UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 67709 / August 22, 2012

INVESTMENT ADVISERS ACT OF 1940
Release No. 3448 / August 22, 2012

INVESTMENT COMPANY ACT OF 1940
Release No. 30179 / August 22, 2012

ADMINISTRATIVE PROCEEDING
File No. 3-14993

In the Matter of **MIDDLECOVE CAPITAL, LLC, AND NOAH L. MYERS,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, SECTIONS 203(e), 203(f), AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940, AND SECTION 9(b) OF THE INVESTMENT COMPANY ACT OF 1940**

I.

The United States Securities and Exchange Commission (the "Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act"), and Section 9(b) of the Investment Company Act of 1940 ("Investment Company Act") against MiddleCove Capital, LLC ("MiddleCove") and Noah L. Myers ("Myers") (collectively, "the Respondents").

II.

After an investigation, the Division of Enforcement alleges that:

A. SUMMARY

1. From approximately October 2008 to February 2011 (the "relevant period"), Noah L. Myers, the sole owner of MiddleCove Capital, LLC, engaged in fraudulent trade allocation – "cherry-picking" – at MiddleCove. During the relevant period, MiddleCove was a registered investment adviser. Myers executed his cherry-picking scheme by unfairly allocating trades that had appreciated in value during the course of the day to his personal and business accounts and allocating trades that had depreciated in value during the day to the accounts of his

advisory clients. He did this by purchasing securities in an omnibus account and delaying allocation of the purchases until later in the day (and sometimes the next day), after he saw whether the securities appreciated in value. When a security appreciated in value on the day of purchase, Myers would often sell the security and disproportionately allocate the purchase and the realized day-trading profit to his own accounts or accounts benefiting himself or his family members. In contrast, for securities that did not appreciate on the day of purchase, Myers would disproportionately allocate these purchases to his clients' accounts and his clients would hold the position for more than one day. Myers carried out his cherry-picking scheme with regard to several securities, but was most active with an inverse and leveraged exchange traded fund (ETF). Myers finally ceased these practices in February 2011 when one of his employees threatened to contact the Commission. As a result of his fraud, Myers realized ill-gotten gains of approximately $460,000. Myers's cherry-picking scheme also resulted in more than $2 million in client losses from his trading in the inverse and leveraged ETF. Neither MiddleCove nor Myers disclosed to clients that they were engaged in cherry-picking and that they would favor Myers's accounts in the allocation of appreciated securities. In addition, Myers and MiddleCove failed to follow the policies stated in MiddleCove's ADV concerning trade allocation.

2. By virtue of their conduct, the Respondents willfully violated Section 10(b) of the Exchange Act [15 U.S.C. §§78j(b)] and Rule 10b-5 [17 C.F.R. §§240.10b-5] promulgated thereunder, and Sections 206(1) [15 U.S.C. §80b-6(1)], 206(2) [15 U.S.C. §80b-6(2)] and 207 [15 U.S.C. §80b-7] of the Advisers Act.

B. RESPONDENTS

3. **MiddleCove Capital, LLC** (SEC File No. 801-68677), is a Connecticut limited liability company with its principal place of business in Centerbrook, Connecticut. It has been registered with the Commission as an investment adviser since 2008 when Myers formed MiddleCove. At its peak in 2011, when MiddleCove had two portfolio managers including Myers, MiddleCove managed approximately $129 million in client assets. MiddleCove is wholly owned and controlled by Myers. In mid-2011, one of MiddleCove's portfolio managers left the firm after being there for approximately one year. As a result of his departure, MiddleCove's assets under management declined by approximately one-half. MiddleCove currently has no employees other than Myers. As of September 31, 2011, MiddleCove managed approximately 350 client accounts and had approximately $53,000,000 under management. MiddleCove's clients are individuals and families.

4. **Noah L. Myers**, age 40, resides in Old Lyme, Connecticut. Myers is the principal, chief investment officer, and sole owner of MiddleCove. Myers formed MiddleCove in early 2008 after an eleven-year career at Citigroup Global Markets Inc. ("Citigroup"). During the relevant time period, Myers was also a registered representative of Purshe Kaplan Sterling Investments, Inc. ("Purshe Kaplan"), a registered broker-dealer located in Albany, New York. Myers asserted his privilege against self-incrimination when he testified in the investigation.

C. OTHER RELEVANT ENTITY

5. **Purshe Kaplan Sterling Investments, Inc.** (SEC File No. 8-46844), is a New York corporation with its principal place of business in Albany, New York. Purshe Kaplan has been registered with the Commission as a broker-dealer since 1994. Myers was a registered representative of Purshe Kaplan during the relevant time period.

D. RESPONDENTS' CONDUCT

The cherry-picking scheme.

