

1993 Annual Report

United States
Securities and Exchange Commission

SECURITIES AND EXCHANGE COMMISSION

Mission

Under the Securities Exchange Act of 1934, Congress created the Securities and Exchange Commission (SEC). The SEC is an independent/ nonpartisan, quasi-judicial regulatory agency. The agency's mission is to administer the federal securities laws that seek to provide protection for investors. The purposes of these laws are to ensure that the securities markets are fair and honest and to provide the means to enforce the securities laws through sanctions where necessary.

Under the direction of the Chairman and Commissioners, the staff ensures that publicly held entities, broker-dealers in securities/ investment companies and advisers, and other participants in the securities markets comply with federal securities laws. These laws were designed to facilitate informed investment analyses and decisions by the investing public, primarily by ensuring adequate disclosure of material information.

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

The Honorable Albert Gore, Jr.
President of the Senate
Washington, D.C. 20510

The Honorable Thomas S. Foley
Speaker of the House
Washington, D.C. 20515

I am pleased to submit the annual report of the Securities and Exchange Commission for fiscal year 1993. 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 II(b) of the Inter-American Development Bank Act; and Section II(b) of the Asian Development Act.

Sincerely,

Arthur Levitt

COMMISSION MEMBERS AND PRINCIPAL STAFF

OFFICERS

(As of November 4, 1493)

Commissioners

Arthur Levitt, *Chairman*

Mary L. Schapiro

Richard Y. Roberts

J. Carter Beese, Jr.

Principal Staff Officers

Colleen P. Mahoney, Executive Assistant

Linda C. Quinn, Director, Division of Corporation Finance

Elisse B. Walter, Deputy Director

William E. Morley, Senior Associate Director

Abigail Arms, Associate Director

Teresa E. Iannaconi, Associate Director

Richard M. Kosnik, Associate Director

Howard F. Morin, Associate Director

Mauri L. Osheroff, Associate Director

Robert A. Bayless, Chief Accountant

David A. Sirignano, Senior Legal Advisor

William R. McLucas, Director, Division of Enforcement

Joseph I. Goldstein, Associate Director

Bruce A. Hiler, Associate Director

Thomas C. Newkirk, Associate Director

Vacant, 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

Thomas S. Harman, Chief Counsel

Brandon Becker, Director, Division of Market Regulation

Robert L.D. Colby, Deputy Director

Larry E. Bergmann, Associate Director

Mark D. Fitterman, Associate Director

Jonathan Kallman, Associate Director

Howard Kramer, Associate Director

Michael A. Macchiaroli, Associate Director

Catherine McGuire, Chief Counsel

Mary Ann Gadziala, Senior Advisor

Vacant, Special Assistant to the Director

Simon M. Lome, General Counsel, Office of the 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

Warren E. Blair, 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

Faith D. Ruderfer, Director, Office of Equal Employment Opportunity

James M. McConnell, Executive Director, Office of the Executive Director

Vacant, Deputy Executive Director

Fernando L. Alegria, Jr., Associate Executive Director

Wilson A. Butler, Jr., Associate Executive Director

Lawrence H. Haynes, Associate Executive Director

John J. Lane, 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 Levitt, 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 is *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, 62, graduated Phi Beta Kappa from Williams College in 1952 before serving two years in the Air Force. Married since 1955 to the former Marilyn Blauner, Mr. Levitt has two children, Arthur III and Lauri.

Mary L. Schapiro

Mary L. Schapiro was sworn in as the 67th member of the Securities and Exchange Commission on December 19, 1989 by the Honorable Sandra Day O'Connor, Associate Justice of the United States Supreme Court. Ms. Schapiro was nominated to the Commission on November 8, 1989 by President George Bush and confirmed by the United States Senate on November 18, 1989. Her term expires in June 1994. Ms. Schapiro had previously been appointed by President Ronald Reagan for a one year term. She was designated Acting Chairman of the SEC by President Clinton in May 1993 and served in that capacity until the confirmation of Chairman Arthur Levitt.

Ms. Schapiro was named chairman of the SEC Task Force on Administrative Process in 1990, with responsibility for comprehensive review and revision of the agency's rules for administrative proceedings. The Task Force Report was published in March 1993. Ms. Schapiro also serves on the Developing Markets Committee of the International Organization of Securities Commissions.

Before being appointed to the Commission, Ms. Schapiro was General Counsel and Senior Vice President for the Futures Industry Association. While at the FIA her work included regulatory, tax and international issues, including extensive liaison with foreign government officials and analysis of state and Federal legislation.

Ms. Schapiro came to the FIA from the Commodity Futures Trading Commission, where she spent four years. She joined the CFTC in 1980 as a Trial Attorney in the Manipulation and Trade Practice Investigations Unit of the Division of Enforcement, and from 1981 to 1984 served as Counsel and Executive Assistant to the Chairman of the agency. In the latter position, Ms. Schapiro advised

on all regulatory and adjudicatory matters pending before the Commission and on legislation. She also represented the Chairman with Federal and state officials, Congress, and the futures industry, in addition to other duties.

A 1977 honors graduate of Franklin and Marshall College (Lancaster, Pennsylvania), Ms. Schapiro earned a Juris Doctor degree (with honors) from The National Law Center of George Washington University in 1980.

Richard Roberts

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 & Odom. 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.

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. Mr. Beese's term expires in June of 1996.

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 readying the securities markets and securities regulators for the challenges of the next century.

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.

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 is a committee member of CHILDHELP USA, and serves on the boards of Preservation Maryland, the Palm Beach Maritime Museum and Ocean Engineering Institute, and the Advisory Board of National Rehabilitation Hospital. Mr. Beese resides in Baltimore, Maryland with his wife, Natalie, and three children, Courtney, John Carter and Wilson.

SEC REGIONAL AND DISTRICT OFFICES

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ENFORCEMENT

The Commission's enforcement program is designed to protect investors and foster investor 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 a 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 1993 Results

In 1993, 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 \$225 million. This included disgorgement orders in insider trading cases requiring the payment of approximately \$12 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) totaled over \$29 million.

In Commission-related cases, criminal authorities obtained 67 criminal indictments or informations and 58 convictions during 1993. The Commission granted access to its files to domestic and foreign prosecutorial authorities in 205 instances.

[table omitted]

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 Commission 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. Both types of investigations generally are conducted on a confidential, nonpublic 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 will be 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.

In addition to civil injunctive actions, the Commission has the authority to institute several types of administrative proceedings. 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 authorizes the Commission to impose penalties and order disgorgement.

The Remedies Act further authorizes 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 program areas in 1993. Defendants or

respondents who consented to settlement 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 1993.

Violations Relating to the Government Securities Markets

During the year, the Commission continued its focus on violations affecting the conduct and fairness of the market for government securities.

The Commission instituted administrative proceedings against three members of the senior management of Salomon Brothers Inc., alleging that they had become aware that Paul W. Mozer, head of the firm's government trading desk, had submitted a false bid in an auction of U.S. Treasury securities (*In the Matter of John H. Gutfreund*¹). The Commission found that the respondents, Gutfreund, Salomon's former chairman and chief executive officer, Thomas W. Strauss/ Salomon's former president, and John W. Meriwether, Salomon's former vice chairman, failed adequately to supervise Mozer in that they took no action to investigate the matter, to discipline him, or to report the matter to the government for a period of several months, during which time Mozer committed additional violations. The respondents consented to the entry of the order by which Gutfreund was barred from holding the positions of chairman or chief executive officer with any regulated entity and was required to pay a civil penalty of \$100,000. Strauss was suspended from association with any regulated entity for a period of six months and ordered to pay a civil penalty of \$75,000. Meriwether was suspended from association for a period of three months and ordered to pay a civil penalty of \$50,000. The order also included a report of

investigation under Section 21 (a) of the Exchange Act with respect to the responsibilities of legal and compliance officers, addressing the activities of Donald M. Feuerstein, Salomon's chief legal officer.

The Gutfreund matter was related to the Commission's injunctive and administrative proceedings previously initiated against Salomon in connection with the firm's activities in the market for U.S. Treasury securities, and to *SEC v. Paul W. Mozer*,² a pending action against Mozer and Thomas F. Murphy, a former managing director of the firm, arising from the defendants' submission of false bids in Treasury auctions.

The Commission also instituted cease and desist proceedings against Daiwa Securities America, Inc., a registered broker-dealer and government-designated primary dealer in U.S. Treasury securities (*In the Matter of Daiwa Securities, Inc.*³). The Commission found that Daiwa submitted a false bid in an auction for U.S. Treasury securities in August 1989. While the tender form indicated that the bid was for Daiwa, the bid was in fact for Salomon Brothers Inc., and permitted Salomon to circumvent Treasury regulations regarding, among other things, the maximum amount that any person could purchase in the auction. The respondents, Daiwa and William M. Brachfeld, an executive vice president of the firm, consented to the entry of the cease and desist order. In addition, Daiwa consented to the entry of an order censuring the firm and ordering it to pay disgorgement and prejudgment interest of \$249,340, and Brachfeld consented to the entry of an order suspending him from association with any regulated entity for a period of three months and requiring him to pay disgorgement and prejudgment interest of \$41,918.

In the administrative proceedings *In the Matter of Donaldson, Lufkin & Jenrette Securities Corp.*,⁴ the Commission found violative conduct with respect to bids in U.S. Treasury auctions. Purportedly to avoid paperwork burdens, Donaldson Lufkin caused bids to be filed that did not accurately reflect the identity of customers seeking to purchase Treasury securities. In addition, bids were submitted in a form that permitted Donaldson Lufkin to purchase approximately \$107 million in Treasury securities for its own account in excess of permitted amounts. Donaldson Lufkin consented to the entry of a cease and desist order, and an order requiring the firm to pay disgorgement and prejudgment interest of \$100,000 and a civil money penalty of \$50,000. In a related action, *In the Matter of Carroll McEntee & McGinley Securities, Inc.*,⁵ a government-designated primary dealer through which Donaldson Lufkin had placed its bids consented to the entry of a cease and desist order and an order requiring it to pay a civil penalty of \$30,000.

The Commission alleged that Daniel O. Teyibo and his company, JFM Government Securities, Inc., defrauded broker-dealer firms in transactions in U.S. Treasury notes and bonds by engaging in free-riding, i.e., the fraudulent practice of ordering securities without the ability or intent to pay (*SEC v. Daniel O. Teyibo*⁶). In the course of soliciting numerous broker-dealer firms to engage in such transactions, Teyibo, among other things, provided phony financial statements, and falsely represented that JFM had accounts with the firms being solicited and that JFM was a registered government securities dealer. Teyibo and JFM also used more than two dozen aliases in connection with the scheme. While Teyibo and JFM accepted profits of approximately \$165,000 from successful trades, they reneged on transactions that resulted in losses, defaulting on at least \$550,000 owed to 27 broker-dealer firms. The Commission

obtained a preliminary injunction, an asset freeze and other emergency relief in this matter, which was pending at the end of the year.

Violations Relating to Financial Institutions

The Commission continued to investigate possible securities law violations by financial institutions and persons associated with them.

The Commission filed an action against Bruce Dickson, formerly the chief lending officer and president of Lincoln Savings and Loan Association and senior vice president and director of Lincoln's parent, American Continental Corporation (ACC) (*SEC v. Bruce Dickson*⁷). This case was related to the Commission's earlier action against Charles H. Keating and other persons associated with Lincoln and ACC. Dickson allegedly aided and abetted ACC in inflating its reported earnings in connection with two real estate transactions that were improperly treated as sales. Dickson consented to the entry of an injunction.

The Commission instituted cease and desist proceedings arising out of violations by Amfed Financial Corporation, a savings and loan holding company which was the parent of American Federal Savings and Loan Association of Colorado (AFS) (*In the Matter of Paul K. Clarkin*,⁸ *In the Matter of Douglas R. Gulling*⁹). Amfed's report on Form 10-K for the fiscal year ended December 31, 1987, and its reports on Forms 10-Q for the first three quarters of 1988 contained misrepresentations, and omitted material information regarding, among other things, Amfed's financial condition, the adequacy of AFS's loan and real estate loss reserves, transfers of interests in real estate improperly recorded as sales, and the status and value of

assets that had been foreclosed in substance. Four of Amfed's former officers and directors consented to the entry of cease and desist orders.

The defendant in *SEC v. Joseph Zilber*TM was a major shareholder in Federated Bank, S.S.B. Senior officers of Firststar Corp. and its subsidiary, First Wisconsin National Bank of Milwaukee, told Zilber of negotiations to acquire Federated, on the assumption that he was already aware of the discussions. Although Zilber allegedly agreed to treat the material nonpublic information as confidential, he nonetheless purchased 26,000 shares of Federated common stock while in possession of the information, Zilber consented to the entry of an injunction and an order requiring him to pay disgorgement of \$184,500 and an ITSA penalty of \$92,250.

Insider Trading

Insider trading occurs when a person in possession of material nonpublic 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 disclose any material nonpublic information or abstain from trading in the securities of their own company. Violations also may arise from the transmission or use of material nonpublic 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, against alleged violators. In addition, the ITSA

penalty provisions authorize 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 nonpublic information, or who unlawfully communicate material nonpublic information to others who trade. Civil penalties also can be imposed upon persons who control insider traders. During 1993, the Commission brought 34 cases alleging insider trading violations.

In *SEC v. C. Robert Dudgeon*,¹¹ the Commission alleged that the defendant, while employed in the corporate strategy and development department of AT&T, obtained material nonpublic information about his employer's plans to make a tender offer for NCR Corporation, and, subsequently, to pursue an acquisition of Teradata Corporation. Dudgeon earned a profit of approximately \$186,000 from his transactions in NCR call options, and over \$76,000 from his transactions in Teradata call options. Dudgeon consented to the entry of an injunction and an order by which he was ordered to disgorge \$262,314, to pay prejudgment interest of \$44,454 and to pay an ITSA penalty of \$262,314.

Insider trading in the shares of The Foxboro Company was alleged in *SEC v. Purnendu Chatterjee*.¹² The Commission alleged that Chatterjee, a former director of Foxboro, communicated material nonpublic information concerning possible tender offers for Foxboro to Sukumar Shah and Anjan Chatterjee. The defendants consented to the entry of injunctions and orders requiring them to disgorge a total of \$643,855 plus prejudgment interest of \$170,362 and to pay total ITSA penalties of \$1,287,710.

The prohibition against insider trading applies to relatives and friends of traditional insiders who trade or tip in breach of a relationship of trust and confidence. The Commission alleged in *SEC v. Jonathan J. Sheinberg*¹³ that Sheinberg overheard his father, the president of MCA Inc., talking about acquisition discussions concerning MCA. Despite his father's instructions to keep the information confidential, Sheinberg tipped the information to others who traded MCA securities. The defendants consented to the entry of injunctions, and Sheinberg consented to the entry of an order requiring him to pay an ITS A penalty of \$417,988. The three other defendants in the action consented to pay disgorgement plus prejudgment interest totaling \$491,088 and civil penalties totaling \$417,988.

The controlling person liability provisions of ITSFEA were applied for the first time in *SEC v. Lee A. Haddad*.¹⁴ In that case, it was alleged that Haddad, a former financial analyst with Morgan Stanley & Co., tipped material nonpublic information to a friend who, in turn, tipped others, including a registered representative at Jeffrey Brooks Securities. The salesman's supervisors at Jeffrey Brooks failed to inquire into his purchases prior to the announcements of two takeovers for which Haddad had provided tips, but instead made trades of their own that followed the salesman's trading patterns on transactions arising from three subsequent tips. The defendants consented to the entry of injunctions. In addition, Haddad consented to the entry of an order imposing an ITSA penalty of over \$2 million, and the salesman consented to pay disgorgement and penalties totaling over \$800,000. Jeffrey Brooks and its principals consented to the payment of a civil penalty of \$405,000 as controlling persons.

A Commission action was filed against an attorney retained by Minnetonka Corporation to provide advice regarding a possible sale of the company (*SEC v. Dean Ambrose Olds*¹⁵). While in possession of material nonpublic information, Olds purchased 6,000 shares of Minnetonka common stock, which he sold for a profit of approximately \$40,909 after Minnetonka's public announcement of its retention of an investment adviser to explore alternatives including possible sale of the company. Olds consented to the entry of an injunction and an order requiring him to pay \$40,909 as disgorgement, plus prejudgment interest, and a civil penalty of \$40,909.

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 36 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 17 cases alleging misconduct by accounting firms or their partners or employees.

The Commission filed an action against four former officers of Financial News Network Inc. (FNN), C. Stephen Bolen, Earl W. Brian, Gary A. Prince and Mitchel H. Young, alleging that they participated in a scheme to inflate FNN's reported revenues and earnings for

fiscal year 1989 and the first three quarters of 1990, and to conceal and perpetuate the fraud during FNN's 1990 audit (*SEC v. C. Stephen Bolen*¹⁶). The inflation of revenues was primarily accomplished through the manipulation of revenues from two companies related to FNN, United Press International, Inc., and Institutional Research Network, Inc. Among other things, the Commission alleged that Bolen caused FNN to pay approximately \$800,000 in unauthorized compensation to a company under his control, and sold FNN stock while in possession of material nonpublic information concerning the inflation of FNN's financial results. In addition to injunctive relief, the Commission is seeking disgorgement and ITSA penalties from Bolen and an order prohibiting him from acting as an officer or director of a public company. Brian consented to the entry of an injunction. This case was pending at the end of the year as to the remaining defendants.

The Commission's complaint in *SEC v. The Software Toolworks, Inc.*¹⁷ alleged that Software Toolworks misled investors in connection with an \$82 million secondary offering. The company made misrepresentations and omissions regarding, among other things, the deterioration in sales of software for Nintendo Entertainment Systems, the offer of \$3.9 million in price concessions to Nintendo customers, and the shipment of \$5.2 million of Nintendo product to certain customers as conditional or fictitious sales. Software Toolworks also overstated its revenues and gross profit for the quarter ended June 30, 1990 by approximately \$7 million and \$2.6 million respectively. Four corporate officers also sold a total of approximately 1.35 million shares of Software Toolworks stock while in possession of material nonpublic information concerning the misrepresentations and omissions in the company's filings. Software Toolworks and three of the individual defendants consented to the

entry of injunctions. Software Toolworks also consented to implement certain accounting procedures and measures to prevent insider trading by its employees. In addition, individual defendants consented to the entry of orders requiring them to disgorge over \$2 million, and one consented to the entry of a bar from acting as an officer or director of a publicly-held company. At the end of the year, this case was pending as to one remaining individual defendant.

In *SEC v. Larry E. Leslie*,¹⁸ the Commission alleged violations of Section 13(b)(5) of the Exchange Act, which explicitly prohibits circumvention of a public company's internal accounting controls. The defendant, a former executive of a subsidiary of the American Express Company, allegedly delayed the write-off of uncollectible Optima credit card accounts, thereby causing the overstatement of American Express's pretax income by \$36.3 million for three quarterly periods. Leslie consented to the entry of an injunction and an order requiring him to pay a civil penalty of \$10,000.

In *SEC v. Harold Sahlen*¹⁹ the Commission alleged that Harold Sahlen, the chairman and chief executive officer of Sahlen and Associates, Inc. (SAI) determined, prior to the end of each fiscal quarter from June 1985 to February 1989, the amount of fictitious revenue to report in SAI's financial statements. Other defendants implemented the scheme by, among other things, recording on SAI's books fictitious revenue attributed to work in process and accounts receivable. The scheme created the appearance that SAI was profitable when, in fact, it was consistently losing money. On the basis of its false financial statements, SAI raised millions from public and private offerings of debt and equity securities and through bank loans. Four defendants consented to the entry of injunctions. This case was pending as to Sahlen and one other defendant at the end of

the year. The Commission filed an action against an accountant based on his improper 1991 audit of College Bound, Inc. (*SEC v. Gordon K. Goldman, C.F.A.*²⁰). The Commission alleged that Goldman's deficient audit resulted in a failure to discover that the principals of College Bound had, among other things, materially inflated College Bound's income by counting the proceeds of note offerings as revenues/ and that the principals also had materially inflated College Bound's fixed assets. This case, which was related to an action against College Bound and its principals filed the previous year, was pending at the end of the year.

Securities 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.

In *SEC v. Towers Financial Corp.*,²¹ the Commission alleged an illegal, unregistered offering of over \$215 million of promissory notes issued by Towers Financial. Among other things, the principal defendants allegedly overstated Towers' collection receivables and fee income, and misrepresented the use Towers would make of the proceeds from its sales of debt to the public. The Commission further alleged that activities by the principal defendants were in violation of an injunction entered against them in 1988. The Commission's

complaint was amended to name five subsidiaries of Towers as additional defendants, and to name three other entities as relief defendants. This case was pending at the end of the year.

The Commission alleged that Premium Sales Corp. and Kenneth Thennen, the president and a director of Premium Sales, raised approximately \$515 million from investors by falsely representing that they were engaged in a form of arbitrage intended to take advantage of variations in grocery prices in different regions of the country (*SEC v. Premium Sales Corp.*²²). Among other things, it was represented that the business could make upwards of a 60 percent annualized return on investments. The complaint alleged that a material portion of the claimed transactions were shams or overstated, and that Premium Sales never made the large profits reported to investors. The court entered a temporary restraining order, and imposed an asset freeze and other emergency relief.

In *SEC v. International Quarter Phones*,²³ the Commission alleged that the defendants raised approximately \$10 million from more than 3,000 investors through the sale of unregistered securities in the form of interests in coin-operated pay telephones. The complaint alleged misrepresentations concerning, among other things, the profitability and business prospects

of International Quarter Phones, contracts with third parties/ the use or application of investor proceeds, and the financial condition and results of operations of International Quarter Phones. The court entered a temporary restraining order and an asset freeze. This case was pending at the end of the year.

The Commission alleged the fraudulent sale of over \$2 million in securities in at least three unregistered offerings of securities in *SEC v. Sam S. Brown*,²⁴ One offering raised more than \$1.2 million from investors by promising returns of \$2 million to \$10 million per \$1,000 invested, purportedly to be paid from the profits of a European financier whose fortune was variously claimed to be worth between \$1,2 trillion and \$157 trillion. This case was pending at the end of the year.

The Commission filed an action against Bosque Puerto Carrillo, a Costa Rican corporation, and two of its officers, Ralf Stefan Jaeckel and Terence James Ennis (*SEC v. Bosque Puerto Carrillo*²⁶). The complaint alleges that the defendants placed advertisements for unregistered securities issued by Bosque in in-flight magazines published by two airlines, and sold such securities to at least forty investors in the United States. Among other things, the defendants failed to disclose that Costa Rican law prohibits the export of unprocessed wood, Bosque's sole product. This case was pending at the end of the year.

Market Manipulation

The Commission is charged with ensuring the integrity of trading on the national securities exchanges and in the over-the-counter markets. The Commission staff, the exchanges, and the NASD engage in market surveillance to detect possible violations of the federal securities laws. Among other things, market surveillance looks for signs of possible stock manipulation, such as purchases or sales intended to affect the price of a security.

The Commission filed an action against Ramon D'Onofrio, eleven other individual defendants, and four corporate entities, alleging a scheme to inflate the price of the stock of Kinesis, Inc., in the over-the-counter market and to create the appearance of an active market through manipulative trading practices (*SEC v. Ramon D'Onofrio*²⁶). Among other things, the complaint alleged a series of prearranged trades through Canadian brokerage accounts designed to inflate the price of Kinesis stock from \$5.00 to \$22.00 per share. As a result of the scheme, over 100,000 shares of Kinesis stock were sold for profits to D'Onofrio and others of approximately \$1.6 million. The complaint also alleged, among other things, that D'Onofrio and others sold Kinesis stock without filing a registration statement with the Commission. This case was pending at the end of the year.

In cease and desist proceedings, the Commission alleged that Bruce B. Bowen, a registered representative associated with PaineWebber, Inc., and Thomas Q. Canon, a registered representative associated with Wilson-Davis, Inc., aided and abetted a scheme by Richard Warner, the chairman of the board of Alpnet, Inc., to manipulate the price of Alpnet stock (*In the Matter of Bruce B. Bozven*²⁷). Warner's scheme involved marking the close, specifically, the purchase of Alpnet stock at or near the end of the trading day to affect the closing price. Bowen and Canon were account executives for certain nominee accounts through which Warner executed illegal transactions. This case was pending at the end of the year.

