraining orders and preliminary injunctions as well as permanent injunctions against any person who is violating or about to violate any provision of the federal securities laws. Once an injunction has been imposed, conduct that violates the injunction is punishable by either civil or criminal contempt, and violators are subject to fines or imprisonment. In addition to seeking such orders, the Commission often seeks other equitable relief such as an accounting and disgorgement of illegal

profits. When seeking temporary restraining orders, the Commission often requests a freeze order to prevent concealment of assets or dissipation of the proceeds of illegal conduct. The Remedies Act authorized the Commission to seek, and the courts to impose, civil penalties for any violation of the federal securities laws (with the exception of insider trading violations for which penalties are available under ITSA). The Remedies Act also affirmed the existing equitable authority of the federal courts to bar or suspend individuals from serving as corporate officers or directors.

The Commission has the authority to institute several types of administrative proceedings, in addition to civil injunctive actions. The Commission may institute administrative proceedings against regulated entities in which the sanctions that may be imposed include a censure, limitation on activities, and suspension or revocation of registration. The Commission may impose similar sanctions on persons associated with such entities and persons affiliated with investment companies. In addition, individuals participating in an offering of penny stock may be barred by the Commission from such participation. In administrative proceedings against regulated entities and their associated persons, the Remedies Act also authorized the Commission to impose penalties and order disgorgement.

The Remedies Act further authorized the Commission to institute administrative proceedings in which it can issue cease and desist orders. A permanent cease and desist order can be entered against any person violating the federal securities laws and may require disgorgement of illegal profits. The Commission also is authorized to issue temporary cease and desist orders (if necessary, on an *ex parte* basis) against regulated entities and their associated persons if the Commission determines that the violation or threatened violation is likely to result in significant dissipation or

conversion of assets, significant harm to investors, or substantial harm to the public interest prior to the completion of proceedings.

Section 8(d) of the Securities Act of 1933 (Securities Act) enables the Commission to institute proceedings to suspend the effectiveness of a registration statement that contains false and misleading statements. Administrative proceedings pursuant to Section 15(c)(4) of the Securities Exchange Act of 1934 (Exchange Act) can be instituted against any person who fails to comply, and any person who is a cause of failure to comply, with reporting, beneficial ownership, proxy, and tender offer requirements. Respondents can be ordered to comply, or to take steps to effect compliance, with the relevant provisions. Pursuant to Rule 2(e) of the Commission's Rules of Practice, administrative proceedings can be instituted against professionals who appear or practice before the Commission, including accountants and attorneys. The sanctions that can be imposed in these proceedings include suspensions and bars from appearing or practicing before the Commission.

The Commission is authorized to refer matters to other federal, state, or local authorities or self-regulatory organizations (SROs) such as the New York Stock Exchange (NYSE) or the National Association of Securities Dealers (NASD). The staff often provides substantial assistance to criminal authorities, such as the Department of Justice, for the criminal prosecution of securities violations.

Enforcement Activities

Set forth below are summaries of significant enforcement actions initiated in various areas during 1994. Defendants or respondents who consented to settlements of actions did so without admitting or denying the factual allegations contained in the complaint or order instituting proceedings. See Table 2 for a listing of all enforcement actions instituted in 1994.

Offering Cases

Securities offering cases involve the offer and sale of securities in violation of the registration provisions of the Securities Act. In some cases, the issuers attempt to rely on exemptions from the registration requirements that are not available under the circumstances. Offering cases frequently involve material misrepresentations concerning, among other things, use of proceeds, risks associated with investments, disciplinary history of promoters or control persons, business prospects, promised returns, success of prior offerings, and the financial condition of issuers.

1. *Telecommunications Technology Cases*

The Commission has filed a number of cases in the past two years arising from the fraudulent, unregistered sale of securities in ventures involved in wireless cable, specialized mobile radio, interactive video and data services, and similar telecommunication technologies. While many telecommunications technology companies raise capital through legitimate means, the Commission has uncovered numerous fraudulent ventures, which often take the form of limited liability companies or partnerships that promoters falsely represent as outside the registration provisions of the federal securities laws, and which often are promoted through "infomercials" and high-pressure telephone sales pitches. Due to their prevalence, the Division of Enforcement issued a general warning to investors to beware of these frauds, indicating that it was particularly concerned about the apparent targeting of retirement funds by promoters of the frauds.[1] In the last year, the Commission filed eleven injunctive actions in this area. Moving quickly to preserve assets for the benefit of defrauded investors, the Commission obtained temporary restraining orders and orders freezing assets, or other emergency

relief, in most of these cases. Each of the cases discussed below was pending at the end of the year.

In *SEC v. Parkersburg Wireless Limited Liability Company,*[2] the Commission alleged that the defendants offered and sold unregistered securities in the form of public investments designated as "membership Units" in Parkersburg Wireless. Parkersburg Wireless raised over $10.5 million, purportedly to acquire or develop a wireless cable television system (i.e., a system using super high frequency transmissions rather than actual cables) in the Parkersburg, West Virginia area. Investors were told that they could expect a "4-to-1" return on investments within four years. The projections had no basis in fact. After the payment of commissions amounting to over fifty percent of the proceeds and payment of fees to the defendants providing telephone solicitation services, Parkersburg Wireless would not have had sufficient capital to remain in business long enough to achieve the projected returns. The Commission obtained preliminary injunctions against Parkersburg and thirteen other individual and corporate defendants and an order freezing the defendants' assets.

The Commission filed an action against Knoxville, LLC, a limited liability company that was seeking to raise $35 million to acquire 80 percent of a joint venture that would acquire and operate a wireless cable system in the Knoxville, Tennessee area (*SEC v. Knoxville, LLC*[3]*).* Prospective investors were solicited by telephone, and up to 52 percent of the proceeds from investors were to be paid as commissions or fees for telephone solicitations. Investors were told that they could expect returns of 300 percent to 400 percent in two to four years; these projections had no basis in fact. The Commission obtained a temporary restraining order and a temporary asset freeze in this case.

The defendants in *SEC v. Continental Wireless Cable Television, Inc.,*[4] were alleged to have raised over $34 million from 2,000 investors by representing that the funds would be used to acquire, develop and market wireless cable television systems in Nashville, Tennessee and New Orleans, Louisiana. Only $7.1 million was used for those purposes. The defendants, Continental Wireless and three of its officers and directors, misappropriated and misused investor funds to pay at least $15 million of the company's own overhead expenses, including $11 million in commissions and other sales expenses and $1.2 million in "loans" to the three individual defendants. The Commission obtained a preliminary injunction and an asset freeze in this case.

In *SEC v. Comcoa Ltd.,*[5] the Commission alleged violations by Comcoa and Thomas W. Berger, the chairman, president, and sole officer and director of Comcoa. Comcoa is purportedly in the business of preparing and filing applications with the Federal Communications Commission (FCC) for specialized mobile radio (SMR) licenses. Comcoa guaranteed that each investor would receive a license and represented that it would arrange for a systems operator to lease or purchase the license when granted. Although SMR licenses were promised, investors in fact obtained Private Carrier licenses. Comcoa raised in excess of $13 million from about 1,200 investors through a boiler room operation and the use of high pressure sales techniques; scripts used by Comcoa's telephone sales representatives and offering materials sent to investors contained material misrepresentations as to the profits to be realized, among other things. The Commission obtained a temporary restraining order and an asset freeze in this case.

A fraud in the offer and sale of interests in purported general partnerships to develop wireless cable television systems in Hot Springs, Arkansas, Clarksville, Tennessee, and Valdosta, Georgia

raised approximately $9 million for one partnership through Transamerica Wireless Systems, Inc., and began raising an additional $10.5 million for a second partnership through Intercontinental Telecommunications Corporation. In the Commission's enforcement action, *SEC v. Transamerica Wireless Systems,* Inc.,[6] the complaint alleged that both companies used television infomercials, mailings, and telephone boiler rooms to sell partnership interests. The companies falsely claimed that they were negotiating for FCC licenses and failed to disclose substantial sales commissions. In addition, they failed to disclose a pending Federal Trade Commission action alleging fraud in the sale of license application preparation and filing services by Danny Sterk, the chief executive officer of both companies and a defendant in the Commission's action. The Commission obtained a temporary restraining order and an asset freeze in this case.

2. *Prime Bank Cases*

During the last two years, the Commission has brought a number of enforcement actions involving so-called "prime bank" securities. The typical case involves the offer and sale of notes, debentures, letters of credit, or guarantees purportedly issued by one or more major international banks. Investors in these schemes are typically promised unrealistic rates of return, e.g., a 150 percent annualized rate of "profits." The Commission filed 11 injunctive actions alleging prime bank schemes during 1994. Common targets of these schemes include both institutional and individual investors, who also may be induced to participate in possible Ponzi schemes, involving the pooling of investors' funds to purchase "prime" bank financial instruments. During the year, the SEC issued a Bulletin to alert investors to these frauds.[7] The SEC also published a warning to investors concerning possible ongoing fraudulent attempts to sell "prime bank" securities purportedly issued by Banka Bohemia, A.S.,

a bank located in Prague, Czech Republic.[8] Despite Banka Bohemia's attempts to retrieve and cancel such securities, approximately $600 million in such securities remained outside the bank's control.

In *SEC v. John D. Lauer,*[9] the Commission alleged a scheme in which at least $12.5 million was raised from at least one investor, the Chicago Housing Authority's (CHA) Benefit Plan, through the offer and sale of interests in a program designed to purchase and trade "Prime Bank Instruments." John D. Lauer, CHA's manager of benefits, failed to disclose to CHA the role of the company under his control in the administration of the purported investment, his receipt of compensation in connection with the investment, and the resulting conflict of interest. Lauer also misappropriated $1.5 million from an account set up to facilitate transactions. The Commission obtained a temporary restraining order and an asset freeze in this case. In an August 25, 1994, opinion, the district court rejected claims by Lauer that the alleged activities were outside the scope of the federal securities laws. This case was pending at the end of the year.

In *SEC v. Northstar Investors Trust,*[10] the Commission alleged that the defendants raised more than $3.2 million from about 20 investors by selling an investment in which funds were pooled and purportedly used to purchase and sell "Prime Bank letters of credit." Investors were told that transactions between the banks and the institutional investors would result in returns of 2 to 3 percent per month (i.e., 24 to 36 percent per year). No bank instruments, letters of credit or other investments were purchased on behalf of investors, and investor funds were in fact diverted for other purposes. Northstar and defendants Stewart W. Cross, James G. Hands, III, Del Olson, and Cross & Associates consented to the entry of injunctions. Injunctions also were entered as a result of the Commission's motion for summary judgment against Stephen Cross and SLM Corp.

The Commission alleged that the defendants in *SEC v. North Pacific Investments,* Inc.,[11] raised at least $10 million from an investor in Hawaii in a scheme that would purportedly purchase and sell "European prime bank debt obligations." The funds were not used to purchase securities on behalf of the investor, but were in fact placed in bank accounts in the names of the defendants and were disbursed for the benefit of the defendants. Funds represented to be profits from prime bank debenture transactions were in fact a return of a portion of the investor's initial investment capital. The Commission obtained a preliminary injunction and an asset freeze in this case. This case was pending at the end of the year.

In *SEC v. Cross Financial Services,* Inc.,[12] the Commission alleged that the defendants offered and sold approximately $21 million in unregistered securities to over 700 investors. Cross Financial and the four individual defendants misrepresented that Cross Financial would use the investor funds to make loans secured by accounts receivable and to purchase bank guarantees or letters of credit. The defendants misappropriated over $12.9 million of the funds raised and engaged in a Ponzi scheme by using new investor funds to make principal and interest payments totalling $4.5 million to prior investors. The Commission obtained a preliminary injunction and an asset freeze in this case, as well as the appointment of a permanent receiver for Cross Financial. This case was pending at the end of the year.

The Commission's complaint in *SEC v. Prime One Partners, Corp.*[13] alleged a fraudulent scheme involving the offer and sale of "general partnership" interests in a prime bank investment program. Defendants Prime One Partners, Corp., Capital Asset Management and Monarch Associates International, Ltd., and their agents marketed the program through investment seminars touting a prime bank investment program in which investors were promised returns

of 80 percent to 400 percent. The defendants consented to the entry of injunctions and orders requiring the disgorgement of investor funds plus prejudgment interest and civil penalties in an amount to be determined. This case was pending at the end of the year as to two individual defendants added by the Commission's First Amended Complaint, filed after entry of the consent injunctions against the original defendants.

3. *Other Offering Cases*

The Commission filed an action against European Kings Club, three other corporate entities and four individuals, alleging a Ponzi scheme involving the offer and sale of unregistered securities in the form of letters of investment (*SEC v. European Kings Club*[14]*).* The letters purported to guarantee annual returns of 71 percent on investments, even though Kings Club had no legitimate means to generate sufficient revenues to pay such returns. Among other things, Kings Club failed to disclose a criminal investigation in Germany or actions by Swiss authorities to freeze and liquidate Kings Club's assets in Switzerland. The defendants consented to the entry of injunctions and orders requiring the payment of disgorgement and prejudgment interest totalling $997,343 and civil penalties totalling $1 million.

In the Commission's action against VestCorp Securities, Inc., First Pension Corporation and eight individuals, *SEC v. William E. Cooper,*[15] the complaint alleged that VestCorp offered and sold securities in the form of real estate limited partnership units, raising approximately $99 million. Many of the investors held their limited partnership interests in self-directed IRA accounts at First Pension. The limited partnerships never generated any income, and investor "returns" were paid by diverting other First Pension client funds. Two of the individual defendants misappropriated approximately $25

million of First Pension funds, and another defendant wrote 114 unauthorized checks totalling over $1 million on First Pension's custodial bank account. The complaint alleged that up to $125 million in investor and pension funds was at risk. The Commission obtained a preliminary injunction and other relief, including an asset freeze and an accounting. This case was pending at the end of the year.

In *SEC v. American Business Securities, Inc.,*[16] the Commission alleged that twelve individual and corporate defendants engaged in the fraudulent offer and sale of securities in the form of limited partnership interests and units of participation in grantor trusts issued by Southwest Energy Consultants, Inc. Through the aggressive sales efforts of American Business Securities, Inc., a registered broker-dealer, and its registered representatives, approximately $40 million was raised from about 1,000 investors. Funds were purportedly to be used to acquire interests in oil and gas producing wells, and annual returns of 12 percent to 20 percent were promised. In fact, returns to investors were preset and were not based on the actual production of the wells, which in some cases were no longer producing oil or gas. American Business Securities, Southwest Energy Consultants, and seven other defendants consented to the entry of injunctions. This case was pending at the end of the year as to two other defendants, against whom the Commission had obtained a temporary restraining order and an asset freeze.

In *SEC v. Norman L. Brooks,*[17] the Commission alleged a scheme by twelve individual and four corporate defendants that raised $3.5 million from over one hundred investors in 25 states through the sale of unregistered securities in the form of promissory notes. The proceeds of the sales were diverted and misused by the defendants. Tens of thousands of unsolicited telephone calls were

made through a boiler room, using scripts that contained material misrepresentations and omitted material facts. Investors were fraudulently induced to purchase the promissory notes by "guarantees" of annual rates of return from 10 percent to 14 percent. In addition, the sales personnel misrepresented that investments would be used in a fully-insured, risk-free consumer automobile financial operation. The Commission obtained a temporary restraining order and an asset freeze in this case. Default injunctions were entered against three corporate entities and two individuals. This case was pending at the end of the year as to the remaining defendants.

Financial Disclosure

Actions involving false and misleading disclosures concerning matters that affect the financial condition of an issuer, or involving the issuance of false financial statements often are complex and, in general, demand more resources than other types of cases. Effective prosecution in this area is essential to preserving the integrity of the full disclosure system. The Commission brought 78 cases containing significant allegations of financial disclosure violations against issuers, regulated entities, or their employees. Many of these cases included alleged violations of the books and records and internal accounting control provisions of the Foreign Corrupt Practices Act. The Commission also brought 31 cases alleging misconduct by accounting firms or their partners or employees.

In cease and desist proceedings, *In the Matter of Comptronix Corporation,*[18] the Commission alleged that, as a result of a fraudulent accounting scheme implemented by three members of Comptronix's senior management, Comptronix reported materially overstated sales, net income, and assets in periodic filings between 1989 and 1992. The inflated sales and earnings enabled Comptronix

falsely to report continued growth in revenues and earnings when the company was not profitable. Overall, Comptronix reported nearly $38 million in sales between 1989 and 1992 that had not taken place and cumulative profits of approximately $14.9 million when the company actually incurred cumulative losses during this period of about $11.8 million.

In *SEC v. Stanley Lepelstat,*[19] the Commission alleged a scheme extending over at least seven years in which six of the former officers and directors of Accuhealth, Inc., diverted corporate cash to fund a variety of off-books cash payments, including payments to officers, directors, and employees, and to make unrecorded purchases of inventory. Accuhealth also manipulated its earnings by overstating year-end inventory from 1989 through 1992. In addition, Stanley Lepelstat, Accuhealth's former chairman and chief executive officer, sold Accuhealth common stock while in possession of material non-public information regarding the company's true financial condition, thereby avoiding losses of $222,496.15. Two of the defendants consented to the entry of injunctions and to orders prohibiting them from serving as officers or directors of public companies; one of the settling defendants also agreed to pay a civil penalty of $10,000. This injunctive action was pending as to the other defendants at the end of the year. In related administrative proceedings*, In the Matter of Accuhealth, Inc.,*[20] the respondents consented to the entry of a cease and desist order. In *In the Matter of William Makadok, CPA,*[21] proceedings instituted pursuant to Rule 2(e), a former principal financial and accounting officer for Accuhealth consented to the entry of an order denying him the privilege of appearing or practicing before the Commission.

In *SEC v. PNF Industries, Inc.,*[22] the Commission alleged a financial fraud in connection with the bid by PNF Industries to become listed on the Emerging Company Marketplace of the

American Stock Exchange in 1992. PNF inflated its stockholder's equity from a deficit of $255,361 to a surplus of $16,125,963 by improperly accounting for a business combination, thereby creating the appearance that the company qualified for the exchange listing. PNF also omitted to state material facts about a licensing agreement and letters of intent with respect to fire retardant products for which it had obtained patents as a result of the business combination. Among other things, a control person of PNF, Alfred Avasso, engaged in insider trading in PNF stock and sold unregistered PNF stock; PNF's auditor, Louis Fox, lacked independence because he had agreed to have convertible preferred PNF stock transferred to a relative's account on his behalf. All but one of the defendants consented to the entry of injunctions. In addition, Avasso was ordered to disgorge $400,000. Fox and two other defendants were ordered to pay civil penalties totalling $50,000. This case was pending as to Otis Hastings, a former PNF officer, at the end of the year. In related administrative proceedings pursuant to Rule 2(e), Martin Halpern, the engagement partner on the audit of PNF's 1991 financial statements, consented to the entry of an order denying him the privilege of appearing or practicing before the Commission *(In the Matter of Martin Halpern, CPA*[23]*).*

The Commission filed an action against C.W. Earl Johnson, the former chief executive officer of Barton Industries, Inc., and Victor L. Joyce, Barton's former chief financial officer (*SEC v.* C.W. *Earl Johnson*[24]*).* The complaint alleged that the defendants directed Barton accounting personnel to falsify recorded inventory, which inflated Barton's pretax income during fiscal 1989 and 1990, and to record phony sales, further inflating pretax income during fiscal 1990. On quarterly reports for the first three quarters of 1990, Barton reported pretax income of $681,524, $719,404, and $1,034,251, instead of losses of at least $838,198, $1,022,301, and $1,254,305, respectively. Both defendants avoided losses by selling or donating

Barton stock while in possession of material non-public information about the falsified financial statements. Johnson consented to the entry of an injunction and a bar from acting as an officer or director of any public company. This matter was pending as to Joyce at the end of the year.

The Commission's complaint against Jere Bradwell, the president, chief executive officer and chairman of Silk Greenhouse, Inc. (SGI); Stuart G. Lasher, SGI's chief financial officer; and William T. Gilbert, SGI's vice president of finance, alleged that SGI, to avoid an expected third quarter loss in 1989 and meet estimated earnings for the quarter, included in its financial statements as "other income" the assets and liabilities of a company created by Bradwell to divert real estate commissions on new SGI store sites (*SEC v. Jere L. Bradwell*[25]*).* The complaint also alleged that $2.6 million of employee payroll expenses were improperly capitalized and deferred to the fourth quarter, and $1.5 million of advertising expenses were deferred. Bradwell sold 62,500 shares of SGI common stock prior to the public announcement of the third quarter results, avoiding losses of approximately $781,000. The defendants consented to the entry of injunctions. Bradwell was ordered to disgorge $781,000 plus prejudgment interest and to pay a civil penalty under ITSA. Lasher and Gilbert, who are certified public accountants, also consented to an order in related Rule 2(e) proceedings, by which they were denied the privilege of appearing or practicing before the Commission. *In the Matter of Stuart* G. *Lasher, CPA.*[26]

In *SEC v. Transmark USA, Inc.,*[27] the Commission alleged that the defendants failed to disclose the nature of certain transactions and materially misstated the financial condition of the company's principal subsidiary, Guarantee Security Life Insurance Company (GSL). The complaint alleged four instances of related sale and repurchase transactions in high yield securities between GSL and

Merrill Lynch. These transactions occurred at year-end and were intended to replace temporarily GSL's portfolio of high yield securities with either a cash receivable or liquid Treasury securities, resulting in increased reported statutory capital and surplus. The defendants consented to the entry of injunctions.

In *In the Matter of Donald F. Withers, CPA,*[28] the Commission found that the respondent, a partner in Coopers & Lybrand, engaged in improper professional conduct In connection with the transactions alleged in *SEC v. Transmark USA, Inc.* Withers consented to the entry of an order suspending him from appearing or practicing before the Commission for a period of five years.

The Commission alleged in *In the Matter of Harry D. Sweeney, CPA,*[29] that Sweeney and Henry Gayer, the engagement partners for audits of Sahlen & Associates in 1988 and 1987, respectively; and Timothy S. Hart, the manager for both audits, caused unqualified audit reports to be issued. The defendants also failed to obtain sufficient competent evidential matter with respect to the existence, valuation, and presentation of at least $45 million of overstated receivables. This matter was pending at the end of the year.

In Rule 2(e) proceedings against Edward Jan Smith, a partner at Price Waterhouse, and Joel E. Reed, a senior manager for the firm, the Commission alleged that the respondents failed to conduct the 1988 and 1989 audits of Amre, Inc., in accordance with generally accepted auditing standards *(In the Matter of Edward Jan Smith, CPA*[30]*)* As a result of a fraudulent scheme by Amre's management, the company's earnings and revenues had been overstated in its 1988 financial statements and understated in fiscal 1989. The respondents consented to the entry of an order denying them the right to appear or practice before the Commission.

Insider Trading

Insider trading occurs when a person in possession of material non-public information engages in securities transactions or communicates such information to others who trade. Insider trading encompasses more than trading and tipping by traditional insiders, such as officers or directors who are subject to a duty to either disclose any material non-public information or abstain from trading in the securities of their own company. Violations also may arise from the transmission or use of material non-public information by persons in a variety of other positions of trust and confidence or by those who misappropriate such information.

In addition to permanent injunctions, the Commission often seeks ancillary relief, including disgorgement of any profits gained or losses avoided. The ITSA penalty provisions authorized the Commission to seek a civil penalty, payable to the United States, of up to three times the profit gained or loss avoided against persons who unlawfully trade in securities while in possession of material non-public information or who unlawfully communicate material non-public information to others who trade. Civil penalties also can be imposed upon persons who control insider traders. During 1994, the Commission brought 45 cases alleging insider trading violations.

In connection with its proceedings involving financial fraud by Comptronix Corporation, the Commission filed an injunctive action against Richard F. Adler, a former director of Comptronix, who learned of the fraud and tipped this information to Harvey L. Pegram, a friend and business associate (*SEC v. Richard F. Adler*[31]*).* Pegram sold his Comptronix stock and tipped Philip L. Choy, who sold Comptronix stock held in the name of his company, Magatronic Trading Limited. Domer L. Ishler, another friend and business associate of Adler's, also unlawfully received the adverse information

and purchased Comptronix put options. Pegram and Choy avoided losses of approximately $2.3 million and $75,000, respectively, and Ishler made a profit of approximately $368,000. This case was pending at the end of the year.

SEC v. Eugene Dines[32] was an action against Bruce Dines, a former director of Colorado National Bankshares (CNB), and his brother, Eugene Dines. In connection with his employment, Bruce Dines learned that First Bank Systems was making an offer to merge with or acquire CNB. He communicated this information to his brother, who purchased 30,000 shares of CNB common stock prior to the public announcement of a merger agreement. Eugene Dines realized profits of $214,000 on his CNB transactions. The defendants consented to the entry of an injunction and an order requiring them to disgorge a total of $214,000 plus prejudgment interest of $12,847 and to each pay a civil penalty under ITSA of $214,000.

The defendant in *SEC v. Jonathan Mayhew*[33] purchased the common stock of Rorer Group, Inc., and call options on such stock, while in possession of material non-public information concerning merger discussions between Rorer and Rhône-Poulenc, S.A. Jonathan Mayhew's trades followed his receipt of a tip from an employee of a human resources consulting firm that had been retained by Rorer in connection with the merger discussions. After the public announcement of the discussions, Mayhew realized profits of $255,000. This case was pending at the end of the year.

Prior to the public announcement of a merger agreement between MidSouth Corp. and Kansas City Southern Industries Inc., a lobbyist for Kansas City Southern working in Washington, D.C. engaged in insider trading in MidSouth common stock (*SEC v. Julia Peck Mobley*[34]*).* The lobbyist, Sydney Probst, misappropriated material non-public information, traded MidSouth securities while in

possession of this information, and recommended the purchase of MidSouth securities to a family member and two friends, Julia Peck Mobley and Rosamond Brown, who also traded. One of Probst's friends tipped an additional person who traded. Probst and the tippees realized aggregate profits of approximately $35,000. Probst consented to an injunction and to an order requiring her to disgorge profits of $13,572 plus prejudgment interest and to pay an ITSA penalty of $13,572. This case was pending as to Mobley and Brown at the end of the year.

Manipulation

The SEC is charged with ensuring the integrity of trading on the national securities exchanges and in the over-the-counter markets. The SEC staff, the exchanges, and the NASD engage in surveillance of these markets.

The Commission charged U.S. Environmental, Inc., Castle Securities Corp., and nine individuals with conducting a fraudulent offering and subsequent manipulation of common stock issued by U.S. Environmental (*SEC v. U.S. Environmental, Inc.*[35]*).* The defendants engaged in a fraudulent "blind pool" offering bringing U.S. Environmental public and thereafter caused the company to make false and misleading representations, including that U.S. Environmental had a proven, cost-effective process for detoxifying hazardous waste and owned a 50 percent interest in a pilot plant. Defendants, who controlled the entire float, manipulated the price from $0.05 per unit to approximately $5.00 per share; the defendants then paid kickbacks to brokerage firms to sell several hundred thousand shares to investors who paid a total of more than $1 million for the stock. The price of the stock reached $7.00 per share before collapsing to between $0.06 and $0.11 per share. U.S. Environmental and two stock promoters, Mark D'Onofrio and Ramon D'Onofrio,

consented to the entry of injunctions, and the D'Onofrios also were jointly and severally ordered to disgorge $940,374.52 plus prejudgment interest. An order was entered prohibiting the D'Onofrios from serving as officers or directors of public companies, and they were enjoined from acting as promoters, finders, consultants, agents or in any other capacity with any broker, dealer, or issuer in the issuance or trading of securities. This case was pending as to the other defendants at the end of the year.