The Commission instituted administrative proceedings against Harry S. Pack, the former president and chairman of Jefferson National Bank, and his brother, Philip Pack, in which it was found that they engaged in the practice of marking the close to manipulate the price of Jefferson National stock and thereby prevent margin calls in

certain accounts in which they held Jefferson National stock (*In the Matter of Harry S. Pack*²⁸). The Packs consented to the entry of cease and desist orders.

In *SEC v. The Cooper Companies*,²⁹ the Commission alleged, among other things, a manipulation by The Cooper Companies and Gary Alan Singer, Cooper's former co-chairman, of the trading price of certain convertible subordinated reset debentures to avoid an interest rate reset that would otherwise have been required. This case was pending at the end of the year.

Corporate Control

The Commission's enforcement program scrutinizes corporate mergers, takeovers and other corporate control transactions, and the adequacy of disclosure made by acquiring persons and entities and their targets. The Commission brought cases involving Sections 13 and 14 of the Exchange Act, which govern securities acquisition, proxy, and tender offer disclosure. The Commission on a number of occasions exercised its cease and desist authority under the Remedies Act to respond to violations in this area.

The Commission instituted administrative proceedings to remedy violations found by the order, arising from the 1990 tender offer by Kelso & Company, an investment banking firm, for the shares of Earle M. Jorgensen Company (*In the Matter of Kelso & Company, Inc.*,³⁰ *In the Matter of William A. Wilson*³¹). At the time of the tender offer, Kelso's chairman and chief executive officer, Joseph S. Schuchert, was engaged in a business relationship with William A. Wilson, an outside director of Jorgensen. Wilson served on the committee formed by Jorgensen to evaluate the Kelso offer and a

competing offer, but the relationship between Schuchert and Wilson was not disclosed to the public or in filings with the Commission. Kelso, Schuchert and Wilson consented to the entry of cease and desist orders.

In *SEC v. Furr's/Bishop's Inc.*,³² the Commission alleged that Furr's/ Bishop's, the successor holding company to Furr's/Bishop's Limited Partnership, made false and misleading statements in certain filings relating to its conversion from limited partnership to corporate form. According to the complaint, filings made with respect to the conversion indicated that Furr's/Bishop's would commence a self tender offer, to be financed by a stock subscription agreement with Michael Levenson, the corporation's chairman. The defendants failed to disclose that Levenson had not obtained sufficient financing to satisfy the maximum amount needed under the stock subscription, that Furr's/Bishop's might have to provide some of the financing, and that the self tender offer might not be concluded on schedule because Furr's/Bishop's recent operating results had been poor. Furr's/ Bishop's and Levenson consented to the entry of injunctions, and Levenson consented to the entry of an order requiring him to pay a civil penalty of \$50,000.

The Commission concluded administrative proceedings that had been instituted at the end of the previous year against Leslie T. Livingston and two entities under his control, including a registered broker-dealer firm (*In the Matter of Leslie T. Livingston*³³). The proceedings arose out of the change of control of Comprehensive Care Corporation (CompCare). The order instituting proceedings found that the respondents failed to promptly disclose their beneficial ownership of CompCare securities, as well as the existence and share ownership of various partnerships in which they had an

interest, at a time when Livingston was leading efforts by a shareholder group to effect a change in control. The Commission further found that the respondents failed promptly to amend the group's Schedule 13D to reflect changes in the intent of the group with respect to CompCare. The respondents consented to the entry of the cease and desist order.

The Commission also instituted and settled cease and desist proceedings alleging failure to make adequate or timely disclosure of changes in beneficial ownership of securities as required by Section 13(d) of the Exchange Act. These included *In the Matter of Bettina Bancroft*,³⁴ in which the Commission found that a director of Dow Jones & Company, Inc., failed promptly to file seventeen Forms 4 reporting her sales of Dow Jones' stock totaling over \$16.8 million. The reports were filed from over one year to over five and one half years late. The respondent consented to the entry of the cease and desist order.

The Commission filed administrative proceedings against Harry Hagerty, Jr., an officer, director and holder of at least ten percent of the stock of CCAIR, Inc., and a director and holder of at least ten percent of the stock of Air Transportation Holding Company (*In the Matter of Harry E. Hagerty, Jr.*³⁵). Hagerty failed in thirty-three instances to make timely filings on Forms 4 and 5 to reflect his transactions in the stock of CCAIR and Air Transportation. The transactions involved more than \$2.76 million of those issuers' stock. Hagerty consented to the entry of a cease and desist order. In a related civil proceeding for imposition of a civil penalty, Hagerty consented to the entry of an order requiring payment of a \$15,000 penalty (*SEC v. Harry E. Hagerty, Jr.*³⁶).

Broker-Dealer Violations

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, as well as violations of books and records provisions. 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.

In October 1993, the Commission filed a civil action and instituted administrative proceedings against Prudential Securities, Inc., in which it was alleged that Prudential had defrauded investors in connection with the offer and sale of limited partnership interests between January 1, 1980 and December 31/1990; in addition, Prudential allegedly failed to reasonably supervise its sales personnel (*SEC v. Prudential Securities Inc.*³⁷). Materially false and misleading statements and omissions were made in connection with Prudential's sale of about \$8 billion in limited partnership interests. The Commission further alleged that Prudential failed to comply with a Commission order entered in 1986 arising from its failure to adequately supervise certain former registered representatives. Prudential consented to the entry of an order requiring the payment of all valid investor claims presented through a court-supervised claims resolution process, the payment of \$330 million to establish a fund for the benefit of defrauded investors, and the payment of all additional valid claims in excess of that amount. Prudential also consented to the entry of a cease and desist order in the administrative proceedings, in which the Commission imposed a \$10 million penalty and ordered Prudential to adopt remedial measures designed to

prevent future violations. In addition to the penalty to be paid in the Commission's action, Prudential agreed to pay \$26 million in fines to various states, and a \$5 million fine to the NASD,

In *In the Matter of PaineWebber Inc.*,³⁸ the Commission found that various registered representatives employed at four PaineWebber branch offices engaged in sales practice abuses, including unsuitable and excessive trading, and misappropriated funds from customer accounts. The Commission found that PaineWebber had failed to supervise the registered representatives. PaineWebber consented to the entry of an order by which it was censured and required to comply with several undertakings, including a prohibition against opening new accounts for thirty days at the offices involved in the sales practice violations and the hiring of an independent consultant to review procedures relating to sales practices and sales of restricted securities.

In *In the Matter of Frederick H. Joseph*,³⁹ the Commission found that the respondent, a former chief executive officer and vice chairman of Drexel Burnham Incorporated, failed to supervise Michael Milken, the former manager of Drexel's high yield and convertible bond department, with a view to preventing Milken's violations (1) in a scheme to manipulate prices and to cause misrepresentations, through Milken-controlled entities, in connection with eighteen new issues of Drexel underwritten securities, and (2) in a scheme to cause a fund manager to use client assets to make improper payments to Drexel. Edwin Kantor, a former senior executive vice president and director of Drexel, also was charged in separate proceedings with failure to supervise Milken with a view to preventing the same violations (*In the Matter of Edwin Kantor*⁴⁰). Both

Joseph and Kantor consented to the entry of orders by which they were barred from association in a supervisory capacity.

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*In the Matter of The Nikko Securities Co. International, Inc.*⁴¹ arose from Nikko's undisclosed loss of \$18 million through speculative foreign exchange trading, Nikko's foreign exchange trader concealed the losses by making repeated false entries in the firm's accounting books and records. Three former executives named as respondents in the proceedings learned of the loss, but decided to restrict knowledge of the loss to a select group of Nikko employees and Nikko's parent corporation in Japan. For approximately five months, Nikko failed to disclose the loss to its own legal or compliance department or its outside auditors, and concealed the loss from the Commission, the NYSE and the public. The respondents consented to the entry of cease and desist orders. Nikko also consented to the entry of orders by which it was censured and required to undertake a compliance review. In addition, two of the individual respondents consented to bars from association, and the third individual respondent consented to a suspension for a period of one year.

A number of cases involved violations arising from the sale of penny stocks. In *SEC v. Leslie Mersky*,⁴² the Commission alleged that thirteen individuals and four corporate entities engaged in a fraudulent scheme to sell approximately \$3.4 million of worthless securities issued by two public shell corporations, Amglo Industries, Inc., and Amglobal Corporation. Certain defendants utilized a fraudulent broker-dealer network and manipulated the market to sell Amglo and Amglobal securities at a substantial profit. The complaint

also alleged that certain defendants prepared false and misleading information about the companies that was disseminated through a series of high pressure sales campaigns. Two of the corporate entities consented to the entry of injunctions. Two of the individual defendants also consented to the entry of injunctions and orders requiring them to disgorge a total of \$50,167, plus prejudgment interest totaling \$21,907. In addition, these two defendants consented to the entry of bar orders in related administrative proceedings. Two other individual defendants consented to the entry of bar orders in related proceedings. The injunctive action was pending at the end of the year.

The Commission alleged in *SEC v. Midwest Investments*,⁴³ that the defendants engaged in a scheme to charge excessive undisclosed markups and to manipulate the price of the stock of Reitz Data Communications, Inc. Using high pressure, "boiler room" sales techniques, the defendants solicited purchases of Reitz stock at arbitrarily inflated prices with markups as high as 215 percent. The defendants also violated the Commission's cold-calling and penny stock disclosure rules in connection with their sales of Reitz stock. The Commission obtained a preliminary injunction, an asset freeze and other ancillary relief in this action, which was pending at the end of the year.

The Commission also instituted actions against other regulated entities involved in the settlement of securities transactions. In *SEC v. Midwest Clearing Corporation*,⁴⁴ the Commission filed an action against Midwest Clearing Corporation (MCC), a registered clearing agency, and the Midwest Securities Trust Company (MSTC), a registered clearing agency for which the Board of Governors of the Federal Reserve System is the primary regulatory agency. The

complaint alleges that MCC and MSTC created false securities positions in their integrated computer records that were transferred to contra clearing corporations before MSTC had actual possession of the securities. As a result, MCC obtained substantial amounts of cash, at times as much as \$35 million, that could be invested for its own benefit. The defendants consented to the entry of injunctions and an order requiring the payment of a civil penalty of \$2 million. MCC also consented to the entry of an order in related administrative proceedings by which it was censured and required to comply with certain remedial undertakings. MSTC consented to the entry of a cease and desist order in related administrative proceedings instituted by the Federal Reserve Board.

Investment Adviser and Investment Company Violations

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

In October 1993, the Commission instituted administrative proceedings against Kemper Financial Services, Inc., in which it was found that a Kemper portfolio manager had delayed designation of the account for which certain trades were being conducted until after the trades were effected (*In the Matter of Kemper Financial Services, Inc.*⁴⁵). The more favorable trades were allocated to a private profit-sharing plan for Kemper's employees, while less favorable trades were allocated to two public mutual funds managed by Kemper. The Commission also found that Kemper failed to reasonably supervise the portfolio manager with a view to preventing violations. Kemper consented to the entry of the cease and desist order and an order by which it was censured. Kemper also consented to pay \$9.2 million into an escrow account for distribution to investors, and to retain an

independent consultant to review its policies and procedures related to trading in connection with its investment adviser and investment company operations.

The Commission instituted proceedings against USAA Investment Management Company, the investment adviser for USAA Tax Exempt Fund, Inc., a registered investment company (*In the Matter of USAA Investment Management Co.*⁴⁶). The Commission found that the Tax Exempt Fund sold, redeemed or repurchased securities issued by one of its series, the Tax Exempt Money Market Fund, without calculating its net asset value in a manner permitted by rules under the Investment Company Act. In particular, the board of directors of the Tax Exempt Fund did not make the required minimal credit risk and comparable quality determinations required by the Investment Company Act with respect to \$177 million in unrated securities. The respondents consented to the entry of orders by which they were censured and USAA was ordered to certify that Tax Exempt Fund's board had undertaken certain measures, policies and procedures. In addition, USAA consented to an order requiring it to pay a civil penalty of \$50,000, and respondent Steven D. Harrop, an officer and portfolio manager, consented to the entry of a cease and desist order.

The Commission found violations arising from undisclosed compensation arrangements in *In the Matter of Aetna Capital Management, Inc.*⁴⁷ Between 1983 and 1991, Aetna Capital Management, Inc. (ACM) and Aetna Life Insurance Company (Aetna Life) paid approximately \$1.8 million in sales commissions and consulting fees to a broker-dealer who provided Aetna with advice regarding the public pension market and product development. The broker also solicited purchasers for Aetna Life's group annuity

contracts and ACM's investment advisory service; entities solicited eventually invested approximately \$240 million with Aetna Life and ACM. The fees paid to the broker were not disclosed to investors or in reports filed with the Commission. Aetna Financial Services, Inc., also offered and sold one of Aetna Life's securities products without disclosing to investors that Aetna paid the broker in part for soliciting purchasers for the product. The respondents consented to the entry of cease and desist orders. In addition, ACM consented to pay a civil penalty of \$500,000.

The Commission alleged that Corporate Capital Resources, Inc., a business development company, issued false and misleading financial statements that materially overstated the value of its holdings of restricted securities (*SEC v. Corporate Capital Resources, Inc.*⁴⁸). The resulting overvaluation of Capital Resources net asset value allegedly ranged from 7 percent to 53 percent over an eighteen month period. The overvaluations were contained in periodic reports filed with the Commission that were used by the defendants in connection with a public offering of Capital Resources' stock. Among other things, the Commission alleged that Capital Resources' valuation committee did not follow the company's valuation procedures, and knew or were reckless in not knowing that the proposed valuations were insupportable. Capital Resources and the four individual defendants consented to the entry of injunctions.

In administrative proceedings, the Commission found that The Bank of California had improperly calculated the net asset value per share of the Tax-Free Fund, a money market fund and a series of The HighMark Group, The bank served as accountant and investment adviser to the fund (*In the Matter of The Bank of California*⁴⁹). While determining the value of the fund's holdings on

July 25, 1991, the bank received from the fund's pricing service a market price of 70 for a tax-exempt bond originally purchased for \$1 million. The bank treated the reduced price as a transmission error, and valued the bond at par, for a number of weeks, even though the pricing service continued to quote a price of 70. When the error was finally recognized, the bank purchased the bond from the fund at par plus interest. The bank consented to the entry of a cease and desist order.

The Commission instituted administrative proceedings, *In the Matter of Merrill Lynch, Pierce, Fenner & Smith*,⁵⁰ alleging that Merrill Lynch repurchased hundreds of thousands of units issued by 570 unit investment trusts (UITs) sponsored by the firm at a price not based on the current net asset value of such securities. Merrill Lynch's formula for calculating the unit price did not include certain sums of cash held by the trustees accumulated in the UITs' income accounts as a result of bonds that were called, sold, or had matured from the UITs' portfolios. Merrill Lynch consented to the entry of a cease and desist order, and an order requiring it to comply with certain undertakings/ including an undertaking to compensate customers whose securities were repurchased at less than net asset value.

Sources For Further Inquiry

The Commission publishes the SEC *Docket*, which includes announcements regarding enforcement actions. The Commission's 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. Since August 1993, OIA has been responsible for coordinating the SEC's technical assistance program for training and advice in countries with developing 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 1993 Results

In 1993, the SEC signed comprehensive Memoranda of Understanding (MOUs) for consultation and cooperation in enforcement-related matters with the Commissione Nazionale per le Società e la Borsa (CONSOB) of Italy and the Superintendencia de Valores y Seguros (SVS) of Chile.

Significant progress was made in the second annual meeting of the Council of Securities Regulators of the Americas (COSRA), which promotes cooperation and communication among securities regulators in the Americas. Agreement was reached on important principles relating to regulation of the secondary markets and investment advisers.

Arrangements for Mutual Assistance and Exchanges of Information

The increasing internationalization of the world's securities markets has raised many new and complex issues that affect the SEC's ability to enforce federal securities laws. For example, because of the internationalization of the markets, it is critical that the SEC be able to collect information located abroad. Ordinarily, this is not possible using the SEC's domestic investigative authority. The SEC has attempted to resolve this problem by developing information-sharing arrangements on a bilateral basis with various foreign authorities.

The information-sharing arrangements allow the SEC to obtain information located abroad while avoiding the conflicts that may result from differences in legal systems. In recent years, the SEC has entered into various arrangements with foreign authorities from nearly 20 nations. These relationships are effective means for obtaining information and developing cooperative relationships between regulators. In addition, the staff works closely with the parties to these information-sharing arrangements to develop ways to implement and improve the arrangements. The SEC also cooperates on an informal

basis with foreign authorities with whom it does not have explicit information-sharing arrangements.

In May 1993, the SEC signed an MOU with the Italian securities regulator, CONSOB. On June 3, 1993, the SEC entered into an MOU with the SVS of Chile. These MOUs concern consultation and cooperation in the administration and enforcement of United States and Italian and Chilean securities laws. The MOUs declare the intent of the SEC and the CONSOB and SVS to provide extensive mutual assistance on a broad range of securities matters to secure compliance with their respective laws and regulations. The MOUs cover matters relating to enforcement and market surveillance, and provide that the SEC and the foreign authorities will utilize their compulsory powers to assist one another. The MOUs also provide for consultations between the parties on all matters relating to the operation of the securities markets of their respective countries, and on the operation of the MOUs. The MOU with the CONSOB built on an earlier Communiqué that had been signed by the SEC and the CONSOB on September 20, 1989.

Examples of the mutual assistance and cooperation provided for by the MOUs include: 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. Each party also represents its intention to engage in consultations to enhance the coordination of their respective market oversight functions. The MOUs identify the type of mutual assistance contemplated by the SEC and the CONSOB and SVS. For example, the parties will provide access to agency files; take testimony and obtain information and documents from persons; and

conduct compliance inspections or examinations of investment businesses. Such assistance is intended to facilitate the investigation, litigation or prosecution of securities matters where information needed by one authority is located in the territory of the other.

Enforcement Matters

Some of the more significant matters in which OIA provided assistance to the Division of Enforcement during 1993, listed with the countries that provided substantial assistance to the SEC, were *SEC v. Antar, et al.*, 89 Civ. 3773 (D.N.J.) (Switzerland, Canada, France, Israel and the United Kingdom); *In the Matter of Basque Puerto Carillo, S,A*, Civ. No. 93-685 (S.D. Fl.) (Costa Rica); *SEC v. D'Onofrio et al*, Civil Action No. 93-2628 SVW (Ex) (C.D. Cal.) (Canada, Andorra, Spain, and the United Kingdom); *SEC v. Pacific Waste Management, Inc. et al.*, Civ. No. CV-N-93-232-ECR (D. Nev.) (Guernsey); *SEC v. Premium Sales Corp. et al.*, Case No. 93-1092-Civ. (S.D. Fla. 1993) (Switzerland); *SEC v. Southwest International Exchange,, et al.*, Civil Action No. 93-1285 AAH (SHx) (CD. Cal.) (Switzerland).

Of particular importance to the SEC's international program are the SEC's recent efforts to freeze and obtain repatriation of funds from abroad. In *Antar*, for example, \$32 million was frozen in Switzerland through the cooperation of the Swiss authorities, and authorities in Canada, France, Israel and the U.K. have assisted in either freezing or obtaining information about the location of assets in those countries. In particular, in May 1993, the SEC was successful, with the assistance of the Quebec Securities Commission, in having over \$1.1 million of *Antar's* ill-gotten gains repatriated to the United States for eventual distribution to defrauded investors. In another

example of extraordinary cooperation, *Pacific Waste Management*, the SEC obtained key information through the assistance of criminal authorities in Guernsey which led to the discovery of a bank account in Guernsey holding some of the defendants' ill-gotten profits. The SEC successfully froze that money through an ancillary proceeding filed in the Royal Court of Guernsey.

Technical Assistance

The SEC has an active technical assistance program, utilizing various means to provide both United States-based and overseas technical assistance to emerging market countries. Such technical assistance is intended to develop a regulatory infrastructure to promote investor confidence in developing markets.

The SEC International Institute for Securities Market Development (the SEC Institute) is the SEC's flagship technical assistance program. The SEC Institute is a two-week, management-level training program covering a full range of topics relevant to the development and oversight of securities markets. The third annual SEC Institute was held in the spring of 1993. Over 265 persons from 62 emerging market countries have participated in the first three SEC Institutes. The SEC's technical assistance efforts in Eastern Europe have included sending SEC staff as advisers to several countries in the region under a program funded by the United States Agency for International Development. The SEC has also participated in a number of short-term assistance projects for the countries of Latin America and the Caribbean, as well as several countries in other regions. In addition, the SEC's MOUs with developing countries include provisions whereby the SEC may agree to provide technical assistance to a signatory country's securities regulatory or self-

regulatory authorities. The SEC also invites foreign securities regulators to participate in the SEC's Annual Enforcement Training Program held in the fall. This year, there were 45 foreign participants from 26 countries, including 18 representatives from 11 emerging market countries.

International Organizations and Multilateral Initiatives

During 1993, the SEC contributed to the work of the following international organizations and multilateral initiatives:

The International Organization of Securities Commissions (IOSCO). The SEC is an active participant in IOSCO. IOSCO is an international forum created to promote cooperation and consultation among regulators overseeing the world's securities markets. IOSCO has over 100 members, including most of the world's securities regulators.

During 1993, IOSCO made substantial progress toward the development of international accounting standards. IOSCO passed a resolution recommending that its members take all steps that are necessary and appropriate in their respective home jurisdictions to accept cash flow statements prepared in accordance with International Accounting Standard (IAS) 7, as amended, in connection with cross-border offerings and continuous reporting by foreign issuers. IAS 7, which would be an alternative to statements prepared in accordance with a country's domestic accounting standards, is the first such standard developed by the International Accounting Standards Committee to be endorsed by IOSCO.

IOSCO working groups prepared several significant documents which were issued during the IOSCO Annual Conference in October 1993. Significant topics studied by the working groups during the year include communication between regulators of related cash and derivative markets during periods of market disruption and protecting investors against international retail securities fraud.

During 1993, the IOSCO Working Party on Enforcement and the Exchange of Information prepared a report entitled *Protecting the Small Investor: Combating Transnational Retail Securities and Futures Fraud*, which was released at the IOSCO Annual Conference. The SEC made significant contributions to this report. Based on the report, IOSCO adopted a resolution defining a number of measures that should be taken by IOSCO members to enhance protection against international retail securities and futures fraud. The report considers problems and challenges that regulators face in the investigation and prosecution of transnational boiler-room fraud. It reviews various domestic measures that countries have adopted to protect investors from boiler-room fraud. Further, it explores the role of international cooperation in combating transnational boiler-room fraud and identifies additional measures that may assist regulators in their efforts to combat the problem.

The IOSCO Working Party on Regulation of Securities Markets prepared a report entitled *Mechanisms to Enhance Open and Timely Communication Between Market Authorities of Related Cash and Derivative Markets During Periods of Market Disruption*, which was released at the IOSCO Annual Conference. The report completes the work of the Working Party on the coordination between cash and derivative markets. On the basis of the report issued this year and related reports issued previously, IOSCO adopted a resolution to

enhance the effective oversight of related cash and derivative markets. This resolution identifies issues which should be considered in the design of derivative product contracts based on stock indices, defines ways to implement measures to minimize market disruption and establishes a number of points of consensus concerning communications between market authorities of related cash and derivative markets during periods of market disruption.

Council of Securities Regulators of the Americas (COBRA). On June 3-4, 1993, the members of COSRA held their Second Annual Meeting in Buenos Aires, Argentina. The meeting was chaired by then Acting SEC Chairman Mary Schapiro. During the meeting, COSRA broke new ground by reaching agreement on important principles for the regulation of secondary markets and international cooperation in the supervision of investment advisers. These principles focus on the development of programs and market structures that will foster the growth and openness of the securities markets of the Americas, and will advance market consistency within the Americas.

The principles considered and adopted by the membership were in four areas vital to the functioning of securities markets. These are transparency in transaction reporting; audit trails; clearance and settlement; and cross-border surveillance of investment advisers. Each of these principles is intended to promote and enhance market integrity and investor confidence, while advancing market development within an international market economy.

The COSRA principles on market transparency focus on the development of systems that provide for the full and immediate dissemination to investors of transaction and quotation information

and other essential trading information in individual securities markets. The principles on audit trails focus on the development of systems that monitor market activity, including the market surveillance activities of self-regulatory organizations. The principles on clearance and settlement focus on the development of systems that provide for the rapid and efficient transfer, recordation, and custody of securities that are traded. The COSRA principles on surveillance of investment advisers identify as a priority the need to develop methods for joint information-sharing and surveillance programs.

The Organization for Economic Cooperation and Development (OECD). The SEC staff, in conjunction with representatives of the Departments of State and Justice, participated in OECD discussions regarding the establishment of international standards to combat illicit payments to government officials and other practices that may affect foreign investment. The SEC also provided technical assistance to other Federal agencies with respect to various work programs of the OECD.

The General Agreement on Tariffs and Trade (GATT). The SEC is an active participant in the effort, through the Uruguay Round of the GATT, to establish a multilateral framework of principles and rules for trade in financial services. Throughout 1993, the SEC has consulted and coordinated with the Office of the United States Trade Representative, the Department of Treasury, and other United States government agencies, in connection with the GATT negotiations.

The North American Free Trade Agreement (NAFTA). As with GATT, the SEC provided Federal agencies with technical assistance in connection with NAFTA. Among other things, the agreement

contains a Financial Services Chapter, which will encompass activities (including cross-border activities) of financial service providers, such as broker-dealers and investment advisers, within NAFTA countries. This Chapter sanctions 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 NAFTA.

The Wilton Park Group (The Group). Her Majesty's Treasury of the United Kingdom sponsors this informal meeting which includes securities regulators from 12 countries. During this year's meeting in May the SEC raised the issue of problems created by underregulated, offshore entities. The Group agreed to begin discussing approaches to addressing these problems. In addition, participants agreed to create a compendium of their experiences in enforcing judgments and provisional measures abroad.

International Requests for Assistance

[table omitted]

REGULATION OF THE SECURITIES MARKETS

The Division of Market Regulation, together with regional and district office examination staff, oversees the operations of the nation's securities markets and market professionals. In calendar year 1992, the Commission supervised over 8,200 broker-dealers with 34,000 branch offices and 427,000 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 trillion in assets and \$62 billion in capital in 1992. The division also monitors market activity, which has experienced significant growth and volatility. In 1992, equity market capitalization stood at \$4.8 trillion in the U.S. and \$11.1 trillion worldwide. The average daily trading volume grew to over 200 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 U.S. broker-dealers and their affiliates is \$4 trillion with an aggregate replacement cost of approximately \$18 billion.

Key 1993 Results

The division undertook significant efforts to strengthen and stabilize market segments. For example, the division issued a comprehensive report concerning the issuance and sale of municipal securities that made recommendations regarding a variety of aspects of the municipal market. The division also conducted significant research and analyses as it moved towards completing the *Market*

2000 study. This study seeks to provide an understanding of how the equity markets have changed over the past 20 years. It will explore how market participants and the rules governing them have served the interests of fairness, efficiency, and competitiveness in the equity markets.

The division also oversaw a number of self-regulatory organization (SRO) initiatives to enhance the stability and integrity of the options market. Further, the division studied and monitored derivative activities through analysis of holding company risk assessment data, examinations and inspections, and discussions with other regulators and industry participants. The Commission issued a concept release relating to treatment of derivatives under the net capital rule.

The Commission bolstered efforts to reduce abuses in the penny stock market with the adoption of amendments proposed by the division. Also, in addition to its usual inspection program, the division coordinated the 1993 penny stock examination sweep involving the examination by the SEC, SROs, and 40 state jurisdictions of 129 broker-dealers.

Securities Markets, Trading and Significant Regulatory Issues

Municipal Securities Market

The division issued a comprehensive report to Congress concerning the adequacy of current laws and regulations governing the issuance and sale of municipal securities.⁵¹ Specifically, the report reviews the current status of the municipal securities markets and provides discussions and recommendations with respect to: (1)

political contributions made by broker-dealers to influence the award of municipal securities underwritings; (2) abusive sales practices; (3) transparency of the municipal securities market; (4) issuer disclosure; and (5) the adequacy of the current regulatory structure. The staff concluded that the regulatory structure of the municipal securities market did not warrant a comprehensive restructuring; however, the report recommended improved coordination between regulatory agencies. In addition, the staff conducted a study of the underwriting, secondary trading and pricing of municipal bonds. The study was initiated in response to congressional concerns and customer complaints. The staff reviewed surveillance techniques and made recommendations for transactional reporting to the SROs for market surveillance purposes.

Market 2000

The division continued its work on the *Market 2000* study. The study is exploring the role that SEC and SRO rules play in maintaining the fairness, efficiency, and competitiveness of the equity markets. In conducting the study, the division is examining equity market issues such as market fragmentation, fair competition between markets, payment for order flow, transparency, and proprietary trading systems, among others. The division collected relevant data, analyzed the 58 comment letters received on the study, issued a rule proposal on payment for order flow, and began preparation of the final report.

National Clearance and Settlement System

The Commission continued to work to enhance all components of the national clearance and settlement system. For example, the

Commission adopted Rule 15c6-1 under the Securities Exchange Act of 1934 (Exchange Act) which establishes three business days as the standard settlement time frame for broker-dealer trades.⁵² The rule becomes effective on June 1, 1995. Generally, Rule 15c6-1 covers broker-dealer trades in corporate and investment company securities and excludes trades in firm commitment underwritings and trades in municipal securities. In adopting the rule, the Commission called on the Municipal Securities Rulemaking Board (MSRB) to implement earlier settlement for trades in municipal securities by June 1, 1995. Rule 15c6-1 is designed to diminish risk in the national clearance and settlement system by reducing the number of unsettled trades in the system at any given time.

Net Capital Concept Release

The Commission issued a concept release⁵³ soliciting public comment on a broad range of issues relating to the appropriate capital treatment of derivative products under the agency's net capital rule. In examining the treatment of derivative products/ and particularly over-the-counter (OTC) derivative products, the Commission's concept release focused primarily on the market and credit risk to which participants in the derivative products market are exposed and presented several alternatives to the current treatment of those instruments under the net capital rule. The purpose of the Commission's release is to explore and evaluate whether the net capital rule⁵⁴ should be modified with respect to the derivative products markets and, in particular, OTC derivative products.

Optical Storage Technology

The Commission proposed for comment amendments to its broker-dealer records preservation rule that would permit broker-dealers to employ, under certain circumstances, optical storage technology to maintain records under Rule 17a-4.⁵⁵ The Commission also authorized the division to issue a no-action letter permitting broker-dealers to employ optical storage technology for record preservation purposes pending final action on the proposed rule.⁵⁶ The comment period closed September 13, 1993.

Risk Assessment

The Commission adopted its risk assessment recordkeeping and reporting rules in 1992. Pursuant to those rules, broker-dealers are required to maintain information concerning affiliated entities whose business activities are reasonably likely to have a material impact on the financial and operational condition of the broker-dealer and to file summaries of that information in quarterly reports with the SEC.⁵⁷ The staff is now tracking financial reports from approximately 250 broker-dealers and 700 affiliated entities.

Automation Review

The staff fully implemented the agency's automation review guidelines as they pertain to the exchanges and the National Association of Securities Dealers, Inc. (NASD).⁵⁸ The primary purpose of the automation review program is to monitor and inspect the electronic data processing (EDP) activities of the SROs. Specifically, the staff's inspections have focused on computer security, system development, capacity, testing, and contingency planning to promote the safety and soundness of individual SRO EDP trading and information dissemination systems and the national

market system. The staff completed 7 on-site inspections of the SRO EDP systems and issued 4 reports with recommendations for improvements, including the need for improvements to SRO internal audit procedures, enhancements of contingency planning efforts, and better use of capacity planning tools.

As part of its EDP oversight role, the staff also held eight meetings with the SRO EDP organizations to ascertain recent and planned SRO changes and improvements in automated systems. The staff also tracked the ability of SROs to respond to systems malfunctions and examined SRO measures to prevent system outages and maintain stable markets.

Government Securities Market

In October 1993, the U.S. House of Representatives (House) passed H.R. 618 to permanently reauthorize the Secretary of the Treasury's rulemaking authority under the Government Securities Act of 1986. This bill reflects an agreement reached between the Commission, Department of the Treasury, House Energy and Commerce Committee, and House Banking Committee. Under the bill, the SEC would be required to monitor the transparency in the government securities market and report its findings to Congress. In addition, the bill would grant the Commission authority to obtain records of government securities transactions in electronic form from all government securities brokers and dealers. The bill also would authorize the NASD to make sales practice qualification and other rules applicable to the activities of its members effecting transactions in government and other exempted securities.

Internationalization

The staff provided information and technical assistance to several emerging market countries, including Mexico, China, Thailand, Taiwan, Nigeria, and Argentina. Pursuant to the SEC's membership in the International Organization of Securities Commissions (IOSCO), the staff participated in the Working Party on the Regulation of Secondary Markets, which discussed issues concerning regulation of screen-based trading systems and transparency of markets. The working party also produced a paper discussing mechanisms to enhance communication among market authorities during periods of market disruption. This paper was approved by the IOSCO Technical Committee and endorsed by IOSCO at its 1993 annual meeting.

Net Capital Rules

The Commission issued two releases regarding the minimum amount of net capital required of registered broker-dealers. The first release adopted final amendments to Rule 15c3-1, the net capital rule, which gradually increase the minimum net capital requirements for certain registered broker-dealers.⁵⁹ The second release proposed for comment additional amendments to the net capital rule that, among other things, would gradually raise the \$5,000 minimum applicable to introducing brokers that do not receive customer securities to \$25,000.⁶⁰

Passive Market Making

The Commission adopted Rule 10b-6A under the Exchange Act to permit "passive" market making by NASDAQ market makers in

connection with certain distributions of NASDAQ securities during the period when Rule 10b-6 otherwise would prohibit such activity.⁶¹ Rule 10b-6A balances concerns about decreased liquidity during distributions of OTC securities and potential manipulation activity. Among other things, the rule limits a passive market maker's bids to the level of bids of market makers who are not participating in the distribution.

Multinational Distributions

The Commission granted a variety of relief under anti-manipulation Rules 10b-6, 10b-7, and 10b-8 for multinational offerings. These actions were taken to permit customary market activities in foreign jurisdictions subject to conditions designed to prevent a manipulative impact on United States markets. For example, the Commission granted exemptions to facilitate distributions in the United States of actively-traded securities of highly capitalized German issuers, subject to conditions relating to security eligibility, notice, disclosure, record keeping, and transaction reporting.⁶² As part of this relief, unconditional exemptions were granted for transactions effected in securities markets that account for less than 10 percent of aggregate world-wide published trading volume in the German security being distributed. Also, the Commission granted expanded class exemptions to permit London Stock Exchange (LSE) market makers to make markets on a "passive" basis when Rule 10b-6 otherwise would require the cessation of trading on the LSE's SEAQ and SEAQ International systems.⁶³ In connection with multinational rights offerings by United Kingdom issuers, the Commission granted exemptions to permit U.K. distribution participants to conduct transactions with customers and to continue trading activities.⁶⁴

The Commission adopted amendments to permit transactions in all jurisdictions without compliance with the trading practices rules during distributions of Rule 144A-eligible securities of a foreign government or a foreign private issuer, if such securities are offered or sold in the United States solely to QIBs or persons reasonably believed to be QIBs.⁶⁵

Penny Stock Disclosure Rules

The Commission adopted amendments to Rule 15c2-6 of the Exchange Act and redesignated it as Rule 15g-9 in order to conform it to the other penny stock disclosure rules, Rules 15g-2 through 15g-6.⁶⁶ These amendments became effective on August 11, 1993. By conforming Rule 15c2-6 with the penny stock rules, the Commission eliminated confusion regarding the operation of the rules and lessened the burden of compliance for broker-dealers subject to the regulatory regime governing transactions in penny stocks. In addition, the Commission amended Rule 15g-2 and Schedule 15G to require broker-dealers to obtain, prior to effecting a transaction in a penny stock, a written acknowledgement from a customer showing that the customer received a risk disclosure document required by Rule 15g-2.⁶⁷

SRO Qualification Standards

The Commission adopted Rule 15b7-1 of the Exchange Act, which prohibits registered broker-dealers from effecting a securities transaction, unless an associated person of that broker-dealer is in compliance with the qualification requirements established by rules of the SRO of which the broker-dealer is a member or to whose

oversight it is subject.⁶⁸ Rule 15b7-1 allows the Commission to proceed directly against broker-dealers, as necessary, in part, because in some cases the Commission is the sole regulatory authority initially investigating a case alleging violations of SRO qualification standards. Accordingly, Rule 15b7-1 will strengthen the self-regulatory system and enhance investor protection by ensuring adequate competency among securities personnel.

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

Broker-Dealer Examination Program

The SEC completed a total of 681 examinations consisting of 424 oversight and 257 cause examinations. The total number of completed examinations is an all time record for the examination program and represents a 24 percent increase over 1992. In addition, the number of cause examinations conducted in 1993 represents an increase of 96 percent over 1992. The increase in cause examinations is consistent with the 1993 objective of conducting a greater number of examinations of major wirehouse branch offices, firms selling low-priced securities and franchised branch offices. Findings from 84 examinations were referred to regional office enforcement staff representing 13 percent of all completed examinations. Referrals to SROs were made in 60 examinations. In addition, the number of referrals to the Division of Enforcement increased 15 percent from 1992.

A significant accomplishment in the broker-dealer examination program involved firms selling low-priced securities. On July 12, 1993, the SEC, NASD, New York Stock Exchange (NYSE) and 40

state securities regulators began a nationwide examination sweep of 129 broker-dealers to determine compliance with Exchange Act Rules 15g-2 through 15g-6 and 15g-9 (formerly 15c2-6). The 1993 penny stock examination sweep represents the largest, most ambitious joint SEC, SRO and state examination project ever undertaken.

The staff also conducted oversight examinations at 10 of the largest NYSE member firms. The staff conducted comprehensive financial and operational reviews at each of the firms. Examination field work regarding a special initiative undertaken in 1992 to review the hiring and supervisory practices at large NYSE member firms with respect to certain salespersons was completed.

The staff continued to meet quarterly with senior staff from the NASD and NYSE to discuss their examination programs and other regulatory and enforcement issues. The SEC's regional and district offices also separately communicated examination results directly to SROs in writing and during periodic meetings.

Training Programs for Examiners

The Division of Market Regulation planned, developed, and conducted four major training programs for headquarters, regional and district office staff. The training programs consisted of: (1) a two-week course for new broker-dealer examiners which emphasized the financial aspects of broker-dealers, (2) a one-week course for new examiners which emphasized the regulation of sales activities of broker-dealers, (3) a one-week course for experienced examiners which addressed topical issues, and (4) a massive training effort in the new penny stock rules. The division obtained national

accreditation of the training courses from the National Association of the State Boards of Accountancy.

Money Laundering

The division continued to work closely with the Department of the Treasury and other government offices to pursue effective policies to combat money laundering. For example, the staff actively participated in the United States delegation to the Financial Action Task Force on Money Laundering, the independent group of major financial center countries and regions, and domestic working groups.

Transfer Agent Examinations and Regulation

The SEC's regional and district offices conducted 170 examinations of registered transfer agents, including 15 federally regulated banks. The division conducted on-the-job training in the agency's field offices and assisted several regions in their inspections. The program resulted in 106 deficiency letters, 8 cancellations or withdrawals, 10 referrals to the Division of Enforcement, 4 staff conferences with delinquent registrants, and 5 referrals to federal bank examiners.

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.⁶⁹ Statistics for calendar year 1992 (the most recent data available) reflect the program's continuing effectiveness. As of December 31, 1992, 23,744 institutions were registered in the program, a 1.4% increase over 1991. The number of securities

reported as lost, stolen, missing, or counterfeit increased from 876,519 to 2,500,521, a 185% increase. The dollar value of these securities increased from \$2.3 billion to \$71 billion, a thirtyfold increase. The aggregate dollar value of the securities contained in the program's data base increased from \$20.1 billion in 1991 to \$90.2 billion in 1992, a 350% increase. In 1992, the number of inquiries from participating institutions that matched previous reports as lost, missing, stolen, or counterfeit securities was 22,538, a 98% increase from 1991, The dollar value of these matches decreased from \$192 million in 1991 to \$135 million in 1992, a 30% decrease. The total number of certificates inquired about through the program rose from 3,876,519 in 1991 to 5,281,185 in 1992, a 36% increase.

Oversight of Self-Regulatory Organizations

National Securities Exchanges

As of September 30, 1993, 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, Chicago Stock Exchange (CHX, formerly the Midwest Stock Exchange), NYSE, Philadelphia Stock Exchange (PHLX), and Pacific Stock Exchange (PSE). The agency granted exchange applications to delist 97 debt and equity issues, and granted applications by issuers requesting withdrawal from listing and registration for 49 issues. In addition, the SEC granted 1,934 exchange applications for unlisted trading privileges.

The exchanges submitted 255 proposed rule changes during 1993. A total of 212 pending and new filings were approved by the

Commission and 39 were withdrawn. Notable rule filings approved by the Commission included proposals to:

- amend the NYSE's priority rules to allow a member who has an order to buy and an order to sell 25,000 shares or more of the same security, where neither order is for the account of a member or a member organization, to cross those orders at a price that is at or within the prevailing quotations without being broken up at the cross price, irrespective of preexisting bids and offers at that price;⁷⁰
- adopt NYSE Rule 410B which requires members to report to the exchange transactions in exchange-listed securities that are not otherwise reported to the consolidated tape;⁷¹ and
- extend the NYSE, AMEX BSE, CHX, PSE, and PHLX pilot programs for off-hours-trading until January 31, 1994.⁷²

National Association of Securities Dealers, Inc.

The NASD, with over 5,200 member firms, is the only national securities association registered with the SEC. It is the operator of NASDAQ, the second largest stock market in the United States, and the second largest in the world (after the NYSE).

The NASD submitted 72 proposed rule changes to the Commission during the year. The Commission approved 71 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:

- implementation of a Fixed Income Pricing System establishing an automated trading marketplace with 90 second transaction reporting for trading of certain non-investment grade debt securities;⁷³
- a requirement of reporting within 90 seconds of transactions of 99 bonds or fewer for convertible bonds listed on NASDAQ/⁴ and the establishment of requirements for 90 second transaction reporting of OTC transactions in equity securities that are not currently reportable on a real-time basis;⁷⁵ and
- expansion of a toll-free telephone listing service plan to provide, with respect to NASD members and associated persons. Central Registration Depository information regarding all pending formal disciplinary proceedings initiated by federal, state or foreign securities agencies and SROs, criminal indictments or informations, civil judgments, and arbitration decisions in securities and commodities disputes involving public customers.⁷⁶

Arbitration

In response to the Commission's recommendation to improve arbitrator training programs and in light of a report issued by the General Accounting Office,⁷⁷ arbitration departments of SROs expanded and improved their arbitrator training programs.⁷⁸

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 NASD arbitration rules that (1) enhance the NASD's ability to discipline members that fail to pay an arbitration award;⁷⁹ (2) make all arbitration awards and their contents public information;⁸⁰ and (3) clarify that employment-related disputes may be arbitrated at the NASD and that arbitration panels deciding discrimination claims will consist of a majority of arbitrators with no ties to the securities industry.⁸¹

The Commission approved other SRO rules designed to enable investors to pursue class actions in courts and clarify discovery procedures for small claim cases.⁸²

SRO Rules on Options and Other Derivative Products

The Commission approved several significant SRO proposals to strengthen market stability and integrity, including extending the use of quarterly expiration Friday auxiliary opening procedures to monthly expiration Fridays on the NYSE.⁸³ In addition, the Commission approved several proposals by the SROs to trade new financial instruments, including the following:

- Standard & Poor's (S&P) 500 Depository Receipts (SPDRs) to trade on the AMEX;⁸⁴
- Flexible Exchange Options, large-size, index options cleared by Options Clearing Corporation and which can be

customized as to strike price, expiration, and settlement procedures to trade on the CBOE and AMEX;⁸⁵

- quarterly expiration index options to trade on the AMEX, CBOE, and NYSE;⁸⁶
- Equity Linked Notes⁸⁷ and Debt Exchangeable for Convertible Securities,⁸⁸ hybrid debt securities whose principal is linked to the performance of a highly capitalized, actively traded common stock;
- Global Telecommunications Market Index Target Term Securities to trade on the NYSE;⁸⁹ and
- options on American Depositary Receipts to trade on the NYSE, AMEX, PSE, CBOE and PHLX.⁹⁰

The Commission also addressed several futures-related matters regarding the Commodity Futures Trading Commission's hybrids and swaps proposals," the designation of certain boards of trade as contract markets for stock Index futures and stock index futures options on certain indexes, and the Chicago Mercantile Exchange's listing for trading on GLOBEX stock index futures and stock index futures options on the S&P 500 Stock Price Index, the MidCap 400 Stock Price Index, and the Russell 2000 Stock Price Index.⁹²

Clearing Agencies

Sixteen clearing agencies were registered with the SEC at year-end. In addition, the Commission extended the temporary registration as a clearing agency for the Government Securities Clearing

Corporation,⁹³ Intermarket Clearing Corporation⁹⁴ Delta Government Options Corporation,⁹⁵ MBS Clearing Corporation,⁹⁶ and Participants Trust Company.⁹⁷

Registered clearing agencies submitted 119 proposed rule changes to the SEC and withdrew 3. The Commission approved 116 proposed rule changes, including the following:

- implementation of the Depository Trust Company's (DTC) Honest Broker Program, which facilitates the liquidation of securities held for DTC participants experiencing financial or operational difficulties;⁹⁸ and
- implementation of National Securities Clearing Corporation's new comparison system for fixed income securities.⁹⁹

Municipal Securities Rulemaking Board

The SEC received 10 new proposed rule changes from the MSRB, A total of 11 new and pending proposed rule changes were approved by the Commission. Of particular note, the Commission approved an amendment to the MSRB's arbitration code to reflect recent amendments to the Uniform Code of Arbitration.¹⁰⁰

Securities Investor Protection Corporation (SIPC)

The SIPC Fund amounted to \$778.4 million on September 30, 1993, an increase of \$64.9 million from September 30, 1992. Further financial support for the SIPC program is available through a \$1 billion confirmed line of credit established by SIPC with a consortium

of banks. In addition, SIPC may borrow up to \$1 billion from the Department of the Treasury, through the SEC.

Inspections of SRO Surveillance and Regulatory Compliance

The staff completed oversight inspections of the advertising programs of NASD, CBOE, and AMEX. The staff also conducted oversight inspections of the NYSE and AMEX, focusing on the sales practice review performed by NYSE Regulatory Review examiners and the sales practice review conducted by AMEX examiners.

The staff completed an inspection of the PHLX Arbitration Department and continued its comprehensive inspection of the arbitration programs administered by the NASD's arbitration department at the NASD. 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 the case management systems, and the role each department played in processing its cases. In addition, consideration was given to whether major rule changes, adopted by the NASD in 1989 and by the PHLX in 1991 in response to Commission concerns regarding the rules and procedures governing SRO-administered arbitration, were successful in improving the documentation and fairness of cases administered by these SROs.

With respect to the PHLX arbitration inspection, the staff recommended that the PHLX establish procedures to improve its efficiency and to provide a more concrete basis for reviewing the PHLX's Arbitration Department by senior management. The

inspection of the NASD arbitration department is still in progress and a report is expected in the near future.

The staff conducted an inspection of AMEX's Emerging Company Marketplace (ECM) as a result of congressional inquiries regarding the screening process undertaken by AMEX for companies seeking to gain listing privileges for their securities on the AMEX's new ECM market. The staff concluded that the AMEX's screening process generally was satisfactory, but indicated that several deficiencies still existed in the administration of the program. The staff's recommendations focused on the AMEX's application of the mandatory quantitative criteria and subjective qualitative criteria of ECM candidates.