In *In the Matter of J. Peek Garlington,* Jr.,[36] the Commission alleged that the respondent, the chairman of Cousins Properties, Inc., engaged in a series of illegal trades in the common stock issued by Cousins. The respondent manipulated the closing price of Cousins common stock by placing orders to buy small lots at the end of the trading day, i.e., by "marking the close," on seventy-seven days over a six-month period. These activities increased the closing price of Cousins common stock, and thereby increased the equity in a margin account in which the respondent held a substantial position of the stock. The purpose of the scheme was to satisfy or prevent margin maintenance calls. The respondent consented to the entry of a cease and desist order by which he was ordered to disgorge $92,750 plus interest in the amount of $29,424.36.

In a case involving the operation of a boiler room by a former registered broker-dealer, Chelsea Street Securities, Inc., the Commission alleged that defendants Gary S. Williky and James J. Romano, and salesmen under their control implemented undisclosed, manipulative sales practices, including "matched" trading, the parking of securities in Chelsea customer accounts, and "wash" purchase and sale transactions (*SEC v. Gary* S. *Williky*[37]*).* These manipulative practices were implemented to generate retail demand for four securities in which the broker-dealer made a market, causing an artificial rise in the price of these securities. Williky

consented to the entry of an injunction and an order requiring him to pay disgorgement and a civil penalty in amounts to be determined. This case was pending at the end of the year.

The Commission filed an action against nine individual defendants, alleging a scheme in which kickbacks were paid to registered representatives to recommend the purchase of common stock issued by Fairmont Resources Inc., a Canadian natural gas company traded on the Alberta Stock Exchange, in an effort to manipulate the price and create the appearance of an active trading market for the stock (*SEC v. Robert L. Shull*[38]*).* Three of the defendants agreed to acquire a controlling interest in Fairmont, to manipulate its stock, and to sell at artificially enhanced prices, Kickbacks totalling more than $400,000 were paid to five other defendants. Manipulative activity caused Fairmont stock to increase from C$0.30 per share to C$3.05 per share in less than six months. The three defendants controlling Fairmont realized illegal profits of as much as US$1 million from the scheme. This case was pending at the end of the year.

The Commission also took action in cases involving fraudulent schemes involving the short sale of securities during the period between the filing of a registration statement for a secondary offering and the time at which sales pursuant to the registration statement may be made. Because short selling in anticipation of a public offering may result in a decrease in the price of the security, such activity may deprive the issuer of offering proceeds that would otherwise have been obtained. In *SEC v. Curtis Ivey,*[39] the Commission alleged that the defendants sold short the securities of Safeway, Inc., Enron Corp., Dillard Department Stores, Inc., and Household International, Inc., prior to the effective dates of registration statements, and then covered with securities purchased in the public offering. The defendants realized profits of $80,365. The

defendants consented to the entry of injunctions and an order requiring them jointly and severally to disgorge $80,365 plus prejudgment interest.

The Commission alleged that Stanley Berk realized profits of $35,500 from short sales of the securities of Dillard Department Stores, Inc., Safeway, Inc., and Household International, Inc., and obtained approximately $5,000 from trading associates who engaged in similar unlawful conduct in connection with public offerings of five other issuers *(In the Matter of Stanley Berk*[40]*).* This case was pending at the end of the year.

Broker-Dealer Cases

Each year, the Commission files a significant number of enforcement actions against broker-dealer firms and persons associated with them. The Commission's actions against broker-dealers often focus on violations of the net capital and customer protection rules, violations of books and records provisions, or fraudulent sales practices. The Commission also takes action against broker-dealer firms and their senior management for failure to supervise employees with a view to preventing violations of the federal securities laws.

Several cases against broker-dealer firms involved violations in the market for United States Treasury securities. The Commission instituted administrative proceedings against The Chicago Corporation (TCC), a registered broker-dealer, alleging that between 1984 and 1991 it had engaged in a practice that resulted in the submission of inaccurate bid tender forms by two primary dealers in Treasury securities in connection with noncompetitive orders in Treasury auctions *(In the Matter of The Chicago Corporation*[41]*).* TCC submitted noncompetitive bids in the names of various individuals in approximately thirty auctions per year, and then purchased the

securities acquired by these individuals pursuant to an "option agreement." This practice allowed TCC to circumvent Treasury regulations prohibiting the purchase of more than $1 million in Treasury securities pursuant to noncompetitive bidding. TCC consented to the entry of a cease and desist order and to an order requiring the disgorgement of $250,000 plus interest and a civil penalty of $250,000.

Similarly, in *In the Matter of Cantor Fitzgerald* & Co.,[42] the Commission alleged that Cantor Fitzgerald & Co., a registered broker-dealer, committed violations in the purchase and sale of Treasury securities issued through the noncompetitive auction process. Cantor Fitzgerald's books and records failed to reflect pre-auction agreements between the firm and its customers to sell the securities awarded in the auction. Cantor Fitzgerald consented to the entry of a cease and desist order requiring the disgorgement of $90,000 plus interest and the payment of a $100,000 civil penalty.

In the Matter of Goldman, Sachs & Co.,[43] cease and desist proceedings against Goldman Sachs & Co., a registered broker-dealer, the Commission alleged that the firm falsely recorded prearranged transactions in Treasury securities with Salomon Brothers, Inc., other broker-dealers, and certain institutional customers during 1985 and 1986 to realize a total of $36.6 million in losses for tax purposes. Goldman Sachs also falsely recorded prearranged trades in four transactions with Salomon during 1986 as an accommodation to Salomon. Goldman Sachs consented to the entry of a cease and desist order by which it was required to pay a civil money penalty of $250,000.

The Commission alleged violations of the books and records provisions *in In the Matter of Merrill Lynch, Pierce, Fenner & Smith, Inc.,*[44] administrative proceedings against Merrill Lynch; Robert

Plunkett, a trader formerly associated with Merrill Lynch; and Frederick Roemer, a Merrill Lynch corporate bond salesman. The Commission found that Merrill Lynch failed to record properly certain securities transactions in two separate matters. The first matter involved related sale and repurchase transactions designed to permit a customer, Guarantee Security Life Insurance Company, temporarily to replace high yield securities with a cash receivable or liquid Treasury securities at year end, thereby avoiding certain reserve requirements of Florida insurance law. The second matter involved a series of sale or repurchase transactions between Merrill Lynch, Reliance Group Holdings, Inc., and a third party, designed to permit Reliance to realize gains on certain securities. Respondents, without admitting or denying the Commission's findings, consented to the entry of a cease and desist order by which they were censured and Merrill Lynch was required to adopt internal procedures, policies, and controls reasonably designed to assure compliance with broker-dealer recordkeeping requirements.

In *In the Matter of George F.M. Lee,*[45] the Commission alleged that the respondent, who was president, general principal, compliance officer and financial principal of a broker-dealer firm, failed reasonably to supervise two former branch managers who had engaged in a scheme to distribute unregistered securities of Pacific Waste Management, Inc. One of the managers sold approximately 80,000 shares for his own account while acting as a promoter for Pacific Waste. The other manager solicited at least 41 customers to purchase approximately 183,020 shares he had received gratuitously from an officer of Pacific Waste. The Commission found that the respondent's failure to provide closer scrutiny of the branch managers' activities contributed to their ability to engage in the wrongful conduct. The respondent consented to the entry of an order suspending him from association in a supervisory capacity for a

period of six months and requiring him to pay a civil penalty of $5,000.

The Commission alleged net capital violations in administrative proceedings against Colonial Management Associates, Inc., a firm dually-registered as a broker-dealer and an investment adviser *(In the Matter of Colonial Management Associates, Inc.*[46]*).* Colonial failed to calculate timely its net capital on a monthly basis for eight months during 1991 and 1992. In addition, Colonial had a net capital deficiency during the period November 2 to December 29,1992, resulting from its use of approximately $16 million from the liquidation of certain securities to reduce the outstanding balance on a revolving credit line maintained by its corporate parent.

SEC oversight of broker-dealers often involves actions alleging fraudulent sales practices. In *SEC v. Thomas Frank Bandyk,*[47] the Commission alleged that the defendant engaged in unauthorized, excessive and unsuitable trading, misrepresented and omitted to state several material facts to customers in connection with such trading, and caused several customers to suffer substantial losses. Among other things, the defendant persuaded customers to sign margin agreements by misrepresenting that the purpose of the agreements was to provide overdraft protection for checks written against the accounts; customers receiving margin calls were told that the calls were the result of computer errors and could be ignored. Bandyk consented to the entry of an injunction.

The Commission has also taken action against persons associated with broker-dealer firms who steal funds intended for the purchase of securities. In administrative proceedings against a registered representative of Advest, Inc., the Commission alleged that the respondent misappropriated approximately $902,291 in customer funds that had been given to him for investment *(In the*

Matter of James M. Coyne, Jr.[48]). The respondent forged customer signatures on liquidation authorization forms and forged endorsements on checks issued by Advest to customers. The respondent consented to a bar from association. In related criminal proceedings, the respondent was sentenced to eighteen months incarceration and ordered to pay restitution of $203,501.99.

Investment Adviser and Investment Company Cases

The Commission instituted several significant cases involving investment advisers and investment companies.

The Commission instituted cease and desist proceedings against Synovus Securities, Inc., a broker-dealer and investment adviser, and Clark L. Reed, the president and director of Synovus at all relevant times *(In the Matter of Synovus Securities, Inc.*[49]*).* Synovus was involved as principal with certain customers and allegedly interpositioned an individual, Richard T. Taylor, who promptly was able to purchase bonds from, or resell bonds to, other brokers at a profit in over 120 municipal bond transactions between 1988 and 1991. Synovus and Reed consented to the entry of a cease and desist order and orders requiring them to pay civil penalties of $200,000 and $50,000, respectively. Reed also consented to a bar from association with regulated entities. Related administrative proceedings against Taylor, *In the Matter of Richard T. Taylor,*[50] were pending at the end of the year.

In *In the Matter of Strong/Corneliuson Capital Management, Inc.,*[51] the Commission alleged violations by Strong/Corneliuson Capital Management, Inc. (SCCM), the investment adviser to eleven mutual funds and to various pension funds and other clients; Richard S. Strong, the founder, controlling shareholder and chairman of SCCM, and chairman of each of the funds managed by SCCM; and Bruce D. Behling, a senior vice president and former president of

SCCM and the former president and treasurer of each of the funds. SCCM and Strong caused the funds to engage in securities transactions with each other and with Harbour Investments Ltd, an investment company in which Strong and Behling had a financial interest; these transactions with affiliated persons were not disclosed by SCCM. SCCM also caused Harbour to invest in securities recommended to SCCM clients, and Strong invested in the securities of three issuers recommended to clients. The respondents consented to the entry of a cease and desist order by which they were censured, and SCCM was ordered to comply with undertakings designed to prevent future violations.

In *SEC v. Donna Tumminia,*[52] the complaint alleged that Donna Tumminia, the head trader for Shearson Lehman Advisors (SLA), concealed from her employer the volume of securities trades that she directed to her husband, Philip Tumminia, who was a direct access broker on the floor of the New York Stock Exchange and a registered representative of Adler, Coleman & Co. Donna Tumminia also failed to disclose to her employer that commissions paid on the transactions were going directly to her husband, minus only a 1¢ per share clearance fee to Adler. The Tumminias caused advisory clients of SLA to pay excessive mark-ups and mark-downs on riskless principal trades executed by Philip Tumminia. The Tumminias consented to the entry of an injunction and orders requiring them to disgorge $617,314.62 plus prejudgment interest and to pay civil penalties of $617,314.62.

The respondent in *In the Matter of Joan Conan*[53] was a portfolio manager in the high yield bond department of a registered investment adviser. While performing research for the funds under her management, Conan learned of certain warrants issued by Champion Parts, Inc., that offered holders the option of paying the exercise price through the surrender of notes issued by Champion.

The notes so used would be valued at par. Although the funds held Champion notes which were then trading at below par, Conan purchased 50,000 Champion warrants for her own account for $12,500, which she sold the following month for $225,000. Conan failed to disclose her transactions to her employer. The Commission found that Oman's activities were in breach of her fiduciary duty to the funds and compromised her independence as a fiduciary. Conan consented to the entry of a cease and desist order by which she was barred from association.

The Commission filed an emergency action in which it alleged that the management of an investment company had become increasingly deadlocked and in disarray (*SEC v. Centurion Growth Fund, Inc.*[54]*).* At the time of the Commission's action, the fund did not have an investment adviser, counsel, underwriter, president, secretary, or treasurer, nor did it have a properly constituted board of directors. The Commission obtained a preliminary injunction and other relief, including the appointment of a receiver, an asset freeze, and an order suspending the offer, sale, and redemption of the fund's shares until permitted by the court. This case was pending at the end of the year.

The Commission instituted proceedings against Seaboard Investment Advisers, Inc., a registered investment adviser with assets in excess of $1.1 billion under management, and two of Seaboard's officers *(In the Matter of Seaboard Investment Advisers, Inc.*[55]*).* The Commission alleged that Seaboard published, circulated, or distributed advertisements that contained false or misleading performance figures covering the period from 1984 through 1991. Seaboard also falsely advertised that its performance results were audited. The respondents consented to the entry of cease and desist orders. In addition, Seaboard was ordered to pay a civil penalty of $1 million.

Cease and desist proceedings against Terence Mulrooney involved allegations that the respondent, a registered representative employed by a bank's brokerage subsidiary, prepared a one-page sales sheet listing some false and misleading characteristics and yields for mutual funds offered by his employer *(In the Matter of Terence Patrick Mulrooney*[56]*).* The sales sheets contained yield figures that were not computed in accordance with statutory requirements, and failed to disclose the time periods to which they corresponded. In some cases, the yield figures were, in actuality, total return figures representing a time span of up to ten years. The Commission alleged that the respondent's conduct violated advertising rules promulgated under the Investment Company Act, Mulrooney consented to the entry of the cease and desist order by which he was censured and suspended from association for a period of twelve months.

The Commission's cease and desist proceedings against Melvin Hirsch, *In the Matter of Melvin L. Hirsch,*[57] arose from the respondent's diversion of funds from Transportation Capital Corporation (TCC), which was a registered closed-end management investment company of which Hirsch was president and chairman. Hirsch caused TCC to make undocumented loans to him that were not in accordance with TCC's stated investment policies and were never properly reflected on TCC's books and records or otherwise disclosed to investors. Hirsch also purchased certain TCC assets without obtaining an exemptive order from the Commission,

Sources For Further Inquiry

The agency publishes the *SEC Docket,* which includes announcements regarding enforcement actions. SEC litigation releases describe civil injunctive actions and also report certain criminal proceedings involving securities-related violations. These

releases typically report the identity of the defendants, the nature of the alleged violative conduct, and the disposition or status of the case, as well as other information. The *SEC Docket* also contains Commission orders instituting administrative proceedings, making findings and imposing sanctions in those proceedings, and initial decisions and significant procedural rulings issued by Administrative Law Judges.

International Affairs

The Office of International Affairs (OIA) has primary responsibility for the negotiation and implementation of information-sharing arrangements, and for developing legislative and other initiatives to facilitate international cooperation, OIA coordinates and assists in making requests for assistance to, and responding to requests for assistance from, foreign authorities. OIA also addresses other international issues that arise in litigated matters, such as effecting service of process abroad and gathering foreign-based evidence under various international conventions, freezing assets located abroad, and enforcing judgments obtained by the SEC in the United States against foreign parties. In addition, OIA operates in a consultative role regarding the significant ongoing international programs and initiatives of the SEC's other divisions and offices. OIA is responsible for the SEC's technical assistance programs for countries with emerging securities markets. OIA also consults with and provides technical assistance to other Federal agencies regarding trade-related issues relevant to the regulation of securities markets in the United States.

Key 1994 Results

OIA made 226 requests for enforcement assistance on behalf of the Commission to foreign governments and responded to 296 requests for enforcement assistance from foreign governments.

The SEC signed a comprehensive Memorandum of Understanding (MOU) for consultation and cooperation in enforcement-related matters with the Australian Securities Commission. Also, the SEC signed an MOU with the China

Securities Regulatory Commission (CSRC) that provides for training and technical assistance to the CSRC, and for mutual enforcement assistance. This brings the total number of MOUs and other less formal agreements executed by the SEC to more than 20.

The SEC's leadership role and active involvement in the Council of Securities Regulators of the Americas (COSRA) and the International Organization of Securities Commissions (IOSCO) have advanced Commission goals for international enforcement assistance and cooperation on a multilateral basis. Two important multilateral resolutions were adopted by COSRA and IOSCO members. First, the membership of COSRA adopted a precedent-setting resolution on enforcement cooperation that will serve as a framework for multilateral collaboration to facilitate the enforcement of COSRA members' securities laws. Second, the members of IOSCO adopted a resolution which calls upon current members and future applicants to make explicit their commitment to the core IOSCO principles of high regulatory standards and mutual assistance.

Arrangements for Mutual Assistance and Exchanges of information

There has been a dramatic increase in the SEC's need to obtain foreign-based information to protect the United States markets and investors from cross-border fraud and other violations of the United States securities laws. In this regard, the SEC has developed ways to enhance international mechanisms for effective market surveillance and information sharing, and for cooperation in the investigation and prosecution of cross-border fraud and market manipulation.

The SEC has worked actively to forge strong bilateral and multilateral relationships with its foreign counterparts. In particular, the SEC has entered into more than 20 MOUs, and other less formal agreements, to establish the means for sharing information and providing comprehensive enforcement assistance in virtually all facets of the securities markets. Such mechanisms have improved the SEC's ability to detect and prosecute violations of the United States securities laws where information is needed from abroad. In addition, the SEC's commitment to international securities organizations has augmented its bilateral and multilateral efforts in the enforcement area.

On October 20, 1993, the SEC entered into an MOU with the Australian Securities Commission (ASC). The MOU creates a framework to facilitate mutual assistance between the SEC and the ASC, and formalizes the excellent working relationship that has existed between the two Commissions. The MOU also provides for consultation on matters relating to the operation of the securities markets of their respective countries and on the operation of the MOU. The MOU further provides for mutual assistance and cooperation in the full range of enforcement and regulatory matters. For example, it provides for assistance in securities matters involving insider trading and other fraudulent or manipulative practices; disclosure requirements for issuers, persons, and regulated entities; and the financial or other qualifications of those involved in the securities industry.

On April 28, 1994, the SEC entered into an MOU with the CSRC, the first such understanding between China and a Western securities regulatory authority. The MOU formalizes a cooperative and consultative relationship between the SEC and the CSRC, and establishes a framework for the SEC to provide technical assistance to the CSRC. The MOU also provides for mutual assistance in

obtaining information and evidence to facilitate the enforcement of the authorities' respective laws relating to United States and Chinese securities matters. Thus, the MOU should facilitate Commission enforcement actions in cases where relevant information is located in China. Because Chinese securities laws and regulations were still being formulated and adopted at the time of the signing of the MOU, the MOU specifically provides that procedures for making and executing requests for assistance, permissible uses of information, and confidentiality requirements are to be addressed on a case by case basis.

On November 3, 1993, the governments of the United States and Switzerland exchanged Diplomatic Notes relating to the Treaty Between the United States and Switzerland on Mutual Assistance in Criminal Matters which expand the Commission's ability to prosecute securities law violations based on information located in Switzerland. Pursuant to the Notes, the SEC now may use information located in Switzerland as evidence in civil and administrative proceedings involving a wide array of securities-related offenses. Based on an exchange of Notes in 1987, the SEC previously had been only able to use such information in cases involving insider trading.

In 1994, the SEC established the first official mechanism by which it may seek legal assistance from Germany. In a Diplomatic Note dated March 22, 1994, the German Foreign Office confirmed that the SEC may seek assistance under the German Law on Legal Assistance in Law Enforcement Matters (*Gesetz über die Internationale Rechtshilfe in Strafsachen*)(IRG*).* The IRG authorizes the German Ministry of Justice to seek through the relevant state *(Länder)* governments, among other things, documents and testimony on behalf of a foreign law enforcement authority in connection with an investigation.

Enforcement Cooperation

The table below summarizes the international requests for assistance made and received by the SEC.

[table deleted]

The case of *SEC v. Jose Antonio Feliu Roviralta,* Lit. Rel. No. 14232, C.A. No. 94-1963 (D.D.C, September 13, 1994) provides an excellent example of how international assistance can further an SEC investigation. Based in part on assistance, including the provision of documents and taking of testimony, provided by Italian, Spanish, and Swiss authorities, the SEC was able to proceed with an insider trading investigation that otherwise might have been closed due to a lack of evidence in the United States. As a result, in September 1994, the Commission filed a civil injunctive action against Jose Antonio Feliu Roviralta, alleging insider trading in connection with his purchase of Altos Computer Systems, Inc. stock. Roviralta, without admitting or denying the allegations of the Commission's complaint, consented to the entry of a final judgment permanently enjoining him from further violations of Section 14(e) of the Exchange Act and Rule 14e-3 and agreed to pay a total of $252,971.66 in disgorgement, prejudgment interest, and penalties.

In addition to ongoing work in the area of enforcement assistance, in August 1994, OIA testified on behalf of the SEC before a subcommittee of the United States Senate Judiciary Committee in support of the International Antitrust Enforcement Assistance Act of 1994. The testimony discussed the SEC's experience with international enforcement cooperation. In 1988, Congress enacted Section 21(a)(2) of the Exchange Act to allow the SEC to gather information about potential violations of foreign securities laws at the request of foreign securities authorities. In addition, the testimony stated that Section 21(a)(2) has "become a model throughout the

world for developing legislation to authorize securities regulators to assist their counterparts in investigating cross-border violations of law." Subsequently, Congress has enacted the antitrust enforcement legislation.

Technical Assistance

The SEC is committed to providing technical assistance to emerging securities markets to the extent to which resources allow it. Such technical assistance is intended to develop a regulatory infrastructure to promote investor confidence in emerging markets. OIA is responsible for coordinating the SEC's overall international technical assistance program.

Each spring the SEC hosts the International Institute for Securities Market Development (Market Development Institute), an intensive two-week, management-level training program covering a full range of topics relevant to the development and oversight of securities markets. The Market Development Institute is intended to promote market development, capital formation, and the building of sound regulatory structures in emerging market countries. The fourth annual Market Development Institute was held in the spring of 1994, with 87 delegates from 50 countries in attendance.

In 1994, the SEC expanded upon the successful Market Development Institute concept by inaugurating a one-week International Institute for Securities Enforcement and Market Oversight (Enforcement Institute) for foreign securities regulators. It is anticipated that the Enforcement Institute will be held on an annual basis, beginning in October 1994. The new program is designed to promote market integrity and foster the development of closer enforcement cooperation, and will include practical training sessions on SEC enforcement investigations, investment company and adviser inspections, broker-dealer examinations, and market

surveillance. Approximately 85 individuals representing 45 countries attended.

To complement its domestic training programs, the SEC has executed agreements with foreign aid organizations, pursuant to which SEC staff may provide technical assistance to foreign regulatory authorities. Most recently, in September 1994, the SEC entered into a comprehensive two-year interagency agreement with the United States Agency for International Development (USAID) to fund SEC technical assistance in Russia and other Newly Independent States of the former Soviet Union. The SEC also has entered into a technical assistance understanding with the Inter-American Development Bank which provides for assistance to emerging securities markets in Latin America.

International Organizations and Multilateral Initiatives

The SEC benefits from the opportunity to better understand foreign regulations, markets, and practices through participation in multilateral organizations. Moreover, through its involvement in international organizations, the SEC has the opportunity to promote its views on important issues that affect the United States securities markets and the SEC's regulatory program, and help develop international consensus on these issues. During 1994, the SEC contributed to the work of the following international organizations and multilateral initiatives:

The International Organization of Securities Commissions

IOSCO is an international forum created to promote cooperation and consultation among regulators overseeing the world's securities markets. With over 100 members, most of the world's securities regulators are represented. The SEC plays a leadership role in IOSCO. Over the years, the SEC has been actively involved in many

aspects of the organization's work, particularly in work relating to: facilitating multinational offerings; identifying accounting and auditing standards that would be used in multinational offerings; developing common capital adequacy requirements; understanding the implications of international settlement requirements; and fostering the international enforcement of securities laws.

The Working Party on Enforcement and the Exchange of Information completed a report entitled, *Issues Raised for Securities and Futures Regulators by Under-Regulated and Uncooperative Jurisdictions,* which was released at the 1994 IOSCO Annual Conference. The report considers the difficulties that regulators face when information they seek in investigating securities or futures violations is located in jurisdictions that cannot or will not share that information with foreign regulators. Based on the report, IOSCO adopted a Resolution on Commitment to Basic IOSCO Principles of High Regulatory Standards and Mutual Cooperation and Assistance. The resolution calls upon IOSCO members to make explicit their commitment to the core IOSCO principles of high regulatory standards and mutual assistance, and requires members to prepare self-evaluations of their regulatory systems. In publishing the report and adopting the resolution, IOSCO took significant steps toward addressing the enforcement problems caused by under-regulation and lack of cooperation. Those actions by IOSCO are of importance to the SEC's international enforcement program because they may serve as a springboard for enhancing enforcement cooperation among lOSCO's overall membership.

During 1994, several other reports were prepared by working parties and released by lOSCO's Technical Committee. These reports dealt with regulatory issues involving cross-border proprietary screen-based trading systems, over-the-counter derivatives, and

cross-border mutual funds. The SEC participated in the preparation of each of these reports.

Council of Securities Regulators of the Americas

In June 1992, the securities regulatory authorities of North, South, and Central America, and the Caribbean announced the creation of a new organization, COSRA, to provide a forum for mutual cooperation and communication in the Americas. The SEC actively promoted the concept of a regional organization and, currently, serves as its Chairman. COSRA's membership represents both advanced and emerging markets, and the organization strives to enhance the efforts of each country to develop and foster the growth of fair and open securities markets.

In June 1994, during the Third Annual Meeting of COSRA, the members reached a precedent-setting, multilateral understanding on enforcement cooperation. From the SEC's perspective, the resolution substantially advances its international enforcement program by developing a broad-based framework for cooperation with countries where bilateral MOUs may not be feasible. In addition, the membership identified principles for the provision of full and fair enterprise-related disclosure, and agreed to use their efforts to implement and maintain a mandatory disclosure system based on these principles.

The enforcement resolution directs COSRA members to use their authority to assist one another, to the fullest extent possible according to their respective laws, in obtaining information necessary to ensure compliance with domestic securities laws. In addition, the resolution calls on the members to strive to obtain the necessary legal authority, or seek the assistance of other government agencies, to allow members to fulfill their pledges of cooperation to one another. Lastly, the resolution directs the members to review and

assess continuously the degree to which assistance can be provided with a view to enhancing cooperation among the membership. The resolution does not modify or supersede in any respect any understandings or agreements otherwise reached among or between COSRA members.

The implementation of disclosure systems based on principles to ensure full and fair enterprise-related disclosure and effective enforcement will strengthen the market of each COSRA member. Recognizing this, the members also adopted a corporate disclosure resolution. The resolution identifies the steps necessary to establish and maintain a mandatory system for corporate disclosure, and incorporates a set of principles governing such things as the timing and content of corporate disclosures. The resolution and its principles are intended to serve as a model for COSRA members to use to implement mandatory disclosure systems in their domestic markets and are similar in large measure to disclosure standards already in place in the United States.

The Organization for Economic Cooperation and Development (OECD)

The anti-bribery provisions of the Foreign Corrupt Practices Act have been criticized as potentially having an anti-competitive impact on companies in the United States because the law prohibits companies with securities listed in the United States from making payments to foreign public officials to obtain or retain business, while no other country applies such prohibitions to its companies. At the direction of Congress, the United States government has initiated and continues to actively participate in the efforts of the OECD to address the issue of illicit payments, and the SEC participates in the United States efforts in that regard. By taking action that will bring other countries up to the United States standard so that bribery of

foreign public officials will be universally proscribed, the goal of ensuring a level playing field will be reached.

In May 1994, the OECD adopted a recommendation on measures that OECD members should take to combat bribery of foreign public officials by their nationals. The SEC worked with the United States Departments of State, Justice, and Commerce in connection with efforts at the OECD to reach consensus on this issue. Essentially, the recommendation urges OECD members to take "concrete and meaningful steps" to meet the goal of combating illicit payments. Under the recommendation, these steps may include: making bribery of foreign public officials a criminal act; adopting civil and administrative laws and regulations to make bribery illegal; amending the existing tax laws that might encourage bribery (such as deductibility of the bribe); and other steps to ensure adequate financial reporting.

The SEC staff provided technical assistance to the United States Department of Treasury in connection with the OECD's examination of regulation in the United States and the OECD Codes of Liberalization of Capital Movements and Liberalization of Current Invisible Transactions. In the course of the examination, aspects of United States regulation pertaining to capital movements and financial services were reviewed in light of the objectives of the Codes, which involve reducing barriers to trade between OECD members.

Also, the staff provided technical assistance to the United States Department of Treasury in responding to an OECD study on corporate “private practices," *i.e.* aspects of corporate governance, that could have a discriminatory impact on foreign investment.

The Wilton Park Group (The Group)

Her Majesty's Treasury of the United Kingdom sponsors this annual program. This year's meeting in June was attended by securities regulators from 13 countries. International regulatory cooperation issues discussed by the Group included secret and under-regulated jurisdictions and coordination of multinational investigations of "boiler rooms" and other fraudulent schemes to ensure investor protection and market integrity.

Trade Negotiations

The SEC's primary responsibility is the regulation of the domestic securities markets, and until recently, it had not been directly involved in trade matters. However, as a result of the globalization of securities markets, the SEC is now regularly engaged in discussions with fellow regulators on ways to facilitate cross-border activities, including offerings, securities trading, and the provision of advisory services. In addition, the SEC increasingly has provided technical assistance to the Administration in its negotiations involving trade and market access issues.

United States-Japan Framework Talks

SEC staff has provided technical assistance to the United States Department of Treasury in connection with Treasury's participation in the Working Group on Financial Services under the United States-Japan Framework for a New Economic Partnership, The purpose of the Group is to work toward reducing barriers to market access in the area of financial services, including the investment adviser industry and the investment trust management business.

General Agreement on Trade in Services (GATS)

The Uruguay Round of the General Agreement on Tariffs and Trade includes GATS, which encompasses financial services.

Throughout the Uruguay Round, the SEC provided assistance to the Treasury Department and the United States Trade Representative, as they worked to negotiate an agreement that will further liberalize trade in financial services. The SEC's approach has been to balance the goals of the Uruguay Round against its mandate to regulate for the protection of investors in the face of new and different regulatory challenges that will be brought about by GATS. The SEC staff has pressed for, and obtained, the flexibility needed by the Commission to regulate prudentially. With respect to financial services, the Commission can take regulatory measures necessary for the protection of investors and to ensure the integrity and stability of the United States financial system. As the negotiations continue, the SEC will continue to work with the Treasury Department and the United States Trade Representative to ensure that this and other provisions of the current GATS, or any new proposals, are interpreted in a manner consistent with the SEC's statutory mandate.

The North American Free Trade Agreement (NAFTA)

NAFTA contains a Financial Services Chapter, which encompasses activities of financial service providers, such as broker-dealers and investment advisers, within NAFTA countries. The Financial Services Chapter contains a strong "prudential carve-out," which enables the SEC to adopt or modify measures for the protection of investors or the securities markets, notwithstanding any other provision of the Agreement. The SEC provided the Department of Treasury with technical assistance in connection with NAFTA and consulted with the Mexican Comisión Nacional de Valores regarding the implementation of certain provisions of the Financial Services Chapter.

Regulation of the Securities Markets

The Division of Market Regulation (Division), together with regional and district office examination staff, oversees the operations of the nation's securities markets and market professionals. In calendar year 1993, the Commission supervised over 8,600 broker-dealers with 34,000 branch offices and over 470,000 registered representatives, 8 active registered securities exchanges, the over-the-counter markets, and 16 registered clearing agencies. Broker-dealers filing FOCUS reports with the Commission had approximately $1.2 trillion in assets and $75.6 billion in capital in 1993. The Division also monitors market activity, which has experienced significant growth. In calendar 1993, equity market capitalization stood at $5.2 trillion in the United States and $14.1 trillion worldwide. The average daily trading volume grew to over 264.5 million shares on the New York Stock Exchange with volume on the NASDAQ Stock Market nearing that number. The fastest growing area has been derivatives activities, where the approximate notional amount for major United States broker-dealers and their affiliates is $6 trillion with an aggregate replacement cost of approximately $31 billion.

Key 1994 Results

The Division continued to direct its efforts towards enhancing market segments, particularly with respect to improving the overall efficiency of the derivatives markets and the disclosure practices of the municipal securities markets. Major market participants were monitored more closely to determine their impact on the securities market. The Division issued the *Market 2000 Study,* which presents a current view of the equity markets and their regulatory structure. The

Division also endeavored to streamline the regulatory process by eliminating the need for review of certain SRO rule filings. The national clearance and settlement system made progress in preparing for a nationwide practice of three business days for settlement of all broker-dealer trades. In addition, the Division conducted several oversight inspections of SROs with a particular focus on sales practice examinations.

Securities Markets, Trading and Significant Regulatory issues

Market 2000

In January 1994, the Division issued its study, *Market 2000: An Examination of Current Equity Market Developments.* The study, while concluding that the equity markets are operating efficiently within the existing regulatory structure, identified four areas where the markets could work better for investors and where competition could work better for the markets. Recommendations regarding transparency, fair treatment of investors, fair market competition, and open market access were formulated to achieve those ends. During the year, the Commission began implementing the recommendations contained in the study with the development of rulemaking addressing payment for order flow practices, broker-dealer automated order routing systems, and customer limit order handling in the over-the-counter (OTC) market.

Derivatives

The Division was actively involved in several derivatives related projects. For example, the Commission issued a release proposing the use of a theoretical pricing model to set capital charges for exchange-traded options and related positions.[58] The director of the Division testified on this release and other issues relating to derivative financial instruments before the United States House of

Representatives, Subcommittee on Environment, Credit and Rural Development. The Division also monitored and discussed derivatives-related issues with the industry. For example, the staff surveyed some of the largest United States securities firms regarding their compliance with the risk management control recommendations contained in the Group of Thirty's report entitled, *Derivatives: Practices and Principles.*[59] In addition, the Division was active in an industry initiative to study a range of policy and regulatory issues related to financial derivatives in the areas of capital, regulatory reporting, internal controls, and counterparty relationships.

The Division also was involved in derivatives projects on the international level. For example, the Commission along with the Commodity Futures Trading Commission and the United Kingdom Securities and Investments Board issued a joint statement concerning the oversight of the OTC derivatives market.[60] This joint statement represents the first international understanding among securities and futures regulators for developing an approach to the oversight of the OTC derivatives market. Subsequently, the Division participated in producing a paper which was issued by the International Organization of Securities Commissions (IOSCO) regarding management control mechanisms for regulators of securities firms doing OTC derivatives business.[61]

Government Securities Market

The Government Securities Act Amendments of 1993 reauthorized the Department of the Treasury's (Treasury) financial responsibility rulemaking authority for the government securities market and included provisions for transaction recordkeeping, large position reporting, and National Association of Securities Dealers (NASD) sales practice rulemaking authority. The amendments also require the Commission to monitor private sector efforts to improve

the timely public dissemination and availability for analytic purposes of information concerning government securities transactions and quotations and to report these developments to Congress annually.

In the past year, GovPx, the entity formed by primary dealers and inter-dealer brokers to provide non-exclusive distribution of government bond data, added coverage of agency securities, zero-coupon bonds, and Treasury strips to its service, and began disseminating real-time quotations and trade information for basis trading in Treasury securities. GovPx now carries data from five out of the six inter-dealer brokers in these securities. GovPx also announced plans to offer theoretical pricing for those Treasury securities for which it does not receive prices from inter-dealer brokers.

Prior to this year, only the prices of inter-dealer broker Cantor Fitzgerald L.P. were provided outside of GovPx and made available in real-time through a vendor's screen (Telerate). In the past year, Liberty Brokerage began to distribute its prices through Dow Jones Telerate and Reuters, and Euro Brokers Inc. began offering its prices through Bloornberg and Knight-Ridder, Finally, this past year saw the introduction of the CrossCom Trading Network, a PC-based system which promises to bring screen-based trading to bond traders.

While efforts have begun to improve transparency in the debt markets generally, the Commission has recognized that some debt markets still lack basic price transparency. The Commission recently emphasized the importance of pricing information in all debt markets in connection with its decision to defer adoption of riskless principal mark-up disclosure in debt securities transactions. In deferring adoption of mark-up disclosure requirements, the Commission urged the industry to review the adequacy of price transparency in certain debt markets, such as the mortgage-backed and corporate debt

markets, and report back to the Commission regarding the adequacy of price information and the need for improvement of price transparency in those markets.

SRO Rule Filings

In June 1994, the Commission proposed amendments to Rule 19b-4 under the Securities Exchange Act of 1934 (Exchange Act) to expand the scope of SRO rule filings that may become effective upon filing under Section 19(b)(3)(A).[62] These amendments would streamline the process by which rule changes of SROs are filed with and approved by the SEC. The Commission also proposed amendments to streamline and conform the annual filing requirements for SROs. These proposals were designed in part to implement the recommendations contained in the *Market 2000* study.

National Clearance and Settlement System

The SEC continued to work to enhance all components of the national clearance and settlement system. In particular, the SEC worked closely with the SROs, broker-dealers, and industry groups to ensure an efficient conversion to a three business day settlement time frame for broker-dealer trades beginning in June 1995. In adopting Rule 15c6-1, which requires settlement of broker-dealer trades in three business days, the Commission called on the Municipal Securities Rulemaking Board (MSRB) to implement earlier settlement for trades in municipal securities concurrently with the effective date of Rule 15c6-1. Subsequently, the MSRB filed a proposed rule change to require that all broker-dealer trades in municipal securities, other than trades done on a "when, as, and if issued" basis, settle within three business days.[63] The SEC also worked with other SROs to bring their rules into compliance with Rule 15c6-1. In addition, the National Securities Clearing Corporation

(NSCC), at the request of the SEC, developed a plan for converting to a three business day settlement time frame.

Internationalization

The staff provided information and technical assistance to several emerging market countries, including China, Thailand, Korea, Taiwan, Russia, and Poland. Pursuant to the SEC's membership in IOSCO, the staff participated in the Working Party on the Regulation of Secondary Markets, which discussed issues concerning the regulation of screen-based trading systems and transparency of markets. The Working Party produced a paper discussing regulatory issues regarding proprietary screen-based trading systems, which was endorsed by IOSCO at its 1994 annual meeting.

The Commission took a variety of actions pertaining to multinational offerings. For example, consistent with its Statement of Policy regarding class exemptions for certain foreign issuers that conduct distributions in the United States,[64] the Commission granted class exemptions from the trading practices rules for distributions of securities by certain highly capitalized French issuers. The exemptions permit distribution participants to effect transactions in France in the security being distributed and related securities, subject to certain disclosure, record keeping, record production, and notice requirements.[65]

Additionally, the Commission clarified its application of cooling-off periods to distributions of foreign securities in the United States under Rule 10b-6.[66]

Extension of Credit

The staff clarified its position with respect to the application of the extension of credit prohibitions of Section 11(d)(1) of the

Exchange Act to the distribution of tranches of collateralized mortgage obligations,[67] and to a clearing broker-dealer extending credit on certain equity securities to a customer of its correspondent broker-dealer.[68]

Employee Retirement Programs and Financial Institution Networking

The staff issued two letters allowing broker-dealers to establish retirement programs for certain of their employees without the employees maintaining their status as registered representatives of the broker-dealer.[69] The retiring employees were permitted to share sales commissions generated by their client accounts with the active employees servicing those accounts, provided that they did not contact their former clients or otherwise remain in the securities business. The programs were limited to retiring employees without a disciplinary history. In addition, having issued over 200 no-action letters during the past decade addressing networking arrangements between broker-dealers and certain financial institutions, the staff issued a definitive letter describing the conditions under which these arrangements may be conducted without the financial institutions or their employees registering under Section 15 of the Exchange Act.[70]

Hedge Funds

In response to Congressional concerns, and in light of the lack of publicly available information about hedge funds and their impact on the markets, Chairman Arthur Levitt wrote to several large hedge funds requesting that they voluntarily provide the Commission with information concerning their hedge fund positions and trading strategies. As a result, the staff entered into ongoing discussions with various hedge funds, as well as consultants to the industry. The staff also explored ways to increase the availability of information regarding the trading activities of large institutional traders, including hedge funds, in key markets. To this end, in February 1994, the

Commission reproposed Rule 13h-1, which would implement the Commission's large trader reporting system.[71]

The proposed large trader reporting system generally is designed to supplement the Commission's existing authority to obtain trading and other records from registered broker-dealers. In reproposing Rule 13h-1, the Commission responded to concerns expressed by numerous commenters and revised certain provisions of the proposed rule. The changes to the proposed rule were intended to clarify the operation of the system and to reduce the costs associated with the system, including the cost of compliance. In addition, the Commission solicited comments regarding the use of other existing industry systems.

Anti-Manipulation Concept Release

The Commission published a concept release seeking comment on a broad range of issues relating to the anti-manipulation regulation of securities offerings under the Exchange Act. In particular, the Commission requested comment on Rules 10b-6, 10b-7, and 10b-8 under the Exchange Act;[72] the concepts underlying these rules; and alternative approaches for applying anti-manipulation principles to persons who may have incentives to artificially influence the market during an offering.

Confirmation Disclosure

The Commission published for comment amendments to Rule 10b-10 that would require disclosure regarding the unrated status of certain debt securities, and assumptions about collateralized debt securities that may affect yield. To address Congressional concerns expressed in the Government Securities Act Amendments of 1993, the amendments also would require broker-dealers that are not members of the Securities Investor Protection Corporation to disclose

that fact to their customers. The Commission also proposed amendments that would require broker-dealers to provide customers immediate written notification of mark-up information for riskless principal transactions in debt securities[73] and a new Rule 15c2-13 that would require similar rnark-up disclosure for transactions in municipal securities. In addition, the Division explored various ways to improve transparency in the municipal securities market. Since the proposals were published for comment on March 9, 1994, the MSRB proposed a program that ultimately would provide same day price reporting of all transactions in municipal securities, including same day reporting of retail trades.

Theoretical Option Pricing Methodology

The Commission proposed for comment amendments to Rule 15c3-1 that would allow broker-dealers to use a theoretical pricing model when calculating capital charges (haircuts) for listed options and related positions.[74] To determine haircuts for broker-dealers' options positions, the Commission proposed that broker-dealers use The Option Clearing Corporation's system for measuring market risk, which is based on the Cox-Ross-Rubenstein binomial option pricing model. By better matching the haircut charges to the market risk of the positions, the proposed amendments provide significant improvement to the Commission's option haircut methodology. Simultaneously with the proposing release, the Division issued a no-action letter that provided broker-dealers the choice of using the theoretical pricing methodology.

Short Sales in Anticipation of an Offering

The Commission permanently adopted Rule 10b-21 under the Exchange Act, which had been adopted on a temporary basis in 1988. Rule 10b-21 is designed to prevent manipulative short sales of

an equity security in anticipation of a public offering by prohibiting the covering of short sales with securities purchased in the offering.[75]

Nationally Recognized Statistical Rating Organizations

In August 1994, the Commission issued a concept release[76] soliciting public comment on a number of questions concerning the use of the term "nationally recognized statistical rating organization" (NRSRO) in the Commission's rules. This concept release examines the process employed by the Commission to designate rating agencies as NRSROs and the nature of the Commission's oversight role with respect to NRSROs.

Money Laundering

The Division continued to work with the Treasury and other United States government offices to develop effective policies to combat money laundering. For example, the staff (1) actively supported Treasury rulemaking projects, (2) submitted comments on the Money Laundering Suppression Act of 1994, (3) provided technical advice to the United States delegation to the Financial Action Task Force on Money Laundering, the independent group of major financial center countries and regions, and (3) provided advice with respect to potential enforcement matters.

Automation Review

The staff continued to perform Automation Review Policy (ARP) inspections of the exchanges and the NASD.[77] The primary purpose of the ARP program is to monitor and inspect the electronic data processing facilities supporting the transaction and information dissemination activities of the SROs in their relationship to the national market system. The staff completed six on-site inspections and issued five reports, which included fifty-one recommendations for

improvements. Typical recommendations included the need for back-up facilities for data centers, enhancements to data security efforts, and better use of capacity planning tools.

The staff held 12 technology briefings with the SROs to ascertain recent and planned changes and improvements in their automated systems. The staff also assessed the ability of SROs to respond to systems malfunctions and examined SRO measures to prevent system outages. In addition, two meetings were held with the 16 clearing agencies to discuss the application of the program to clearing agencies.

Broker-Dealer Trading Systems

In response to the recommendations of the *Market 2000* study, the Commission adopted Rule 17a-23 under the Exchange Act to establish recordkeeping and reporting requirements for brokers and dealers that operate automated trading systems.[78] Registered broker-dealer sponsors of these systems would be required to maintain participant, volume, and transaction records, and to report system activity periodically to the Commission.

Examination and Oversight of Brokers, Dealers, Municipal Securities Dealers, and Transfer Agents

Broker-Dealer Examination Program

The SEC completed a total of 680 examinations, consisting of 478 oversight and 202 cause examinations. Findings from 124 examinations were referred for enforcement consideration. Referrals to SROs were made in 47 examinations. A description of particularly significant examinations follows.

The Division, working in conjunction with the New York Stock Exchange (NYSE) and the NASD, completed a review of the hiring, retention, and supervisory practices of nine of the country's largest broker-dealers.[79] Staff from the SEC, NYSE, and NASD conducted 170 broker-dealer examinations of both home and branch offices of the nine firms and focused their review on 268 registered representatives who had been the subject of sales practice-related customer complaints, litigation, arbitration, or disciplinary actions. Forty of these examinations resulted in enforcement referrals,

In June 1994, the Division issued the *Joint Regulatory Penny Stock Examination Sweep Report.*[80] The report was the culmination of the largest, most ambitious joint SEC, SRO, and state project ever undertaken. The nationwide sweep involved examinations of 130 penny stock firms by SEC regional and district office staff, the NASD, the NYSE, and 40 states. The SEC coordinated the sweep and drafted the report.

Lost and Stolen Securities

Rule 17f-1 of the Exchange Act sets forth participation, reporting, and inquiry requirements for the SEC's Lost and Stolen Securities Program.[81] Statistics for calendar year 1993 (the most recent data available) reflect the program's continuing effectiveness. As of December 31, 1993, 24,039 institutions were registered in the program, a 1 percent increase over 1992. The number of securities reported as lost, stolen, missing, or counterfeit decreased from 2,500,521 in 1992 to 1,634,161 in 1993, a 35 percent decrease. The dollar value of these securities decreased from $71 billion to $4 billion, a 94 percent decrease. The aggregate dollar value of the securities contained in the program's database increased from $90.3 billion in 1992 to $92.6 billion in 1993, a 3 percent increase. In 1993, the number of inquiries from participating institutions that matched

previous reports as lost, missing, stolen, or counterfeit securities was 44,902, a 99 percent increase from 1992. The dollar value of these matches increased from $135 million in 1992 to $252 million in 1993, an 87 percent increase. The total number of certificates inquired about through the program rose from 5,281,185 in 1992 to 6,553,308 in 1993, a 24 percent increase.

Oversight of Self-Regulatory Organizations

National Securities Exchanges

As of September 30, 1994, there were eight active securities exchanges registered with the SEC as national securities exchanges: American Stock Exchange (AMEX), Boston Stock Exchange (BSE), Chicago Board Options Exchange (CBOE), Cincinnati Stock Exchange (CSE), Chicago Stock Exchange (CHX), NYSE, Philadelphia Stock Exchange (PHLX), and Pacific Stock Exchange (PSE). The SEC granted exchange applications to delist 72 debt and equity issues, and granted applications by issuers requesting withdrawal from listing and registration for 47 issues. In addition, the SEC granted 1,591 exchange applications for unlisted trading privileges. The exchanges submitted a total of 319 proposed rule changes during 1994. A total of 292 pending and new filings were approved by the Commission, and 127 were withdrawn. Some of the significant rule filings approved by the Commission included proposals to:

- amend and extend through May 18,1995 the existing pilot program of the CSE relating to the preferencing of public agency market and marketable limit orders by approved dealers and proprietary members;[82]

- permit competing specialists on the floor of the BSE for a one year pilot period ending May 18, 1995;[83] and

- adopt the NYSE, AMEX, BSE, CHX, PSE, and PHLX programs for off-hours-trading on a permanent basis.[84]

National Association of Securities Dealers, Inc.

The NASD, with over 5,300 member firms, is the only national securities association registered with the SEC. It is the operator of the NASDAQ Stock Market (formerly NASDAQ), the second largest stock market in the United States, and the second largest in the world (after the NYSE).

The NASD submitted 75 proposed rule changes to the Commission during the year. The Commission approved 81 proposed rule changes, which included many of the proposed rule changes submitted during the year and several proposed rule changes submitted in prior years. Among the significant changes approved by the Commission were:

- more stringent listing and maintenance requirements for issuers on the NASDAQ Stock Market;[85]

- a comprehensive short sale rule applicable to the OTC market;[86]

- greater limit order protection in the NASDAQ Stock Market;[87]

- a requirement that all Consolidated Quotation System market makers in Rule 19c-3 securities register as Intermarket Trading System/ Computer Assisted Executed Service market makers;[88] and

- implementation of requirements imposed upon the NASD by the Limited Partnership Roll-up Reform Act of 1993.[89]

Clearing Agencies

Sixteen clearing agencies were registered with the SEC at year-end. In addition, the SEC extended the temporary registration as a clearing agency for the Participants Trust Co.,[90] MBS Clearing Corporation (MBSCC)[91] and the International Securities Clearing Corporation.[92] The Intermarket Clearing Corporation notified the SEC of its intention to let its temporary registration expire and requested that the SEC no longer consider its request for permanent registration.[93]

Registered clearing agencies submitted 124 proposed rule changes to the SEC and withdrew 11. The SEC approved 139 proposed rule changes, including the following:

- implementation of the first three stages of The Depository Trust Company's enhancements to its Institutional Delivery System that facilitate communications between broker-dealers and their institutional customers;[94]

- implementation of the Government Securities Clearing Corporation's (GSCC) Auction Takedown System, which includes within GSCCs netting system Treasury security purchases made at auction by GSCC members;[95] and

- the sale of MBSCC by the CHX to NSCC and the participants of MBSCC.[96]

Municipal Securities Rulemaking Board

The SEC received 16 new proposed rule changes from the MSRB. A total of 12 new and pending proposed rule changes were approved by the Commission. In particular, the Commission approved MSRB Rule G-37, which prohibits municipal securities dealers from conducting certain types of municipal securities business with an issuer within two years after any contribution by the

dealer or certain affiliated persons to officials of the issuer who could influence the awarding of municipal securities business.[97] The Commission also approved changes to MSRB Rule G-19 concerning suitability of recommendations, and Rule G-8 concerning recordkeeping to ensure that dealers, before making a recommendation to a customer, take appropriate steps to determine that the municipal securities transaction is suitable.[98]

Inspections of SRO Surveillance and Regulatory Compliance

The staff completed oversight inspections of the sales practice examination programs of the CBOE, AMEX, and NYSE. The staff completed an inspection of the advertising program of the NASD relating to investment company communications, non-investment company communications, and bank affiliate communications. The staff also conducted oversight inspections of the NYSE's preliminary investigation program and full investigation program. In addition, the staff conducted an inspection of the MSRB.

The staff conducted inspections of the arbitration programs administered by the NASD and NYSE. These inspections were designed to evaluate the effectiveness of these SRO programs in processing and resolving disputes between SRO members and their customers. In particular, the staff reviewed the adequacy and thoroughness of case documentation, the efficiency of case management systems, and arbitrator qualification and training procedures. Consideration also was given to whether major rule changes, adopted by the NASD and NYSE in 1989 in response to Commission concerns regarding the rules and procedures governing SRO-administered arbitration, were successful in improving the fairness and efficiency of these programs.

The staff reviewed the surveillance, investigatory, and disciplinary programs of the CSE and AMEX. The staff also reviewed

the Intermarket Trading System operations of participating SROs and conducted an examination of multiple traded options at the five options exchanges.

Arbitration

In response to the Commission's recommendations to enhance facilities for arbitration matters involving employment discrimination claims, and in light of a General Accounting Office report,[99] arbitration departments of SROs began to (1) implement procedures to track and analyze employment discrimination cases, (2) evaluate the backgrounds of arbitrators, and (3) appoint arbitrators with appropriate expertise for these matters.[100]

The Commission approved proposed rule changes by the NASD and national securities exchanges that were designed to strengthen the arbitration rules governing disputes among broker-dealers and between broker-dealers and investors. In particular, the Commission approved amendments to arbitration rules that (1) enabled securities industry parties to pursue class actions in courts[101] and (2) reinforced the ability of arbitrators to refer matters to disciplinary committees.[102]

SRO Final Disciplinary Actions

Section 19d-1 of the Exchange Act and Rule 19d-1 thereunder require all SROs to file reports with the SEC of all final disciplinary actions. Rule 19d-1 reports filed with the SEC were distributed as follows: AMEX—21; CBOE—70; NYSE—192; PHLX—19; PSE—11; CHX—1; NSCC—2; BSE—1; CSE—none; and NASD—729.