The staff also conducted an inspection of the PSE option and equity surveillance, investigatory and disciplinary programs. The staff found that the investigations conducted by the options and equity surveillance departments were timely, thorough, and adequately documented. However, the staff questioned the handling of some enforcement matters because the sanctions stipulated by the PSE's disciplinary committees were not always commensurate with the severity of the violations and may not discourage future violations. An inspection of PHLX equity and foreign currency options, and equity surveillance, investigatory and disciplinary programs conducted in October and November 1992 found these programs to be functioning satisfactorily. The staff made several recommendations to the PHLX regarding certain deficiencies found during the inspection.

The staff conducted an inspection of the surveillance and investigatory programs of the NASD's Market Surveillance Department in November 1992. The staff found that the programs'

procedures were operating effectively and that the NASD had significantly improved its automation and enhanced its surveillance procedures. In December 1992, the staff conducted an inspection of the regulatory programs of the BSE and the settlement and financial monitoring procedures of the Boston Stock Exchange Clearing Corporation (BSECC). Overall, the staff found that the BSE programs for surveillance and investigation were satisfactory, and that the BSE compliance and the BSECC financial surveillance programs were adequate but in need of improvement. An inspection of the CBOE surveillance, investigatory and disciplinary programs for trading violations conducted in February 1993 found these programs to be functioning satisfactorily and that the CBOE had made several improvements since the previous inspection. However, the staff did raise questions regarding the adequacy of staffing levels.

The staff conducted an inspection of the surveillance, investigatory and disciplinary programs for upstairs trading at the NYSE. The staff reviewed the NYSE's automated surveillance systems administered by its Division of Market Surveillance, investigations of member firm trading conducted by its Department of Market Trading Analysis, and disciplinary actions by its Division of Enforcement. The staff found that the NYSE continues to maintain effective programs in each of these areas. In addition, the staff conducted an inspection of the NYSE's Options and Special Product unit's surveillance, investigatory and disciplinary functions for program trading and related intermarket trading strategies. The staff found significant improvement in the NYSE's surveillance and investigatory operations for program trading and that the surveillance and investigatory programs for options trading were functioning adequately.

The regional offices conducted routine oversight inspections of regulatory programs administered by 7 of the NASD's 11 districts. Inspections of NASD district offices included evaluations of districts' broker-dealer examinations, their financial surveillance and formal disciplinary programs, as well as investigations of customer complaints, terminations of registered representatives for cause, and members' notices of disciplinary action. Although the inspections disclosed minor deficiencies involving a variety of issues, overall, the NASD districts conducted effective regulatory programs for member firms.

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 as follows: the AMEX filed 42; the CBOE filed 98; the NYSE filed 172; the PHLX filed 38; the PSE filed 9; the CHX filed 3; the registered clearing agencies, BSE, and CSE filed none; and the NASD filed 703.

[table omitted]

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 1993, the number of SRO filings pursuant to Rule 19h-1 processed by the staff decreased 33 percent, from 79 in 1992 to 53 in 1993. Of the 53 filings, the NASD made 33 and the NYSE

made 20. One application was denied, and the staff declined to take a no-action position in another.

INVESTMENT COMPANIES AND ADVISERS

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 1993 Results

In 1993, the Commission required mutual funds to discuss in their prospectus, or annual report to shareholders, those factors, strategies, and techniques that materially affected fund performance during the most recently completed fiscal year and to provide a line graph comparing a fund's performance to that of an appropriate securities market index. The Commission also permitted closed-end funds to make repurchase offers to their shareholders at net asset value either periodically, pursuant to a fundamental policy, or not more than once every two years, on a discretionary basis. Amendments to Rule 482 under the Securities Act of 1933 (Securities Act), which would allow investors the option of purchasing mutual fund shares directly from special "off-the-page prospectuses" containing order forms, were proposed for public comment.

Concerning the jurisdictional reach of the Investment Advisers Act with respect to foreign investment advisers, the staff stated that it would not recommend enforcement action if foreign affiliates of an adviser that is registered under the Investment Advisers Act gave

investment advice to United States clients through the registered adviser without the foreign affiliates themselves registering under the Investment Advisers Act. With regard to a foreign investment adviser that has registered under the Investment Advisers Act, the staff made clear that it does not interpret the Investment Advisers Act as being applicable to the foreign investment adviser's relationships with its foreign clients so long as they do not involve conduct in the United States, or have effects on United States clients.

Program Overview

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 omitted]

The number of registered investment companies increased by 12 percent during 1993. 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 900 separate portfolios under one investment company registration. The number of portfolios increased by about 13 percent during 1993. In addition, the Commission was responsible for regulating 20,000 investment advisers at the end of 1993, a 23 percent increase since 1989.

Investment Company and Adviser Inspection Program

During 1993, program resources were focused on inspections of funds in the largest 100 investment company complexes, all money

market mutual funds, and investment advisers with assets under management in excess of \$1 billion. The 100 largest investment company complexes managed \$1.6 trillion in assets, which represented 67 percent of total investment company industry assets of \$2.4 trillion. The total assets under management of the over 1,000 money market portfolios were \$562 billion, which represented 23 percent of all investment company assets.

Results Achieved by the Program

The division and regional office staff conducted inspections of funds within the 100 largest investment company complexes as well as limited inspections of 156 smaller complexes and stand-alone funds. These inspections focused on portfolio management activities. Each of the 1,044 money market funds was reviewed for compliance with Rule 2a-7, which specifies the quality and maturity of permissible instruments that may be held by investment companies and requirements for portfolio diversification. The staff inspected 711 investment advisers, of which 181 managed more than \$1 billion. These inspections focused on the portfolio management and trading activities of advisers. As a result of all inspections during 1993, the staff sent 1,073 deficiency letters to registrants requiring that they eliminate violative activities. In 75 inspections where the registrant appeared to be engaged in serious misconduct, the staff referred the inspection results to the enforcement program for further investigation.

Regulatory Policy

Significant Investment Company Developments

The Commission implemented a number of recommendations made by the division in its 1992 report, *Protecting Investors: A Half Century of Investment Company Regulation (Protecting Investors)*.TM In September 1993, the Commission adopted amendments to Rules 10f-3, 17a-7, 17e-1, 17f-4, and 22c-1 under the Investment Company Act to eliminate the requirement that directors of investment companies annually review certain procedures and arrangements, and to require instead that directors make and approve certain changes only when necessary.¹⁰² The amendments are intended to enhance the effectiveness of investment company boards.

Also in September 1993, the Commission adopted amendments to Rule 12d3-1 under the Investment Company Act to simplify the conditions under which registered investment companies are permitted to acquire securities issued by securities-related businesses.¹⁰³ The amendments remove the margin security requirement and the requirement that investment company boards of directors determine whether debt securities of securities-related businesses are investment grade. The amendments will permit registered investment companies to pursue a broader range of investment objectives consistent with shareholder interests.

In April 1993, the Commission adopted Rule 23c-3 under the Investment Company Act to allow closed-end management investment companies to make repurchase offers to their shareholders at net asset value.¹⁶⁴ The repurchase offers may be made either periodically, pursuant to a fundamental policy, or not more frequently than once every two years on a discretionary basis. Periodic repurchase offers will allow investors in closed-end companies a limited opportunity to resell their shares in a manner traditionally available only to shareholders in open-end companies.

Closed-end investment companies making discretionary repurchase offers will be able to do so with an exemption from some of the requirements of the Securities Exchange Act of 1934 (Exchange Act). In a companion release, the Commission also proposed rule amendments under the Securities Act to permit funds that make periodic repurchase offers to offer their stock on a continuous or delayed basis, and to obtain automatic registration effectiveness for additional securities.¹⁰⁵

In March 1993, the Commission proposed for public comment amendments to Rule 482 under the Securities Act to allow investors the option of purchasing mutual fund shares directly from special "off-the-page prospectuses" containing order forms.¹⁰⁶ An "off-the-page prospectus" would be required to contain critical information about the fund and would be subject to various liability provisions under the Securities Act and the Exchange Act. The amendments would give investors in direct marketed funds the same purchasing option that investors now have through commissioned salespersons.

Also in March 1993, the Commission proposed for public comment amendments to Rule 0-5 under the Investment Company Act and to Rule 30-5 to establish an expedited procedure for certain exemptive applications relying on precedent, and to expand the delegated authority of the Director of the Division of Investment Management.¹⁰⁷ The amendments are intended to streamline the review procedure for exemptive applications.

In addition to implementing the recommendations in the *Protecting Investors* report as discussed above, the Commission undertook two other rulemaking initiatives. In August 1993, the Commission adopted Rules 2a19-2 and 2a3-1 under the Investment

Company Act to except general and certain limited partners of limited partnership investment companies from the definitions of "interested person" and "affiliated person," respectively.¹⁰⁸ The new rules enable limited partnership investment companies to register under the Investment Company Act without first obtaining start-up exemptive relief for their general and limited partners.

In July 1993, the Commission proposed for public comment Rule 3a-8 under the Investment Company Act to provide a non-exclusive safe harbor from investment company status for *bona fide* research and development companies meeting certain requirements.¹⁰⁹ The rule would allow eligible companies to invest their cash reserves in securities that present limited investment risk without subjecting the companies to regulation under the Investment Company Act.

Significant Disclosure Program Developments

In April 1993, the Commission adopted amendments to Form N-1A, the registration form used by open-end management investment companies under the Investment Company Act and the Securities Act, and related rules and forms.¹¹⁰ The amendments require a mutual fund to include in its prospectus or, alternatively, its annual report to shareholders: (1) a discussion of those factors, strategies, and techniques that materially affected its performance during its most recently completed fiscal year; and (2) a line graph comparing its performance to that of an appropriate securities market index. The amendments also require a mutual fund to identify its portfolio manager and revise the summary financial information in the prospectus.

In September 1993, the Commission proposed amendments to Rule 485, which, among other things, sets forth standards for the filing of 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,¹¹¹ The proposed revisions would simplify the operation of the current rule and expand the conditions under which post-effective amendments filed by investment companies are permitted to become effective automatically. In addition, insurance company separate accounts would be permitted to use Rule 485, and Rule 486 (the current rule governing post-effective amendments filed by separate accounts) would be rescinded.

Amendments to Form N-2, the registration form used by closed-end investment companies under the Investment Company Act and the Securities Act, became effective on January 1, 1993. The revisions incorporated certain new features not previously included in closed-end fund registration statements, such as disclosure of the identity of the fund's portfolio manager and a tabular presentation of expenses. The revised form also permits, but does not require, closed-end funds to use a simplified, two-part disclosure document, similar to that used by mutual funds registering on Form N-1 A. Approximately one-third of the closed-end registrations filed during 1993 used the new, simplified format. Overall, the number of closed-end offerings increased 44 percent over the previous year. Municipal stock offerings, rights offerings, and funds concentrating in foreign countries were three of the more commonly filed types of closed-end registrations.

Considerable staff time and attention were devoted to new products and methods of distribution and the related disclosure and

policy issues. For example, funds were seeking incrementally greater returns by engaging in the use of derivative and other instruments. These derivatives, and other relatively new financial instruments, presented regulatory and other issues, including how to ensure that they are not used to create excessive leverage, how to elicit meaningful disclosure about their effect on performance, and how they should be reflected in fund financial statements and records. Funds continued to look for ways to tailor their distribution and shareholder services for particular dealers and investors. A new rule issued by the National Association of Securities Dealers (NASD) concerning asset-based sales charges and service fees became effective July 7, 1993 and has had a significant effect on the way these fees are charged, accounted for, and disclosed.

The number of bank proprietary mutual funds increased during the year to a total of over 900 portfolios. Staff concerns about the names used by mutual funds affiliated with banks and the potential confusion by investors of mutual fund shares with insured deposits were communicated to investment companies in two staff letters during 1993.

In 1993, the staff received 1,194 new open-end fund portfolios, 9,345 existing open-end portfolios, 264 new closed-end portfolios, 564 existing closed-end fund portfolios, 2,043 new unit investment trust portfolios, and 12,833 existing unit investment trust portfolios. These figures include portfolios that exist in connection with insurance products.

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 ended June 30, 1993, 1,100 managers filed Form 13F reports, for total holdings in excess of \$2.3 trillion. Under Rule 13f-2T, these managers may elect to file the report on magnetic tape submitted to the SEC's Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system.

Form 13F reports are available to the public at the agency's Public Reference Room promptly after filing. Two tabulations of the information contained in these reports are available for inspection: (1) an alphabetical list of the individual securities showing the number held by the managers reporting the holding; and (2) an alphabetical list of all reporting managers showing the total number of shares of securities held. These tabulations are generally available two weeks after the date on which the reports must be filed.

Significant Insurance Products Developments

The staff devoted considerable effort in developing 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. The new form also will introduce simplified prospectus disclosure and standardized illustrations for use in prospectuses and supplemental sales literature.

In letters to the NASD, the staff set forth its position on the use of fund performance data in advertisements or supplemental sales

literature for variable life insurance (VLI) products.¹¹² The staff stated that, because contract owners cannot obtain the benefit of the underlying fund without incurring the charges assessed at the separate account level, it is misleading for a VLI issuer to show fund performance without also disclosing separate account performance.

Significant Public Utility Holding Company Act Developments

Under congressional direction to adopt rules to protect the domestic public utility subsidiaries of registered holding companies and their consumers from the risk of new ventures in exempt wholesale generators (EWGs) or foreign utility companies, the Commission adopted Rules 53, 54 and 57 under the Holding Company Act¹¹³ Rule 53 creates a partial safe harbor with respect to the issue and sale of a security by a registered holding company to finance the acquisition of an EWG, or the guaranty by the parent of the securities of an EWG. Rule 54 provides that, in determining whether to approve the issue or sale of a security by a registered holding company for purposes other than the acquisition of an EWG or a foreign utility company, or other transactions by such registered holding company or its subsidiaries other than with respect to EWGs or foreign utility companies, the Commission will not consider the effect of the capitalization or earnings of any EWG or foreign utility company subsidiary on a registered system if the conditions of the safe harbor under Rule 53 are satisfied. Rule 57 and Forms U-57 and U-33-S address notification and reporting requirements for foreign utility companies and their associate public utility companies. The Commission also amended Forms U5S and U-3A-2 to add reporting requirements concerning EWG and foreign utility company activities. The Commission decided to defer action on proposed Rules 55 and

56, regarding foreign utility companies, pending further consideration.¹¹⁴

In view of the Energy Policy Act of 1992, the new legislation concerning EWGs and foreign utility companies, the Commission also proposed an amendment to Rule 87 under the Holding Company Act,¹¹⁵ The present rule allows subsidiaries of a registered holding company, subject to compliance with certain requirements, to perform services for associate non-utility companies without the need to apply for, or obtain, prior Commission approval. The proposed amendment would specifically exclude services rendered to EWGs and foreign utility companies. The Commission believes the amendment is necessary to ensure that utility personnel are not improperly diverted to EWG or foreign utility company activities, to the detriment of the operations of the integrated public utility system.

As of September 30, 1993, 14 public utility holding company systems were registered with the SEC. The 14 registered systems were comprised of 93 public utility subsidiaries, 158 non-utility subsidiaries, and 33 inactive companies, for a total of 298 companies and systems operating in 26 states. These holding-company systems had aggregate assets of approximately \$111.2 billion as of June 30, 1993, an increase of \$12.1 billion over September 30, 1992. Total operating revenues for the 12 months ended June 30, 1993 were approximately \$40.2 billion, a \$2.1 billion increase from the 12 months ended September 30, 1992.

During 1993, the SEC authorized registered holding-company systems to issue \$4.0 billion in short-term debt, \$3.3 billion in long-term debt, and \$712.6 million in common and preferred stock. Long-term debt authorization decreased by over \$5 billion in 1993 from the

previous fiscal year, as a result of an increase in the amount of internally generated cash available, a decrease in construction expenditures, a decrease in interest rate charges, and the continued effects of Rule 52, which exempts certain financings by public utility subsidiary companies, if solely for the purpose of financing the business of the public utility company and expressly authorized by the relevant state commission. The SEC approved pollution control financings of \$1.4 billion, an increase of 424 percent over fiscal year 1992. Refinancings, made in order to capture substantial reductions in interest rates, were the primary cause of the increase in these financings over 1992. The SEC approved \$409 million of investments in cogeneration facilities that were "qualifying facilities" under the Public Utility Regulatory Policies Act of 1978 and rules thereunder. The SEC also approved \$114.5 million of investments in EWGs and foreign utility companies/ and \$65.1 million in enterprises engaged in demand-side and energy management. Total financing authorizations of approximately \$10.1 billion represented an approximately 42 percent decrease over such authorizations in 1992.

The SEC examines service and special purpose subsidiary companies of registered holding company systems. During 1993, seven examinations were completed, six of special purpose corporations and one of a service company. The SEC 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 agency's activities during 1993 resulted in savings to consumers of approximately \$8.7 million.

Two bills were introduced in 1993 that would transfer the administration of the Holding Company Act from the SEC to the Federal Energy Regulatory Commission. The two bills, S. 544 and S. 635, which contain substantially the same language, would also amend the Holding Company Act and the Federal Power Act to address concerns arising from the decision in *Ohio Power Co. v. FERC*.¹¹⁶ Among other things, the bills amend Sections 13(b) and 13(d) of the Holding Company Act by substituting "at a price not to exceed cost" for the current "at cost" language.

The Commission submitted written testimony regarding S. 544 on May 25, 1993. In its testimony, the Commission explained its understanding of the implications of the *Ohio Power* decision and expressed its willingness to provide further assistance to the Senate Committee on Energy and Natural Resources. In addition, the Commission stated that the pricing of the coal purchased by Ohio Power from a captive coal subsidiary is the subject of a request for investigation filed by the municipal wholesale electric customers of Ohio Power.

Significant Applications and Interpretations

Investment Company Act Matters

The Commission issued an order under Section 3(b)(2) of the Investment Company Act declaring that ICOS Corporation (ICOS), a research and development company, is engaged primarily in a business other than that of investing, reinvesting, owning, holding, or trading in securities.¹¹⁷ Because virtually all of ICOS' capital is invested in securities pending its use in funding the company's research and development programs, a question arose whether ICOS

is an investment company under Section 3(a). Under the Commission's traditional Section 3(b)(2) analysis, an issuer generally is deemed to be engaged primarily in the business of investing in securities if most of its assets are securities and most of its income is derived from such securities. Given the unique nature of research and development companies, the Commission determined that it was appropriate to modify the analysis for determining the primary business of such companies. If a company demonstrates that it is engaged actively in *bona fide* research and development activities, the Commission will consider the use, rather than simply the composition, of the company's assets and income. Under this revised analysis, ICOS qualified for a Section 3(b)(2) order.

The Commission issued a conditional order under Section 17(d) of, and Rule 17d-1 under, the Investment Company Act to the Fidelity family of funds amending a prior order that allowed the funds to invest jointly in repurchase agreements with maturities of seven days or less.¹¹⁸ By investing jointly, the funds reduce transaction fees and ticket errors, receive higher rates of return, and avoid the administrative time and expense of investing in many small repurchase agreements. To expand the savings and the potential for enhanced yield, the new order allows joint investment in repurchase agreements with maturities of up to sixty days, and in certain short-term money market instruments and tax-exempt obligations. The new order also allows certain non-investment company entities associated with Fidelity to participate in the joint investments.

The Commission issued a conditional order to allow certain open-end investment companies (Public Funds) advised by American Capital Assets Management to invest in a specially created investment company—the American Capital Small Capitalization

Fund (Small Cap Fund).¹¹⁹ The Small Cap Fund is intended to serve as an efficient way for the Public Funds to invest in small capitalization stocks and also achieve further diversification. Most significantly, the order provides an exemption from Section 12(d)(1) of the Investment Company Act, which limits an investment company's ability to invest in the securities of other investment companies. Section 12(d)(1) is designed to protect investors in fund holding companies from two layers of expenses and to prevent fund holding companies from exercising undue influence over portfolio investment companies by the threat of large scale redemptions. To address these concerns, the order requires that the Small Cap Fund not charge an advisory fee or a sales charge, and that American Capital Asset Management, as adviser to the Public Funds and the Small Cap Fund, develop procedures to prevent large scale redemptions from disrupting the Small Cap Fund.

The staff continued to receive and respond to requests for no-action relief involving the status of foreign entities as eligible foreign custodians under the Investment Company Act. In twelve no-action letters under Section 17(f) and Rule 17f-5, the staff stated that it would not recommend enforcement action if various entities acted as eligible foreign custodians for registered investment companies. Ten of the letters involved foreign securities depositories or clearing agencies seeking assurances concerning their status as an operator of "the central system for the handling of securities or equivalent book-entries" in a particular country under subparagraph (c)(2)(iii) of the rule.¹²⁰ Two of the letters involved foreign banks and their ability to satisfy the shareholders' equity requirement in subparagraph (c)(2)(i) of the rule.¹²¹

The staff stated that it would not recommend enforcement action under Section 18(f)(1) of the Investment Company Act if mutual funds borrowed from certain foreign banks that conduct banking activities in the United States. While Section 18(f)(1) permits a mutual fund to borrow from a bank, foreign banking institutions generally do not fall within the Investment Company Act's definition of bank. The relief was limited to treating these foreign banks as banks for purposes of Section 18(f)(1), not for any other purpose under the Investment Company Act.¹²²

The staff granted conditional no-action relief to a foreign investment company that proposed to register with the Commission under the Investment Company Act without first conforming its capital structure to the requirements of Section 18 of the Act. The foreign company had long-term warrants outstanding. Section 18(d) of the Investment Company Act prohibits a registered closed-end fund from issuing warrants unless they expire within 120 days of issuance. The staff agreed that Section 18 does not require the company to conform its preregistration capital structure, but conditioned the relief on the warrants being listed on a United States stock exchange, so that members of the public would be aware of their existence before purchasing common stock that was subject to dilution.¹²³

The staff stated that it would not take enforcement action if a mutual fund treated an investment in municipal bonds refunded with escrowed United States Government securities as an investment in United States Government securities for purposes of Section 5(b)(1) of the Investment Company Act. Section 5(b)(1) limits the extent to which a diversified investment company may invest in any one issuer, but excludes from this limit investments in United States Government securities.¹²⁴

The staff declined to grant no-action assurance under Section 17(e) of the Investment Company Act to permit a fund's custodian, which was also a sub-adviser to one of the fund's portfolios, to enter into a securities lending arrangement with some of the other portfolios of the fund (Portfolios). Section 17(e)(1) makes it unlawful for any affiliated person of an investment company, or any affiliated person of such person (second-tier affiliate), acting as agent, to accept any compensation from any source for the purchase or sale of any property to or for the investment company. Since the Portfolios and the portfolio for which the custodian served as sub-adviser were under common control, the custodian was a second-tier affiliate of the Portfolios. In denying relief, the staff stated that where a second-tier affiliate of an investment company negotiates and accepts a fee for arranging a loan of a fund's securities, the transaction presents the potential for a conflict of interest that Section 17(e) was designed to address. The staff took the position that a loan of a Portfolio's securities involves a sale of property of a Portfolio for purposes of Section 17(e).¹²⁵

The staff granted no-action relief to a transfer agent that proposed to store on an optical disk system certain investment company records, in a manner consistent with the requirements of Rule 31a-2(f) under the Investment Company Act. Rule 31a-2(f) permits records to be maintained and preserved on magnetic tape, disk or other computer storage medium. The staff required that the information be stored on a non-rewritable, non-erasable optical disk, and that adequate backup copies be maintained.¹²⁶

Investment Advisers Act Matters

The 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 affiliates gave investment advice to United States clients through a United States registered adviser, without the foreign affiliates themselves having to register under the Investment Advisers Act.¹²⁷ The staff's response permits a United States registered adviser to draw on the personnel and expertise of its multinational affiliates as long as the persons and entities providing advice consent to United States jurisdiction, are under the supervision of the registered entity, and maintain certain records. In addition, the staff granted no-action relief to certain foreign advisers to permit them to give advice directly to United States clients without subjecting the foreign advisers' relationships with their foreign clients to the Investment Advisers Act.¹²⁸ The staff's response makes clear that a registered foreign adviser's relationships with foreign clients would not be subject to the Investment Advisers Act so long as its acts do not involve conduct, or have effects, in the United States, or have effects on United States clients. This position allows multinational advisory complexes to register under the Investment Advisers Act and give advice directly to United States persons without having the Investment Advisers Act apply with respect to the foreign adviser's foreign clients.