[table deleted]

Applications for Re-entry

Rule 19h-1 under the Exchange Act prescribes the form and content of, and establishes the mechanism by which the SEC reviews, proposals submitted by the SROs to allow persons subject to a statutory disqualification to become or remain associated with member firms. In 1994, the number of SRO filings pursuant to Rule 19h-1 processed by the staff increased 40 percent, from 53 in 1993 to 74 in 1994. Of the 74 filings, the NASD made 52, the NYSE made 21, and the CBOE made one. One application was denied, and the staff declined to take a no-action position in another.

Investment Management Regulation

The Division of Investment Management oversees the regulation of investment companies and investment advisers under two companion statutes, the Investment Company Act of 1940 (Investment Company Act) and the Investment Advisers Act of 1940 (Investment Advisers Act), and administers the Public Utility Holding Company Act of 1935 (Holding Company Act).

Key 1994 Results

In 1994, a large part of the work of the Division of Investment Management focused on three areas: improving and simplifying communications to investment company shareholders; enhancing the integrity of participants in the investment management industry; and evaluating the use of derivatives by investment companies. Key steps taken to improve disclosures to investment company shareholders included the Division's initiative to simplify investment company prospectuses and rule changes modernizing the investment company proxy rules. In April 1994, the Commission adopted amendments to Rules 204-1 and 204-3 and Form ADV under the Investment Advisers Act relating to wrap fee programs. The amendments specify the content, format and delivery requirements of the brochure that a wrap fee program sponsor must provide to clients and prospective clients. Also, the Commission proposed amendments to Rule 2a-7, under the Investment Company Act, which regulates money market funds. The amendments, among other things, would tighten the risk-limiting conditions imposed on tax exempt money market funds, and clarify the manner in which the rule applies to certain types of adjustable rate securities.

On September 27, 1994, the Division of Investment Management released a report, *Personal Investment Activities of Investment Company Personnel,* which describes the results of the staff's special examination of the personal investment activities of over 600 portfolio managers employed by 30 fund groups and analyzes the regulatory scheme that governs those investment activities. If implemented, the report's recommendations to improve the regulatory scheme would make available to the public additional information about fund policies on personal investments, enhance the oversight of personal investment policies by fund boards of directors, make it easier for both agency and fund staff to monitor the personal transactions of fund personnel, and clarify the scope of activities prohibited by fund personnel.

The Division has taken a multi-faceted approach to mutual fund use of derivatives, focusing on a broad range of issues, including disclosure, pricing, liquidity, leverage, and risk management. In December 1993, the Division formed a task force to study how investment companies use derivatives, how the Commission regulates derivatives, and whether legislative or regulatory changes are necessary or appropriate. In a September 1994 report, the Division recommended to Chairman Arthur Levitt that the Commission: (1) seek public comment on requiring some form of quantitative risk measure in fund prospectuses; (2) reexamine how the leverage restrictions of the Investment Company Act apply to derivatives; (3) consider reducing the ceiling on mutual fund illiquid holdings; and (4) submit to Congress legislation that would enhance the Commission's ability to monitor fund use of derivatives.

Program Overview

Investment Company and Adviser Inspection Program

During 1994, the investment company and adviser inspection program shifted its focus towards small and medium investment company complexes (those outside of the largest 100 investment company groups) and new entrants to the fund business. Examiners emphasized fund share distribution and portfolio management activities during inspections. In particular, examiners looked closely at the use and effects of derivative investment products on registrants' disclosures, returns, and internal control systems. The program also set a goal of examining investment advisers with discretionary management authority that have not been examined since 1990.

The tables below show the number of registered investment companies and investment advisers and the amount of assets under management. All figures are reported for fiscal year-end.

[table deleted]

The number of registered investment companies increased by more than 5 percent during 1994. Many investment companies combine several separate portfolios or investment series in one investment company registration statement. The number of portfolios generally ranges from three to ten. However, some unit investment trusts group as many as 1,400 separate portfolios under one Investment Company Act registration. The number of portfolios increased by almost 6 percent during the year.

Results Achieved by the Program

The inspection staff completed 313 investment company inspections during the year. The 313 complexes inspected managed 1,669 portfolios, approximately 25 percent of the mutual fund and closed-end fund portfolios in existence at the beginning of 1994. This indicates an average inspection frequency of once every four years. Of 313 inspections completed, 21 were referred to the Division of Enforcement (Enforcement) as compared to 8 referrals during 1993. An additional 244 inspections resulted in deficiency letters being sent to investment companies.

The inspection staff completed 963 investment adviser examinations during the year including examinations of 684 advisers with discretionary management authority. This represents a 35 percent increase over 1993, reflecting a shift in focus towards smaller advisers. The 684 inspections of discretionary advisers covered 9 percent of such advisers indicating an average inspection cycle of once every 11 years. The overall inspection cycle for advisers was an average of once every 22 years.

Of the 963 examinations, 94 were referred to Enforcement, Twenty-seven percent of referrals included deficiencies related to investment policies and/or prohibited transactions, and 46 percent involved potential conflicts of interest in personal investing by access persons (persons with direct knowledge of the portfolio). Over 90 percent of all investment adviser examinations resulted in either a deficiency letter, an enforcement referral, or both.

Special Reports

In 1994, the Division prepared two special reports, one addressing mutual fund use of derivatives and the other addressing personal investment activities of investment company personnel.

Mutual Fund Use of Derivatives

The Division has taken a multi-faceted approach to mutual fund use of derivatives, focusing on a broad range of issues, including disclosure, pricing, liquidity, leverage, and risk management. In December 1993, the Division formed a task force to study how investment companies use derivatives, how the Commission regulates derivatives, and whether legislative or regulatory changes are necessary or appropriate. The task force reviewed the disclosures of 100 investment companies, and the Division's fund disclosure review staff has given heightened scrutiny to derivatives disclosure in prospectuses. The Division has encouraged registrants to modify their existing disclosure to enhance investor understanding of pertinent risks.[103] In addition, the Division's inspection staff has examined and reported on the derivatives activities of each fund inspected, and has conducted special examinations of certain funds holding significant positions in derivatives.

On September 26, 1994, the Division reported to Chairman Levitt on mutual fund use of derivatives.[104] In this report, the Division recommended that the Commission: (1) seek public comment on requiring some form of quantitative risk measure in fund prospectuses; (2) reexamine how the leverage restrictions of the Investment Company Act apply to derivatives; (3) consider reducing the ceiling on mutual fund illiquid holdings; and (4) submit to Congress proposed legislation that would enhance the Commission's ability to monitor fund use of derivatives. Chairman Levitt presented the Division's report to Congress in September 1994.[105]

Personal Investment Activities of Investment Company Personnel

On September 27, 1994, the Division of Investment Management released a report, *Personal Investment Activities of Investment Company Personnel,* which describes the results of the

staff's special examination of the personal investment activities of over 600 portfolio managers employed by 30 fund groups. The report analyzes the regulatory scheme that governs those investment activities. With some exceptions, the fund managers examined generally did not appear to invest extensively for their personal accounts, and potential conflicts of interest between a manager's investments and those of his or her fund appeared to be infrequent. The data collected suggested that the existing regulatory scheme generally has worked well, but can be improved. The Division made several recommendations, some of which can be accomplished administratively. Others will require action by Congress or the National Association of Securities Dealers (NASD). If implemented, the staff's recommendations would make available to the public additional information about fund policies on personal investment, enhance the oversight of personal investment policies by the fund board of directors, make it easier for both agency and fund staff to monitor the personal transactions of fund personnel, and clarify the scope of prohibited activities by fund personnel.

Regulatory Policy

Significant Investment Company Developments

In December 1993, the Commission proposed amendments to Rule 2a-7, under the Investment Company Act, which regulates money market funds. The proposed amendments would, among other things, tighten the risk-limiting conditions on tax-exempt money market funds, apply Rule 2a-7 to asset-backed and synthetic securities, and clarify the manner in which the rule applies to certain types of adjustable rate securities. The Commission also proposed related amendments to Form N-1A to impose additional disclosure requirements on tax-exempt money market funds. The amendments are designed both to increase the safety of money market funds and

to increase investor awareness of the risks of investment in a money market fund.[106]

In December 1993, the Commission proposed for public comment Rule 18f-3 under the Investment Company Act, and related amendments to other rules under that Act and the Securities Act of 1933 (Securities Act). Proposed Rule 18f-3 would allow open-end management investment companies to issue multiple classes of shares without the need to apply for and receive an order of exemption from the Commission, largely codifying over 150 exemptive orders issued by the Commission during the past decade. Proposed amendments to Form N-1A, the registration form used by open-end management investment companies,[107] would make consistent the disclosure requirements of multiple class and master-feeder funds (funds which consist of one or more feeder funds investing in the same portfolio, or master fund). The proposal also would make conforming changes to several advertising and sales literature rules.

In May 1994, the Commission proposed for public comment Rule 17f-6 under the Investment Company Act to permit registered management investment companies to use futures commission merchants and commodity clearing organizations as custodians of their assets in connection with futures contracts and commodity options regulated under the Commodity Exchange Act.[108] Currently, investment companies must maintain special accounts with their custodian banks for these transactions. The proposed rule would enable investment companies to effect their commodity trades in the same manner as other market participants under conditions designed to ensure the safekeeping of investment company assets.

In August 1994, the Commission adopted an amendment to Rule 415 under the Securities Act, which governs the registration of

securities for the shelf. The amendment permits closed-end funds that make periodic repurchase offers, known as closed-end interval funds, to offer their shares on a continuous or delayed basis.[109] The amendment is intended to facilitate offerings by closed-end interval funds to replenish assets that may be depleted by periodic repurchases.

Significant Investment Adviser Developments

In January 1994, the Commission proposed and in April 1994, the Commission adopted amendments to Rules 204-1 and 204-3 and Form ADV under the Investment Advisers Act relating to wrap fee programs. A wrap fee program provides an investor with two types of services: investment advisory services and execution services for a single wrap fee, usually a percentage of assets under management The amendments specify the content, format, and delivery requirements of the brochure that a sponsor of a wrap fee program must provide clients and prospective clients and are intended to facilitate the development of clear, concise and informative wrap fee brochures.[110]

In March 1994, the Commission proposed for public comment two new rules under the Investment Advisers Act, Proposed Rule 206(4)-5 would make express the fiduciary obligation of an investment adviser to make only suitable recommendations to a client, after a reasonable inquiry into the client's financial situation, investment experience, and investment objectives. An express suitability rule would underscore the importance of this requirement, particularly to the many new entrants into the investment advisory industry, and increase the level of attention given to suitability determinations by advisory firms. Proposed Rule 206(4)-6 would prohibit registered investment advisers from exercising investment discretion with respect to client accounts unless they have a

reasonable belief that the custodians of those accounts send account statements to the clients no less frequently than quarterly. These account statements would provide clients with independent reports of account activity and permit clients to protect themselves against wrongful or questionable conduct such as inappropriately high levels of trading, unauthorized transactions, or unsuitable investments.[111]

Significant Disclosure Program Developments

In August 1994, the Commission adopted amendments to Rule 485 under the Securities Act. Among other things, Rule 485 sets forth standards for filing post-effective amendments to registration statements filed by open-end management investment companies and unit investment trusts and permits certain amendments to become effective automatically. The adopted amendments simplify the operation of the rule and expand the conditions under which post-effective amendments filed by investment companies are permitted to become effective automatically. The Commission adopted new Rule 486 that permits closed-end management investment companies, which make repurchase offers to their shareholders at net asset value in accordance with Rule 23c-3 under the Investment Company Act, to obtain automatic registration effectiveness for additional securities using procedures similar to those in Rule 485.[112]

In December 1993, the Commission proposed and, in October 1994 the Commission adopted, amendments to Schedule 14A under the Securities Exchange Act (Exchange Act) to add a new item 22 that includes the specific requirements applicable to the proxy statements of registered management investment companies. Item 22 replaced Rules 20a-2, 20a-3, and 20a-4 under the Investment Company Act, which were rescinded. These amendments update the proxy rules applicable to investment companies to reflect current matters on which investment company shareholders are commonly

asked to vote, to improve the disclosure provided to shareholders, and to simplify the preparation of investment company proxy statements. The Commission also amended Form N-14, the form used by management investment companies to register securities issued in connection with business combination transactions, to require a comparative fee table in the disclosure documents delivered in connection with such transactions.[113]

In August 1994, the Commission proposed amendments to Rule 6-07 of Regulation S-X, the regulation setting forth form and content requirements for financial statements included in registration statements, proxy statements, annual reports, and shareholder reports under the various securities laws, and Forms N-1 A, N-2, N-3, and N-4, the registration forms used by management investment companies and insurance company separate accounts (funds) under the Securities Act and the Investment Company Act. The proposed amendments would require a fund to adjust the amount of expenses reflected in the statement of operations in its financial statements to include amounts the fund would have paid to its service providers had a broker-dealer or any affiliate of the broker-dealer not paid or agreed to pay those service providers on behalf of the fund in connection with the allocation of fund transactions to the broker-dealer. The proposed amendments also would require that the adjusted expenses be reflected in the fee table, the financial highlights table included in fund prospectuses, and yield quotations. In addition, the proposed amendments would require that the financial highlights table disclose the average commission rate paid by the fund. The amendments are designed to allow investors to evaluate fully the expenses of a fund that pays for services with commission dollars and accurately compare expenses and yields among funds.[114]

Considerable staff time and attention were devoted to efforts to simplify and improve prospectus disclosure. The staff utilized focus groups to research the views and opinions of investors in an effort to identify areas for enhanced prospectus disclosure. The staff began to reevaluate the process through which it comments on registration statements filed by investment companies. This project is designed to enhance the clarity of disclosure by reducing technical and legal prose. The staff also participated in drafting a brochure to assist consumers who invest in mutual funds.

The staff continued to focus on the disclosure and policy issues raised by funds investing in new products. For example, derivatives, structured financing arrangements and strategic transactions were analyzed in terms of adequacy of risk disclosure, potential for leverage, liquidity, and assurance of accurate pricing. The staff also reviewed the disclosure and policy issues raised by the increasing number of funds investing in emerging markets or previously closed, centrally-planned economies.

In 1994, the staff reviewed filings by 508 new open-end fund portfolios, 616 existing open-end portfolios, 202 new closed-end portfolios, 5 existing closed-end fund portfolios, 450 new unit investment trust portfolios, and 387 existing unit investment trust portfolios. In connection with its regulation of variable insurance products, the staff reviewed filings by 76 new open-end funds, 245 existing open-end funds, 257 new sub-accounts funded by variable annuity contracts, 482 existing sub-accounts funded by variable annuity contracts, 112 new variable life insurance products, and 273 existing variable life insurance products. In addition, the staff reviewed 579 proxy filings by funds and insurance product separate accounts.

Section 13(f)(1) of the Exchange Act and Rule 13f-1 require "institutional investment managers" exercising investment discretion over accounts holding certain equity securities with a fair market value of at least $100 million to file quarterly reports on Form 13F. For the quarter ending June 30, 1994, 1,222 managers filed Form 13F reports, for total holdings of approximately $2 trillion.

Significant Insurance Products Developments

The staff of the Division's Office of Insurance Products continued efforts to develop a new registration form to be used by separate accounts offering variable life insurance contracts. Currently, separate accounts register as unit investment trusts under the Investment Company Act on Form N-8B-2 and also register their securities under the Securities Act on Form S-6. The new Form N-6 will replace this procedure with a single, three-part form that will integrate registration under both Acts.

In 1994, the staff began receiving registration statements involving the two-tiered "master-feeder" structure. In this structure, the master fund holds and manages the investment portfolio while one or more feeder funds *(i.e.,* insurance company separate accounts) offer shares to insurance contract owners and invest all of the separate account assets in the master fund.[115] As in master-feeder registrations outside the insurance products context, the registration statements reviewed for feeders discuss both the features of the variable insurance product as well as the operation of the underlying master fund.

Significant Public Utility Holding Company Act Developments

The Commission began an evaluation of the Holding Company Act to review the regulatory framework in light of developments in recent years and to consider how federal regulation of utility holding

companies can best serve the interests of investors, consumers, and the general public in the future. The Commission inaugurated the review with a roundtable discussion, in Washington, D.C. on July 18 and 19, 1994 in which representatives of the utility industry; consumer groups; trade associations; investment banks; rating agencies; state, local, and federal regulators; and others participated. The study is expected to be completed by the summer of 1995.

The Commission adopted amendments to rules and forms to modernize and streamline regulation under the Holding Company Act. The amendments expand certain exemptions and generally update and clarify the requirements of the rules. The Commission rescinded Rule 50 under the Holding Company Act, which required competitive bidding in connection with the purchase or underwriting of securities by companies in a registered system. The rulemaking is intended generally to reduce regulatory burdens under the Holding Company Act.

As of September 30, 1994, there were 14 public-utility holding companies registered under the Holding Company Act. The registered systems were comprised of 91 public utility subsidiaries, 193 non-utility subsidiaries and 31 inactive subsidiaries, for a total of 329 companies and systems operating in 26 states. These holding company systems had aggregate assets of approximately $121.7 billion as of September 30, 1994. Operating revenues for twelve months ending September 30, 1994, were approximately $43.9 billion.

During 1994, the Commission authorized registered holding company systems to issue $8.6 billion in short-term debt, $3.7 billion in long-term debt, and $2.7 billion in common and preferred stock. Short-term debt authorization increased by over $4 billion in 1994 from the previous year, with common and preferred stock equity

increasing by $2 billion. The Commission approved pollution control financings of $1.8 billion, an increase of 29 percent over 1993. The agency approved $240 million of investments in cogeneration projects that were "qualifying facilities" under the Public Utility Regulatory Policies Act of 1978 and rules thereunder. The Commission also approved $418 million of investments in exempt wholesale generators and foreign utility companies, an increase of over 263 percent over 1993, and $42 million in enterprises engaged in demand-side and energy management. Total financing authorizations of approximately $17.5 billion represented a 73 percent increase over such authorizations in 1993.

In overseeing compliance with the Holding Company Act, the staff examines service companies, special purpose companies, and exempt wholesale generator and foreign utility company subsidiaries of registered holding company systems. During 1994, six examinations were completed, three of foreign utility companies, two of service companies, and one of special purpose corporations, respectively. The staff continued to review the accounting policies, cost determination, intercompany transactions, and quarterly reporting requirements of all service companies and special purpose corporations. Through the examination program, and by uncovering misapplied expenses and inefficiencies, the Commission's activities during 1994 resulted in savings to consumers of approximately $11 million.

The Commission approved a joint legislative proposal by its staff and the staff of the Federal Energy Regulatory Commission (FERC), intended to resolve the issues raised by *Ohio Power Co. v. FERC.* The proposal would amend section 318 of the Federal Power Act (FPA) to permit the FERC, in the exercise of its ratemaking authority, to disallow costs incurred pursuant to Section 13(b) of the Holding

Company Act on a finding that recovery of such costs would be inconsistent with the standards of the FPA.

On May 26, 1994, Commissioner Richard Roberts, on behalf of the Commission, testified before the Subcommittee on Energy and Power of the House Committee on Energy and Commerce, regarding policy issues raised by *Ohio Power,* and other issues generally related to regulation under the Holding Company Act. The testimony focused on the Commission's efforts to address concerns that the decision can be read to challenge the ability of the FERC, and state and local ratemakers, to protect consumers through traditional ratemaking proceedings.

On June 24, 1994, Representatives Boucher, Dingell, Markey and Sharp introduced H.R. 4645. This legislation, which was substantially similar to the Commission-FERC joint staff proposal, would amend the FPA to authorize the FERC to disallow Commission-approved costs on a finding that recovery of such costs was inconsistent with the requirements of the FPA. The legislation does not contain any provision for transfer of administration of the Holding Company Act to the FERC.

On August 11, 1994, an amendment to S, 1822, the Communications Act of 1994, was reported by the Senate Committee on Commerce, Science and Transportation. Among other things, the legislation would permit registered holding companies to engage in telecommunications activities, generally without limit under the Holding Company Act. The Commission had previously submitted a statement to that Committee and the Senate Committee on Banking, Housing and Urban Affairs focusing on the need for effective consumer protection if registered holding companies were to be permitted to engage in telecommunication activities.

Significant Applications And Interpretations

Investment Company Act Matters

The Commission issued an order under Section 9(c) of the Investment Company Act exempting First Investors Corporation (First Investors) and certain of its corporate affiliates from Section 9(a) in connection with an injunction entered in 1992 in federal court.[116] The Commission also issued an order exempting First Investors and certain individual affiliates from Section 9(a) in connection with four state court injunctions.[117] Both the federal and state injunctions were based on fraudulent sales practices relating to two high yield, high risk bond funds.

Section 9(a) prohibits any person from serving as an employee, officer, director, or investment adviser of any registered investment company if the person has been enjoined from engaging in any conduct in connection with the purchase or sale of any security, As a condition to its order, First Investors agreed to submit to the Commission annual reports prepared by an independent consultant on its broker-dealer operations for a period of five years. The first report stated that First Investors had centralized and standardized its procedures and systems concerning its sale practices in order to comply with the federal securities laws, and had recruited new senior management. The Commission granted relief to the applicants based on these changes and certain continuing obligations agreed to by First Investors.

The Commission issued an order under Sections 6(c), 17(b), and 17(d) of the Investment Company Act and Rule 17d-1 to allow Emerging Markets Growth Fund (the Fund), a United States closed-end investment company, to invest in New Europe East Investment Fund, a foreign closed-end investment company.[118] Capital International, Inc., a United States registered investment adviser, is

the investment adviser of both the domestic and foreign funds. The Fund seeks to achieve long-term capital growth by investing in equity securities of developing countries. Consistent with this objective, the Fund invests up to 2 1/2 percent of its assets in the New Europe Fund, which invests in Eastern Europe and the former Soviet republics. By purchasing securities of the New Europe Fund, the Fund can invest in the emerging markets of Eastern Europe and former Soviet republics while benefiting from the economies and diversification provided by pooled investments. The Fund purchases shares of the New Europe Fund at the same purchase price and on the same basis as all other purchasers of the shares. The arrangement required relief because the applicants are affiliated persons of each other.

The Commission issued an order under Section 6(c) of the Investment Company Act to allow Invesco Treasurer's Series Trust, a registered open-end investment company, to base its registration fee for shares registered under the Securities Act on net sales, rather than gross sales, pursuant to Rule 24f-2 under the Investment Company Act.[119] Invesco had filed a declaration pursuant to Rule 24f-2 to register an indefinite number of shares under the Securities Act. The rule provides that an investment company that has filed a declaration must file notices with the Commission indicating the number of shares sold during the prior year. If the notice is filed within two months of the company's fiscal year-end, the investment company may pay a registration fee based on net sales *(i.e.,* the aggregate sales price of the shares sold minus the aggregate sales price of the shares redeemed); if not, the fee is based on gross sales. Invesco mailed its notice for fiscal year 1993 seven days before the two month deadline; the notice arrived at the Commission one day after the deadline, Invesco stated that it acted reasonably and in good faith mailing its Rule 24f-2 notice seven days before the end of the two-month period. It also noted that, at the time the notice was

mailed, the United States Postal Service's performance was comparatively poor. The Commission granted the application after finding that the relief was appropriate and Invesco was not at fault. In addition, the Commission indicated that its staff would apply a four-day standard in evaluating future exemptive requests in which an investment company used the Postal Service to deliver its Rule 24f-2 notice and the notice was not delivered timely.

The staff provided its views on several interpretive issues concerning Rule 3a-7 under the Investment Company Act. Rule 3a-7 excludes from the definition of investment company any issuer that pools certain eligible financial assets and issues non-redeemable securities backed by those assets (so-called structured financing programs). The staff stated that cumulative preferred stock that has no determinable liquidation date is not an eligible asset because it does not by its terms convert into cash within a finite time period, as required by the rule. The staff also determined that structured financing programs may be deemed to issue redeemable securities when they issue two classes of securities and give the holders of one class the absolute or conditional right to withdraw portfolio securities upon presentation to the issuer of a certain amount of both classes of securities. Whether such programs issue redeemable securities will depend on whether there are substantial enough restrictions on the investor's right to withdraw portfolio securities. The staff recited a number of factors it considered important to make this determination.[120]

The staff concurred in the view that the board of directors of a registered, open-end investment company may conditionally determine that certain commercial paper issued in reliance on the exemption from registration in Section 4(2) of the Securities Act (4(2) Paper) is liquid. Generally, an open-end investment company may not invest more than 15 percent of its assets in illiquid assets. An

illiquid asset is one which may not be sold or disposed of in the ordinary course of business within seven days at approximately the value at which the investment company has valued the asset. The staff stated that to be considered liquid the 4(2) Paper must not be traded flat or be in default as to principal or interest. The staff also required the board of directors to consider the rating and the trading market for the 4(2) Paper in making the liquidity determination. Finally, the staff concurred in the view that the board of directors may delegate to the investment company's investment adviser the responsibility for determining and monitoring the liquidity of 4(2) Paper in the investment company's portfolio, provided the board retains sufficient oversight.[121]

The staff stated that it would not recommend enforcement action if a newly created fund formed by the merger of three predecessor funds advertised its performance using the historical performance data of the predecessor fund that most closely resembled the newly created fund.[122] To determine which predecessor fund, if any, a surviving or new fund resulting from a reorganization most closely resembles, the staff stated that funds should compare: the various funds' investment advisers; investment objectives, policies, and restrictions; expense structures and expense ratios; relative asset size; and portfolio composition. The staff noted that these factors are substantially similar to the factors to be considered in determining the accounting survivor of a business combination involving investment companies.

The staff granted no-action relief under Section 11 (a) of the Investment Company Act to a mutual fund offering to waive its front-end sales load (while imposing a contingent deferred sales load) to attract shareholders of unaffiliated funds that charge front-end sales loads. The staff stated that the purpose of Section 11 (a) is to prevent brokers from "switching," or inducing shareholders of an investment

company to exchange their shares for those of a different investment company solely for the purpose of exacting additional sales charges. The staff concluded that the legislative history of Section 11 (a) suggests that it should not apply to every offer involving unaffiliated funds. Moreover, the Rules of Fair Practice of the NASD and federal securities laws other than the Investment Company Act provide the principal regulatory means to address concerns about brokers imprudently switching investors between unaffiliated funds. Finally, the staff noted that Section 11(a) does not prohibit waiver of a front-end sales load for shareholders who redeem shares of a fund that imposes a contingent deferred sales load.[123]

Investment Advisers Act Matters

The Division staff continued to develop its interpretation regarding the jurisdictional reach of the Investment Advisers Act with respect to foreign advisers. In one no-action letter, the staff stated that it would not recommend enforcement action if foreign research affiliates of a U.S. registered adviser provided research to the adviser, but did not separately register under the Investment Advisers Act.[124] The staff's response permits a U.S. registered adviser to draw on the research of its multinational affiliates as long as the affiliates do not have access to recommendations given to the registered adviser's U.S. clients. In a second letter, the staff permitted a foreign affiliate of a registered foreign adviser to provide advice directly to U.S. clients and still rely on the exemption from registration under the Investment Advisers Act for private advisers. This relief was given on the condition that the affiliate operate separately and independently from the registered foreign adviser.[125]

Insurance Company Matters

The Commission issued an exemptive order limiting the disqualification provisions of Section 9(a) of the Investment Company

Act to persons who participate directly in the management, administration, or sale of the variable annuity contracts issued by an insurance company and its affiliates.[126] Insurance companies already have such relief with respect to variable life insurance contracts pursuant to paragraphs (b)(4) and (b)(15)(ii) of Rules 6e-2 and 6e-3(T), respectively, under the Investment Company Act.

The staff, pursuant to delegated authority, issued orders granting exemptive relief (class relief) to the extent necessary to permit the deduction of mortality and expense risk charges not only from assets of the separate account applicant(s) under certain variable annuity contracts, but also from: (1) the assets of the separate account applicant(s) under any materially similar variable annuity contracts offered in the future by the separate account applicant(s); or (2) the assets of any other separate account established in the future by the insurance company depositor(s) of the separate account applicant(s) under materially similar variable annuity contracts.[127] The staff stated that it would not recommend enforcement action to the Commission if a variable annuity separate account changed the manner of calculating the contingent deferred sales load without amending its existing order permitting the deduction of mortality and expense risk charges.[128] The staff took the position that it would not object if any separate account lowers any of its charges without seeking an amended order.

Holding Company Act Matters

The Commission authorized the acquisition by Entergy Corporation, a registered holding company, of Gulf States Utilities Company and related transactions. In its findings under Section 10(b)(1) of the Holding Company Act, the Commission relied in part on the existence of a FERC approved open-access tariff to mitigate any potential anticompetitive effects of the merger. The order was

appealed by, among others, Houston Lighting & Power Company. Before the appeal was decided, the U.S. Court of Appeals for the District of Columbia Circuit remanded the FERC order approving the open access tariff. Based on that decision, the Commission has requested remand of its order.

The Commission authorized Central and South West Corporation, a registered holding company, to form a special-purpose telecommunications subsidiary.

Full Disclosure System

The full disclosure system is administered by the Division of Corporation Finance, The system is designed to provide investors with material information, foster investor confidence, contribute to the maintenance of fair and orderly markets, facilitate capital formation, and inhibit fraud in the public offering, trading, voting, and tendering of securities.

Key 1994 Results

Spurred by the continuing need for capital by small and large businesses, a record level of common stock offerings totalling more than $330 billion were filed for registration in 1994, including over $82 billion for initial public offerings (IPOs). The total of over $810 billion in securities filed for registration during the year, equity and debt, was exceeded only by the record level reached in 1993.

Foreign companies' participation in the United States markets continued to show dramatic growth in 1994. One hundred thirty-eight foreign companies from 17 countries, including Bank of Montreal, Shandong Huaneng Power Development Company and Huaneng Power International Inc., P.T. Indonesia Satellite Corp., Reed International plc, Elsevier NV, TeleDanmark, and Pharmacia Corp., entered the United States public markets for the first time. At year-end, there were more than 635 foreign companies from 41 countries filing reports with the Commission. Foreign companies registered public offerings totalling $36 billion in 1994.

[graphic deleted]

The Commission adopted several initiatives to simplify and lower the cost of registration and reporting for domestic issuers and foreign companies accessing the United States public securities markets. These initiatives included eliminating supplemental financial schedules for both domestic and foreign registrants, as well as expanding the availability of short-form and shelf registration for foreign issuers to the same extent as available for United States issuers. In addition, reconciliation requirements applicable to foreign private issuers were streamlined by, among other things, (1) reducing first-time registrants' reconciliation requirements to the two most recent fiscal years plus interim periods and (2) permitting the use of the international accounting standard (IAS) for cash flow statements without reconciliation. The Commission also proposed to allow the use of IAS 21, "The Effects of Changes in Foreign Exchange Rates," and IAS 22, "Business Combinations." These proposals were later adopted.

Highly publicized defaults as well as the tremendous level of growth during the past two years in the market for municipal securities have raised concerns regarding the adequacy of municipal market disclosure both for primary offerings and in the secondary market. In this regard, the Commission published interpretive guidance regarding the disclosure obligations of issuers and underwriters in the primary and secondary municipal securities markets. The Commission also adopted amendments to limit municipal dealers' underwriting activities to issuers that undertook to provide secondary market disclosure and to enhance dealers' awareness of this secondary market information when recommending such securities.

A number of public companies reported significant losses attributable to derivatives activities and positions during the year. The staff conducted a targeted review of disclosures of derivatives

activities of approximately 500 filings. Through the comment process, the staff requested expanded disclosures in those filings where necessary to investors' understanding of the type, extent and potential effects of such activities.

In response to the increasing incidence of corporate restructuring transactions, the staff issued a public announcement about accounting and disclosure practices in connection with such restructurings and undertook a targeted review of several hundred companies that had announced such transactions.

As a follow-up to a 1993 special proxy review project to evaluate compliance with new executive compensation disclosure rules, the staff reviewed the compensation disclosures in 785 proxy statements.

Review of Filings

The staff conducted 3,400 reporting issuer reviews. A total of 1,599 new company registration statements also were reviewed. The reporting issuer reviews were accomplished through the full review of 977 registration statements and post-effective amendments to registration statements filed under the Securities Act of 1933 (Securities Act*),* 1,540 annual and subsequent periodic reports, 163 merger and going private proxy statements, and 1,405 full financial reviews of annual reports.

The following table summarizes filings reviewed during the last five years. The increases and declines in reviews of new issuer filings, tender offers, contested solicitations, and going private transactions, all of which are subject to review, reflect the increases and decreases in the number of filings received.

[table deleted]

Rulemaking, Interpretive, and Legislative Matters

Municipal Securities

The Commission published interpretive guidance regarding the disclosure obligations of issuers and underwriters in the primary and secondary municipal securities markets.[129] The interpretive release highlighted areas that create a risk of misleading investors and suggested disclosure practices to minimize those risks. Municipal dealers also were advised that they must have a reasonable basis for recommendations of securities in the secondary market. Finally, the release reiterated the Commission's support for legislation repealing the exemption from the registration requirements of the federal securities laws for corporate obligations underlying certain non-governmental conduit securities.

The Commission adopted amendments to its rules that prohibit a broker, dealer or municipal securities dealer from acting as an underwriter of an issue of municipal securities before making a reasonable determination that an issuer or obligated person has undertaken to provide certain information to nationally recognized municipal securities information repositories and/or the Municipal Securities Rulemaking Board and state information depositories.[130] The amendments also prohibit dealers from recommending a municipal security subject to a disclosure covenant unless the dealer has a system reasonably designed to notify the dealer of material information regarding the security before the recommendation is made. The amendments were first proposed on March 9, 1994 in a companion release to the Commission's interpretive guidance.[131]

International Initiatives

The Commission adopted a number of amendments to its rules and regulations to simplify registration and reporting requirements for

foreign private issuers. Amendments to Form F-3 were adopted to expand the class of foreign issuers eligible to use short form registration and primary delayed shelf offerings pursuant to Rule 415.[132] The amendments shortened the minimum issuer reporting period from 36 to 12 months, imposed a requirement that one annual report on Form 20-F be filed, and reduced the public float requirement for primary offerings of non-investment grade securities from $300 million to $75 million. The amendments also permit registration of debt/ equity and other securities on a single unallocated shelf registration statement, without having to specify the amount of each class of securities to be offered.

The financial statement reconciliation requirements applicable to foreign private issuers were streamlined to permit: (1) cash flow statements prepared in accordance with IAS 7, "Cash Flow Statements," without any additional information to reconcile to generally accepted accounting principles in the United States (GAAP); (2) first-time registrants to reconcile only the two most recent years plus interim periods rather than the previously required five years; (3) separate financial statements of significant acquisitions and significant equity investees without a reconciliation to GAAP unless a defined size test was exceeded; (4) foreign private issuers to omit differences in classification or display that result from using proportionate consolidation; and (5) elimination of six financial statement schedules.[133]

The Commission adopted amendments to Regulation S-X to permit foreign private issuers additional time to update their financial statements. The amendments are intended to coincide with the updating requirements of the home country of a substantial majority of foreign private issuers.[134]

The Commission proposed amendments to its rules and forms to allow foreign issuers flexibility in selecting the reporting currency used in filings with the Commission.[135] In addition, under the amendment, a foreign private issuer that accounts for its operations in hyperinflationary environments in accordance with IAS 21 would not have to reconcile the differences that would have resulted from the application of GAAP. At the same time, the Commission amended Form 20-F to streamline the financial statement reconciliation requirements for foreign private issuers that have entered into business combinations.[136] The amendment eliminated the requirements to reconcile certain differences attributable to the determination of the method of accounting for a business combination and the amortization period of goodwill and negative goodwill provided the financial statements comply with IAS 22. The amendments were subsequently adopted.

The Commission adopted amendments to the rules and forms that would extend provisions adopted for foreign issuers to domestic issuers that are required to provide financial statements for significant foreign equity investees and acquired businesses.[137] These provisions address the age of financial statements, nature of reconciling information and thresholds for providing such reconciliations. The amendments also eliminated certain financial schedules that both domestic and foreign issuers were required to include in annual reports and registration statements filed with the Commission. In addition, the amendments eliminated the asset test for determining the significance of investee financial statements.

Multijurisdictional Disclosure System

The Commission adopted amendments to the multijurisdictional disclosure system for Canadian issuers to: (1) amend the eligibility requirements for use of Securities Act registration statement Forms

F-9, F-10 and 40-F to shorten the reporting history requirement from 36 to 12 months, (2) eliminate the market capitalization requirements under such forms and (3) change the minimum public float requirement to United States $75 million.[138] The Commission also adopted amendments to Form F-9 that recognize investment grade ratings by those rating organizations that are accepted by Canadian securities regulators in addition to those that are accepted under the SEC's rules.

Offering Publicity

The Commission adopted two new safe harbor rules covering announcements of unregistered offerings and broker-dealer research reports.[139] The first safe harbor, under Rule 135c, is available to all United States and foreign companies that are reporting under the Exchange Act and to foreign companies that are exempt under Exchange Act Rule 12g3-2(b). It also parallels the safe harbor which is available for announcements in connection with registered public offerings. The second safe harbor extends the previously existing safe harbor, under Rule 139, for broker-dealer research reports distributed in the normal course of business with reasonable regularity to those reporting foreign companies that meet the eligibility requirements for short-form registration, other than reporting history, and that have traded offshore for at least 12 months.

Safe Harbor for "Forward Looking" Information

Responding to concerns raised by companies about liabilities for disclosure of "forward looking" information, the Commission issued a concept release soliciting comment on investor need for "forward looking" information, the impediments to providing such information, and various proposals to reduce such impediments.[140]

Debt Securities

The Commission adopted new Rule 3a12-11 and amendments to certain Exchange Act rules to reduce existing regulatory distinctions between debt securities listed on a national securities exchange and those traded in the over-the-counter market.[141] The rule provides exemptive relief to issuers listing debt securities on a national securities exchange from the restrictions on borrowing under Section 8(a) of the Securities Act and most of the proxy regulation of Sections 14(a), 14(b), and 14(c) of the Exchange Act. Thus, debt securities listed on a national securities exchange are exempt from the proxy and information statement rules, except that the antifraud proscriptions, the provisions relating to the transmission of materials to beneficial owners, and related definitions still apply. In addition, the amendments simplify the filing requirements for registration under the Exchange Act.

The Commission also solicited comments on extending reporting obligations to issuers with significant levels of outstanding debt securities whether or not listed on an exchange.

Security Ratings Disclosure

The Commission published for comment proposals to mandate disclosure of security ratings in place of the current policy of voluntary security ratings disclosure.[142] In publishing these proposals, the Commission recognized that ratings disclosure has remained largely static despite the development of a vast market for derivative financial instruments and increased variation in the scope and meaning of security ratings. The proposals would require disclosure of nationally recognized statistical rating organizations (NRSROs) security ratings obtained by the issuer, as well as disclosure of any rating (whether or not assigned by an NRSRO) that is used by a participant in a Securities Act offering. The proposals

also would require disclosure of material rating changes in an Exchange Act report Form 8-K.

Section 16

The Commission issued a release soliciting public comment on proposed amendments to the rules and forms under Section 16.[143] The proposals are intended to streamline the Section 16 regulatory scheme, particularly with regard to the treatment of transactions involving employee benefit plans, simplify and clarify certain reporting requirements, codify staff interpretive positions, and establish new categories of transactions exempt from short-swing profit recovery. The Commission also extended the phase-in period for compliance with the substantive conditions of Rule 16b-3 regarding employee benefit plan transactions until September 1, 1995, or such different date as the Commission may set in further rulemaking.[144]

In a subsequently issued release, the Commission solicited additional public comment on a broad variety of approaches to cash-only instruments, including narrowing or restructuring the current exemption.[145]

Roll-ups

The Commission proposed amendments to its proxy, tender offer and disclosure rules to implement the provisions of the Limited Partnership Roll-up Reform Act of 1993 (Roll-up Act).[146] The amendments revise the Commission's definition of a roll-up transaction to conform it more closely to the definition in the Roll-up Act and extend the protections of the Roll-up Act to proxy and tender offer rules in the areas of shareholder communications, security holder lists, and contingent or differential compensation. These amendments and minor modifications to the roll-up disclosure rules were subsequently approved by the Commission,

Timely Distribution of Proxy and Other Soliciting Material

The Commission published a release reminding registrants of their obligation under Rule 14a-13 to timely distribute proxy and other soliciting material to banks and brokers for forwarding to beneficial owners.[147] This release was issued in response to complaints from several beneficial owners who did not receive their material in sufficient time to make an informed proxy voting decision during the 1993 proxy season.

Electronic Data Gathering, Analysis, and Retrieval System

The Commission issued three releases to further implement the operational EDGAR system. In the first release,[148] the Commission established September 1,1994 as the date on which Financial Data Schedules would be required. The Commission also adopted an updated edition of the EDGAR Filer Manual to accommodate the preparation and submission of Financial Data Schedules.[149] Finally, in the third release, the Commission proposed minor and technical changes to the rules governing the submission of EDGAR filings and identified some common filing mistakes.[150]

Conferences

SEC Government-Business Forum on Small Business Capital Formation

The thirteenth annual SEC Government Business Forum on Small Business Capital Formation was held in Washington, D.C. on September 8-9, 1994. Approximately 150 small business representatives, accountants, attorneys and government officials attended the forum. Numerous recommendations were formulated with a view to eliminating unnecessary governmental impediments to small businesses' ability to raise capital. A final report will be

provided to interested persons, including Congress and regulatory agencies, setting forth a list of recommendations for legislative and regulatory changes approved by the forum participants.

SEC/NASAA Conference Under Section 19(c) of the Securities Act

The eleventh annual federal/state uniformity conference was held in Washington, D.C. on April 18, 1994, Approximately 60 SEC officials met with approximately 60 representatives of the North American Securities Administrators Association to discuss methods of effecting greater uniformity in federal and state securities matters. After the conference, a final report summarizing the discussions was prepared and distributed to interested persons and participants.

Accounting and Auditing Matters

The Chief Accountant is the principal advisor to the Commission on accounting and auditing matters arising from the administration of the various securities laws. The primary Commission activities designed to achieve compliance with the accounting and financial disclosure requirements of the federal securities laws include:

- *rule-making and interpretation that supplements private-sector accounting standards, implements financial disclosure requirements, and establishes independence criteria for accountants;*

- *review and comment process for agency filings directed to improving disclosures in filings, identifying emerging accounting issues (which may result in rulemaking or private sector standard-setting), and identifying problems that may warrant enforcement actions',*

- *enforcement actions that impose sanctions and serve to deter improper financial reporting by enhancing the care with which registrants and their accountants analyze accounting issues; and*

- *oversight of private sector efforts, principally by the Financial Accounting Standards Board (FASB) and the American Institute of Certified Public Accountants (AICPA), which establish accounting and auditing standards designed to improve financial accounting and reporting and the quality of audit practice.*

Key 1994 Results

The Commission continued its involvement in initiatives directed toward reducing the disparities that currently exist between different countries' accounting and auditing standards. In April 1994, the Commission revised its rules so that foreign private issuers may now submit a cash flow statement prepared in accordance with International Accounting Standard 7 (IAS 7) without reconciliation to United States standards. This represents the first time that the Commission has accepted an international standard for cross-border offerings and filings.

Accounting-Related Rules and Interpretations

The agency's accounting-related rules and interpretations supplement private-sector accounting standards, implement financial disclosure requirements, and establish independence criteria for accountants. The agency's principal accounting requirements are embodied in Regulation S-X, which governs the form and content of financial statements filed with the SEC.

Discontinued Operations. The staff issued interpretive guidance regarding accounting and disclosures relating to discontinued operations.[151] The guidance was issued in response to a perceived deterioration in compliance with the authoritative accounting literature governing the reporting of discontinued operations by public companies.

Oversight of Private-Sector Standard-Setting

The SEC monitors the structure, activity, and decisions of the private-sector standard-setting organizations, which include the FASB. The Commission and its staff worked closely with the FASB in an ongoing effort to improve the standard-setting process, including

the need to respond to various regulatory, legislative, and business changes in a tirnely and appropriate manner. A description of FASB activities in which the staff was involved is provided below.

The FASB continued a joint project with standard-setters in Canada and Mexico to compare accounting standards in the three countries. The goal of this project is to develop recommendations for consideration by standard-setters in the United States, Canada, Mexico, and the International Accounting Standards Committee (IASC) concerning actions that can and should be taken to move towards greater comparability.

As part of its consolidations project, the FASB continued a joint undertaking with the Accounting Standards Board of the Canadian Institute of Chartered Accountants (CICA) to consider the current reporting requirements under *Statement of Financial Accounting Standards No, 14,* "Financial Reporting for Segments of a Business Enterprise." An invitation to comment was issued as part of the first phase of a standard-setting project that will seek to develop common standards on disaggregated disclosures. The invitation to comment was based on an FASB Research Report and a CICA Research Study published earlier.

The FASB Issued Statement 119 requiring disclosures about the amount/ nature/ and terms of derivative financial instruments.[152] Statement 119 amends certain provisions of existing Statements 105 and 107 to elicit disclosures about derivative financial instruments – including futures, forward, swap, and option contracts, and other financial instruments with similar characteristics. Statement 119 requires that a distinction be made between financial instruments held or issued for trading purposes and those instruments held or issued for purposes other than trading. The statement is effective for financial statements issued for fiscal years ending after December

15, 1994, except for entities with less than $150 million in total assets (for which effectiveness is delayed one year).

The FASB adopted an amended standard on accounting for loan impairment by creditors.[153] The amendment revised the existing standard on recognizing a loss on impairment of a loan. The amended standard allows creditors to use existing methods for recognizing interest income on impaired loans.

The FASB continued its deliberations on an exposure draft (ED) of a proposed standard on accounting for stock compensation.[154] Under the ED's approach, compensation cost arising from awards of stock or options under both fixed and performance stock compensation plans would be measured as the fair value of the award at the date it is granted. The estimated value at the grant date would be subsequently adjusted, if necessary, to reflect the outcome of performance conditions and service-related factors such as forfeitures before vesting. No adjustment would be made for changes in the market price of the stock. The comment period on the ED expired on December 31, 1993. Public hearings were held during early 1994 and a field test was conducted.

In 1994, Congress continued to pursue accounting and accountants' liability issues that were addressed during the previous session. For instance, opposing bills were introduced last year in reaction to the FASB's ED on the accounting for employee stock-based compensation. These bills would have either required or prohibited the recognition of employee stock options as compensation expense in income statements. In January 1994, Chairman Arthur Levitt, responding to Senators' request for his views in this area, stated that it is inappropriate for Congress to prescribe accounting standards. He supported the integrity and independence of the FASB standard-setting process and indicated that the FASB

project should be permitted to continue.[155] On May 3, 1994, however, the Senate passed two resolutions related to the FASB's project. One resolution stated that the FASB should not change the current accounting for employee stock options,[156] while the second resolution stated that Congress should not impair the objectivity of the FASB's decisionmaking process by legislating accounting rules.[157] In an additional action related to the employee stock compensation issue, at the end of the term a bill was introduced in the Senate to mandate that accounting standards or principles may be used in filings with the Commission only after an affirmative vote of a majority of the members of the Commission.[158] No action was taken on this bill.

Congress also considered litigation reform issues that impact the accounting profession.[159] These bills not only addressed litigation allegedly being filed against accounting firms, but would have changed the substantive standards for accountants' liability in the federal securities laws and created an accountants' self-regulatory organization under the indirect oversight of the Commission. Divergent views were expressed on these bills at Congressional hearings and they were not voted on during the 103d Congress.

Finally, there was significant Congressional interest in the accounting for derivative financial instruments. Commission testimony described then proposed FASB Statement 119 and indicated that the Commission would consider additional quantitative disclosures in this area.[160] The Commission also noted that improved accounting for and disclosure about derivatives would be more beneficial to investors than auditor reporting on management's assessments of the registrant's internal control system related to derivatives transactions.[161]

The FASB's Emerging Issues Task Force (EITF), in which the Commission's Chief Accountant participates, continued to identify

and resolve accounting issues. During 1994, the EITF reached consensus on a number of issues involving accounting for restructuring charges, thereby narrowing divergent reporting practices in public companies' financial statements.[162]

Oversight of the Accounting Profession's Initiatives

The Commission and its staff continued to be active in overseeing the audit standard-setting process and other activities of the accounting profession, A discussion of the activities in which the SEC staff was involved follows.

AICPA. The SEC oversaw various activities of the accounting profession conducted primarily through the AICPA. These included (1) the Auditing Standards Board (ASB), which establishes generally accepted auditing standards; (2) the Accounting Standards Executive Committee (AcSEC), which provides guidance through its issuance of statements of position and practice bulletins and prepares issue papers on accounting topics for consideration by the FASB; and (3) the SEC Practice Section (SECPS), which seeks to improve the quality of audit practice by member accounting firms that audit the financial statements of public companies through various requirements, including peer review.

ASB. The staff continued to work with the ASB to enhance the effectiveness of the audit process. The ASB issued a series of annual Audit Risk Alerts to provide auditors with an overview of recent economic, professional, and regulatory developments that may affect 1994 year-end audits.

SECPS. The accounting profession's quality control endeavors for SEC audit practice are coordinated by two committees of the SECPS. The Peer Review Committee administers the triennial peer reviews that are required of all SECPS member firms and the Quality

Control Inquiry Committee (QCIC) conducts timely inquiries into the quality control implications of litigation against member firms alleging audit failures in connection with audits of public companies.

Staff review of these two functions is conducted in coordination with the Public Oversight Board (POB), which is independent of the AICPA (except for funding). The POB facilitates SEC oversight of the accounting profession's quality control efforts, and also engages in other activities directed towards improvements in the financial reporting process.[163]

Each year the staff selects for review a random sample of peer reviews. For the selected peer reviews the staff reads the workpapers of the peer reviewer and the oversight file of the POB. Questions that arise during these reviews are generally answered by the POB staff and occasionally by contacting the peer reviewer directly. This oversight has shown that the peer review process contributes significantly to maintaining the quality control systems of member firms and, therefore, enhances the consistency and quality of practice before the Commission.

The staff also reviews all closed-case summaries prepared by the QCIC and related FOB files. These reviews, plus discussions with the FOB and QCIC staffs, provide the staff with enough information to conclude that the QCIC process provides added assurances, as a supplement to the peer review process, that major quality control deficiencies, if any, are identified and addressed on a timely basis. Therefore, the Commission believes that the QCIC process benefits the public interest.

AcSEC. The AcSEC issued statements of position on the accounting for advertising costs[164] and revisions to the existing guidance on accounting for employee stock ownership plans.[165] A proposed audit and accounting guide on broker-dealers in securities

was issued during 1994.[166] Also, the AcSEC substantially completed a project calling for enhanced disclosures about risks and uncertainties[167] and initiated a project to develop an accounting guide on environmental liabilities.

International Accounting and Auditing Standards

Significant differences in accounting and auditing standards currently exist between countries. These differences are an impediment to multinational offerings of securities. The SEC, in cooperation with other members of the International Organization of Securities Commissions (IOSCO), actively participated in initiatives by international bodies of professional accountants to establish appropriate international standards that might be considered for use in multinational offerings. Since the completion in November 1993 of the lASCs project on comparability and improvements, which reduced alternative accounting treatments and improved guidance and disclosures in nine IASC standards, the staff worked with the IASC to improve other existing accounting standards and to develop new standards. During 1994 the IASC had major projects in process on earnings per share,[168] financial instruments,[169] intangible assets,[170] reporting financial information by segment,[171] and income taxes.[172]

The IOSCO Working Party on Multinational Disclosures and Accounting (Working Party) informed the IASC of the necessary core accounting standards that would comprise a comprehensive body of principles for enterprises (not in a specialized industry) undertaking cross-border offerings and listings. In June 1994, the Working Party provided the IASC with its evaluation of the acceptability of existing and recently improved IASC standards and identified the projects that would be necessary to complete the development of a core set of standards. In addition to existing standards and projects, the Working

Party believes that projects on employee benefits, interim reporting, discontinued operations and other restructurings, and hedging for commodities, are necessary to complete the standards. In the Working Party's view, further improvements also are required to IAS 9 "Research and Development Costs," IAS 10 "Contingencies and Events Occurring after the Balance Sheet Date," IAS 17 "Accounting for Leases," IAS 19 "Retirement Benefit Costs," and IAS 25 "Accounting for Investments." In addition, a project to review the alternatives for identifying and measuring impairment of the cost or carrying amount of long-lived assets, identifiable intangibles, and goodwill is considered important.

In April 1994, the Commission revised financial statement requirements so that foreign private issuers may now submit, without reconciliation, a cash flow statement prepared in accordance with IAS 7 "Cash Flow Statements." At the same time, the Commission proposed to eliminate the need to reconcile the differences that would result from the application of SFAS No. 52 "Foreign Currency Translation," if the issuer accounts for its operations in hyperinflationary economies in accordance with IAS 21 "The Effects of Changes in Foreign Exchange Rates."[173] Also, the Commission proposed to eliminate the requirements to reconcile certain differences attributable to the method of accounting for a business combination (pooling of interests or purchase) and the amortization period of goodwill and negative goodwill, provided that the financial statements comply with IAS 22 "Business Combinations."[174]

The staff also devoted substantial efforts to the review and analysis of three exposure drafts issued by the International Auditing Practices Committee (IAPC) of the International Federation of Accountants. These exposure drafts related to the IAPC's efforts to codify the International Standards on Auditing (ISA) that were endorsed provisionally by IOSCO in October 1992. As a result of its

analysis, the staff determined that substantial changes had been made to the provisionally endorsed ISAs. The principal change was the introduction of black lettering, which resulted in portions of the standards that were deemed by the IAPC to represent "basic principles and essential procedures" to be presented in bold type. The result of those changes was that uncertainty was introduced into the standards regarding the amount of work to be performed by an auditor in order to represent that his or her audit complied with the ISAs. The staff's concerns were communicated to IOSCO and, through IOSCO, to the IAPC. The IAPC did not address lOSCO's concerns in its final standards. As a result, IOSCO was unable to reach a consensus to endorse the codified ISAs. The staff advised the IAPC that additional changes to the final codified standards are necessary before the staff would recommend that the Commission support an IOSCO endorsement of the ISAs.