Insurance Company Matters

The Commission issued an exemptive order permitting the College Retirement Equities Fund (CREF) to invest in the College Credit Trust (Trust).¹²⁹ The Trust was created by the Teachers Insurance and Annuity Association of America (TIAA) and the College Entrance Examination Board to make educational loans, most of

which will be guaranteed student loans. The Student Loan Marketing Association will administer the Trust and the loans, and provide related services. The order permits certain transactions between TIAA and CREF by which CREF would acquire an interest in the Trust directly or indirectly from TIAA. Hearing requests were received by the Commission during the notice period. The issues raised in the hearing requests, however, did not bear on the determination of whether to grant the requested relief under the Investment Company Act. The requests, therefore, were denied by the Commission.

The division, pursuant to delegated authority, issued three exemptive orders under the Investment Company Act permitting certain variable life insurance issuers to deduct a charge related to tax changes in the Omnibus Budget Reconciliation Act of 1990 (Budget Act).¹³⁰ The Budget Act requires insurance companies to capitalize and amortize certain policy acquisition expenses over a ten year period rather than continuing to deduct these expenses in the year in which they are incurred. Applicants obtained relief to deduct a charge to recover the increased expense associated with the new tax treatment.

The division, pursuant to delegated authority, exempted an insurance company from various sections of the Investment Company Act to permit the sale of certain variable annuities with an asset allocation feature.¹³¹ In general, holders of these annuities will receive asset allocation advice from an investment adviser unaffiliated with the insurance company. The adviser will be compensated by deducting a charge from the assets of the separate account funding the contracts.

The staff stated that it would not recommend enforcement action to the Commission if, without first obtaining an exemptive order, an insurance company collected an asset allocation fee from investors in certain variable annuity contracts through the periodic cancellation of units attributable to an investor's participation in a unit investment trust.¹³² The staff's response noted, among other things, that a variable annuity holder would receive advice as to allocating his or her contract values among the separate account's various subaccounts only if he or she affirmatively opted for that service. The staff noted, however, that a mandatory fee deducted in this manner would require an exemptive order because the fee would be indistinguishable from an asset-based fee under Section 26 of the Investment Company Act.

The staff declined to grant no-action assurance in connection with proposals by two insurance companies to legally segregate the assets of non-unitized separate accounts used in connection with the offer and sale of certain market value adjustment annuity contracts (MVA Contracts) without registering the separate accounts under the Investment Company Act.¹³³ The staff took the position that legally insulated non-unitized separate accounts that support liabilities under MVA Contracts are issuers for purposes of Section 3(a) of the Investment Company Act, and possibly investment companies.

Holding Company Act Matters

The Commission authorized Entergy Corporation (Entergy), a registered holding company, and Entergy Enterprises, Inc. (Enterprises), its wholly owned non-utility subsidiary company, to organize and acquire a new wholly owned non-utility subsidiary of Enterprises (NEWCO) which provides energy management services

to commercial, industrial and institutional customers.¹³⁴ NEWCO would acquire 9.95 percent of Systems and Service International, Inc., a closely-held company whose principal product to date is a monitoring device anticipated to improve the efficiency of fluorescent lighting fixtures by up to 50 percent. State and local regulators initially had intervened in the matter in opposition to SEC authorization of the transaction, arguing that consumers would not be protected from the detrimental effects, if any, of the proposed activities. AH but one of the intervenors subsequently withdrew their interventions pursuant to a settlement agreement with Entergy. The withdrawal of the interventions was contingent upon the SEC's incorporation in its order of certain conditions designed to insulate core utility operations from the unregulated businesses. The Commission denied the request for a hearing by the remaining intervenor, Louisiana Public Service Commission, on the grounds that the transaction presented no dangers to consumers and that NEWCO's provision of energy services was an appropriate non-utility business under the Holding Company Act that would primarily serve the integrated public utility system.

The Commission authorized The Columbia Gas System, Inc. (Columbia), a registered holding company and a debtor-in-possession under Chapter 11 of the Bankruptcy Code, to engage in intrasystem financing with its subsidiaries. Columbia and its wholly owned subsidiary company, Columbia Gas Transmission Corporation (Transmission), filed for protection with the Bankruptcy Court for the District of Delaware on July 31, 1991, after financial difficulties relating to the obligations of Transmission under certain "take or pay" gas purchase contracts.¹³⁵ Prior to the filing by Columbia of a plan of reorganization, the bankruptcy court authorized Columbia to continue the financing of its non-debtor subsidiaries "in the ordinary course of

business [as] ... necessary to maintain business operations/' subject to approval of the Commission. The Commission found that sufficient cash and income was available for Columbia and the lenders to the Columbia money pool to make the proposed investments, and for the subsidiary companies to service the proposed debt, subject to certain reservations of jurisdiction.¹³⁶

The Commission considered a proposal by Entergy Corporation, a registered holding company, to acquire Gulf States Utilities Company (Gulf States) in a stock and cash exchange valued at approximately \$2.3 billion.¹³⁷ Entergy has four public utility subsidiaries that provide retail electric service to approximately 1.7 million customers in an approximately 45,000 square-mile area in Arkansas, Louisiana, and Mississippi. Gulf States is a public utility company that provides retail electric service to approximately 583,000 customers in a 28,000 square-mile area in southeast Texas and central Louisiana. In addition to its principal electric business, Gulf States distributes natural gas at retail to approximately 84,000 customers in the Baton Rouge area. State regulators, consumer groups and business competitors have intervened in the matter and have requested a hearing, arguing that the purchase price is excessive, the acquisition will not result in benefits to the utility systems, and that the merger could have anticompetitive effects.

The Commission issued orders authorizing registered holding companies to invest in demand-side and energy management. Demand-side and energy management are measures that, among other things, enable utility customers to use energy more efficiently. The Commission authorized HEC Inc., a subsidiary company of Northeast Utilities, a registered holding company, to expand the types of demand-side and energy management services it provides, and to

provide consulting services without limitation.¹³⁸ The Commission authorized American Electric Power Company, Inc., a registered holding company/ to provide, through a subsidiary, additional funding to Intersource Technologies, Inc., which is developing electronic light bulb technology and new lighting products that are anticipated to use substantially less electricity and have substantially longer lives than traditional light bulbs.¹³⁹ The Commission also authorized Arkansas Power & Light Co., an electric public utility subsidiary company of Entergy Corporation, a registered holding company, to institute a demand-side management program for its customers.¹⁴⁰

The Commission authorized Utilil Corporation, a registered holding company, to create a new subsidiary company that would engage in consulting services to non-associate companies on a variety of energy related matters, including serving as brokering agent for electric power and serving as purchasing agent for a utility or other bulk power purchaser.¹⁴¹

The Commission authorized Eastern Utilities Associates (EUA) and certain of its subsidiaries to engage in transactions under a settlement agreement with bondholders of EUA Power Corporation (EUA Power), a wholly owned subsidiary of EUA.¹⁴² EUA Power filed for protection under Chapter 11 of the United States Bankruptcy Code on February 28, 1991, in the Bankruptcy Court for the District of New Hampshire and has since been operating its business as a debtor-in-possession. Under the settlement agreement, EUA Power would redeem its outstanding shares of common and preferred stock from EUA, after which EUA Power would be a standalone company.

The Commission granted an exemption under Section 3(a)(5) to National Power Company, a closely-held California corporation, and

an exemption under Section 3(b) to Power Barge Impedance, L.P. (Partnership), a California limited partnership.¹⁴³ The Partnership would own and operate a 28-mega watt barge-mounted electric generating plant. The barge will operate and sell power exclusively outside of the United States, primarily to foreign countries or U.S. territories or possessions in Latin America, Central America, and the Caribbean, which may be experiencing seasonal power shortages.

FULL DISCLOSURE SYSTEM

The full disclosure system is administered by the Division of Corporation Finance (Division). 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 1993 Results

The decline in interest rates, the burgeoning need for capital for businesses, small and large, and investor demand helped to fuel a record level of offerings filed for registration in 1993. More than \$868 billion in securities were filed for registration, including over \$112 billion of initial public offerings, equity and debt, and over \$46 billion by foreign companies.

Foreign companies' participation in the United States markets continued to show dramatic growth in 1993. In addition to a record high level of offerings filed for registration, 88 foreign companies from 21 countries, including Daimler Benz, Shanghai Petrochemical, Corporacion Bancaria de Espana ("Argentaria"), Venezuelan Petroleum Inc. and YPF, Inc., entered the United States public market for the first time. At year-end, there were more than 550 foreign companies from 40 countries filing reports with the SEC.

[table omitted]

The 1993 proxy season was the first in which companies were subject to the Commission's new executive compensation disclosure rules. The Division undertook a special review of approximately 1,000 proxy statements to evaluate compliance with the new rules and, on the basis of that review, the Commission published a release providing further disclosure guidance and proposing several refinements to the rules. Those refinements were adopted in November 1993 in time to be effective for the 1994 proxy season.

Early in 1993, the Commission implemented initiatives to facilitate capital raising and the securitization of assets. Those initiatives included expansion of short form and shelf registration to an estimated additional 450 reporting companies and the introduction of unallocated shelf registration. Unallocated shelf registration, intended to facilitate equity offerings, allows eligible companies to file one registration statement covering the sale of all the company's securities without requiring a specific allocation among classes of securities. More than \$66 billion of securities were registered on an unallocated shelf basis in 1993.

A streamlined transitional disclosure system for small business issuers first entering the Commission's disclosure system was added to the Commission's new integrated disclosure system for small business issuers. In the first 14 months of the new small business disclosure system, 335 registration statements covering over \$4 billion worth of securities were filed. In addition, during the first full year under the new rules 78 Regulation A filings were made, covering a total of approximately \$206 million in securities, an increase of approximately 5 times the amount of Regulation A offerings filed in the same period prior to the new rules.

The Commission proposed to expand the multijurisdictional disclosure system (MJDS) for Canadian issuers by decreasing the size of companies eligible to participate and recognizing investment grade ratings by Canadian securities rating organizations. More than \$10 billion in MJDS offerings have been filed with the SEC since the introduction of the process in 1991.

Review of Filings

The staff conducted a record 3,474 reporting issuer reviews. The reporting issuer reviews were accomplished through the full review of 1,218 registration statements and post-effective amendments to registration statements filed under the Securities Act; 1,826 annual and subsequent periodic reports; 149 merger and going private proxy statements; and 1,155 full financial reviews of annual reports. The number of documents reviewed exceeded the number of reporting issuer reviews because in many cases more than one document filed by the same issuer received a full review during the year.

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 omitted]

Rulemaking, Interpretive, and Legislative Matters

Executive Compensation

In 1992, the Commission adopted amendments to its proxy rules to make executive compensation disclosure clearer, more concise/ and more useful to shareholders.¹⁴⁴ Specific provisions were made for small businesses to minimize costs of compliance with the disclosure requirements where consistent with shareholder interests.

Based on the review of approximately 1,000 proxy statements, the Commission issued a release reporting on the first year's experience with the new compensation rules.¹⁴⁵ In the release, the Commission identified common issuer mistakes in complying with the new rules and discussed several questions of general application. In addition, the requirements of the compensation committee report were reviewed using examples drawn from actual filings. The Commission also proposed for comment several refining and technical amendments to the executive compensation rules. These amendments would (1) expand the persons covered by the rules to include chief executive officers and top paid executive officers who left the company during the year, (2) require disclosure of the assumptions underlying any option values reported, (3) require disclosure of the named executive officers' restricted stock holdings, and (4) change the weighting of any issuer constructed peer group from the end to the beginning of the measurement period. The proposals were adopted in November 1993.

Simplification of Registration Procedures for Primary Securities Offerings

The Commission adopted amendments to Form S-3 to expand the class of issuers eligible to use short-form registration and primary delayed shelf offerings pursuant to Rule 415.¹⁴⁶ The amendments shortened the minimum issuer reporting period from 36 to 12 months

for offerings of non-asset backed securities, reduced the public float requirement for primary offerings of non-investment grade securities from \$150 million to \$75 million, and eliminated the trading volume test. Investment grade asset-backed securities, including small business loans, are now eligible for shelf registration on Form S-3 regardless of the issuer's reporting history. Additional amendments provide for same-day, automatic effectiveness of dividend or interest reinvestment plan registration statements and permit changes in the offering price and decreases in the amount of the securities to be reflected after effectiveness without the need to file a post-effective amendment if the changes would not materially change the disclosure in the registration statement at effectiveness.

The amendments also permit registration of debt/equity and other securities on a single shelf registration statement, without having to specify the amount of each class of securities to be offered. Since these amendments were adopted in October 1992, there have been 85 unallocated shelf registration statements filed/ registering a total of approximately \$64 billion in securities.

Multijurisdictional Disclosure System

The Commission proposed amendments to the MJDS to amend the eligibility requirements for use of Forms F-9, F-10 and 40-F to shorten the reporting history requirement from 36 months to 12 months/ to eliminate the market capitalization requirements under such forms and to change the minimum public float requirement to U.S. \$75 million.¹⁴⁷ The Commission also proposed amendments to Form F-9 that would recognize investment grade ratings by those rating organizations which are accepted by Canadian securities regulators in addition to those which are accepted under the SEC's

rules. The Commission also adopted amendments to Forms F-10 and 40-F in order to continue the requirement that financial statements included in filings on such forms include a reconciliation to U.S. generally accepted accounting principles,¹⁴⁸

Survey of Financial Statement Reconciliations by Foreign Registrants

The Division conducted a survey of the reconciliations included in the filed reports of 528 foreign companies. Subsequently, a report analyzing the nature and size of the reconciling items by home country of the foreign companies was prepared and issued on May 1, 1993.

Blank Check Offerings

The Commission proposed to revise the "penny stock" definition for purposes of its rules relating to the registration statements filed by blank check companies under the Securities Act¹⁴⁹ The proposal would make the exclusion from the penny stock definition for securities priced at \$5 or more inapplicable to securities offerings subject to Section 7(b) of the Securities Act and Rule 419. The rule was effective on October 29, 1993.

Trust Indenture Act

The Commission adopted amendments to Rules 4d-9 and 10a-5 under the Trust Indenture Act of 1940 that rescinded the exclusion of British Columbia trust indentures and trust companies from exemptions presently available in MJDS offerings of debt securities.¹⁵⁰ Pursuant to Rule 4d-9, as amended, a British Columbia obligor may offer its debt securities in a MJDS offering pursuant to a

trust indenture that complies with the Company Act of British Columbia (Company Act). Further, the amendments to Rule 10a-5 generally permit any Canadian trust company, including those regulated under the Company Act, to act as sole trustee. The amendments followed amendment of the Company Act and issuance of a contemporaneous "blanket order" exempting United States obligors from the requirements of the Company Act, including the residency requirement for institutional trustees, by the British Columbia Securities Commission.

Section 16

The Commission extended the phase-in period for compliance with the substantive conditions of new Rule 16b-3 regarding employee benefit plan transactions under the Exchange Act pending further notice and rulemaking under that provision.¹⁵¹ The phase-in period was extended until September 1, 1994, or such earlier date as set in further rulemaking under Section 16.

Additional Small Business Initiatives

In response to favorable comment on its small business initiatives and the use of the question-and-answer disclosure format, the Commission adopted revisions to the rules and forms under the Securities Act and the Exchange Act to provide a transitional disclosure system for small business issuers first entering the reporting system.¹⁵² This system allows small business issuers to make the transition from non-reporting to reporting status using the Regulation A disclosure format, with the added requirement of audited financial statements. The transitional disclosure forms may be used for registering offerings of up to \$10 million under the

Securities Act and for registration and reporting under the Exchange Act, The transitional system includes: (1) new Securities Act registration statement Form SB-1; (2) modified disclosure formats in periodic report Exchange Act Forms 10-QSB, 10-KSB and 10-SB; (3) modified disclosure formats for annual reports to shareholders and proxy and information statements; and (4) a provision for graduating from the transitional disclosure forms if more than \$10 million is raised in any continuous 12-month period or a non-transitional disclosure form (other than for proxy purposes) is used.

The Commission also adopted two changes to the financial statement requirements for small business issuers. These revisions provide an automatic waiver of the audited financial statements requirements with respect to specified business acquisitions where such financial statements are not otherwise available. The revisions also permit small business initial public offerings to use the same rule as reporting companies in determining whether they may use prior year's audited financial statements in the 90 days following the end of the fiscal year,

The Commission adopted revisions to the non-financial statement disclosure requirements of Regulation D which base those requirements upon both the offering amount and the issuer's eligibility for the small business issuer disclosure system. In addition, the Regulation A "test-the-waters" procedure was amended to exclude a "test-the-waters" document that complies with applicable requirements from the definition of prospectus.

Electronic Data Gathering Analysis and Retrieval System

The Commission adopted rules and amendments to implement the operational phase of the EDGAR system, through which most filings and related correspondence are to be submitted electronically.¹⁵³ The Commission also published a list identifying approximately 14,000 companies whose filings are processed by the Division that will become subject to the electronic filing requirements over a three-year period, together with their respective phase-in dates. The first mandated electronic filings were received on April 26, 1993. At the end of 1993, approximately 925 non-investment company issuers had become EDGAR filers. Phase-in of the remaining issuers is expected to be completed by mid-1996.

Conferences

SEC Government-Business Forum on Small Business Capital Formation

The twelfth annual SEC Government-Business Forum on Small Business Capital Formation was held in Washington/ D.C. on September 9 and 10, 1993. 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 setting forth a list of recommendations for legislative and regulatory changes approved by the forum participants was prepared and provided to interested persons, including Congress and regulatory agencies.

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

On April 26, 1993, approximately 60 SEC senior officials met with approximately 60 representatives of the North American Securities Administrators Association in Washington, D.C. 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.

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:

- *rulemaking and interpretations that supplement 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 1993 Results

The Commission continued its involvement in initiatives directed toward reducing differences in accounting and auditing standards that currently exist between countries. During 1993, significant progress was achieved by international accounting standard-setting bodies toward the acceptance of cash flow statements prepared in accordance with International Accounting Standard 7 (IAS 7). In November 1993, the Commission proposed a rule for comment that would not require a reconciliation of a cash flow statement prepared in accordance with IAS 7 to United States standards. This was the first time that the Commission proposed accepting 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.

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Loss Contingencies. The staff issued interpretive guidance regarding the appropriate accounting and disclosures relating to loss contingencies.¹⁵⁴ The guidance was issued to narrow diversity in

practice among public companies of reporting the effects of significant loss contingencies such as environmental liabilities.

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 financial accounting and reporting, including the need to respond to various regulatory, legislative, and business changes in a timely 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 intends to consider the current reporting requirements under *Statement of Financial Accounting Standards No. 14*, "Financial Reporting for Segments of a Business Enterprise." This effort has been undertaken jointly with the Accounting Standards Board of the Canadian Institute of Chartered Accountants (CICA). An invitation to comment was issued in May 1993 as part of the first phase of a standard-setting project that will seek to develop common standards on disaggregated disclosures. As a result of an FASB Research Report issued in February 1993 and CICA Research Study published in August 1992,

an invitation to comment was issued in May 1993 as part of the first phase of a standard-setting project. This standard-setting project will seek to develop common standards on disaggregated disclosures.

The FASB adopted a final standard to establish the appropriate accounting for certain investments in debt and equity securities.¹⁵⁵ Under the final standard, debt securities for which an entity has the positive intent and ability to hold until maturity should be classified as being *held to maturity* and reported at amortized cost. Debt and equity securities held for current resale are to be classified as *trading securities* and reported at fair value with unrealized gains and losses included in earnings. Other debt and equity securities should be classified as *securities available for sale* and reported at fair value, with unrealized gains and losses shown as a separate component of shareholders' equity. The new FASB standard is effective for fiscal years beginning after December 15, 1993.

The new standard is part of a larger FASB project initiated at the Commission's request in 1985 to address accounting for financial instruments. This project will ultimately address the comprehensive use of market value accounting for all securities and other financial instruments and related liabilities. The project is continuing, and the FASB is considering whether certain liabilities should also be marked to market.

The FASB adopted a final standard on accounting for loan impairment by creditors.¹⁵⁶ Under its provisions, a loss on impairment of a loan should be recognized when it is probable that a creditor will be unable to collect all principal and interest when due under the terms of the loan agreement.

The FASB issued an exposure draft (ED) requesting public comment on a proposed standard on accounting for stock compensation.¹⁵⁷ 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 expires on December 31, 1993. Public hearings are scheduled for early 1994 and a field test will be conducted.

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 closely with the ASB to enhance the effectiveness of the audit process. The ASB adopted a revised auditing standard that, among other things, governs the availability of comfort letters, which are provided to underwriters in relation to the underwriters' due diligence reviews pertaining to securities offerings.¹⁵⁸ The standard as adopted was responsive to the staffs concern that such letters continue to be available in private securities' offerings. The ASB also issued a series of annual Audit Risk Alerts to provide auditors with an overview of recent economic, professional, and regulatory developments that may affect 1993 year-end audits.

SECPS. The SECPS, through its Peer Review Committee and Quality Control Inquiry Committee (QCIC), administers two programs that are designed to ensure that financial statements of SEC registrants are audited by accounting firms with adequate quality control systems, A peer review of member firms by other accountants is required every three years and the QCIC reviews, on a timely basis, the quality control implications of litigation against member firms that involves public clients.

The SECPS peer review and QCIC programs are monitored by the Public Oversight Board (FOB), which is independent of the AICPA (except for funding). The SEC continued its oversight of the activities of the SECPS during 1993. 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 reviewed closed-case summaries of the QCIC and related POB files. This review and discussions with the POB staff provide the staff with enough information to allow the staff to conclude that the QCIC process provides added assurances, as a supplement to the SECPS 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. The Commission understands that improvements suggested by the SEC staff have been implemented by the QCIC and the FOB, and believes that such ongoing improvements will provide greater assurance of the efficacy of the QCIC.

AcSEC. The AcSEC issued three separate statements of position on accounting issues unique to investment companies.¹⁵⁹ The AcSEC also substantially completed statements of position on (1) the appropriate treatment of operating results relating to foreclosed assets, (2) the appropriate accounting for advertising costs, and (3) revisions to the existing guidance on accounting for employee stock ownership plans. Also, the AcSEC solicited public comment on a proposal calling for enhanced disclosures about risks and uncertainties by entities generally.¹⁶⁶

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. For example, the staff worked with the IASC to reduce accounting alternatives as an initial movement toward appropriate international accounting standards. The SEC staff also monitored the IASC's projects to address issues relating to the extent of implementation guidance, adequacy of disclosure requirements, and the completeness of international accounting standards. In November 1993, the IASC adopted a package of ten standards constituting its project on comparability and improvements.¹⁶¹

In August 1993, the IOSCO Working Party on Disclosures and Accounting informed the IASC that the IOSCO Technical Committee would recommend that IOSCO endorse IAS 7 (revised 1992), Cash Flow Statements, for use in cross-border offerings and listings. Subsequently, the IOSCO Presidents Committee recommended that IOSCO members take all steps that are necessary and appropriate in their respective home jurisdictions to accept cash flow statements prepared in accordance with IAS 7, as amended, as one alternative to statements prepared in accordance with their domestic accounting standards relating to cash flow statements in connection with cross-border offerings and continuous reporting by foreign issuers. In November 1993, the Commission proposed a rule for comment that would not require a reconciliation of a cash flow statement prepared in accordance with IAS 7 to U.S. standards.¹⁶² The Working Party also 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.