Other Litigation and Legal Activities

The General Counsel represents the Commission in all litigation in the United States Supreme Court and the courts of appeals. The General Counsel defends the SEC and its employees when sued in district courts, prosecutes administrative disciplinary proceedings against attorneys, appears amicus curiae in significant private litigation involving the federal securities laws, and oversees the regional offices' participation in corporate reorganization cases. The General Counsel analyzes legislation that would amend the federal securities laws or other laws affecting the work of the agency, drafts congressional testimony, prepares legislative comments, and advises the Commission on issues arising from the agency's regulatory and enforcement activities including all public releases and rule proposals. In addition, the General Counsel advises the Commission in administrative proceedings under various statutes, and advises the Commission and prepares opinions with respect to appeals from administrative law judges' decisions and self-regulatory organizations' (SRO) disciplinary actions.

Key 1994 Results

Issues of major importance were litigated by the SEC in 1994. In a 5-4 decision in *Central Bank of Denver v. First Interstate Bank of Denver,*[175] in which the Commission filed an *amicus curiae* brief, the United States Supreme Court held that although investors may sue to obtain money from those who themselves commit fraud in violation of Commission Rule 10b-5, the investors may not sue those who merely give assistance to, *i.e.,* aid and abet, the violators. The SEC has subsequently argued that the decision does not apply to its own

enforcement actions. In *Gustafson v. Alloyd* Co.,[176] the SEC filed an *amicus curiae* brief urging the United States Supreme Court to hold that buyers may recover under Section 12(2) of the Securities Act for false or misleading representations in all types of securities sales, not only public or initial sales, In *SEC v. Posner*,[177] the Court of Appeals for the Second Circuit held that, in appropriate circumstances, the district courts may exercise their inherent equitable powers to bar individuals who have engaged in securities fraud from serving as officers or directors of public companies. In all, the number of litigation cases opened in 1994 Increased 29 percent to 339.

The number of legislative matters handled by the staff grew 46 percent in 1994 from 180 to 263. In 1994, Congress passed the Unlisted Trading Privileges Act of 1994 (P.L. No. 103-390), which revised the application and approval process by which exchanges may obtain unlisted trading privileges in securities. It also simplified the securitization of small business loans in the Riegle Community Development and Regulatory Improvement Act of 1994 (P.L. No. 103-325). Many of the securities bills, however, were debated out but not passed. Among these were bills to strengthen the SEC's investment adviser inspection program and bills to change the private securities litigation system.

The adjudicatory program eliminated what was once a substantial and chronic adjudication case backlog. The staff submitted to the Commission 72 draft opinions, a 12 percent increase from 1993. In 1994, the staff also planned and held a successful inaugural conference on SRO adjudication, as had been recommended in the report of a Commission task force on administrative proceedings.

Significant Litigation Developments

Aiding and Abetting Liability

In *Central Bank of Denver v. First Interstate Bank of Denver,* the United States Supreme Court held, in a 5-4 decision, that although investors may sue to obtain money damages from those who themselves commit fraud in violation of Commission Rule 10b-5, the investors may not sue those who merely give assistance to, *i.e.,* aid and abet, the violators. The SEC has subsequently argued in two courts of appeals that the decision does not apply to its own enforcement actions. In the Ninth and Eleventh Circuits, the SEC has stressed that its enforcement cases are different from class action law suits brought by private investors. First, the Commission sues for injunctions to vindicate the public interest, not for money damages as private plaintiffs do. Also, Congress expressly provided for Commission enforcement of Section 10(b), but was silent on damage suits by private investors. The Ninth Circuit has yet to decide the case before it, while the Eleventh Circuit sent the case back to the district court to reconsider, among other things, whether the *Central Bank* decision applies to Commission enforcement actions.

Statutes of Limitation

The SEC, as *amicus curiae* in numerous cases, defended Section 27A of the Exchange Act against constitutional attack. Section 27A eliminates the retroactive application of the one-year/three-year statute of limitations for Section 10(b) private actions announced by the United States Supreme Court in *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson.*[178] It preserves the application of the statutes of limitation then in effect for all cases filed before *Lampf* was decided. The constitutionality of Section 27A as applied to cases that were pending when the statute was enacted has been upheld by the Courts of Appeals for the First, Second,

Fourth, Seventh, Ninth, Tenth and Eleventh Circuits.[179] This year, in its first consideration of a case that had been reinstated after final judgment pursuant to Section 27A, the United States Supreme Court affirmed by an equally divided court a decision of the Court of Appeals for the Fifth Circuit holding that Section 27A did not violate separation of powers principles or due process.[188] The Court subsequently agreed to hear a case in which the Court of Appeals for the Sixth Circuit held that such reinstatement violates separation of powers principles.[181] The SEC filed *amicus* briefs in both cases jointly with the Department of Justice.

Scope of Section 12(2) of the Securities Act

In *Gustafson v. Alloyd Co*.,[182] the SEC filed an *amicus curiae* brief urging the United States Supreme Court to hold that Section 12(2) of the Securities Act is not limited to only public or initial sales of securities but instead applies to all types of sales. Section 12(2) gives buyers a right of rescission against sellers who make false or misleading representations.

Definition of Security

In *Pollack v. Laidlaw Holdings,* Inc.,[183] the Court of Appeals for the Second Circuit held, as urged by the SEC as *amicus curiae,* that participation in mortgages sold to the investing public are securities under the Securities Act and the Exchange Act. The court of appeals' decision also made clear the limited scope of its 1992 decision in *Banco Espanol de Credito v. Security Pacific National Bank,*[184] which held that certain loan participation that were not offered or sold to individual investors are not securities.

Regulation of Securities Professionals

In *Patrick v. SEC*,[185] the Court of Appeals for the Second Circuit affirmed a disciplinary sanction imposed by the New York Stock Exchange (NYSE) on the president of Baird, Patrick & Co., Inc., a NYSE member firm, for failing to discharge his supervisory duties reasonably when he neglected either to supervise or to delegate responsibility for supervising a firm vice president who was engaged in improper floor trading.

Officer-Director Bar

In *SEC v. Posner,*[186] the Court of Appeals for the Second Circuit held that, in appropriate circumstances, the district courts may exercise their inherent equitable powers to bar individuals who have engaged in securities fraud from serving as officers or directors of public companies.

Disgorgement and Related Issues

In *SEC v. Bilzerian,*[187] the Court of Appeals for the District of Columbia Circuit held that a disgorgement order entered in an SEC case is not punitive where the amount ordered to be disgorged is a fair approximation of the fruits of wrongdoing. The court also held that the double jeopardy clause of the Constitution therefore does not prevent disgorgement being ordered against a defendant who had previously been criminally convicted for the same offense.

Markups

In *First Independence Group v. SEC*,[188] *Amato v. SEC*,[189] and *Orkin v. SEC*,[190] the Courts of Appeals for the Second, Fifth, and Eleventh Circuits upheld the SEC's policies as to (1) how retail markups on securities are to be calculated by securities dealers and

(2) what constitutes an excessive markup. Both *Amato* and *Orkin* specifically upheld the liability of securities salesmen where they had reason to know that customers were being charged excessive markups.

Requests for Access to Commission Records

The Commission received approximately 125 subpoenas for documents and testimony in 1994. In some of these cases, the SEC declined to produce the requested documents or testimony because the information sought was privileged. The SEC's assertions of privilege were upheld in every decided case when the party issuing the subpoena challenged the assertion in court.

The Commission received 2,261 requests under the Freedom of Information Act (FOIA) for access to agency records and 5,659 confidential treatment requests from persons who submitted information. There were 35 appeals to the SEC's General Counsel from initial denials by the FOIA Office. None of these appeals resulted in district court litigation. Two FOIA appeals that resulted in district court litigation in 1993 remain pending.

Actions Under the Right to Financial Privacy Act

Seventeen actions were filed under the Right to Financial Privacy Act to quash SEC subpoenas for customer records from financial institutions. Ten of these challenges were dismissed by district courts after the courts found, in each case, that the records were relevant to legitimate law enforcement inquiries.[191] Three of the challenges were withdrawn,[192] one was granted,[193] and three remain pending.[194]

Actions Against Professionals Pursuant to Commission Rule 2(e)

In *In re David L. Kagel,* the Commission, pursuant to Rule 2(e) of its Rules of Practice,[195] permanently barred attorney David L. Kagel from appearing or practicing before the Commission. This action was based upon an injunction entered against him for violating antifraud provisions of the federal securities laws.[196] Kagel had orchestrated a fraudulent scheme to take a private company public through acquisition by a public shell company and, in doing so, prepared and filed with the Commission several filings that contained false and misleading statements of material fact.

Two court actions were filed against the Commission challenging its authority to prosecute Rule 2(e) proceedings. In *Checkosky and Aldrich v. SEC*,[197] the United States Court of Appeals for the District of Columbia Circuit issued a *per curiam* decision which found that the Commission was authorized to promulgate Rule 2(e) under its general rulemaking authority. The court found that the rule represents an attempt by the Commission to protect the integrity of its processes by ensuring that professionals perform their tasks with a reasonable degree of competence.

In the other action, *Danna and Dentinger v. SEC*,[198] the United States District Court for the Northern District of California granted the Commission's motion to dismiss an action filed by two auditors seeking to enjoin a Rule 2(e) proceeding brought against them for improper professional conduct in connection with an audit. The auditors argued that the Commission could not predicate a Rule 2(e) proceeding based on negligent – as opposed to willful – conduct. The court upheld the Commission's authority to institute Rule 2(e) proceedings based on negligent conduct. A two week trial of the underlying administrative proceeding was completed in March 1994 and a decision is pending.

Motions for Attorney's Fees Under the Equal Access to Justice Act

Five defendants who prevailed in Commission enforcement actions filed motions under the Equal Access to Justice Act seeking attorney's fees and expenses aggregating approximately $3 million.[199] In each of these cases, the Commission opposed the motion arguing that it was substantially justified in bringing the action or that special circumstances made an award unjust. The Commission was successful in each of the actions that was decided.

Wells Submission

In *In re Salomon Brothers Treasury Litigation,*[200] the Second Circuit found, as urged in the *amicus* brief filed by the Commission, that disclosure to the Commission of a Wells submission waives the work-product privilege for that document The court also found that the Commission may enter into an agreement with a witness in an investigation to maintain the confidentiality of a privileged document produced to the Commission.

Scope of the Joint Defense Privilege

The Commission filed an *amicus curiae* brief in *Durkin v. U.S. District Court for the Southern District of California,*[201] urging the United States Court of Appeals for the Ninth Circuit to hold that the joint defense privilege does not apply when there is subsequent litigation between the parties to the agreement.

Significant Adjudication Developments

The staff submitted to the Commission 72 draft opinions, a 12 percent increase from 1993's record number, and the Commission issued 70 opinions. This continued high productivity eliminated what was once a substantial and chronic backlog in opinions.

The Commission received 60 appeals in 1994, down from 1993's record of 71. It is anticipated, however, that appeals from SRO disciplinary actions will return to prior levels. The adjudicatory caseload handled by the Office of the General Counsel will be further expanded as a result of (1) the Commission's increase in the number of administrative proceedings against aiders and abettors, in the wake of the Supreme Court's recent decision limiting private suits for aiding and abetting fraud, and (2) the Office of the General Counsel's assumption, in late 1994, of responsibility for advising the Commission with respect to appeals from Commission Rule 2(e) proceedings against professionals other than attorneys.

Significant Adjudicatory Decisions in 1994

In 1994, the Commission reviewed a number of cases finding sales practice abuses. In *Frank J. Custable, et al.*,[202] for example, the Commission found that a Chatfield Dean & Co. registered representative used deceptive and fraudulent practices to induce a customer to purchase securities, and purchased securities for a second customer without the customer's authorization or consent. Also, the Commission concluded that the firm and Custable's immediate supervisor failed to supervise Custable properly and sustained the bar imposed on Custable by the National Association of Securities Dealers (NASD). In *Vanden J. Catli,*[203] the Commission also sustained a permanent bar. Catli's misconduct included misappropriating customer funds, trading in customer accounts without authorization, effecting unsuitable transactions for and making misstatements to customers, improperly advising customers to ignore margin calls, and making misrepresentations to the NYSE. In another NYSE-instituted case, the Commission concluded that a former salesman for NYSE member firm Merrill Lynch, Pierce, Fenner & Smith, Inc. recommended to customers various mutual funds that were unsuitable in light of the customers' expressed desire

for low-risk, income-producing investments, and effected margin transactions without his customer's authorizations.[204] The Commission sustained the NYSE's order suspending the salesman for one year and placing him under heightened supervision for an additional year.

On review of a complex and novel NASD action finding that a member firm that bought and sold direct participation program (DPP) securities in the secondary market had charged customers unfair markups, the Commission set aside the findings and sanctions.[205] In the majority of the DPP transactions at issue, the firm dealt solely with registered broker-dealers who negotiated the price on behalf of the buyers. The Commission concluded that these buyers were not the firm's customers, and therefore that these transactions were not covered by the NASD's markup policy. In other transactions, the firm dealt directly with a buyer, or dealt through a third-party intermediary that was not a broker-dealer. With respect to these transactions, the Commission held that the NASD did not establish violations of its markup requirements. The Commission noted that, among other things, the NASD failed to demonstrate a prevailing market price for the securities.

Finally, in a case arising under the Public Utility Holding Company Act of 1935 (Holding Company Act),[206] the Commission rejected a proposal by Central and South West Corporation (CSW), a registered holding company, and CSW's wholly owned non-utility subsidiary, CSW Credit, Inc., to increase CSW's investment in the subsidiary. The proposal contemplated that CSW's increased investment would be used to expand the subsidiary's business to factor accounts receivable of non-affiliate utilities. The Commission concluded that this expansion would be inconsistent with the statutory requirement that operations of public utility holding companies be limited to such other businesses as are "reasonably

incidental, or economically necessary or appropriate" to the operations of the utility system.

Legal Policy Developments

The General Counsel, as principal legal adviser to the Commission, provided independent advice on legal and policy issues arising from rulemaking and enforcement actions, and ensured that Commission actions satisfied applicable administrative law and other legal requirements. The staff drafted legislative proposals, developed the Commission's position on pending bills in Congress, and prepared Commission testimonies for congressional hearings. The staff also participated in the Commission's program of technical assistance to emerging securities markets.

In November 1993, the Commission proposed for comment comprehensive revisions to its Rules of Practice, which govern the conduct of Commission administrative proceedings. The proposed revisions are designed to improve the efficiency of the Commission's administrative processes and to implement authority granted in the Securities Enforcement Remedies and Penny Stock Reform Act.[207]

Significant Legislative Developments

In 1994, a number of securities bills were enacted into law. Amendments to the Government Securities Act and a bill to reform "roll-ups" of limited partnerships were passed late in the first session of the 103rd Congress. In its second session, the 103rd Congress adopted legislation to facilitate the securitization of small business and commercial loans, and legislation revising the application and approval process for exchanges to obtain unlisted trading privileges. Although Congress actively considered important securities bills in a number of other areas, it failed to reach agreement on final legislation. Thus, Congress considered but did not pass bills relating

to investment advisers, litigation reform, the regulation of derivatives, and the question of SEC self-funding.

Government Securities

Important legislation involving the regulation of the government securities markets was enacted early in the fiscal year. The Government Securities Act Amendments of 1993 was signed into law by the President on December 17, 1993 (Pub. L. No. 103-202). The amendments represent the culmination of three years' efforts. The House, in the 103rd Congress, sought passage of broad reform legislation, including large position reporting, sales practice rules, and targeted antifraud provisions. The Senate bill was much narrower. The final legislation provides, among other things, for: (1) permanent authorization of Treasury rulemaking under the Government Securities Act; (2) SEC authority to obtain trade records in machine-readable form; (3) Treasury authority to require large position reporting; (4) SEC antifraud authority over government securities brokers and dealers under Section 15(c) of the Exchange Act; (5) sales practice rulemaking under the Government Securities Act; (6) antifraud provisions governing bids in connection with primary offerings of government securities; (7) two studies of aspects of the regulatory system for government securities; and (8) reforms to the Treasury auction process.

Limited Partnership Roll-ups

"Roll-ups" are limited partnership reorganizations that usually involve the merger of limited partnerships into new, larger, corporate entities. In response to perceived abuses in roll-up transactions, Congress passed roll-ups legislation as Title III of the Government Securities Act Amendments (Pub. L. No. 103-202, discussed above). This legislation also was the product of three years' efforts. The final legislation makes it unlawful for any person to solicit a proxy,

consent, or authorization concerning a roll-up transaction, or to make a tender offer in furtherance of a roll-up transaction (as statutorily defined), unless the transaction is conducted in accordance with SEC rules. The SEC must have such rules effective within 12 months from the date of the bill's enactment; a rulemaking is currently pending. The statute also requires the NASD or the exchanges, again within 12 months, to adopt rules and establish listing standards for limited partnership roll-ups. To a large extent, the final legislation codifies rules adopted by the SEC in 1991 and NASD rules currently pending before the SEC.

Small Business and Commercial Loan Securitization

H.R, 3474, the Riegle Community Development and Regulatory Improvement Act of 1994, passed the House and Senate in August 1994; it was signed into law by President Clinton on September 23, 1994 (Pub. L, No. 103-325). This law contains small business securitization provisions derived from a bill originally introduced in the Senate by Senator D'Amato in 1993. The SEC testified in support of the bill's securities law amendments before the Senate in 1993, and before the House Energy Committee's Subcommittee on Telecommunications and Finance on June 14,1994. The legislation also includes provisions relating to community development banking, money laundering, and regulatory relief for banks,

The small business provisions of H.R. 3474 build on the framework for securitization established by the Secondary Mortgage Market Enhancement Act (SMMEA). The legislation amends the Exchange Act to relax the margin, credit, and collateral requirements applicable to qualifying "small business related securities." It also amends federal banking law to permit banks to invest in small business related securities, and preempts state blue sky and legal investment laws with respect to such securities. In addition, the

legislation mandates a joint SEC-Federal Reserve study on the impact of the small business securitization provisions on the credit and securities markets.

H.R. 3474 also contains other provisions that directly affect the work of the SEC. One such provision amends SMMEA to include mortgages on commercial real estate within the SMMEA securitization framework. A separate provision establishes a new exemption from the registration requirements of the Securities Act for equity securities issued or exchanged in the context of qualifying reorganizations of banks or thrifts into holding company structures.

Unlisted Trading Privileges

H.R. 4535, a bill revising the application and approval process for unlisted trading privileges (UTP) passed the House in August 1994 and the Senate in October 1994. It was signed into law October 22, 1994 (Pub. L. No. 103-389). The UTP legislation embodies an agreement negotiated by the SEC among the regional exchanges and the NYSE in November 1993. Under the legislation, trading in an initial public offering (IPO) pursuant to UTP is no longer subject to a time-consuming application and approval process. Instead, exchanges may extend UTP to an IPO on the third day of trading on the listing exchange. The SEC must undertake rulemaking within 180 days from enactment of the new law to determine whether to require any delay in trading of IPOs pursuant to UTP. The SEC testified before the House Telecommunications and Finance Subcommittee in support of H.R. 4535 in June 1994.

Investment Advisers

In the 103rd Congress, both the House and the Senate passed legislation to provide for enhanced SEC inspection of investment advisers. However, the efforts of a House/Senate staff conference to

reconcile the two bills failed in the waning hours of the 103rd Congress.

The bill developed by the staff conference dropped certain provisions that had been included in the House bill (H.R. 578) regarding recordkeeping and transaction reporting, risk-based inspection of advisers, and suitability. Notably, in March 1994, the SEC had proposed rules defining an investment adviser's suitability obligations, thus eliminating the need for a statutory provision. The compromise bill, however, did incorporate other measures that were present in H.R. 578 but absent from the Senate-passed bill (S. 423), such as provisions for SEC designation of one or more SROs; periodic SEC surveys of unregistered advisers; an electronic listing providing disciplinary information about advisers; and an SEC study of steps to disclose advisers' felony convictions. The compromise bill was approved by the House on October 5, 1994, but the legislation was blocked from coming to the Senate floor.

Litigation Reform

Both the House and Senate showed interest in the issue of litigation reform. Senators Dodd and Domenici introduced S. 1976, a bill designed to curb abuses in private securities lawsuits, including class actions in particular, in March 1994. The Senate also held a hearing in May 1994 regarding the effects of the Supreme Court's *Central Bank of Denver* decision on private litigation and the SEC's antifraud enforcement program. Senator Metzenbaum later introduced S. 2306, a bill aimed at restoring aiding and abetting liability for violation of Exchange Act Section 10(b).

On the House side, the Subcommittee on Telecommunications and Finance held a hearing in July 1994 on the issue of litigation reform. In testimony before the Subcommittee, the SEC noted support for some of the measures included in S. 1976 and in H.R.

417 (a House litigation reform bill introduced in 1993). The SEC also called for legislation to restore aiding and abetting liability and to extend the statute of limitations for securities fraud actions.

SEC Authorization and Appropriation

In 1993, the House passed an SEC authorization bill for 1994-95, which contained a provision for SEC self-funding. Senate budgetary rules, and the opposition of some Senators to the concept of SEC self-funding, prevented the Senate from taking comparable action. The SEC's fiscal 1995 appropriation, which relied on a form of self-funding to offset the SEC's appropriation, was supported by the SEC's appropriations subcommittees but ultimately fell to disagreements over SEC fees and self-funding generally. As a result of these disagreements, Congress passed a stopgap SEC appropriation bill in August 1994 providing only $125 million (Pub. L. No. 103-317), with the intention of revisiting the issue of SEC funding and passing a supplemental appropriations bill within five months. OMB determined, however, that applicable federal law required the SEC to apportion that partial appropriation as if it were the full appropriation for the fiscal year. Consequently, the SEC faced a budget shortfall of approximately $172 million and the possibility of severe curtailment of operations.

Due to jurisdictional disputes in the House, the availability of an additional SEC appropriation was conditioned on the enactment of separate revenue legislation, raising SEC registration fees, that would offset the SEC's additional appropriation. Thus, to fund the SEC fully, it was necessary for Congress to pass two separate pieces of legislation in the two month period before the end of the session – an additional appropriation and a separate revenue bill.

The bill providing for an additional SEC appropriation of $192 million was signed into law on September 30, 1994 (Pub. L. No. 103-

335). The revenue legislation, H.R. 5060, which set the filing fees under Securities Act Section 6(b) at the rate of 1/29th of one percent, passed the House on September 27, 1994, but was held up in the Senate as various Senators sought to add unrelated provisions to the last major revenue bill of the 103rd Congress. H.R. 5060 finally passed the Senate on October 8, and was signed into law on October 10, 1994 (Pub. L. No. 103-352), thus bringing SEC funding to $297 million.[208] In the early days of fiscal 1995 before the revenue bill's passage, the SEC had to curtail inspections, enforcement activity, and other "non-essential" services. In addition, since Section 6(b) filing fees had decreased from 1/29th of one percent to 1/50th of one percent, the Treasury lost approximately $20 million in filing fee receipts over the period.

Other Legislative Initiatives

Several other legislative initiatives of interest to the SEC were considered during the 103rd Congress. For example, a number of bills were considered that addressed the SEC's jurisdiction under the Holding Company Act and/or would have authorized registered holding companies to diversify into telecommunications. In the derivatives area, several bills were considered, and hearings held, on derivative financial instruments. Also, congressional and General Accounting Office (GAO) studies of the derivatives market were conducted. In the mutual fund area, the House held hearings on several bills that would have regulated bank sales of mutual funds and other investment products and also held oversight hearings regarding the personal trading of fund managers. In addition, GAO conducted two congressionally-requested reviews of the mutual fund activities of banks. In the enforcement area, the House held a hearing on the problem of "rogue brokers." Finally, with respect to small businesses, the House considered a bill, and held a hearing, on the Commission's small business initiative.

Corporate Reorganizations

The Commission acts as a statutory advisor in reorganization cases under Chapter 11 of the Bankruptcy Code to see that the interests of public investors are protected adequately. Commission participation is generally limited to cases involving debtors with publicly traded securities.

Committees

Official committees negotiate with debtors on reorganization plans and participate generally in all aspects of the case. The Bankruptcy Code provides for the appointment of an official committee for stockholders where necessary to assure adequate representation of their interests. During 1994, the Commission successfully supported motions for the appointment of investor committees in two cases.[209]

Estate Administration

In *In re Envirodyne Industries, et al.*[2l0] and *In re MEI Industries, Inc*.,[211] the Commission argued that the bankruptcy court is required to find that an indenture trustee's fees are reasonable before they can be paid from plan distributions to bondholders. In *Envirodyne,* the indenture trustee agreed to allow the bankruptcy court to pass on the reasonableness of its fee request. In *MEI Industries,* the court followed the decision of the court in *In re National Convenience Stores, Inc.*[212] which had rejected the Commission's request for a bankruptcy court determination of reasonableness of fees.[213]

In *ln re MEI Industries,* Inc.[214] and *In re Phar-Mor, Inc*.,[215] the Commission argued, as it has previously,[216] that the Bankruptcy

Code allows discharge of the liabilities of only a debtor – not of third parties like officers and directors – unless there is separate consideration or unless the discharge of liability is voluntary. This issue is of significance because in many cases debtors seek to use the Chapter 11 process to protect officers and directors from personal liabilities for various kinds of claims, including liabilities under the federal securities laws. In *ME/ Industries,* the court, agreeing with the Commission, struck the plan provision that sought to protect the indenture trustee from liability. The matter is pending in *Phar-Mor.*

In *In re Amdura Corporation, Inc.,*[217] the district court, agreeing with the Commission, reversed the bankruptcy court's order disallowing a class proof of claim filed on behalf of public investors who allegedly were victims of securities fraud by the debtors. The district court rejected the bankruptcy court's conclusion that the decision in this case was controlled by the ruling of the Tenth Circuit in *In re Standard Metals,* 817 F.2d 625 (10th Cir. 1987), holding that a class proof of claim is not permissible in bankruptcy. Rather, the district court agreed with the Commission that the Tenth Circuit decision is dictum, and thus not controlling authority. The district court, as pointed out by the Commission, agreed that the better reasoned view, represented by several subsequent circuit and district court decisions,[218] is to permit class proofs of claim in bankruptcy cases.

In *In re First City Bancorporation of Texas,*[219] the Commission filed a memorandum supporting securities fraud plaintiffs' motion to withdraw consideration of its class claim from the bankruptcy court pursuant to 28 U.S.C. 157(d) so that the district court may rule on the question. This provision requires a district court to withdraw a proceeding from the bankruptcy court when "resolution of the proceeding requires consideration of both the Bankruptcy Code and

other laws of the United States regulating organizations or activities affecting interstate commerce," such as the federal securities laws. The issue became moot after the parties agreed to a revised claim filing procedure and to resolve the securities claim by settlement.