The staff also continued working with the International Federation of Accountants (IFAC) to revise International Standards

on Auditing (ISA). Auditors in different countries are subject to different independence standards, perform different procedures, gather varying amounts of evidence to support their conclusions, and report the results of their work differently. The staff, as part of an IOSCO working group, worked closely with IFAC to expand and revise ISAs to narrow these differences, and significant progress was made. Most notable was the issuance of a final standard addressing an auditor's responsibilities when a client is suspected of committing an illegal act.¹⁶³

OTHER LITIGATION AND LEGAL ACTIVITIES

The General Counsel represents the SEC in all litigation in the United States Supreme Court and the courts of appeals. The General Counsel defends the Commission and its employees when sued in district courts, prosecutes administrative disciplinary proceedings against certain securities professionals, 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 serves as the Commission's principal legal adviser on issues arising from all of its regulatory and enforcement activities. The General Counsel analyzes legislation that would amend the federal securities laws, drafts congressional testimony, and prepares legislative comments. In addition, the General Counsel advises the Commission in administrative proceedings under various statutes.

Key 1993 Results

Issues of major importance were litigated by the Commission in 1993. As urged by the Commission in an *amicus curiae* brief, the U.S. Supreme Court recognized the right of contribution in private actions brought under the Securities and Exchange Act of 1934 (Exchange Act) Section 10(b) and Commission Rule 10b-5 in *Musick, Peeler & Garrett v. Employers Insurance of Waussaw*.¹⁶⁴ In *Central Bank of Denver v. First Interstate Bank of Denver*,¹⁶⁵ the Commission filed an *amicus curiae* brief urging the U.S. Supreme Court to hold that there is an implied private right of action for aiding and abetting violations of Section 10(b) and Rule 10b-5, In *SEC v. Rind*,^{*66} the Court of

Appeals for the Ninth Circuit agreed with the Commission that no statute of limitations binds Commission enforcement actions.

Significant progress was made in the adjudicatory program. The staff submitted to the Commission a record 64 draft opinions, a 23 percent increase from 1992. Moreover, the number of opinions issued by the Commission increased by 69 percent over 1992, from 48 to 81. The task force on administrative proceedings issued its report, *Fair and Efficient Administrative Proceedings Report of the Task Force on Administrative Proceedings of the United States Securities and Exchange Commission (Report of the Task Force on Administrative Proceedings)*.

Significant Litigation Developments

Liability in Private Actions

In *Musick, Peeler & Garrett v. Employers Insurance of Wassaw*,¹⁶⁷ the U.S. Supreme Court, as urged by the Commission in an *amicus curiae* brief, recognized the right of contribution in private actions brought under the Exchange Act Section 10(b) and Commission Rule 10b-5. Holding that federal courts have the power to continue to flesh out the right of action judicially implied under the statute and the rule, the U.S. Supreme Court agreed with the Commission that a right of contribution should be recognized to conform the implied right of action to the analogous express rights of action contained in the Exchange Act.

In *Central Bank of Denver v. First Interstate Bank of Denver*,¹⁶⁸ the Commission filed an *amicus curiae* brief urging the U.S. Supreme Court to hold that aiding and abetting liability is encompassed within

the established implied private right of action under Section 10(b) and Rule 10b-5. The Commission also urged that recklessness is sufficient to satisfy the knowledge element of aiding-and-abetting liability under Section 10(b) where the defendant's substantial assistance of the primary wrongdoing is accomplished through some affirmative action, even if the defendant owes the plaintiff no independent duty.

Statutes of Limitation

The Commission *as amicus curiae* defended the recently enacted Section 27A of the Exchange Act against constitutional attack in numerous cases. Section 27A eliminated the retroactive application of the one-year/three-year statute of limitations for Section 10(b) private actions announced by the U.S. Supreme Court in *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*¹⁶⁹ by preserving the application of the statutes of limitation then in effect for all cases filed before *Lampf*-was decided. The constitutionality of Section 27A has been upheld by the U.S. Courts of Appeals for the First, Second, Fourth, Seventh, Ninth, Tenth and Eleventh Circuits as applied to cases which were pending when the statute was enacted.¹⁷⁰ In addition, the U.S. Court of Appeals for the Fifth Circuit held as urged by the Commission, that the reinstatement pursuant to Section 27A of cases which had been finally dismissed when the statute was enacted does not violate separation of powers principles or due process.¹⁷¹ The U.S. Court of Appeals for the Sixth Circuit in contrast, held that such reinstatement violates separation of powers principles,¹⁷² and the U.S. Court of Appeals for the Tenth Circuit held that reinstatement violates due process and separation of powers principles.¹⁷³

The Supreme Court has granted a writ of certiorari to the U.S. Court of Appeals for the Fifth Circuit in *First Republicbank Corp., et al. v. Pacific Mutual Life Insurance Co.* to resolve the issue.¹⁷⁴

In *SEC v. Rind*,¹⁷⁵ the U.S. Court of Appeals for the Ninth Circuit agreed with the Commission that no statute of limitations binds Commission enforcement actions which are brought to vindicate public rights pursuant to an express right of action that contains no limitations period. The defendant had asserted that the Commission's disgorgement action was time-barred by the one-year/three-year statute of limitations established in *Lampf*.

Inclusion of Shareholder Proposals in Proxy Materials

In *ACTWU v. SEC*¹⁷⁶ the U.S. Court of Appeals for the Second Circuit agreed with the Commission that a Commission affirmation of a staff no-action letter declining to recommend enforcement action if a company omitted a shareholder proposal from its proxy statement is not a reviewable order under the Exchange Act, because it does not bind anyone involved.

In *NYCERS v. SEC*¹⁷⁷ the U.S. District Court for the Southern District of New York held that the Commission had engaged in rulemaking without notice and comment, in violation of the Administrative Procedure Act, when it affirmed a staff no-action letter agreeing with a company's decision to exclude a shareholder proposal. The court found the no-action letter applied an interpretation of the ordinary business exception that differed from an interpretation contained in a 1976 Commission release issued in conjunction with the adoption of amendments to the shareholder

proxy proposal rule. The court enjoined the Commission from issuing no-action letters inconsistent with the 1976 interpretation.

Disgorgement

In *SEC v. Huffman*¹⁷⁹ and *SEC v. AMX International, Inc.*,¹⁷⁹ the U.S. Court of Appeals for the Fifth Circuit held, as the Commission had urged, that a disgorgement order is not a debt as defined in the Federal Debt Collection Procedures Act of 1990.¹⁸⁰ Thus, the defendants were not entitled to use the exemptions contained in that act to avoid paying disgorgement

Insider Trading

The U.S. Supreme Court has denied petitions for certiorari seeking review of two decisions of the U.S. Court of Appeals for the Second Circuit affirming convictions for insider trading.

In *United States v. Teicher*,¹⁸¹ the court of appeals, in *dicta*, indicated its agreement with the Commission's longstanding position that a defendant may be liable for trading while in possession of misappropriated inside information, whether or not he trades on the basis of such information. The court's holding, however, was that on the facts of this case, any alleged error in the jury instructions on this point was harmless. The government's brief in opposition to certiorari argued that this holding is correct. The brief also noted that, in any event, a possession test would be correct.

In *United States v. Liberal*¹⁸² the defendant argued that the misappropriation theory of liability for insider trading, which prohibits trading while in possession of wrongfully obtained material nonpublic

information, should not apply where, as in this case, the owner of the information is a business publication with no interest in the securities traded. The government's brief in opposition to certiorari argued that there is no statutory or case law basis for such a distinction.

Regulation of Securities Professionals

In *F.B. Horner & Associates, Inc. v. SEC*¹⁸³ the U.S. Court of Appeals for the Second Circuit affirmed a Commission decision in which the Commission affirmed sanctions imposed by the National Association of Security Dealers (NASD) on a broker-dealer after finding that the dealer charged unfair markups on sales of a debt security. The court approved the Commission's reliance on the firm's contemporaneous cost as evidence of the inter-dealer price on which to calculate the markups.

Market Regulation

In *Timpinaro v. SEC*,¹⁸⁴ the U.S. Court of Appeals for the District of Columbia Circuit upheld the Commission's approval of an NASD rule change that gave market makers a 15-second period after executions on the NASD's Small Order Execution System to update their quotations, during which time they could decline to accept unpreferenced orders. However, the court remanded without vacating the Professional Trader Rule, which expanded the definitions of professional trading account and day trade. While finding that the Commission had proceeded on a sound theory of market behavior in approving the Professional Trading Rule, the court expressed concern over the lack of data demonstrating that the benefits of the rule exceed its costs. The court directed the Commission to address

this issue on remand and to determine whether the rule comports with the constitutional proscription against vagueness.

Requests for Access to Commission Records

The SEC received approximately 100 subpoenas for documents and testimony in 1993. 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 SEC received 1,837 requests under the Freedom of Information Act (FOIA) for access to agency records and 4,382 confidential treatment requests from persons who submitted information. There were 53 appeals to the SEC's General Counsel from initial denials by the FOIA Office. Three of these appeals resulted in district court litigation, all of which are now pending,¹⁸⁵

One FOIA case filed against the Commission in 1992 was decided favorably to the Commission. In *Alexander & Alexander Services, Inc. v. SEC*,¹⁸⁶ plaintiff brought an action against the Commission under the Administrative Procedure Act, 5 U.S.C. 701-06, seeking to enjoin the Commission from disclosing certain of its documents in response to a FOIA request. Alexander claimed that the documents were exempt from disclosure by 5 U.S.C. 552(b)(4) because they contained confidential commercial information, the disclosure of which would allegedly harm Alexander's competitive position. Alexander alleged that the Commission did not afford it an adequate opportunity to substantiate its claim for confidential treatment. The court ruled in favor of the Commission in all material

respects. Most importantly, the court found that the SEC's procedures afforded Alexander a more than adequate opportunity to substantiate its confidential treatment request. The court further held that, both in its original request to the agency's FOIA Office and in its appeal to the Office of the General Counsel, Alexander failed to meet its burden of substantiating its claim.

The SEC also was successful in obtaining a reversal of a district court order sealing a portion of the record in an SEC injunctive action, including the permanent injunction and the transcript of the hearing in open court in which the injunction had been entered. In *SEC v. Van Waegenberghe*,¹⁸⁷ the court of appeals adopted the SEC's reasoning that there had been an abuse of discretion in sealing the records as there is a strong public interest in making injunctions entered in SEC enforcement proceedings public.

Actions Under the Right to Financial Privacy Act

Seven actions were filed under the Right to Financial Privacy Act to quash SEC subpoenas for customer information from financial institutions. Four 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,¹⁸⁸ one of these challenges was withdrawn,¹⁸⁹ and two remain pending.¹⁹⁰

Actions Against Professionals Under Commission Rule 2(e)

During 1992, the SEC issued a ruling under Rule 2(e) affirming the decision of an Administrative Law Judge that two partners of a major accounting firm had engaged in improper professional conduct during five audits of Savin Corporation.¹⁹¹ That decision was

appealed to the Court of Appeals for the District of Columbia, where the accountants argued that the Commission lacked authority to promulgate Rule 2(e) and to sanction accountants. The Commission's brief argues that Rule 2(e) represents a valid exercise of the Commission's general rulemaking authority and that the authority for agencies generally to discipline professionals is well established. Petitioners also argue that a showing of knowledge is required before receiving a sanction for improper professional conduct under Rule 2(e). The Commission's brief argues that negligent conduct is a sufficient basis for imposing discipline for improper professional conduct because of the significant potential impact of negligent or incompetent accountants upon the investing public. The appeal is pending.

The staff also prosecuted certain other Rule 2(e) disciplinary proceedings. In *In re Robert J. Iommazzo*,¹⁹² the Commission accepted a settlement barring a public accountant from practicing before the Commission as an auditor for 10 years because he had material unsecured loans from his client bank during the course of three audits. In *In re Gregory Melson*,¹⁹³ the engagement partner on the audit of Kahler corporation consented to a Commission Order finding he had engaged in improper professional conduct during the 1988 and 1989 audits of Kahler Corporation.

The Commission suspended Melson for nine months. Proceedings continue against the concurring partner. In *In re Martin G. Brortme*¹⁹⁴ the Commission suspended an engineer under Rule 2(e) on the basis of a prior injunction finding he had prepared a false and misleading engineering report which was incorporated into a filing made with the Commission.

Significant Adjudication Developments

Significant progress was made in the adjudicatory program in 1993. The staff submitted to the Commission a record 64 draft opinions, a 23 percent increase from 1992. The post-briefing age of the staff's case inventory remained at approximately 170 days. Moreover, the Commission issued a record 81 opinions (an increase of almost 69 percent over the prior year's 48). However, the Commission received 65 new adjudicatory cases in 1993, a 16 percent increase over 1992.

Significant Adjudicatory Decisions Involving Broker-dealers and Market Professionals

As in 1992, a number of the most significant opinions issued by the Commission in 1993 involved the setting of prices charged to customers for securities. In *Investment Planning, Inc.*,¹⁹⁵ the Commission expressly found excessive markups as low as 4 percent in high-quality zero-coupon municipal securities and interest-bearing corporate bonds. Building on the decision in *Investment Planning, Inc.*,¹⁹⁶ the Commission held in *First Honolulu Securities, Inc. and Charles Jacobson*¹⁹⁷ that markups on thinly-traded and volatile municipal debt securities below even four percent may be unfair.

Ordinarily, the fairness of retail prices is determined vis-a-vis the inter-dealer market. The market for the securities at issue in *Bison Securities, Inc.*,¹⁹⁸ however, had long periods of no inter-dealer activity, during which the firm sold the securities to customers. The Commission's opinion in this matter therefore described the appropriate method for determining prevailing market price in the

absence of inter-dealer transactions and the propriety of using historical cost to determine markups.

In *Patten Securities Corp, and John L. Patten*,¹⁹⁹ the Commission was presented with an unusual method of manipulating a security's market price. The *Patten* firm had been the sole underwriter of an offering of securities, all of which it then sold to firm customers. Using the firm's power over market price resulting from exclusive control over supply, the firm and its president caused a sharp and unwarranted rise in the market price of the securities through sales to other dealers, not, as is usual with a manipulation, by activity on the purchase side. The firm also furthered the manipulation by absorbing excess securities into its inventory. Reasoning that the respondents had attempted to conduct a one-sided market at an artificial level, the Commission found that the price of the securities had been manipulated during a two-week period in which respondents raised the price they charged other dealers to twice the offering price. The Commission concluded, however, that the evidence was insufficient to find a manipulation for the remainder of the period charged in the NASD's complaint. Market conditions for the security had improved, and the firm's sales of the security substantially exceeded its purchases during that period.

A number of the Commission's opinions involved issues of procedural fairness. In *Allan Mace Leavitt*,²⁰⁰ the Commission found that the American Stock Exchange had failed to invoke its jurisdiction over a former employee of a member firm within the time period prescribed by that exchange's rules, and therefore set aside the disciplinary action. Another matter, *Datek Securities Corp.*,²⁰¹ involved an NASD expedited remedial proceeding concerning transactions in the Small Order Execution System of NASDAQ, many

of which involved firms that employed two of the three members of the NASD panel that heard the proceeding. The Commission found that, under the circumstances, the two members of the hearing panel had a fundamental conflict of interest that was not curable by the Commission's *de novo* review. Accordingly, the Commission set aside the NASD's findings and sanctions.

Task Force on Administrative Proceedings

In March 1993, the *Report of the Task Force on Administrative Proceedings* was issued. The task force found the Commission's adjudicatory program to be both fair and effective. At the same time, though, the task force noted areas where the program could be improved, and recommended new procedures, policies and rules. The task force recommended that the Office of the General Counsel be given the responsibility for coordination of all staff duties with respect to adjudicatory matters, including implementation of the recommended procedures, policies and rules. The office has assumed this role. As the result of implementation of interim steps recommended by the task force in 1991 and 1992 as well as the adoption of recommendations made with publication of the final report, the Commission's pending adjudicatory case backlog was substantially brought up to date. Subsequent to publication of the report, the Commission issued proposed new Rules of Practice.

Counseling and Regulatory Policy Services

The dynamic nature of the U.S. capital markets continues to present the Commission with novel and complex legal and regulatory issues. The General Counsel is the principal legal advisor to the Commission, and provides independent analysis and advice to the

Commission and its Divisions and Offices on the merits and risks of proposed action in all areas of agency practice. During 1993, as a result of developments in such areas as market structure, capital formation, and mutual fund investment, the General Counsel advised the Commission and its staff on a range of significant issues relating to federal securities, administrative and Constitutional law. In connection with the Commission's enforcement program, the General Counsel provided advice on complex legal issues and significant litigation risks. Resolution of these issues facilitated achievement of the Commission's statutory goals, with particular attention to promoting balanced, consistent and cost-effective regulatory action.

Significant Legislative Developments

By the close of 1993, only one securities bill (H.R. 616, regarding managed accounts) had been enacted into law. In addition, the House and Senate had each passed separate versions of legislation in the areas of government securities and limited partnership roll-ups. The House also had passed an investment advisers bill, and legislation providing for Commission self-funding as part of the Commission's 1994-1995 authorization. Notably, many of the securities bills actively considered during the first session of the 103rd Congress, including those relating to government securities, limited partnership roll-ups, and investment advisers, were reintroduced from the 102nd Congress.

Managed Accounts

H.R. 616, signed by the President in August 1993 (P. L. No. 103-68), repeals provisions in Exchange Act Section 11(a) restricting the ability of certain institutional investors (including investment company

affiliates) to execute trades on the floor of an exchange for managed accounts without the involvement of an independent floor broker. The advent of negotiated commission rates and open access to exchange memberships in the years since enactment of Section 11(a) greatly reduced competitive concerns that were grounds for the managed account restrictions. Accordingly, in 1991, the Commission testified in support of legislation to exempt managed accounts from Section 11 (a), subject to disclosure requirements designed to limit conflicts of interest. H.R. 616, as enacted in the 103rd Congress, contained such provisions.

Government Securities

Important legislation involving the regulation of the government securities markets was considered in 1993 but not enacted during 1993. H.R. 618, the *Government Securities Reform Act*, was introduced in January 1993. The Commission testified in support of H.R. 618 in March 1993, advocating in particular its provisions relating to recordkeeping and reporting, sales practices, and transparency.

H.R. 618, as introduced, was very similar to a bill that failed to pass in the 102nd Congress due to jurisdictional disagreements between the House Banking and Energy and Commerce Committees. Anticipating a renewal of these differences, the Commission worked with the U.S. Treasury (Treasury) and the committees and succeeded in reaching a compromise position on H.R. 618. The compromise included, among other important features, permanent reauthorization of Treasury's rulemaking power, large position reporting, sales practice and anti-fraud provisions.

By contrast, the Senate in July 1993 passed a narrower bill, S. 422, to reauthorize Treasury's rulemaking authority and provide more limited reforms for the government securities market. Together with the roll-ups bills (discussed below), the different versions of the government securities legislation were being considered by House and Senate staff in conference.

Limited Partnership Roll-ups

In March 1993, the House passed H.R. 617, a bill intended to combat certain inequities perceived as associated with limited partnership roll-up transactions. On the Senate side, S. 424 was passed in August 1993, subject to a Dodd-Grumm compromise limiting the scope of the legislation. The two roll-ups bills were being considered by House and Senate staff in conference at the close of 1993.

Investment Advisers

In 1993, the House (but not the Senate) passed legislation to provide for enhanced Commission inspection of investment advisers. Among other things, H.R. 578 would establish a fee schedule for investment advisers to cover the cost of such an inspection program, a suitability requirement, Commission authority to designate a self-regulatory organization to examine investment advisers, enhanced disclosure requirements and fidelity bonding. A narrower Senate bill, S. 423, also would provide for new fees to cover the costs of enhanced Commission inspections, although it omits the suitability requirements and certain other substantive provisions included in H.R. 578. While S. 423 was reported out of Committee, it was not passed by the Senate until after the close of 1993.

SEC Authorization

The House, but not the Senate, has also passed legislation providing for Commission self-funding. On May 24, 1993, Chairman Dingell introduced H.R. 2239, the Commission's authorization bill for fiscal years 1994-1995. As introduced, H.R. 2239 contained only the Commission's appropriation request. The Energy and Commerce Committee subsequently approved an amendment providing for a form of Commission self-funding, and the House ultimately passed H.R. 2239 with the self-funding provision.

Other Legislative Initiatives

Finally, other legislative initiatives of interest to the Commission in the first session of the 103rd Congress included: (1) a Congressionally-requested review of regulation of the municipal securities market, including issues such as repeal of the Tower Amendment and disclosure of political contributions related to municipal and state securities issuers; (2) several bills designed to increase the flow of capital to small businesses; (3) a House bill and Senate hearings regarding litigation reform under the federal securities laws; (4) a bill to transfer jurisdiction over the administration of the Public Utility Holding Company Act of 1935 from the Commission to the Federal Energy Regulatory Commission; (5) a bill to merge the Commodity Futures Trading Commission with the Commission; and (6) a series of oversight hearings relating to issues raised by the Commission's Market 2000 Study, including hearings on soft dollars, payment for order flow and proprietary trading systems.

Foreign Technical Assistance

The agency received a three-year grant in 1992 from the U.S. Agency for International Development totaling \$2.8 million to support technical assistance programs related to the development and regulation of capital markets in Central and Eastern European countries. Under the grant, Robert Strahota, an SEC attorney, served as an adviser to the Polish Securities Commission in Warsaw from June 1992 to June 1993. Mr. Strahota advised the Polish Securities Commission on revising the Polish securities law and in developing securities regulations and systems. During 1993 other SEC attorneys advised on securities regulation questions arising in Bulgaria, Costa Rica, Czechoslovakia, Thailand and Uzbekistan.

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 adequately protected. Commission participation is generally limited to cases involving debtors with publicly traded securities. In 1989, the Commission authorized a review of its role in reorganization cases. The staff review is complete and awaits Commission consideration.

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 1993, the Commission moved

for appointment of investor committees in two cases²⁰² and opposed dissolution of a committee in one case.²⁰³

Estate Administration

The Commission protects the interests of public investors by participating in selected matters involving administration of the debtor's estate. In *In re National Convenience Stores, Inc.*,²⁰⁴ 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 another matter involving indenture trustees, the Commission successfully argued *In re MCorp Financial, Inc.*,²⁰⁵ that a trust indenture is not an executory contract that can either be rejected or accepted. Requiring the debtor to accept the indenture would result in an unwarranted priority for indenture trustee fees; rejection could leave bondholders unrepresented. In *In re Master Mortgage Investment Fund, Inc.*,²⁰⁶ the Commission argued, as it has previously,²⁰⁷ that the Bankruptcy code only allows discharge of the liabilities of 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 their officers and directors from personal liabilities for various kinds of claims, including liabilities under the federal securities laws.

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 new securities pursuant to a

Bankruptcy Code exemption from registration under the Securities Act of 1933. The Commission prevented the unlawful issuance of securities in two cases.²⁰⁸ The Commission reviews disclosure statements of publicly-held companies or companies likely to be traded publicly after reorganization. During 1993, the staff reviewed 104 disclosure statements and commented on 83. Most of the Commission's comments were adopted by debtors; formal objections were filed in two cases.²⁰⁵

Ethical Conduct Program

The General Counsel is the Designated Agency Ethics Official for the SEC. In 1993, the demand for ethics counseling services continued to increase due to issues relating to new areas of inquiry by the Commission (e.g., issues related to bank holding companies, insurance companies, the government bond market); significant turnover in senior staff; and the implementation of new government-wide Standards of Ethical Conduct for Employees of the Executive Branch and the new government-wide confidential disclosure system. Routine or repetitive inquiries were handled by ethics liaison officers and deputies located within each division and office, consistent with the field system established in 1992. Unique or novel issues were directed to the Ethics Counsel. In 1993, the Ethics Counsel and staff responded to requests for counseling at the rate of approximately 20 new matters per week.

The staff conducted a two-day training workshop in January 1993 to acquaint ethics liaison officers and senior staff with new ethics provisions. 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. Training

materials (video and written) were prepared and procedures were put in place to complete both initial ethics training for all employees and annual training for senior and mid-level employees. Procedures were established for implementing the new government-wide program for confidential disclosure of financial interests.

Workload Increases

The General Counsel's Office has experienced substantial increases in productivity and workload in recent years. In 1993, workload in the office continued to experience substantial increases or leveled off at the already heightened 1992 levels.

[table omitted]

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 in capital markets around the world and major program initiatives affecting the United States financial services industry, markets, and investors.

Key 1993 Results

In 1993 the Office of Economic Analysis directed its efforts in a number of areas including enforcement cases/ executive compensation, and market structure issues. The staff provided technical assistance to the Division of Enforcement, helped to develop executive compensation disclosure rules, provided economic analysis in connection with the *Market 2000* study, and reported on the financial health of the securities industry. For the third consecutive year, the staff coordinated the International Institute for Securities Market Development.

Economic Analysis and Technical Assistance

The staff provided technical assistance to the Division of Enforcement in approximately 40 cases of insider trading, market manipulation, and fraudulent financial reporting. This support role has become increasingly important in establishing violations based on statistical evidence and determining materiality in many cases. The

staff uses financial theory and event analysis to provide the empirical support key to numerous enforcement cases. In such instances, the staff advises the Division of Enforcement regarding materiality and/or the amount of disgorgement that should be sought. The staff assisted the U.S. Attorney's Office in the successful prosecution of a bribery case involving an investment manager.

In recent years, public and shareholder concern over senior executive and director compensation has intensified. Thus, the matter has become a policy issue with significant economic implications. Consequently, the staff studied the function of options in corporate compensation and helped to develop the Commission rules that require disclosure of the value of executive options. Following the adoption of the rule, the staff applied options pricing models to the valuation of executive stock options to monitor compliance with the Commission's disclosure rules.

The staff provided advice, technical assistance, and analyses in connection with the *Market 2000* study. Specifically, the staff examined the economic effects of market fragmentation and analyzed the effects of payment for order flow on retail customers. The staff also studied the effect of active Small Order Execution System (SOES) trading on NASDAQ bid-ask spreads and prepared an analysis of the empirical evidence submitted by experts on the impact of the SOES on spreads, volatility, and liquidity.

The staff continued to monitor the securities industry and developments in the domestic and international securities markets. The staff produced quarterly reports on the financial health of the securities industry, reported on trends in the composition of bank asset portfolios, analyzed trends in the capital and profitability of New

York Stock Exchange specialists, and reported on the financial condition of penny stock dealers. The staff also prepared capital market briefing reports that assessed economic, institutional, and regulatory developments outside the United States, and provided technical support to the SEC's international regulatory program.

In addition, the staff provided advice on the effects of market value accounting on banks, monitored developments in the markets for hybrid products and derivative securities, analyzed data from the 1993 penny stock examination sweep, and used economic models to value derivative securities for purposes of determining regulatory jurisdiction of certain equity-linked securities. The staff also analyzed 90 rule proposals to assess their potential effects on small entities, as required by the Regulatory Flexibility Act of 1980.

The staff coordinated the third annual SEC International Institute for Securities Market Development (Institute) conference, which provided training and technical assistance on the formation and operation of securities markets and related regulatory systems. The Institute, held April 26 to May 7, 1993, was attended by 94 senior level capital market officials from 47 countries with new and emerging securities markets. After the two-week Institute program, 61 of the attendees participated in internships with various securities organizations, including self-regulatory organizations, securities firms, and clearing organizations.

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, Information and Consumer Services.

Key 1993 Results

The Commission held 61 meetings and considered 322 matters. Major activities of the Commission included adoption of

comprehensive revisions of the Commission's shareholder communications rules, adoption of regulations on disclosure of executive compensation, and adoption of rules improving mutual fund disclosure of performance and changes in the portfolio's manager.

The agency collected fees for the United States Treasury in excess of its appropriation for the eleventh consecutive year. The SEC's total fee collections in 1993 were \$517 million and the net gain to the Treasury was \$248 million.

Policy Management

Commission Activities. The Commission held 61 meetings in 1993, during which it considered 322 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:

- adopting comprehensive amendments to shareholder communications (proxy) rules;
- adopting revisions to Commission Rule 144A providing a safe harbor exemption from registration requirements under the Securities Act of 1933 (Securities Act) for resales of restricted securities to qualified institutional buyers;
- adopting amendments to rules governing disclosure of compensation for corporate executive officers and directors;

- adopting amendments to improve disclosure of open-end management companies' performance and portfolio managers;
- adopting a rule enabling closed-end management companies to repurchase shares at periodic intervals at net asset value; and
- adopting amendments to the Commission's net capital rule for broker-dealers.

Congressional interest in the agency's activities and initiatives remained high. The Commission and staff members testified at 12 congressional hearings during the year. In addition, the Congress actively considered a number of important issues under the Commission's jurisdiction. These were most notably;

- 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 and municipal securities markets;
- limited partnership "roll-ups" and their impact on limited partner investors;
- securities litigation reform;
- reforms relating to accountants' responsibilities;

- legislation to facilitate improved access to capital for small businesses, including the Small Business Investment Incentive Act that was originally proposed by the SEC;
- the state of the investment company industry and the adequacy of the SEC's inspection program for investment companies;
- 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 agency activities to those interested in or affected by Commission actions, including the press, regulated entities, the general public, and employees of the agency.

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. Information on Commission activities also was disseminated through notices of administrative actions, litigation releases, and other materials.

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 52 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 over 62,000 requests for specific information on the agency or its activities.

The staff provided support for activities related to the International Organization of Securities Commissions, the SEC's International Institute for Securities Markets Development, and meetings of the Market Transactions Advisory Committee. In addition, programs for 586 foreign visitors were coordinated during the year.

Management Activities. The Office of the Executive Director coordinated special projects, such as the restructuring of the regional offices, and initiated 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 and the Government Performance and Results Act of 1993. 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 the agency authorization request for fiscal years 1994 and 1995 to Congress.

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 programs.

The primary services provided by the compliance program included counseling and alternative dispute resolution, investigating complaints of employment discrimination, and issuing final agency decisions based on the investigations. The affirmative employment program developed databases and monitored statistics for mandatory reports to the Equal Employment Opportunity Commission and for self-evaluation of the Commission's success in attracting, retaining, and promoting a diverse work force. Significant accomplishments included:

- improving the EEO counseling process by providing training in alternative dispute resolution to EEO counselors;
- improving the quality of investigations of EEO complaints due to the use of in-house attorney/investigators for 89% of the complaints investigated;
- training Senior Executive Service employees in new procedures for resolving disputes and processing complaints under the EEO system;
- completing an agency-wide mandatory training program designed to prevent sexual harassment;
- implementing better procedures for informing all new SEC employees of their rights under federal civil rights statutes;
- providing in-house EEO training to new supervisors; and

- expanding the EEO special emphasis programs to include a Disability Issues Advisory Committee sponsored in cooperation with the Office of Administrative and Personnel Management.

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 1,893 FOIA requests and appeals, 21 Privacy Act requests, 35 Government in the Sunshine Act requests, 9 government referrals, and 4,391 requests and appeals for confidential treatment. All FOIA/Privacy Act requests were responded to within the statutory time frame.

Administrative Support

Financial Management and Operations. For the eleventh straight year, the SEC collected fees in excess of its appropriation. The SEC's total fee collections in 1993 were \$517 million, 204 percent of the agency's appropriated spending authority of \$253 million (which consisted of \$127 million in appropriated funds, \$96 million in current year offsetting fee collections, and \$30 million from a carry-over of prior year offsetting fee collections). The \$517 million in total fee collections, minus the SEC's current year spending authority of \$223

million (\$253 million less the \$30 million from prior year offsetting fee collections) and \$46 million in additional offsetting fee collections, resulted in a net gain of \$248 million to the United States Treasury.

The SEC's total fee revenue in 1993 was collected from four basic sources: registrations of securities under Section 6(b) of the Securities Act of 1933 (comprising 83 percent of total fee collections); transactions of covered exchange listed securities (15 percent); tender offer and merger filings (1 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-thirty-second of one percent.

The most significant financial management accomplishment was an upgrade of the agency's mainframe accounting system, the Federal Financial System. This upgrade greatly expanded the system's security functions and facilitated the decentralized input and on-line review of data allowing direct input of employee travel orders and vendor obligations. Staff also continued work on the design of various new and improved financial management systems affecting agency-wide time and attendance, payroll, filing fee, and inventory processes.

In other financial areas, the staff developed a frequent flyer program and a salary offset policy. Due to the mandatory use of direct deposit, the number of paper salary checks was reduced to less than one percent of the SEC's total employee population. In addition, a pilot credit card system was developed for the agency's library and small procurement acquisitions to facilitate the prompt delivery of materials and reduce the number of purchase orders written and vouchers processed.

Information Resources Management. The Office of Information Technology (OIT) made progress in the development and enhancement of SEC information resources. Notably, Electronic Data Gathering Analysis and Retrieval (EDGAR) software development continued on schedule, and a system upgrade resulted in additional functionality and improved performance. In October 1992, a memorandum of understanding with the EDGAR contractor was executed which transferred responsibilities for management operation, and implementation of the EDGAR local area network to the Commission's automation staff. This initiative will save an estimated one million dollars over the life of the contract, as well as facilitate the Commission's efforts to fully integrate data communications services.

Special emphasis was placed on restructuring within OIT to better recognize and respond to users' needs. An End User Advisory Committee was formed, consisting of senior representatives from each of the program divisions. The Committee reviewed the development of the agency's strategic automation plan, external data service funding requirements, and other automation issues. Also, a quality assurance and system design function within OIT was established to ensure that systems developed meet the specifications of the system design.

A disaster recovery plan was developed to provide the agency with automation backup capabilities in the event a disaster occurs at either of its computer facilities – the main Operations Center in Alexandria or at the Headquarters building. An initial backup capability will be in place by 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 the systems will monitor the activity of large traders in the markets and enable the SEC to monitor the financial health 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, In July 1993, the Office of Administrative and Management Support and the Office of Human Resources Management were consolidated into the new Office of Administrative and Personnel Management (OAPM). OAPM provided a wide range of office support services and personnel functions, including space acquisition, lease administration, procurement and contracting, facilities management, printing, mail services, desktop publishing, property management, recruitment and staffing, employee compensation and benefits, training, performance management, labor relations, counseling, disciplinary actions, personnel security and suitability, and maintenance of official employee records.

The agency executed a 15-year lease for the headquarters building in July 1993. The new lease included renovations of the entire building. However, on November 22, 1993, the landlord of the building notified the Commission that it was exercising the termination clause in the new 15-year lease as a result of the unavailability of non-recourse financing and various other reasons. The Commission reverted to the five-year option on its original lease.

An annex building in Virginia was acquired under a 15-year lease and houses the Office of Filings, Information, and Consumer

Services (OFICS). Additional space and improved working conditions were obtained for the district offices in Boston and San Francisco. The agency administered 16 leases for an approximate total of 800,000 square feet of office and related space.

The agency awarded contracts and purchase orders in excess of \$36 million during 1993. Printing production increased from 67 million units to 71 million units, incoming mail increased by 10 percent, and outgoing mail increased by 15 percent.

The staff recommended specific strategies for increasing workforce diversity, and continued to monitor turnover rates to assist in formulating hiring strategies to avoid personnel shortfalls. The SEC's recruitment program continued to emphasize active participation in job fairs, on-campus recruitment interviews at law schools, and the use of various available hiring programs and authorities.

Twelve new or revised policies were published in the *Personnel Operating Policies and Procedures Manual* to provide managers and employees with updated human resources program guidance. Policies were developed on: the use of experts and consultants; special hiring authorities for veterans and persons with disabilities, including veterans and disabled veterans; position classification; appeals of classification decisions; approval of pre-appointment interview expenses; and implementation of Office of Personnel Management regulations under the Federal Employee Pay Comparability Act of 1990.

During the year, employees attended a total of 5,772 training courses which included half-day sessions for 2,651 employees in an

agency-wide mandatory training course in preventing sexual harassment. Fourteen SEC training programs were granted approval for awarding Continuing Professional Education Credits by the National Association of the State Boards of Accountancy.

Consumer Affairs. OFICS was responsible for:

- responding to 34,713 investor complaints and inquiries;
- screening information received for referrals to SEC operating divisions, self-regulatory agencies, states, or other federal agencies;
- preparing educational materials to assist investors in protecting their interests; and
- developing and implementing the agency's consumer protection program.

Of the 34,713 contacts by letter, telephone call, or walk-in visit, 16,550 were complaints and 18,163 were inquiries. Approximately 42 percent of the complaints involved broker-dealers, while the remainder involved issuers, mutual funds, banks, transfer agents, clearing agents, and investment advisers. The two most frequent complaints against broker-dealers involved allegations of unauthorized transactions executed in customer accounts and recommendations by the broker-dealers of unsuitable investments. Over 1,300 complaints were referred to SEC operating divisions, self-regulatory agencies, or other regulatory entities for review and/or action.

Public Reference. OFICS also was responsible for making available to the public all company filings and Commission rules, orders, studies, and reports. These documents (dating from 1933 through the present) were available in the public reference room and could be obtained by writing the agency or contacting the agency's dissemination contractor.

The public reference staff provided assistance to 44,820 visitors to the headquarters reference room, responded to 5,296 written requests for documents, 444 formal requests for certifications of filings and records, and 121,370 telephone inquiries. A total of 25,374 electronic filings received via EDGAR were available for requestors. In addition, the agency added a total of 380,445 paper documents and 458,154 microfiche records to its existing library of publicly available information.

ENDNOTES

¹*In the Matter of John H. Gutfreund*, Exchange Act Release No. 31554 (Dec. 3, 1992), 52 SEC Docket 4370.

²*SEC v. Paul W. Mozer*, Litigation Release No. 13453 (Dec. 2, 1992), 52 SEC Docket 4530.

³*In the Matter of Daiwa Securities, Inc.*, Exchange Act Release No. 31924 (Feb. 25, 1993), 53 SEC Docket 1693.

⁴*In the Matter of Donaldson, Lufkin & Jenrette Securities Corp.*, Exchange Act Release No. 32827 (Sept 2, 1993), 54 SEC Docket 2402.

⁵*In the Matter of Carroll McEntee & McGinley Securities*, Exchange Act Release No. 32828 (Sept. 2, 1993), 54 SEC Docket 2407.

⁶*SEC v. Daniel O. Teyibo*, Litigation Release No. 13530 (Feb. 24, 1993), 53 SEC Docket 1790.

⁷*SEC v. Bruce Dickson*, Litigation Release No. 13570 (Mar. 18, 1993), 53 SEC Docket 2617.

⁸*In the Matter of Paul K. Clarkin*, Exchange Act Release No. 32672 (July 26, 1993), 54 SEC Docket 1740.

⁹*In the Matter of Douglas R. Gulling*, Exchange Act Release No. 32673 (July 26, 1993), 54 SEC Docket 1745.

¹⁰*SEC v. Joseph Zilber*, Litigation Release No. 13586 (Apr. 1, 1993), 53 SEC Docket 3550.

¹¹ *SEC v. C. Robert Dudgeon*, Litigation Release No. 13556 (Mar. 10, 1993), 53 SEC Docket 2526.

¹² *SEC v. Purnendu Chatterjee*, Litigation Release No. 13491 (Jan. 13, 1993), 53 SEC Docket 945.

¹³ *SEC v. Jonathan J. Sheinberg*, Litigation Release No. 13465 (Dec. 10, 1992), 52 SEC Docket 4708.

¹⁴ *SEC v. Lee A. Haddad*, Litigation Release No. 13473 (Dec. 17, 1992), 53 SEC Docket 221.

¹⁵ *SEC v. Dean Ambrose Olds*, Litigation Release No. 13595 (Apr. 8, 1993), 53 SEC Docket 3702.

¹⁶ *SEC v. C. Stephen Bolen*, Litigation Release No. 13684 (June 28, 1993), 54 SEC Docket 1322.

¹⁷ *SEC v. The Software Tool-works, Inc.*, Litigation Release No. 13813 (Sept. 30, 1993), 55 SEC Docket 411.

¹⁸ *SEC v. Larry E. Leslie*, Litigation Release No. 13651 (May 26, 1993), 54 SEC Docket 540.

¹⁹ *SEC v. Harold Sahlen*, Litigation Release No. 13480 (Dec. 21, 1992), 53 SEC Docket 544.

²⁰ *SEC v. Gordon K. Goldman, C.P.A.*, Litigation Release No. 13501 (Jan. 28, 1993), 53 SEC Docket 1227.

²¹ *SEC v. Towers Financial Corp.*, Litigation Release No. 13514 (Feb. 8, 1993), 53 SEC Docket 1481.

²² *SEC v. Premium Sales Corp.*, Litigation Release No. 13668 (June 9, 1993), 54 SEC Docket 860.

²³ *SEC v. International Quarter Phones*, Litigation Release No. 13661 (June 3, 1993), 54 SEC Docket 735.

²⁴ *SEC v. Sam S. Brown*, Litigation Release No. 13413 (Oct. 22, 1992), 52 SEC Docket 3228.

²⁵ *SEC v. Basque Puerto Carrillo*, Litigation Release No. 13600 (Apr. 12, 1993), 53 SEC Docket 3885.

²⁶ *SEC v. Ramon D'Onofrio*, Litigation Release No. 13627 (May 6, 1993), 54 SEC Docket 97.

²⁷ *In the Matter of Bruce B. Bowen*, Exchange Act Release No. 31938 (Mar. 2, 1993), 53 SEC Docket 2213.

²⁸ *In the Matter of Harry S. Pack*, Exchange Act Release No. 32374 (May 27, 1993), 54 SEC Docket 486.

²⁹ *SEC v. The Cooper Companies*, Litigation Release No. 13432 (Nov. 10, 1992), 52 SEC Docket 3750.

³⁰ *In the Matter of Kelso & Company, Inc.*, Exchange Release No. 31639 (Dec. 23, 1992), 53 SEC Docket 314.

³¹ *In the Matter of William A. Wilson*, Exchange Act Release No. 32392 (June 1, 1993), 54 SEC Docket 656.

³² *SEC v. Furr's/Bishop's Inc.*, Litigation Release No. 13461 (Dec. 7, 1992), 52 SEC Docket 4704.

³³ *In the Matter of Leslie T. Livingston*, Exchange Act Release No. 31785 (Jan. 28, 1993), 53 SEC Docket 1070.

³⁴ *In the Matter of Bettina Bancroft*, Exchange Act Release No. 32033 (Mar. 23, 1993), 53 SEC Docket 2886.

³⁵ *In the Matter of Harry E. Hagerty, Jr.*, Exchange Act Release No. 32657 (July 19, 1993), 54 SEC Docket 1623.

³⁶ *SEC v. Harry E. Hagerty, Jr.*, Litigation Release No. 13714 (July 19, 1993), 54 SEC Docket 1701.

³⁷ *SEC v. Prudential Securities Inc.*, Litigation Release No. 13840 (Oct. 21, 1993), 55 SEC Docket 830.

³⁸ *In the Matter of PaineWebber Inc.*, Exchange Act Release No. 31889 (Feb. 18, 1993), 53 SEC Docket 1526.

³⁹ *In the Matter of Frederick H. Joseph*, Exchange Act Release No. 32340 (May 20, 1993), 54 SEC Docket 282.

⁴⁰ *In the Matter of Edwin Kantor*, Exchange Act Release No. 32341 (May 20, 1993), 54 SEC Docket 293.

⁴¹ *In the Matter of The Nikko Securities Co. International, Inc.*, Exchange Act Release No. 32331 (May 19, 1993), 53 SEC Docket 264.

⁴² *SEC v. Leslie Mersky*, Litigation Release No. 13812 (Sept. 30, 1993), 55 SEC Docket 409.

⁴³ *SEC v. Midwest Investments*, Litigation Release No. 13605 (Apr. 15, 1993), 53 SEC Docket 3889.

⁴⁴ *SEC v. Midwest Clearing Corp.*, Litigation Release No. 13427 (Nov. 6, 1992), 52 SEC Docket 3746.

⁴⁵ *In the Matter of Kemper Financial Services, Inc.*, Investment Advisers Act Release No. 1387 (Oct. 20, 1993), 55 SEC Docket 783.

⁴⁶ *In the Matter of USAA Investment Management Co.*, Investment Advisers Act Release No. 1359 (Jan. 22, 1993), 53 SEC Docket 1085.

⁴⁷ *In the Matter of Aetna Capital Management, Inc.*, Investment Advisers Act Release No. 1379 (Aug. 19, 1993), 54 SEC Docket 2209.

⁴⁸*SEC v. Corporate Capital Resources, Inc.*, Litigation Release 13460 (Dec. 7, 1992), 52 SEC Docket 4704.

⁴⁹*In the Matter of The Bank of California, N.A.*, Investment Company Act Release No. 19545 (June 28, 1993), 54 SEC Docket 1300.

⁵⁰*In the Matter of Merrill Lynch, Pierce, Fenner & Smith*, Investment Company Act Release No. 19425 (Apr. 22, 1993), 53 SEC Docket 4031.

⁵¹The Division of Market Regulation, Securities and Exchange Commission, *Staff Report on the Municipal Securities Market*, (Sept. 1993).

⁵²Securities Act Release Nos. 33-7022, 34-33023, and IC-19768 (Oct. 6, 1993), 58 FR 52891 (Oct 13, 1993).

⁵³Exchange Act Release No. 32256 (May 4, 1993), 58 FR 27486 (May 10, 1993).

⁵⁴17 C.F.R. 240.15c3-1.

⁵⁵Exchange Act Release No. 32609 (July 9, 1993), 58 FR 38092 (July 9, 1993).

⁵⁶Letter to Mr. Michael D. Udoff, Chairman, *Ad Hoc* Record Retention Committee, Securities Industry Association, Inc. from Michael A. Macchiaroli, Associate Director, Division of Market Regulation, dated June 18, 1993.

⁵⁷Exchange Act Release No. 30929 (July 16, 1992), 57 FR 32159 (July 21, 1992).

⁵⁸Exchange Act Release Nos. 27445 and 29185 (Nov. 16, 1989 and May 9, 1991).

⁵⁹Exchange Act Release No. 31511 (Nov. 24, 1992), 57 FR 56973 (Dec. 2, 1992).

⁶⁰Exchange Act Release No. 31512 (Nov. 24, 1992), 57 FR 57027 (Dec. 2, 1992).

⁶¹Exchange Act Release No. 32117 (Apr. 8, 1993), 58 FR 19598 (Apr. 15, 1993).

⁶²Letter regarding Distributions of Certain German Securities, Exchange Act Release No. 33022 (Oct. 6, 1993), 58 FR 53220 (Oct. 14, 1993).

⁶³Letter regarding Distributions of Certain SEAQ and SEAQ International Securities, dated July 12, 1993.

⁶⁴Letter regarding British Airways PLC, dated May 19, 1993 and Letter regarding Saatchi & Saatchi Company PLC, dated May 19, 1993.

⁶⁵Exchange Act Release No. 33137 (Nov. 3, 1993), 58 FR 60324 (Nov. 15, 1993).

⁶⁶Exchange Act Release No. 32576 (July 2, 1993), 58 FR 37413 (July 12, 1993).

⁶⁷*Id.*

⁶⁸Exchange Act Release No. 32261 (May 4, 1993), 58 FR 27656 (May 11, 1993).

⁶⁹17 C.F.R. § 240.17f-1 (1992).

⁷⁰Exchange Act Release No. 31343 (Oct. 21, 1992), 57 FR 48645 (Oct. 27, 1992).

⁷¹Exchange Act Release No. 31358, International Series Release No. 479 (Oct. 26, 1992), 57 FR 49736 (Nov. 3, 1992).

⁷²Exchange Act Release Nos. 32362 (May 25, 1993), 58 FR 31565 (June 3, 1993) (NYSE); 32363 (May 25, 1993) (58 FR 31558) (June 3, 1993) (AMEX); 32365 (May 25, 1993), 58 FR 31560 (June 3, 1993) (BSE); 32368 (May 25, 1993) 58 FR 31563 (June 3, 1993) (CHX); 32367 (May 25, 1993), 58 FR 31570 (June 3, 1993) (PSE), and 32364 (May 25, 1993), 58 FR 31574 (June 3, 1993) (PHLX).