In October 1994 *In re NVF Company,*[220] the Commission supported the right of shareholders to compel an annual shareholders meeting. NVF Company is controlled by Victor Posner who has been barred by a federal district court from serving as an officer or director of any company subject to the reporting requirements of the federal securities laws and ordered to place into a voting trust shares in public companies that he controls.[221] The Commission argued that convening a shareholders' meeting would serve the public interest and the best interest of the bankruptcy estate by giving shareholders the opportunity to remove the existing Posner controlled directors and choose an independent board to guide the reorganization process. The Commission also argued that allowing shareholders to exercise their corporate governance rights during the plan negotiation stage of a Chapter 11 reorganization is consistent with existing law. The matter is pending.

Disclosure Statements/Plans of Reorganization

A disclosure statement is a combination proxy and offering statement used to solicit acceptances for a reorganization plan. Such plans often provide for the issuance of large quantities of new unregistered securities pursuant to an exemption from Securities Act registration contained in the Bankruptcy Code. The Commission reviews disclosure statements of publicly-held companies or companies likely to be traded publicly after reorganization. During 1994, the staff reviewed 109 disclosure statements and commented on 79. Most of the Commission's comments were adopted by debtors; formal objections were filed in four cases.[222] In addition, the

Commission prevented the unlawful issuance of securities in two cases.[223]

In *In re Enviropact, Inc.,*[224] the Commission filed an objection to the debtor's reorganization plan that sought to discharge claims of creditors and sell the assetless public shell corporation in order to make limited payments to creditors. The Commission contended that this would contravene Section 1141(d)(3) of the Bankruptcy Code, which precludes a debtor from obtaining a discharge if it has liquidated all or substantially all of its assets and does not engage in business after consummation of the reorganization plan. Following the filing of the Commission's objection, the debtor withdrew its reorganization plan.

Ethical Conduct Program

The General Counsel is the Designated Agency Ethics Official for the SEC. In 1994, the Ethics Counsel and staff continued to respond to a demand for counseling services at the rate of approximately 20 new matters per week. These inquiries reflected unique or novel issues, while routine or repetitive inquiries were handled by ethics liaison officers and deputies located within each division and office.

The staff implemented the annual training requirements for senior and mid-level employees and the new government-wide program for confidential disclosure of financial interests. In addition, major portions of the review of the Commission's rule on securities holdings and transactions of members and employees and their families were completed.

Workload

The General Counsel's Office has experienced substantial increases in productivity and workload in recent years. In 1994, workload in the litigation and legislative areas continued to experience substantial increases.

[table deleted]

Economic Research and Analysis

The Office of Economic Analysis provides technical support and analysis to the Commission's regulatory program. The economics staff provides the Commission with research and advice on rule proposals, policy initiatives, and enforcement actions. The staff also monitors developments and major program initiatives affecting the United States financial services industry, investors, and international capital markets.

Key 1994 Results

In 1994, the Office of Economic Analysis focused its efforts on a number of areas including enforcement cases, mutual fund disclosure, and market structure issues. The staff provided technical assistance to the Division of Enforcement, initiated a mutual fund disclosure project, provided economic analysis in connection with market structure and rulemaking issues, and reported on the financial health of the securities industry.

Economic Analysis and Technical Assistance

The staff provided technical assistance to the Division of Enforcement in more than 40 cases of insider trading, market manipulation, fraudulent financial reporting, and other violations of securities laws. The staff uses financial theory and event analysis to provide the empirical support key to numerous enforcement cases. In addition, the staff advises the Division of Enforcement regarding materiality and/or the amount of disgorgement that should be sought. The staff assists in taking testimony in cases involving complex

financial instruments and in evaluating the testimony of experts and the reports of consultants hired by opposing parties. The staff assisted the U.S. Attorney's Office by providing expert testimony in the sentencing hearing for *SEC v. Antar, et al.*

The staff began several projects in the area of mutual fund disclosure. Focus group discussions designed to survey the public's understanding of the risks associated with mutual funds identified significant misconceptions. In response, the staff designed a survey to evaluate how mutual fund materials help investors make informed decisions. This survey will be conducted in early 1995. In connection with improved risk disclosure, the staff studied various risk measures for mutual funds to evaluate their stability and predictive power.

The staff provided advice, technical assistance, and analyses on several market structure and rulemaking issues. The staff provided advice on disclosure of payment for order flow. The staff analyzed a National Association of Securities Dealers (NASD) report on passive market making and studied the impact of the NASD's modification of the small order execution system on bid-ask spreads. The staff also studied the effects of over-the-counter trading by exchange members in exchange-listed stocks on market quality.

The staff continued to monitor the securities industry and developments in the domestic and international securities markets. The staff analyzed data from the 1993 penny stock examination sweep and reported on the financial condition of penny stock dealers. In addition, the staff developed a monthly analysis of investor complaints against broker-dealers which is being integrated into the SEC's enforcement and examination programs.

The staff provided advice on and monitored developments in the markets for hybrid products and derivative securities. The staff assisted the Office of the Chief Accountant on issues related to the

financial reporting of quantitative risk measures for derivatives and other financial instruments. The staff also analyzed 90 rule proposals to assess their potential effects on small entities, as required by the Regulatory Flexibility Act of 1980.

Policy Management and Administrative Support

Policy management and administrative support provide the Commission and operating divisions with the necessary services to accomplish the agency's mission. Policy management is provided by the executive staff, including the Office of Legislative Affairs; the Office of the Secretary; the Office of Public Affairs, Policy Evaluation and Research; the Office of the Executive Director; and the Office of Equal Employment Opportunity. The responsibilities and activities of policy *management include developing and executing management policies, formulating and communicating program policy, overseeing the allocation and expenditure of agency funds, maintaining liaison with the Congress, disseminating information to the press, and facilitating Commission meetings.*

Administrative support includes services such as accounting, financial management, fee collection, information technology management, data processing, space and facilities management, human resources management, and consumer affairs. Under the direction of the Office of the Executive Director, these support services are provided by the Offices of the Comptroller, Information Technology, Administrative and Personnel Management, and Filings and Information Services.

Key 1994 Results

In 1994, the Commission celebrated its 60th anniversary. During the year, the Commission held 59 meetings and considered 317 matters. Major activities of the Commission included adoption of a three-day securities transaction settlement rule, simplification of

registration and reporting requirements for foreign companies, requirements for disclosure by investment advisers regarding wrap fee programs, and requirements for enhanced disclosure by broker-dealers of payment for order flow practices.

The agency collected fees for the United States Treasury in excess of its appropriation for the twelfth consecutive year. The SEC's total fee collections in 1994 were $588 million and the net gain to the Treasury was $340 million.

Policy Management

Commission Activities. The Commission held 59 meetings in 1994, during which it considered 317 matters, including the proposal and adoption of Commission rules, enforcement actions, and other items that affect the stability of the nation's capital markets and the economy. Significant regulatory actions taken by the Commission included:

- adoption of a three-day securities transactions settlement rule;
- adoption of amendments to the multi-jurisdictional disclosure system for Canadian issuers;
- adoption of executive compensation disclosure requirements concerning security holder lists and mailing requests;
- simplification of registration and reporting requirements for foreign companies; and
- adoption of requirements for disclosure by broker-dealers of payment for order flow practices.

Congressional interest in the agency's activities and initiatives remained high. The Commission and staff members testified at 20

congressional hearings during the year, an increase of 66 percent over the prior year. In addition, the Congress actively considered a number of important issues under the Commission's jurisdiction. These were most notably:

- issues posed by derivatives investments;
- proposed amendments to the Investment Advisers Act of 1940, including fee provisions to fund more frequent Commission inspections of investment advisers;
- possible reforms in the government securities markets;
- limited partnership "roll-ups" and their impact on investors;
- securities litigation reform;
- legislation to facilitate improved access to capital for small businesses;
- issues affecting the mutual fund industry;
- the SEC staff's report entitled *Market 2000: An Examination of Current Equity Market Developments* and the Unlisted Trading Privileges Act of 1994, a bill to reduce procedural delays with respect to unlisted trading privileges;
- proposals to curtail frivolous securities litigation; and
- the SEC's budget authorization and appropriation.

Public Affairs. The Office of Public Affairs, Policy Evaluation and Research (OPAPER) communicated information on Commission activities to those interested in or affected by Commission actions,

including the press, regulated entities, the general public, and employees of the agency.

Many of the agency's actions are of national and international interest. When appropriate, these actions are brought to the attention of regional, national, and international press. A total of 145 news releases on upcoming events, agency programs, and special projects were issued. Additionally, congressional testimony, speeches, opening statements and fact sheets presented by Commissioners and senior staff were maintained on file and disseminated in response to requests from the public and the press. The staff responded to 60,000 requests for specific information on the agency or its activities.

The OPAPER staff published daily the *SEC News Digest* which provided information on rule changes, enforcement actions against individuals or corporate entities, registration statements, acquisition filings, interim reports, releases, decisions on requests for exemptions, Commission meetings, upcoming testimony by Commission members and staff, lists of Section 16 letters, and other events of interest. During the year, the *Digest* was computerized and is now available to the staff on the SEC Local Area Network (LAN) bulletin board and publicly accessible on FedWorld, a federal electronic bulletin board.

The staff provided support for activities related to the SEC's International Institute for Securities Markets Development, Consumer Affairs Advisory Committee, Chairman Arthur Levitt's Consumer Education Program, and the 60th anniversary of the Commission. In addition, programs for 624 foreign visitors were coordinated during the year.

Management Activities. The Office of the Executive Director coordinated special projects, such as the restructuring of several

divisions and offices, and completed an assessment of the agency's operational efficiency. The staff also coordinated the agency's compliance with and response to actions under the National Performance Review (NPR) and the Government Performance and Results Act of 1993, including completion of the agency's Customer Service Plan. Working closely with other senior officials, the staff formulated the agency's budget submissions to the Office of Management and Budget and the Congress, and prepared and submitted to Congress the agency's authorization request for fiscal years 1995 through 1997.

Equal Employment Opportunity. The Office of Equal Employment Opportunity (EEO) provided the agency with support for compliance with Title VII of the Civil Rights Act of 1964, as amended; the Age Discrimination in Employment Act of 1967; the Rehabilitation Act of 1973; and Equal Pay Act of 1963. This support was provided through the EEO Office's compliance and affirmative employment activities,

The primary services provided by the compliance activity included counseling and dispute resolution, administrative fact-finding investigations, and final agency decisions on formal complaints of employment discrimination. In connection with the affirmative employment activity, EEO prepared the agency's annual accomplishment report to the Equal Employment Opportunity Commission; conducted in-house EEO training of supervisors and orientation of new employees; provided legal support for the agency-wide sexual harassment prevention training program that was completed in 1994; administered the Federal Women's Program, the Hispanic Employment Program, and the Black Employment Program; and sponsored the SEC's Disability Awareness Month Program.

Freedom of Information Act and Privacy Act, The Office of Freedom of Information Act (FOIA) and Privacy Act Operations responded to requests for access to information pursuant to FOIA, the Privacy Act, and the Government in the Sunshine Act, and processed requests under the agency's confidential treatment rules. Confidential treatment requests were generally made in connection with proprietary corporate information and evaluated in conjunction with access requests to prevent the unwarranted disclosure of information exempt under the FOIA.

The agency received 2,288 FOIA requests and appeals, 8 Privacy Act requests, 45 Government in the Sunshine Act requests, 9 government referrals, and 5,667 requests and appeals for confidential treatment. All responses to FOIA/Privacy Act requests were made within the statutory time-frame.

Administrative Support

Financial Management and Operations. For the twelfth straight year, the SEC collected fees in excess of its appropriation. The SEC's total fee collections in 1994 were $588 million, 226 percent of the agency's appropriated spending authority of $260 million (which consisted of $58 million in appropriated funds, $172 in current year offsetting fee collections, and $30 million from a carry-over of prior year offsetting fee collections). The $588 million in total fee collections, minus the SEC's current year spending authority of $230 million ($260 million less the $30 million from prior year offsetting fee collections) and $18 million in additional offsetting fee collections, resulted in a net gain of $340 million to the United States Treasury.

The SEC's total fee revenue in 1994 was collected from four basic sources: registrations of securities under Section 6(b) of the Securities Act of 1933 (comprising 78 percent of total fee collections), transactions of covered exchange listed securities (17 percent),

tender offer and merger filings (4 percent), and miscellaneous filings (1 percent). Offsetting fee collections were generated from an increase in the fee rate under Section 6 (b) of the Securities Act from one-fiftieth of one percent to one-twenty-ninth of one percent.

The Office of the Comptroller (OC) prepared an updated Five-Year Financial Management Plan that responds to current financial system issues, recognizes new legislative and NPR requirements, and is consistent with the agency's information technology plan.

In 1994, the agency's central accounting system, the Federal Financial System, was upgraded to provide enhanced user security, and accounts receivable, payment processing, and direct on-line system functions to headquarters and field offices. Development continued on the new "paperless" electronic time and attendance system, an agency-wide Property Management Program, and the Entity Filing and Fee System. Testing began on the General Services Administration's approved credit card system for the procurement of small purchases. When fully implemented, this system will facilitate the prompt delivery of materials and reduce the number of purchase orders written and vouchers processed.

The OC assisted the Office of the Executive Director in working with the staff of the Office of Management and Budget and the members and staff of the congressional committees on appropriations, authorization, finance, and ways and means to provide the SEC a 1995 spending level of $301 million and 2,844 Full-Time Equivalents (FTEs), increases of $32 million and 171 FTE over 1994 levels.

Information Resources Management. The Office of Information Technology (OIT) progressed in the development and enhancement of SEC information resources. Operation of the Electronic Data Gathering, Analysis and Retrieval (EDGAR) project continued, and a

system upgrade in February 1994 resulted in additional functionality and significantly improved response time for SEC staff. The staff completed its evaluation of the significant test period (January 1 through June 30, 1994). A report on the findings was prepared and submitted to the Commission,

Continued emphasis was placed on improving OIT's responsiveness to users' needs. The End User Advisory Committee, consisting of senior representatives from each of the program divisions, reviewed the development of the agency's strategic automation plan, external data service funding requirements, and other automation issues. A greater emphasis on quality assurance and system design functions within OIT helped ensure that developed systems met the specifications of the system design.

The agency's disaster recovery plan was expanded to provide the agency with automation backup capabilities for its Local Area Network (LAN) in the event of a disaster at either of its computer facilities – the main Operations Center in Alexandria, Virginia or the Headquarters building in Washington, D.C. Initial backup capability for the SEC mainframe was put in place in January 1994.

Development continued on the Large Trader and the Market Risk Assessment systems, as mandated by the Market Reform Act of 1990. Once completed these systems will monitor the activity of large traders in the markets and enable the SEC to monitor the financial condition of broker-dealer parent firms and minimize the market risks associated with broker-dealer/affiliate relationships. Phased development of the systems will continue through 1996.

Administrative and Personnel Management. The Office of Administrative and Personnel Management (OAPM) provided a wide range of personnel and office support functions, including recruitment and staffing, position management and classification, employee

compensation and benefits, training, performance management, employee recognition, labor relations, counseling, disciplinary actions, personnel security and suitability, personnel action processing, and maintenance of official employee records. The support activities include procurement and contracting, space acquisition, lease administration, facilities management, property management, desktop publishing, printing, publications, and mail services.

The SEC's personnel activity was designated as a "reinvention lab" and registered with the NPR. Internal focus groups were established to assess staffing, recruitment, and performance management processes, and flexiplace options. The focus group on alternate work schedules and flexiplace considered various alternatives to expand the agency's policies on these issues, in an effort to assist staff in balancing work and family demands. The focus group on performance management evaluated implementation of how the agency's current performance appraisal system was being implemented and explored a variety of alternative systems. Recommendations from these groups are pending final management decision.

As part of Chairman Arthur Levitt's diversity initiative, OAPM and EEO established an internal affirmative recruitment task force. This group focused on increasing recruitment activities aimed at underrepresented minority groups and providing information on diverse recruitment sources to managers throughout the agency. The SEC's recruitment program continued to emphasize active participation in job fairs, on-campus recruitment interviews at law schools, and the use of available hiring programs and authorities. As a result, approximately 40 percent of the employees hired in 1994 were minorities.

OAPM coordinated the agency's response to Executive Order 12861, calling for agencies to eliminate one-half of Executive Branch internal regulations within three years. As a result, approximately 11 percent of the page count of internal policy documents was eliminated through revisions or deletions. Plans were initiated to overhaul the *Personnel Operating Policies and Procedures Manual* within the next two years. This would include simplifying the numbering system (which was based on the now defunct Federal Personnel Manual) and reducing the total number of pages.

The OAPM began initial testing of the new automated Personnel Resource System (PRS). Phase I of PRS is expected to be operational during the second quarter of fiscal year 1995. When fully implemented, PRS will enable the on-line review and processing of requests for personnel actions.

During 1994, 1,405 employees attended a total of 2,784 training events lasting one day or longer. Twenty-six employees graduated from the SEC's Upward Mobility Program, a two-year career development program initiated in June 1992. This program enables competitively selected clerical and administrative employees to move into para-professional and professional positions via "bridge positions." In other initiatives, the policy framework for Executive, Management, and Supervisory Development training was developed and mandatory training courses to strengthen supervisory and management skills were identified.

The agency administered 15 leases for an approximate total of 773,442 square feet of office and related space. Also, a new property accountability system utilizing bar-coding was implemented. All field and headquarters offices were inventoried using the new system.

Printing operations were enhanced through the installation of a Xerox DocuTech, a high speed publishing and finishing system. The

new system improved timeliness of service, while reducing staffing requirements. Also, plans and equipment purchases were finalized for a new copy center, largely for litigation support. Due, in part, to agency initiatives to disseminate documents through the agency's LAN and through FedWorld, printing production decreased from 71 million pages to 60 million. The OAPM successfully accomplished the transition from franked to metered mail as mandated by the U.S. Postal Service. Mail service was improved by expanding hours to process emergency mail, particularly time-sensitive litigation documents.

The agency awarded contracts and purchase orders in excess of $35 million during 1994. Plans were initiated in the development of electronic commerce (EC) designed to streamline procurement in compliance with efforts to reinvent government. OAPM is working with the Treasury Department and the Small Agency Council's Information Resource Management Committee to develop a pilot project that would provide an EC vehicle for the SEC and other small agencies. The current plan is to establish EC connectivity through the Treasury Department.

Public Reference. The Commission maintains public reference rooms in its Washington, D.C., New York, and Chicago offices. In a continuing interest to better serve the public, the procedures in the headquarters public reference room were enhanced to expedite identification, location, and retrieval of documents and microfiche. The public reference room is responsible for making copies of company filings, and Commission rules, orders, studies, reports, and speeches available to the public.

During 1994, the staff provided assistance to 42,099 visitors to the headquarters public reference room, answered 5,560 requests for documents, processed 582 requests for certifications of filings and

records, and responded to 100,812 telephone inquiries. A total of 48,368 electronic filings, received via the Commission's EDGAR system, were available for requestors. In addition, the public reference staff received and filed over 500,000 paper documents and 505,479 microfiche records to the existing library of publicly available information.

Consumer Affairs. In 1994, the agency enhanced its commitment to the protection of consumers. Initiatives to improve public awareness and to educate investors included:

- town meetings and focus groups for individual investors;
- telephone consumer surveys on mutual funds;
- publication of informational and educational brochures for investors;
- the establishment of a toll-free information line to provide callers with access to general information about the SEC;
- the dissemination of investor-related information via an electronic bulletin board; and
- the creation of a Consumer Affairs Advisory Committee through which the SEC can receive information to assist the agency to better address the needs of the investors.

The Commission received 38,702 complaints and inquiries during 1994, an increase of approximately 11 percent over the prior year. The staff also responded to 2,742 letters concerning public reference matters. Of the 38,702 complaints and inquiries, 42 percent were complaints and 58 percent were inquiries. Approximately 40 percent of the complaints received involved broker-dealers, while the remainder involved issuers, mutual funds, banks, transfer agents,

clearing agents, investment advisers, and various financial and non-financial matters.

More than 2,500 complaints were referred to the SEC operating divisions, self-regulatory organizations, or other regulatory entities for review and/or action. This represents an 80 percent increase over last year.

Endnotes

[1]*Division of Enforcement Warns of Fraud in the Sale of Unregistered Securities of Telecommunications Technology Ventures,* Press Release 94-105 (Sept. 16, 1994).

[2]*SEC v. Parkersburg Wireless Limited Liability Company,* Litigation Release No. 14085 (May 16, 1994), 56 SEC Docket 2278.

[3]*SEC v. Knoxville,* LLC, Litigation Release No. 14155 (July 12, 1994), 57 SEC Docket 441.

[4]*SEC v. Continental Wireless Cable Television, Inc.,* Litigation Release No. 14118 (June 7, 1994), 56 SEC Docket 2778.

[5]*SEC v. Comcoa Ltd.,* Litigation Release No. 14080 (May 10, 1994), 56 SEC Docket 2156.

[6]*SEC v. Transamerica Wireless Systems, Inc.,* Litigation Release No. 14218 (Sept 2, 1994), 57 SEC Docket 1601.

[7]*So-Called "Prime" Bank and Similar Financial Instruments,* Information for Investors Bulletin No. II-l-l (Oct. 1993).

[8]*Division of Enforcement Warns of Possible Prime Bank Fraud in Connection with Banka Bohemia Securities,* Press Release No. 94-14 (Mar. 11, 1994).

[9]*SEC v. John D. Lauer,* Litigation Release No. 14143 (June 30, 1994), 57 SEC Docket 111.

[10]*SEC v. Northstar Investors Trust,* Litigation Release No. 13887 (Nov. 23, 1993), 55 SEC Docket 1697.

[11]*SEC v. North Pacific Investments,* Inc., Litigation Release No.

14011 (Mar. 16, 1994), SEC Docket 893.

[12]*SEC v. Cross Financial Services, Inc.,* Litigation Release No. 14135 0une 24, 1994), 57 SEC Docket 103.

[13]*SEC v. Prime One Partners, Corp.,* Litigation Release No. 14114 (June 6, 1994), 56 SEC Docket 2772.

[14]*SEC v. European Kings Club,* Litigation Release No. 13871 (Nov. 15, 1993), 55 SEC Docket 1552.

[15]*SEC v. William E. Cooper,* Litigation Release No. 14090 (May 18, 1994), 56 SEC Docket 2283.

[16]*SEC v. American Business Securities, Inc.,* Litigation Release No. 14171 (July 25, 1994), 57 SEC Docket 727.

[17]*SEC v. Norman L, Brooks,* Litigation Release No. 14048 (Apr. 11, 1994), 56 SEC Docket 1366.

[18]*In the Matter of Comptronix Corporation,* Exchange Act Release No. 33829 (Mar. 29, 1994), 56 SEC Docket 1038.

[19]*SEC v. Stanley Lepelstat,* Litigation Release No. 14222 (Sept. 8, 1994), 57 SEC Docket 1604.

[20]*In the Matter of Accuhealth, Inc.,* Exchange Act Release No. 34646 (Sept. 8, 1994), 57 SEC Docket 1502.

[21]*In the Matter of* William *Makadok, CPA,* Exchange Act Release No. 34645 (Sept. 8, 1994), 57 SEC Docket 1551.

[22]*SEC v. PNF Industries,* Inc., Litigation Release No. 14257 (Sept. 27, 1994), 57 SEC Docket 2112.

[23]*In the Matter of Martin Halpern, CPA,* Exchange Act Release No. 34727 (Sept. 27, 1994), 57 SEC Docket 1948.

[24]*SEC v. C. W. Earl Johnson,* Litigation Release No. 13943 (Jan. 25, 1994), 55 SEC Docket 3077.

[25]*SEC v. Jere L Bradwell,* Litigation Release No. 13933 (Jan. 13, 1994), 56 SEC Docket 2790.

[26]*In the Matter of Stuart G. Lasher, CPA,* Exchange Act Release No. 33465 (Jan, 13, 1994), 55 SEC Docket 2716.

[27]*SEC v. Transmark USA, Inc.,* Litigation Release No. 14124 (June 13, 1994), 56 SEC Docket 2916.

[28]*In the Matter of Donald F. Withers, CPA,* Exchange Act Release No. 34537 (Aug. 17, 1994), 57 SEC Docket 1101.

[29]*In the Matter of Harry D. Sweeney, CPA,* Exchange Act Release No. 33930 (Apr. 20, 1994), 56 SEC Docket 1522.

[30]*In the Matter of Edward Jan Smith, CPA,* Exchange Act Release No. 33963 (Apr. 26, 1994), 56 SEC Docket 1696.

[31]*SEC v. Richard F. Adler,* Litigation Release No. 14198 (Aug. 18, 1994), 57 SEC Docket 1195.

[32]*SEC v. Eugene Dines,* Litigation Release No. 13900 (Dec. 10, 1993), 55 SEC Docket 1972.

[33]*SEC v. Jonathan Mayhew,* Litigation Release No. 14189 (Aug. 9, 1994) 57 SEC Docket 1061.

[34]*SEC v. Julia Peck Mobley,* Litigation Release No. 14123 (June 13, 1994), 56 SEC Docket 2915.

[35]*SEC v. U.S. Environmental, Inc.,* Litigation Release No. 14233 (Sept 13, 1994), 57 SEC Docket 1758.

[36]*In the Matter of* J. *Peek Garlington,* Jr., Exchange Act Release No, 34656 (Sept. 13, 1994), 57 SEC Docket 1629.

[37]*SEC v. Gary S. Wlliky,* Litigation Release No. 14280 (Sept. 30, 1994), 57 SEC Docket 2272.

[38]*SEC v. Robert L. Skull,* Litigation Release No. 14213 (Aug, 31, 1994), 57 SEC Docket 1447.

[39]*SEC v. Curtis Ivey,* Litigation Release No. 14042 (Apr. 5, 1994), 56 SEC Docket 1262.

[40]*In the Matter of Stanley Berk,* Exchange Act Release No. 33932 (Apr. 20, 1994), 56 SEC Docket 1524.

[41]*In the Matter of The Chicago Corporation,* Exchange Act Release No. 33777 (Mar. 17, 1994), 56 SEC Docket 818.

[42]*In the Matter of Cantor Fitzgerald & Co.* Exchange Act Release No. 33776 (Mar. 17, 1994), 56 SEC Docket 812.

[43]fn *the Matter of Goldman, Sachs & Co.,* Exchange Act Release No. 33576 (Feb. 3, 1994), 55 SEC Docket 3208.

[44]*In the Matter of Merrill Lynch, Pierce, Fenner & Smith, Inc.,* Exchange Act Release No. 33367 (Dec. 22, 1993), 55 SEC Docket 2281.

[45]*In the Matter of George F.M. Lee,* Exchange Act Release No. 34658 (Sept. 13, 1994), 57 SEC Docket 1534.

[46]*In the Matter of Colonial Management Associates, Inc.,* Investment Advisers Act Release No. 1419 0une 15, 1994), 56 SEC Docket 2850.