⁷³Exchange Act Release No. 32019 (Mar. 19, 1993), 58 FR 16428 (Mar. 26, 1993).

⁷⁴Exchange Act Release No. 32517 (June 25, 1993), 58 FR 35995 (July 2, 1993).

⁷⁵Exchange Act Release No. 32647 (July 16, 1993), 58 FR 32962 (July 22, 1993). Currently, transactions effected by NASD members in equity securities are not required to be reported on a real-time basis if those securities are not included in NASDAQ or traded on a national securities exchange.

⁷⁶Exchange Act Release No. 32568 (July 1, 1993), 58 FR 36723 (July 8, 1993). The NASD toll-free telephone listing service plan previously reported past and present employment history of NASD members, all final disciplinary actions taken by federal, state or SROs which relate to securities or commodities transactions and all criminal convictions reported on Form BD or Form U-4.

⁷⁷General Accounting Office, *Securities Arbitration: How Investors Fare*, GGD-92-74 (May 1992).

⁷⁸Letter from Deborah Masucci, Vice-President, Arbitration, NASD, to William H. Heyman, Director, Division of Market Regulation, SEC, dated November 4, 1992.

⁷⁹Exchange Act Release No. 31763 (Jan. 26, 1993), 58 FR 6829 (Feb. 2, 1993).

⁸⁰Exchange Act Release No. 32740 (Aug. 12, 1993), 58 FR 43968 (Aug. 18, 1993),

⁸¹Exchange Act Release No. 32802 (Aug. 25, 1993), 58 FR 45932 (Aug. 31, 1993).

⁸²Exchange Act Release Nos. 32702 (July 30, 1993), 58 FR 42588 (Aug. 10, 1993) (Pacific Stock Exchange); 32780 (Aug. 20, 1993), 58 FR 45365 (Aug. 27, 1993) (MSRB); and 32864 (Sept 10, 1993), 58 FR 48680 (Sept 17, 1993) (AMEX).

⁸³Exchange Act Release No. 31733 (Jan. 14, 1993), 58 FR 6034 (Jan, 25, 1993).

⁸⁴Exchange Act Release No. 31591 (Dec. 11, 1992), 57 FR 60253 (Dec. 18, 1993). SPDRs are securities issued by a unit investment trust holding the securities comprising the S&P 500 Index.

⁸⁵Exchange Act Release Nos. 31920 (Feb. 24, 1993), 58 FR 12280 (Mar. 3, 1993); 32694 (July 29, 1993), 58 FR 41814 (Aug. 5, 1993) (CBOE); and 32781 (Aug. 20, 1993), 58 FR 45360 (Aug. 27, 1993) (AMEX). Currently, the CBOE lists and trades FLEX Options based on the S&P 100 and 500 Stock Indexes, and the Russell 2000 Index, while the AMEX trades FLEX Options based on the Major Market Index (XMI), the Institutional Index (XII), and S&P MidCap Index (MID).

⁸⁶Exchange Act Release Nos. 31844 (Feb. 9, 1993), 58 FR 8796 (Feb. 17, 1993) (AMEX); 31800 (Feb. 1, 1993), 58 FR 7274 (Feb. 5, 1993), and 32693 (July 29, 1993), 58 FR 41817 (Aug. 5, 1993) (CBOE); and 32793 (Aug. 24, 1993), 58 FR 46260 (Sept 1, 1993) (NYSE). The AMEX trades QIXs on the XMI, XII, and MID Indexes; the CBOE trades QIXs on the S&P 100, S&P 500, and Russell 2000 Indexes; and the NYSE trades QIXs on the New York Composite Index.

⁸⁷Exchange Act Release No. 32343 (May 20, 1993), 58 FR 30833 (May 27, 1993).

⁸⁸Exchange Act Release No. 32950 (Sept 23, 1993), 58 FR 50985 (Sept. 29, 1993). ELNs trade on the AMEX and DECS trade on the NYSE.

⁸⁹Exchange Act Release No. 32840 (Sept 2, 1993), 58 FR 47485 (Sept 9, 1993). At maturity, a holder of a MITT is entitled to receive from the issuer 90% of the principal amount plus an amount based upon an increase in the market value of the Global Telecommunications portfolio.

⁹⁰Exchange Act Release Nos. 31528 (Nov. 28, 1992), 57 FR 57256 (Dec. 3, 1992) (NYSE);31529(Nov. 28, 1992),57 FR 57248 (Dec. 3, 1992)(AMEX);31530(Nov. 28,1992), 57 FR 57262 (Dec. 3, 1992) (PSE); 31531 (Nov. 28, 1992), 57 FR 57250 (Dec. 3, 1992) (CBOE); and 31532 (Nov. 28, 1992), 57 FR 57264 (Dec. 3, 1992) (PHLX).

⁹¹Letter from Jonathan G. Katz, Secretary, SEC, to Jean A. Webb, Secretary, CFIC, dated January 4, 1993.

⁹²Letter from William H. Heyman, Director, Division of Market Regulation, SEC to Stephen A. Sherrod, Chief, Financial Instruments Unit, Division of Economic Analysis, CFTC, dated January 22, 1993 (futures only). Letter from Brandon Becker, Director, Division of Market Regulation, SEC, to Stephen A. Sherrod, Financial Instruments Unit Chief, CFTC, dated Augusts, 1993 (futures options only). Letter from Brandon Becker, Acting Director, Division of Market Regulation, SEC, to Stephen A. Sherrod, Chief, Financial Instruments Unit Division of Economic Analysis, CFTC, dated June 18, 1993,

⁹³Exchange Act Release No. 32385 (June 3, 1993), 58 FR 32405 (June 9, 1993).

⁹⁴Exchange Act Release No. 32098 (Apr. 2, 1993), 58 FR 18277 (Apr. 8, 1993).

⁹⁵Exchange Act Release No. 31856 (Feb. 11, 1993), 58 FR 9005 (Feb. 18, 1993).

⁹⁶Exchange Act Release No. 31750 (Jan. 21, 1993), 58 FR 6424 (Jan. 28, 1993).

⁹⁷Exchange Act Release No. 32040 (Mar. 23, 1993), 58 FR 16902 (Mar. 31, 1993).

⁹⁸Exchange Act Release No. 32759 (Aug. 17, 1993), 58 FR 44865 (Aug. 25, 1993).

⁹⁹Exchange Act Release No. 32747 (Aug. 13, 1993), 58 FR 44530 (Aug. 23, 1993).

¹⁰⁰Exchange Act Release No. 32780 (Aug. 20, 1993), 58 FR 45365 (Aug. 27, 1993).

¹⁰¹Division of Investment Management, SEC, Protecting Investors: A Half Century of Investment Company Regulation (May 1992).

¹⁰²Securities Act Release No. 7013(Sept 17, 1993), 54 SEC Docket 0004; Investment Company Act Release No. 19719 (Sept. 17, 1993), 54 SEC Docket 0004.

¹⁰³Investment Company Act Release No. 19716 (Sept 16, 1993), 54 SEC Docket 2190; International Series Release No. 582 (Sept 16, 1993), 54 SEC Docket 2190.

¹⁰⁴Securities Act Release No. 6990 (Apr. 7, 1993), 53 SEC Docket 3569; Exchange Act Release No. 32116 (Apr. 7, 1993), 53 SEC Docket 3569; Investment Company Act Release No. 19399 (Apr. 7, 1993), 53 SEC Docket 3569.

¹⁰⁵Securities Act Release No. 6989 (Apr. 7, 1993), 53 SEC Docket 3565; Investment Company Act Release No. 19391 (Apr. 7, 1993), 53 SEC Docket 3565.

¹⁰⁶Securities Act Release No. 6982 (Mar. 19, 1993), 53 SEC Docket 2847; Investment Company Act Release No. 19342 (Mar. 19, 1993), 53 SEC Docket 2847.

¹⁰⁷Investment Company Act Release No. 19362 (Mar. 26, 1993), 53 SEC Docket 2124.

¹⁰⁸Investment Company Act Release No. 19658 (Aug. 25, 1993), 54 SEC Docket 1848.

¹⁰⁹Investment Company Act Release No. 19566 (July 9, 1993), 54 SEC Docket 1553.

¹¹⁰Investment Company Act Release No. 19382 (Apr. 6, 1993), 53 SEC Docket 3555.

¹¹¹Investment Company Act Release No. 19722 (Sept 21, 1993), 55 SEC Docket 0013.

¹¹²Letters to R. Clark Hooper, National Association of Securities Dealers, Inc. from Clifford E. Kirsch, Assistant Director, Office of Insurance Products, Division of Investment Management, SEC, dated March 5 and September 23, 1993.

¹¹³17 C.F.R. §§ 250.53, 250.54, 250.57.

¹¹⁴Holding Company Act Release No. 25886, International Series Release No. 583 (Sept. 23, 1993), 58 FR 51488 (Oct 1, 1993).

¹¹⁵Holding Company Act Release No. 25887, International Series Release No. 584 (Sept. 23, 1993), 58 FR 51508 (Oct 1, 1993).

¹¹⁶*Ohio Power Co. v. FERC*, 954 F.2d 779 (D.C. Cir. 1992), *cert. denied*, 113 S. Ct 483 (1992) (on remand, holding that SEC orders should be read as requiring Ohio Power to pay a price "equal to cost" for Southern Ohio coal).

¹¹⁷Investment Company Act Release Nos. 19274 (Feb. 18, 1993) (53 SEC Docket 10 (Notice) and 19334 (Mar. 6, 1993), 53 SEC Docket 14 (Order).

¹¹⁸Investment Company Act Release Nos. 19594 (July 26, 1993), 54 SEC Docket 13 (Notice) and 19647 (Aug. 23, 1993), 54 SEC Docket 17 (Order).

¹¹⁹Investment Company Act Release Nos. 19660 (Aug. 26, 1993), 54 SEC Docket 17 (Notice) and 19730 (Sept 21, 1993), 55 SEC Docket 0166 (Order).

¹²⁰*Bolsade Valores de Sao Paulo* (pub. avail. Oct. 28, 1992), *Camara de Liquidacao e Custodia S/A* (pub. avail. Oct. 28, 1992), *Austradear Limited* (pub. avail. Apr. 6, 1993), *Custody of B Shares Trading on the Shenzhen and Shanghai Securities Exchanges* (pub. avail. Apr. 26, 1993) *Jardine Fleming China Region Fund, Inc.* (pub. avail. Apr. 26, 1993), *Korean Securities Depository Corporation* (pub. avail. May 14, 1993), *Malaysian Central Depository Sdn. Bhd.* (pub. avail. May 19, 1993), *Reserve Bank of New Zealand* (pub. avail. May 24, 1993), *The Stock Exchange of Thailand* (pub. avail. Aug. 26, 1993), and *Japan Securities Depository Center* (pub. avail. Aug. 31, 1993).

¹²¹*Union Bank of Norway* (pub. avail. Nov. 30, 1992) and *Pictet & Cie* (pub. avail. Sept. 8, 1993).

¹²²*Alliance Capital Management L.P.* (pub. avail. Apr. 7, 1993).

¹²³*The South America Fund N.V.* (pub. avail. Sept 2, 1993).

¹²⁴*T. Rowe Price Tax-Free Funds* (pub. avail. June 24, 1993).

¹²⁵United Services Funds (pub. avail, Apr. 17, 1993).

¹²⁶DST Systems, Inc., *et al.* (pub. avail. Feb. 2, 1993).

¹²⁷Mercury Asset Management (pub. avail. Apr. 16, 1993).

¹²⁸The National Mutual Group (pub. avail. Mar. 8, 1993).

¹²⁹*College Retirement Equities Fund*, Investment Company Act Release Nos. 18630 (Mar. 24, 1992) (Notice) and 19463 (May 6, 1993) (Order).

¹³⁰*Provident Mutual Life Insurance Company of Philadelphia*, Investment Company Act Release Nos. 19515 (June 4, 1993) (Notice) and 19552 Only 1, 1993) (Order); *Merrill Lynch Life Insurance Company*, Investment Company Act Release Nos. 19476 (May 17, 1993) (Notice) and 19521 (June 9, 1993) (Order); *The Manufacturers Life Insurance Company of America, et al.*, Investment Company Act Release Nos. 18891 (Aug. 11, 1992) (Notice) and 18942 (Sept 10, 1992) (Order).

¹³¹*American Skandia Life Assurance Corporation*, Investment Company Act Release Nos. 19787 (Oct. 13, 1993) (Notice) and 19850 (Nov. 10, 1993) (Order).

¹³²The Travelers Insurance Company et al. (avail. Sept. 3, 1993).

¹³³Fortis Benefits (avail, June 8, 1993); The Travelers T-Mark Annuity (avail. May 13, 1993).

¹³⁴*Entergy Corporation, et al.*, Holding Company Act Release No. 25718 (Dec. 28, 1992) 53 SEC Docket 620.

¹³⁵The cases have been consolidated for procedural purposes and are jointly administered under the caption *In re The Columbia Gas System, Inc. and Columbia Gas Trans. Corp.*, No. 91-803 (Bankr. D. Del.).

¹³⁶*The Columbia Gas System, Inc., et al.*, Holding Company Act Release No. 25896 (Sept 24, 1993), 55 SEC Docket 296.

¹³⁷*Entergy Corporation, et al*, Holding Company Act Release No. 25669 (Nov. 6, 1992), 52 SEC Docket 3721.

¹³⁸*Northeast Utilities, et al.*, Holding Company Act Release No. 25900 (Sept 30, 1993), 55 SEC Docket 347.

¹³⁹*American Electric Power Company, Inc., et al.*, Holding Company Act Release No. 25871 (Aug. 25, 1993), 54 SEC Docket 2347.

¹⁴⁰*Arkansas Power & Light Co.*, Holding Company Act Release No. 25761 (Mar. 16, 1993), 53 SEC Docket 2568.

¹⁴¹*Unitil Corporation, et al.*, Holding Company Act Release No. 25816 (May 24, 1993), 54 SEC Docket 502.

¹⁴²*Eastern Utilities Associates, et al.*, Holding Company Act Release No. 25719 (Dec. 29, 1992), 53 SEC Docket 634.

¹⁴³*ESJ Energy, Inc., et al.*, Holding Company Act Release No. 25654, International Series Release No. 474 (Oct. 16, 1992), 52 SEC Docket 3163.

¹⁴⁴Securities Act Release No. 6962 (Oct. 16, 1992), 52 SEC Docket 2980.

¹⁴⁵Exchange Act Release No. 32723 (Aug. 6, 1993), 54 SEC Docket 1979.

¹⁴⁶Securities Act Release No, 6964 (Oct. 22, 1992), 52 SEC Docket 3014.

¹⁴⁷Securities Art Release No, 6997 (Apr. 28, 1993), 53 SEC Docket 6775.

¹⁴⁸Securities Act Release No. 7004 (June 28, 1993), 54 SEC Docket 1121.

¹⁴⁹Securities Act Release No. 7006 (July 2, 1993), 54 SEC Docket 1339.

¹⁵⁰Securities Act Release No. 7002 (June 10, 1993) 54 SEC Docket 759.

¹⁵¹Exchange Act Release No. 32574 (July 2, 1993), 54 SEC Docket 1341.

¹⁵²Securities Act Release No. 6996 (Apr. 28, 1993), 53 SEC Docket 4129.

¹⁵³Securities Act Release No. 6977 (Feb. 23, 1993), 53 SEC Docket 1798.

¹⁵⁴Staff Accounting Bulletin No. 92 (June 8, 1993), 54 SEC Docket 864.

¹⁵⁵Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities" (May 1993).

¹⁵⁶Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan" (May 1993).

¹⁵⁷Proposed Statement of Financial Accounting Standards, "Accounting for Stock-based Compensation" (June 30, 1993).

¹⁵⁸Statement on Auditing Standards No. 72, "Letters for Underwriters and Certain Other Requesting Parties" (Feb. 1993).

¹⁵⁹Statement of Position 93-1, "Financial Accounting and Reporting for High Yield Securities by Investment Companies" (Jan. 28, 1993); Statement of Position 93-2, "Determination, Disclosure,

and Financial Statement Presentation of Income, Capital Gain, and Return of Capital by Investment Companies" (Feb. 1, 1993); and Statement of Position 93-4, "Foreign Currency Accounting and Financial Statement Presentation for Investment Companies" (Apr. 22, 1993).

¹⁶⁰Proposed Statement of Position, "Disclosure of Certain Significant Risks and Uncertainties and Financial Flexibility" (Mar. 31, 1993).

¹⁶¹IAS 2 (revised 1993), Inventories; IAS 8 (revised 1993), Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies; IAS 9 (revised 1993), Research and Development Costs; IAS 11 (revised 1993), Construction Contracts; IAS 16 (revised 1993), Property, Plant and Equipment; IAS 18 (revised 1993), Revenue; IAS 19 (revised 1993), Retirement Benefit Costs; IAS 21 (revised 1993), The Effects of Changes in Foreign Exchange Rates; IAS 22 (revised 1993), Business Combinations; and IAS 23 (revised 1993), Borrowing Costs.

¹⁶²Release No 33-7029 (Nov. 3, 1993), 55 SEC Docket 979.

¹⁶³ISA 31, "Consideration of Laws and Regulations in an Audit of Financial Statements" (July 1993).

¹⁶⁴*Musick, Peeler & Garrett v. Employers Insurance of Wassau*, 113 S. Ct 2085 (1993).

¹⁶⁵*First Interstate Bank of Denver v. Pring*, 969 F.2d 891 (10th Cir. 1992), petition for *cert.* granted sub nom. *Central Bank of Denver v. First Interstate Bank of Denver*, 113 S. Ct. 2927(1993).

¹⁶⁶*SEC v. Rind*, 991 F.2d 1486 (9th Cir. 1993), *cert. denied*, 114 S. Ct 439 (1993).

¹⁶⁷*Supra*, note 1.

¹⁶⁸*Supra*, note 2.

¹⁶⁹Lampf, Pleva, Upland, Prupis & Petigrow v. Gilbertson, 111 S. Ct 2773 (1991).

¹⁷⁰Cooperativa de Ahorro y Credito Aguada v. Kidder, Peabody & Co., 993 R2d 269 (1st Or. 1993), *petition for cert. filed*, (U.S. Oct. 12, 1993) (No. 93-564)

¹⁷¹*Pacific Mutual Life Insurance Co. v. First Republicbank Corp.*, 997 F.2d 39 (5th Or. 1993), *petition for cert. filed*, 62 U.S.L.W. 3165 (US, Aug. 26, 1993) (No. 93-313).

¹⁷²*Plaut v. Spendthrift Farm, Inc.*, 1 F.3d 1487 (6th Or, 1993).

¹⁷³*Johnston v. Cigna Corp.*, Slip op., No, 92-1186 (10th Cir. Dec. 7, 1993).

¹⁷⁴*Supra* note 8.

¹⁷⁵*SEC v. Rind*, 991 F.2d 1486 (9th Cir. 1993), *cert. denied*, 114 S. Ct. 439 (1993).

¹⁷⁶*ACTWU v. SEC*, No. 93-4120 (2nd Cur. Jan. 13, 1994).

¹⁷⁷*NYCERS v. SEC*, 93 Civ. 1233 (S.D.N.Y., Oct. 15, 1993), *appeal pending*, No. 93-6314 (2nd Or.),

¹⁷⁸*SEC v. Huffman*, 996 F.2d 800 (5th Cir. 1993).

¹⁷⁹*SEC v. AMX International, Inc.*, No. 92-1376 (5th Cir.).

¹⁸⁰28 U.S.C. 3001 *et. seq.*

¹⁸¹*United States v. Teicher*, 987 F.2d 112 (2nd Cir. 1993), *cert. denied*, 114 S. Ct. 467 (1993).

¹⁸²*United States v. Libera*, 989 F.2d 596 (2nd Cir. 1993), *cert. denied sub nom., Sablone v. United States*, 114 S. Ct 467 (1993).

¹⁸³*F.B. Horner & Associates, Inc. v. SEC*, 994 F.2d 61 (2nd Cir. 1993).

¹⁸⁴*Timpinaro v. SEC*, 2 F.3d 453 (D.C. Cir. 1993).

¹⁸⁵*Freeman v. SEC*, No. 093-866-SAW (D.D.C); *Denardo v. SEC*, Civ. No. 93-1757 (RCL); *Weingueter Baron K.S. von Strauss Erben Trust v. SEC*, No. 93-1925 (D.D.C.)

¹⁸⁶*Alexander & Alexander Services, Inc. v. SEC*, No. 92-1112 (D.D.C. October 19, 1993).

¹⁸⁷*SEC v. Van Waegenberghe*, No. 92-1000 (5th Cir. May 17, 1993).

¹⁸⁸*Creative Investment Services, Inc. v. SEC*, No. 93-C-83 (D. Colo.); *in the Matter of Public Funding*, No. 93-336 Civ. Atkins (S.D. Fla.) (presently on appeal to the 11 th Circuit No. 93-781).

¹⁸⁹*Moler v. SEC*, No. 93-Z-1094 (D. Goto.).

¹⁹⁰*Alwrez v. SEC*, No. C93-29 VRW Misc. (N.D. CaL); *Whitney v. SEC*, No. C93-28 VRWMisc.(N.D.Cal.).

¹⁹¹*In re Checkosky and Aldrich*, Exchange Act Release No. 31094 (Aug. 26, 1992), 52 SEC Docket 1389, appeal pending, No. 92-5158 (D.C Or.).

¹⁹²*In re Robert J. Iommazzo*, Exchange Act Release No. 31 726 (Jan. 12, 1993),53 SEC Docket 870.

¹⁹³*In re Gregory Melson*, Exchange Act Release No. 32917 (Sept. 17, 1993), 55 SEC Docket 38.

¹⁹⁴*In re Martin G. Broume*, Exchange Act Release No. 32854 (Sept. 16, 1993), 54 SEC Docket 2542.

¹⁹⁵ *Investment Planning Inc.* Exchange Act Release No. 32687 (July 28, 1993) (54 SEC Docket 1770).

¹⁹⁶ *Id.*

¹⁹⁷ *First Honolulu Securities, Inc. and Charles Jacobson*, Exchange Act Release No. 32933 (Sept 21, 1993), 55 SEC Docket 73.

¹⁹⁸ *Bison Securities, Inc.*, Exchange Act Release No. 32034 (Mar, 23, 1993), 53 SEC Docket 2892.

¹⁹⁹ *Patten Securities Corporation and John L Patten*, Exchange Act Release No. 3261 (July 12, 1993), 54 SEC Docket 1472.

²⁰⁰ *Allan Mace Leavitt*, Exchange Act Release No. 32441 (June 10, 1993), 54 SEC Docket 813.

²⁰¹ *Datek Securities Corp.*, Exchange Act Release No. 32560 (June 30, 1993), 54 SEC Docket 11 196.

²⁰² *In re Leslie Fay Companies, Inc.*, Case No. 93-B41724 TLB (Bankr. S.D.N.Y.) and *In re Wang Laboratories, Inc.*, Case No 92-18525 (WCH) (Bankr. D. Mass.).

²⁰³ *In re American West Airlines, Inc.*, Case No. 91-07505-PHX-RGM (Bankr. D. Ariz.).

²⁰⁴ *In re National Convenience Stores, Inc.*, Case No. 91-49816-H2-11 (Bankr. S.D. Tex.).

²⁰⁵ *In re MCorp Financial Inc.*, Case Nos. 89-02312-H3-1 1, 89-02324-H5-11 and 89-02848-H2-11 (Bankr. N.D. Tex.).

²⁰⁶ *In re Master Mortgage Investment Fund, Inc.*, Case No. 92-41306-211 (Bankr. W.D. Mo.).

²⁰⁷See, e.g., *In re Prime Motor Inn*, *In re Servico Corp.*, *In re The Washington Corp.* and *In re Lomas 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 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).

²⁰⁸*In re Bioplasty, Inc.*, Case No. 4-93-02600 (Bankr. D. Minn.) and *In re The Centennial Group, Inc.*, Case No SA 9-41813 JW (Bankr. CD. Cal.).

²⁰⁹*Id.*