[47]*SEC v. Thomas Frank Handyk,* Litigation Release No. 14113 0une *6, 199*4), 56 SEC Docket 2771.

[48]*In the Matter of James M, Coyne, Jr.,* Exchange Act Release No. 34587 (Aug. 24, 1994), 57 SEC Docket 1234.

[49]*In the Matter of Synovus Securities, Inc.,* Investment Advisers Act Release No. 1423 (July 5, 1994), 57 SEC Docket 138.

[50]*In the Matter of Richard T. Taylor,* Exchange Act Release No. 34315 (July 5, 1994), 57 SEC Docket 143.

[51]*In the Matter of Strong/Corneliuson Capital Management, Inc.,* Investment Advisers Act Release No. 1425 (July 12, 1994), 57 SEC Docket 1451.

[52]*SEC v. Donna Tumminia,* Litigation Release No. 14217 (Sept *1, 199*4), 57 SEC Docket 1451.

[53]*In the Matter of Joan Conan,* Investment Advisers Act Release No. 1446 (Sept. 30, 1994), 57 SEC Docket 2239.

[54]*SEC v. Centurion Growth Fund, Inc.,* Litigation Release No. 14052 (Apr. 14, 1994), 56 SEC Docket 1370.

[55]*In the Matter of Seaboard Investment Advisers, Inc.,* Investment Advisers Act Release No. 1388 (Oct. 22, 1993), 55 SEC Docket 916.

[56]*In the Matter of Terence Patrick Mulrooney,* Investment Company Act Release No. 20615 (Oct. 13, 1994), 57 SEC Docket 2320.

[57]*In the Matter of Melvin L Hirsch,* Investment Company Act Release No. 20335 (June 3, 1994), 56 SEC Docket 2750.

[58]Exchange Act Release No. 33761 (Mar. 15, 1994), 59 FR13275 (Mar. 21, 1994). At the same time these rule amendments were proposed, the Commission authorized the Division of Market Regulation to issue a no-action letter that authorizes broker-dealers to use the theoretical pricing model to determine haircuts. Letter from Brandon Becker, Director, Division of Market Regulation to Mary L. Bender, The Chicago Board Options Exchange and Timothy Hinkas, The Options Clearing Corporation (Mar. 15, 1994).

[59]Group of Thirty, *Derivatives: Practices and Principles* (July 1993).

[60]Statement of the Securities and Exchange Commission, Commodity Futures Trading Commission and the Securities and Investments Board (Mar. 15, 1994).

[61]Technical Committee of IOSCO, *Operational and Financial Risk Management Control Mechanisms for Over-the-Counter Derivatives Activities of Regulated Securities Firms* (July 1994).

[62]Exchange Act Release No. 34140 0une 1, 1994), 59 FR 29393 June 7, 1994).

[63]Exchange Act Release No. 34541 (Aug. 17, 1994), 59 FR 43603 (Aug. 24, 1994).

[64]Exchange Act Release No. 33137 (Nov. 3, 1993), 58 FR 60324 (Nov. 15, 1993).

[65]Letter regarding Distributions of Certain French Securities, Exchange Act Release No. 34176 (June 7, 1994), 59 FR 31274 (June 17, 1994.)

[66]Exchange Act Release No. 33862 (Apr. 4, 1994), 59 FR 17125 (Apr. 11, 1994).

[67]Bear, Stearns & Co. Inc. (pub. avail. Aug. 29, 1994).

[68]Bear Stearns and Bear Stearns Securities Corp. (pub. avail. July 7, 1994).

[69]Shearson Lehman Brothers Inc. (pub. avail. Mar. 25, 1993); Prudential Securities Inc. (pub. avail. Oct. 11, 1994).

[70]Chubb Securities Corp. (pub. avail. Nov. 24, 1993).

[71]Exchange Act Release No. 33608 (Feb. 17, 1994), 59 FR 7917 (Feb. 22, 1994).

[72]Exchange Act Release No. 33924 (Apr. 19, 1994), 59 FR 21681 (Apr. 26, 1994).

[73]Exchange Act Release No. 33743 (Mar. *9, 199*4), 59 FR12767 (Mar. 17, 1994).

[74]Exchange Act Release No. 33761 (Mar. 15, 1994), 59 FR 13275 (Mar. 21, 1994).

[75]Exchange Act Release No. 33702 (Mar. 2, 1994), 59 FR 10984 (Mar. 9, 1994).

[76]Exchange Act Release No. 34616 (Aug. 31, 1994), 59 FR 46314 (Sept. 7, 1994).

[77]Exchange Act Release Nos. 27445 and 29185 (Nov. 16,1989 and May 9, 1991), 54 FR 48703 and 56 FR 22490 (Nov. 24,1989 and May 15, 1991).

[78]Exchange Act Release No. 35124 (Feb. 20, 1994), 59 FR 66702 (Dec. 28, 1994).

[79]The Division of Market Regulation and the Division of Enforcement, Securities and Exchange Commission, *The Large Firm Project: A Review of Hiring, Retention and Supervisory Practices* (May 1994).

[80]National Association of Securities Dealers, Inc., New York Stock Exchange, Inc., North American Securities Administrators Association, Inc., U.S. Securities and Exchange Commission, *Staff Report on the Joint Regulatory Penny Stock Examination Sweep* (June 1994).

[81]17 C.F.R. S240.17M (1993).

[82]Exchange Act Release No. 34493 (Aug. 5, 1994), 59 FR 41531 (Aug. 12, 1994).

[83]Exchange Act Release No. 34078 (May 18, 1994), 59 FR 27082 (May 25, 1994).

[84]Exchange Act Release Nos. 33992 (May 2, 1994), 59 FR 23907 (May 9, 1994) (NYSE); 33993 (May 2, 1994), 59 FR 23902 (May 9, 1994) (AMEX); 33991 (May 2, 1994), 59 FR 23904 (May 9, 1994) (BSE, CHX, PSE, and PHLX).

[85]Exchange Act Release No. 34151 (June 3, 1994), 59 FR 29843 (June 9, 1994).

[86]Exchange Act Release No. 34277 (June 29, 1994), 59 FR 34885 (July 7, 1994).

[87]Exchange Act Release No. 34279 (June 29, 1994), 59 FR 34883 *(July* 7, 1994).

[88]Exchange Act Release No. 34280 (June 29, 1994), 59 FR 34880 (July 7, 1994).

[89]Exchange Act Release No. 34533 (Aug. 15, 1994), 59 FR 43147 (Aug. 22, 1994).

[90]Exchange Act Release No. 33734 (Mar, 8, 1994), 59 FR 11815 (Mar. 14, 1994).

[91]Exchange Act Release No. 33348 (Dec. 15, 1993), 58 FR 68183 (Dec. 23, 1993).

[92]Exchange Act Release No. 33233 (Nov. 22, 1993), 58 FR 63195 (Nov. 30, 1993).

[93]Letter from James C Yong, Vice President and Assistant Secretary, ICC, to Jonathan G. Katz, Secretary, Commission (Mar. 24, 1994).

[94]Exchange Act Release Nos. 34166 (June 6, 1994), 59 FR 30066 and 34199 (June 10, 1994), 59 FR 31660 (June 20, 1994).

[95]Exchange Act Release No. 33984 (May 2, 1994), 59 FR 24491 (May 11, 1994).

[96]Exchange Act Release No. 34512 (Aug. 10, 1994), 59 FR 42320 (Aug. 17, 1994).

[97]Exchange Act Release No. 33868 (Apr. 7, 1994), 59 FR 17621 (Apr. 13, 1994).

[98]Exchange Act Release No. 33869 (Apr. 7, 1994), 59 FR 17632 (Apr. 13, 1994).

[99]*Employment Discrimination: How Registered Representatives Fare in Discrimination Disputes* (GAO/HEHS 94-17, Mar. 1994).

[100]Letter from Deborah Masucci, Vice-President, Arbitration, NASD, to Brandon Becker, Director, Division of Market Regulation, SEC, dated September 30, 1994.

[101]Exchange Act Release No. 33939 (Apr. 20, 1994), 59 FR 22032 (Apr. 28, 1994).

[102]Exchange Act Release No. 34348 (July 11, 1994), 59 FR 36242 (July 15, 1994).

[103]Letter to Registrants from Carolyn B. Lewis, Assistant Director, Division of Investment Management (Feb. 25, 1994).

[104]Memorandum from Division of Investment Management to Chairman Levitt regarding Mutual Funds and Derivative Instruments (Sept. 26, 1994).

[105]*See* Testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission, Concerning Issues Affecting the Mutual Fund Industry, before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce, U.S. House of Representatives (Sept. 27, 1994).

[106]Investment Company Act Release No. 19959 (Dec. 17, 1993), 55 SEC Docket 2220.

[107]Investment Company Act Release No. 19955 (Dec. 15, 1993), 55 SEC Docket 2027.

[108]Investment Company Act Release No. 20313 (May 24, 1994), 56 SEC Docket 2480.

[109]Securities Act Release No. 7084 (Aug. 17, 1994), 57 SEC Docket 1084; Investment Company Act Release No. 20487 (Aug. 17, 1994), 57 SEC Docket 1084.

[110]Investment Advisers Act Release No. 1401 (Jan. 13, 1994), 55 SEC Docket 2760 (proposal); Investment Adviser Act Release No. 1411 (April 19, 1994), 56 SEC Docket 1605 (adoption).

[111]Investment Advisers Act Release No. 1406 (Mar. 16, 1994), 56 SEC Docket 858.

[112]Investment Company Act Release No. 20486 (Aug. 17, 1994), 55 SEC Docket 1075.

[113]Investment Company Act Release No. 19957 (Dec. 16, 1993), 55 SEC Docket 2045 (proposal); Investment Company Act Release No. 20614 (Oct. 13, 1994), 57 SEC Docket 2305 (adoption).

[114]Investment Company Act Release No. 20472 (Aug. 11, 1994), 57 SEC Docket 882.

[115]*E.g.*, Keynote Series Account (File No. 33-19836); Diversified Investors Variable Funds (File No. 33-73734).

[116]Investment Company Act Release Nos. 18778 (June 12, 1992), 51 SEC Docket 1128 (Notice and Temporary Order) and 20338 (June 7, 1994), 56 SEC Docket 2408 (Permanent Order).

[117]Investment Company Act Release Nos. 19967 (Dec. 20, 1993), 55

SEC Docket 2083 (Notice and Temporary Order) and 20337 (June 7, 1994), 56 SEC Docket 2407 (Permanent Order).

[118]investment Company Act Release Nos. 20236 (April 20, 1994), 56 SEC Docket 1461 (Notice) and 20305 (May 17, 1994), 56 SEC Docket 1968 (Order).

[119]Investment Company Act Release Nos. 20503 (Aug. 25, 1994), 57 SEC Docket 1227 (Notice) and 20564 (Sept. 20, 1994), 57 SEC Docket 1644 (Order).

[120]Brown & Wood (pub. avail. Feb. 24, 1994).

[121]Merrill Lynch Money Markets Inc. (pub. avail. Jan. 14, 1994).

[122]North American Security Trust (pub. avail. Aug. 5, 1994).

[123]Alexander Hamilton Funds (pub. avail. July 20, 1994).

[124]Kleinwort Benson Investment Management Limited (pub. avail. Dec. 5, 1993).

[125]Murray Johnstone Holdings Limited (pub, avail. Oct. 7, 1994).

[126]*The Equitable Life Assurance Society of the United States,* Investment Company Act Release Nos. 20568 (Sept. 22, 1994) (Notice) and 20637 (Oct. 19, 1994) (Order).

[127]*National Home Life Assurance Company, et al,* Investment Company Act Release Nos. 20357 (June 14, 1994) (Notice) and 20402 (July 13, 1994) (Order); *The Variable Annuity Life Insurance Company, et al,* Investment Company Act Release Nos. 20345 (June 8, 1994) (Notice) and 20387 (July *7, 199*4) (Order).

[128]WM Life Insurance Company and Empire Life Insurance Company (pub. avail. Jan. 19, 1994).

[129]Securities Act Release No, 7049 (Mar. 9, 1994), 56 SEC Docket

596.

[130]Exchange Act Release No. 34961 (Nov. 10, 1994), 57 SEC Docket 2993.

[131]Exchange Act Release No. 33742 (Mar. 9, 1994), 56 SEC Docket 648.

[132]Securities Act Release No. 7053 (Apr. 19, 1994), 56 SEC Docket 1414.

[133]Securities Act Release No. 7053 (Apr. 19, 1994), 56 SEC Docket 1414.

[134]Securities Act Release No. 7026 (Nov. 3, 1993), 55 SEC Docket 969.

[135]Securities Act Release No. 7054 (Apr. 19, 1994), 56 SEC Docket 1428.

[136]Securities Act Release No. 7056 (Apr. 19, 1994), 56 SEC Docket 1439.

[137]Securities Act Release No. 7055 (Apr. 19, 1994), 56 SEC Docket 1432.

[138]Securities Act Release No. 7025 (Nov. 3, 1993), 55 SEC Docket 964.

[139]Securities Act Release No. 7053 (Apr, 19, 1994), 56 SEC Docket 1414.

[140]Securities Act Release No. 7101 (Oct. 18, 1994), 57 SEC Docket 2292.

[141]Exchange Act Release No. 34922 (Nov. 1, 1994), 57 SEC Docket 2800.

[142]Securities Act Release No. 7086 (Aug. 31, 1994), 57 SEC Docket 1320.

[143]Exchange Act Release No. 34514 (Aug. 10, 1994), 57 SEC Docket 932.

[144]Exchange Act Release No. 34513 (Aug. 10, 1994), 57 SEC Docket 931.

[145]Exchange Act Release No. 34681 (Sept. 16, 1994), 57 SEC Docket 1780.

[146]Securities Act Release No. 7113 (Sept 1, 1994), 57 SEC Docket 1333.

[147]Exchange Act Release No. 33768 (Mar. 16, 1994), 56 SEC Docket 807.

[148]Securities Act Release No. 7072 (July 8, 1994), 57 SEC Docket 239.

[149]Securities Act Release No. 7073 (July 8, 1994), 57 SEC Docket 243.

[150]Securities Act Release No. 7074 (July 8, 1994), 57 SEC Docket 245.

[151]Staff Accounting Bulletin No. 93 (Nov. 4, 1993), 55 SEC Docket 1110.

[152]Statement of Financial Accounting Standards No. 119, "Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments" (Oct. 1994).

[153]Statement of Financial Accounting Standards No. 118, "Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures" (Oct. 1994).

[154]Proposed Statement of Financial Accounting Standards, "Accounting for Stock-based Compensation" 0une 30, 1993).

[155]Letters dated January 10, 1994 from Arthur Levitt, Chairman, U.S. Securities and Exchange Commission, addressed to Senators Boren, Daschle, Durenburger, Levin, and Simpson.

[156]140 Cong. Rec. S5032 (daily ed. May 3, 1994).

[157]140 Cong. Rec. S5039 (daily ed. May 3, 1994).

[158]S. 2525,103d Cong., 2d Sess. (1994).

[159]S. 1976, 103d Cong., 2d Sess. (1994), and H.R. 417, 103d Cong., 1st Sess. (1993).

[160]Testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission, Concerning Derivative Financial Instruments, Before the Subcommittee on Telecommunications and Finance of the House Committee on Energy and Commerce (May 25, 1994).

[161]*Id.*

[162]EITF Issue 94-3, Accounting for Restructuring Charges.

[163]See *In the Public Interest — A Special Report by the Public Oversight Board* (Mar. 5, 1993) and *Strengthening the Professionalism of the Independent Auditor — Report to the Public Oversight Board from the Advisory Panel on Auditor Independence* (Sept. 13, 1994).

[164]Statement of Position 93-7, "Reporting on Advertising Costs" (Dec. 29, 1993).

[165]Statement of Position 93-6, "Employers' Accounting for Employee Stock Ownership Plans" (Nov. 22, 1993).

[166]Proposed Audit and Accounting Guide, "Audits of Brokers and

Dealers in Securities" (Aug. 16, 1994).

[167]Proposed Statement of Position, "Disclosure of Certain Significant Risks and Uncertainties and Financial Flexibility" (Mar. 31, 1993).

[168]Draft Statement of Principles, Earnings Per Share (Oct. 1993).

[169]Exposure Draft E48, Financial Instruments (Jan. 1994).

[170]Draft Statement of Principles, Intangible Assets (Jan. 1994).

[171]Draft Statement of Principles, Reporting Financial Information by Segment (Sept. 1994).

[172]Exposure Draft E49, Income Taxes (Oct. 1994).

[173]Release No. 33-7054 (Apr. 19, 1994).

[174]Release No. 33-7056 (Apr. 19, 1994).

[175]114 S.Ct. 1439(1994)

[176]114 S.Ct. 1215 (1994) (granting *certiorari* in *Alloyd Co. v. Gustafson,* No. 92-2514, 1993 WL 616681 (7th Cir. June 11, 1993)).

[177]16 F.3d 520 (2d Cir. ,), *petition for cert, filed,* 63 U.S.L.W. 3325 (U.S. Oct. 7, 1994) (No. 94-645).

[178]111 S.Ct. 2773(1991).

[179]*Cooperativa de Ahorro y Credito Aguada v. Kidder, Peabody & Co.,* 993 F.2d 269 (1st Cir. 1993), *petition for cert, filed, 62* U.S.L.W. 3299 (U.S. Oct. 12, 1993) (No. 93-564); *Axel Johnson, Inc. v. Arthur Andersen & Co., 6* F,3d 78 (2d Cir. 1993); *Cooke v. Manufactured Homes, Inc.,* 998 F.2d 1256 (4th Cir. 1993); *Berning v. A,G. Edwards & Sons, Inc.,* 990 F.2d 272 (7th Cir. 1993); *Gray v. First Winthrop Corp.,* 989 F.2d 1564 (9th Cir. 1993); *Anixter v. Home-Stake Production Co.,* 977 F.2d 1533 (10th Cir. 1992), *cert, denied sub*

nom. Cross v. Thorner, 113 S.Ct. 1842 (1993); *Henderson v. Scientific-Atlanta, Inc.,* 971 F.2d 1567 (11th Cir. 1992), *cert, denied,* 114 S. Ct. 95 (1993).

[180]*Morgan Stanley & Co. v. Pacific Mutual Life Insurance Co.,* 114 S.Ct 1827 (1994) (affirming *Pacific Mutual Life Insurance Co. v. First Republic Bank Corp.,* 997 F.2d 39 (5th dr. 1993)).

[181]*Plaut v. Spendthrift Farm, Inc.,* 1 F.3d 1487 (6th Cir. 1993), *cert, granted,* 114 S.Ct 2161 (U.S. 1994).

[182]114 S.Ct. 1215 (1994) (granting *certiorari* in *Alloyd Co. v. Gustafson,* No. 92-2514, 1993 WL 616681 (7th Cir. June 11, 1993)).

[183]27F.3d 808 (2d Cir.), *cert, denied,* 63 U.S.L.W. 3181 (U.S. Oct. 31, 1994) (No. 94-433).

[184]973 F.2d 51 (2d Cir, 1992), *cert, denied,* 113 S.Ct, 2992 (1993).

[185]19 F.3d 66 (2d Cir.), *cert, denied,* 115 S.Ct. 54 (1994).

[186]16 F.3d 520 (2d Cir.), *petition far cert, filed,* 63 U.S.L.W. 3325 (U.S. Oct. 7, 1994) (No. 94-645).

[187]29 F.3d 689 (D.C. Cir. 1994).

[188]37 F.3d 30 (2d Cir. 1994).

[189]18 F.3d 1281 (5th Cir.), *cert, denied,* 63 U.S.L.W. 3290 (U.S. Oct. 11, 1994) (No. 94-105).

[190]31 F.3d 1056 (11th Cir. 1994).

[191]*Libra Investments v. SEC,* 94-832A (E.D. Va.);*Howe v.* SEC 93 Civ. 5573 (LLS) (S.D.N.Y.); *Verdiramo v.* SEC, 94 Civ. 44 (D.N.J.), *Johnson v. SEC,* M18304 (S.D.N.Y.); *Badger v. SEC,* 93-C-1149G (D. Utah); *Grundman v. SEC,* 393-MC-374 (D. Conn.); *Grundman v. SEC,* 393-MC-372 (D. Conn.); *Bernard &>* Co. *v. SEC,* H-94-060

(S.D. Tex.); *Fenster v. SEC,* 93-2-2106 (D. Colo.); *Diamond Entertainment v. SEC,* 94-CV-79B (D. Utah).

[192]*La Barca v. SEC,* 94-1917 (CBA) (E.D.N.Y.); Boss *v. SEC,* 94-C-22J (D. Utah); *Weeks v. SEC,* 94-C-56S (D. Utah).

[193]Purcell v. SEC, CV94-3562-1H (CD. Cal.).

[194]*Greer v. SEC,* M18-304 (S.D.N.Y.); *Bradley v. SEC,* M-28 (S.D.N.Y.); *Beatty v. SEC,* 94-NC-015T (D. Utah).

[195]17 CFR. 201.2(d).

[196]*SEC v. David L. Kagel, et al*$_t$ Civil Action No. 93-0855-ER (CD. Cal).

[197]*Sheckovsky and Aldrich v. SEC, 2*3 F.3d 452 (D.C. Cir. 1994).

[198]*Danna and Dentinger v. SEC,* 1994 WL 315877 (N.D. Cal. Feb. 8, 1994).

[199]*SEC v. Kaufman,* 835 F. Supp. 157 (S.D.N.Y. 1993), appeal pending, *SEC v. Price Waterhouse,* No. 94-6045 (2d Cir.); *SEC v. Morelli,* No. 3874 (S.D.N.Y.); *SEC v. Littler,* No. 88-C-619 (D. Utah); *SEC v. Grosby,* No. 1P921411 (S.D. Ind.); *SEC v. Atchison,* No. 91-6785 SVW (C.D. Cal. August 29, 1994).

[200]*In re Salomon Brothers Treasury Litigation, 9* F.3d 230 (2d Cir. 1993).

[201]*Durkin v. U.S. District Court for the Southern District of California,* No. 94-70479 (9th Cir.) (filed Oct. 28, 1994).

[202]*Frank J. Custable, Jr., et al,* 51 S.E.C. 855 (1993).

[203]*Vanden J. Catli,* 51 S.E.C. 1057 (1994).

[204]*Timoleon Nicholaou,* 51 S.E.C. 1215 (1994).

[205]*Partnership Exchange Securities Company, et al,* 51 S.E.C. 1198 (1994).

[206]CSW *Credit, Inc. and Central and Southwest Corporation,* 51 S.E.C. 984 (1994).

[207]Exchange Act Release No. 33163 (Nov. 5, 1993), 55 SEC Docket 1128.

[208]The SEC's total funding request was $306 million, including $8.6 million if the investment ad viser legislation was enacted. The investment adviser legislation, however, was not enacted. The $297,4 million includes $74.9 million in appropriations, $30.5 million in a carry-over of unobligated prior year budget authority, and $192 million in estimated current year offsetting fee collections.

[209]*In re Rose's Stores, Inc.,* Case No. 93-01365-5-ATS (Bankr. E.D. N.C.) and *In re Merry-Go-Round Enterprises, Inc.,* Case No. 94-501615D (Bankr, D. Md.).

[210]*In re Enmrodyne Industries, et al.ƒ* Case Nos. 93 B 310,93 B 312 through Nos. 93 B 316, 93 B 318, 93 B 319 (Bankr. N.D. III).

[211]*In re MEI Industries, Inc.,* Case Nos. 4-93-3170 through 4-93-3178 (Bankr. D. Minn.).

[212]*In re National Convenience Stores, Inc.,* Case No. 91-49816-H2-11 (Bankr. S.D, Tex.). *See* 59th Annual Report at 72 (1993).

[213]*See In re National Convenience Stores, Inc.,* B.R. (Bankr. S.D. Tex.)

[214]*In re MEI Industries, Inc.,* Case Nos. 4-93-3170 through 4-93-3178 (Bankr. D. Minn.).

[215]*In re Phar-Mor, Inc.,* Case Nos. 92-41599 through 92-11614 (Bank. N.D. Ohio).

[216]See, *e.g., In re Master Mortgage Investment Fund, Inc.,* 59th Annual Report at 72 (1992) (objection to confirmation of reorganization plan); *In re Prime Motor Inn, In re Servico Corp., In re The Washington Corp.* and *In re Lamas Financial Corp.,* 58th Annual report at 77 (1992) (objection to confirmation of reorganization plan); *In re Amdura Corp.* and *In re Banyan Corp.,* 57th Annual Report at 82 (1991) (objection to confirmation of reorganization plan);*In re Southmark Corp.* and *In re SIS Corp.,* 56th Annual Report at 91 (1990) (objection to confirmation of reorganization plan); *In re Custom Laboratories, Inc.,* 53rd Annual Report at 74 (1987) (objection to disclosure statement); *In re Energy Exchange Corp. and Vulcan Energy Corp.* and *In re Storage Technology Corp.,* 53rd Annual Report at 74-75 (1987) (objection to confirmation of reorganization plan).

[217]*In re Amdura Corporation, Inc.,* No. 91 N 1521 (D. Colo.). *See* 57th Annual Report at 81 (1991).

[218]*See In re American Reserve Corp.,* 840 F.2d 487 (7th Cir. 1988); *In re The Charter Co., 876* R2d 866 (11th Cir. 1989), *petition for cert, dismissed,* 110 S.Ct 3232 (1990); and *Reid v. White Motor Corp.,* 886 F.2d 1462 (6th Cir. 1989), *cert, denied,* 110 S.Ct 1809 (1990). *See also In re Chateaugay Corp.,* 104 B.R. 626 (S.D.N.Y. 1989); and *In re Zenith Laboratories, Inc.,* 104 B.R. 659 (D.N.J. 1989). *Cf. In re Mortgage & Realty Trust,* 125 B.R. 575 (Bankr. C.D. Cal. 1991).

[219]*In re First City Bancorporation of Texas,* Case No. 392-39474-HCA-l 1 (Bankr. S.D. Tex.).

[220]*In re NVF Company,* Case No. 93-1020(PJW) (Bankr. D. Del.).

[221]See Litigation Release No. 13891, Dec *2, 199*3.

[222]*In re Enviropact, Inc.,* Case No. 93-10038-BKC-AJC (Bankr. S.D. Fla.), *In re Penn Pacific Corporation, Case No. 94-00230-C (Bankr. N.D. Okla.), In re Phar-Mor, Inc., Case No. 92-41599 through 92-41614 (Bankr. N.D. Ohio) and In re Interlogic Trace, Inc., Case No.*

94-521272-C (Bankr. W.D. Tex.)

[223]*In re Penn Pacific Corporation,* Case No. 94-Q0230-C (Bankr. N.D. Okla.) and *In re Phar-Mor, Inc.,* Case No. 92-41599 through 92-41614 (Bankr. N.D. Ohio).

[224]*In re Enviropact, Inc.,* Case No. 93-10038-BKC-AJC (Bankr. S.D. Fla.).