6. Myers formed MiddleCove in February 2008, and, in April 2008, Myers began using an omnibus account ("master account") at Charles Schwab & Co., Inc. ("Charles Schwab"), the custodian for all of MiddleCove's accounts, to place orders for his personal and client transactions. When he used the master account to purchase securities, Myers would place a block trade in the master account and then allocate the shares to his personal and client accounts.

7. Prior to October 2008, Myers was relatively inactive in his own accounts as compared to his client accounts. However, Myers began day-trading his own accounts in October 2008 and actively traded his own accounts over the next two years. From October 2008 to February 2011, Myers allocated approximately $60 million in securities purchased in the master account to his personal and business accounts, compared to approximately $200 million in securities purchased in the master account and allocated to MiddleCove's clients. Myers's personal trading activity, including his day-trading, slowed considerably after a MiddleCove employee confronted Myers in late 2010 about his cherry-picking scheme.

8. From October 2008 to February 2011, Myers engaged in a cherry-picking scheme to misappropriate profitable transactions to his personal and business accounts. Myers made block purchases of securities in the master account sometime during the trading day before the 4 P.M. close of the U.S. stock market. After making a purchase, Myers delayed allocating it until he knew whether there was a gain or loss on the trade on the day of purchase. During the relevant time period, approximately 65% of the purchases that Myers allocated to his clients were not allocated until after 4 P.M. on the day of the purchase. On some occasions, Myers would even wait until the next day to allocate a purchase and then mark the allocated trade "As Of" the day it was purchased in the market. This timing difference made it possible for Myers to selectively allocate profitable trades to his own accounts. If the security increased in price on the day of purchase, Myers would often sell the security on the same day he purchased it (a "day trade") and disproportionately allocate the day-trade profit to his personal and business accounts. However, if the security's price did not increase on the day of purchase, Myers disproportionately allocated the purchase to his clients' accounts.

9. Myers's scheme often involved purchasing a security in the master account for consecutive days over several weeks, or even months, and then allocating the security depending on its performance. If it increased in value on the day of purchase, he disproportionately allocated the security to his own accounts. If the security decreased in value on the day of purchase, Myers disproportionately allocated it to his clients' accounts. Thus, the securities on

which Myers was disproportionately making money were the same securities on which his clients were disproportionately losing money. In fact, during the relevant time period, when Myers allocated a trade to his own accounts, he had almost always allocated the same security to his clients' accounts on a different trading day within one month of the allocation to his own accounts. The only consistent difference in whether Myers allocated a security to his own accounts or his clients' accounts was whether the security appreciated in value on the day it was purchased.

The scheme is identified.

10. Charles Schwab had an internal program that flagged Myers's accounts as potentially receiving favorable allocation of profitable day trades. A MiddleCove employee investigated Myers's trading patterns after he received a call from an employee of Charles Schwab in November 2010. The Schwab employee indicated that Schwab had flagged the allocation of MiddleCove's block trades as potentially giving profitable trades to an account that benefited Myers. As a result of the call, the MiddleCove employee analyzed Myers's trade allocation for a stock (Research in Motion or RIMM) and a leveraged ETF (ProShares UltraShort Financials or SKF). From his analysis of Myers's trade allocation of these two securities, the employee suspected that Myers was cherry-picking trades in favor of his own account at the expense of his clients. Specifically, the employee believed, based on his review of Myers's trade allocation, that Myers was allocating trades that lost money at the end of the day to clients instead of himself and that the performance for Myers's accounts was much more profitable than his clients' accounts.

11. Following the MiddleCove employee's analysis of Myers's cherry-picking scheme, all four of MiddleCove's employees confronted Myers about his trade allocation in mid-December 2010. As a result of the confrontation, Myers agreed to use a trading method that required Myers to place all of his client trades through a certain Charles Schwab trade application, and to use a different method for his own trades.

12. On February 18, 2011, the same MiddleCove employee who had analyzed Myers's trading in November noticed Myers had allocated a day trade profit to himself using the Charles Schwab trade application that Myers had agreed to only use for clients' trades. The employee confronted Myers and threatened to report Myers to the Commission if he did not re-allocate the trade. Myers agreed to re-allocate the trade to a client. After this confrontation, Myers stopped cherry-picking and did relatively little trading in his own accounts.

13. Commission examination staff interviewed Myers in November 2011 about his own securities trading. Myers admitted that he had a day-trading strategy in one of his personal accounts that was profitable about 95% of the time, but he did not offer a plausible explanation for his stellar day-trading performance.

Myers profited at his clients' expense.

14. During the relevant time period, trades that Myers made in his own accounts increased in value by an average of approximately 67 basis points (or .67 of one-percent) on the day that Myers purchased the security. This 67 basis-point increase resulted in approximately

$408,000 in first-day profits for Myers's own accounts. In contrast, during the relevant time period, trades that Myers allocated to his clients' accounts *decreased* by approximately 32 basis points on the day that Myers purchased the security. This difference in return is highly statistically significant – the likelihood of Myers experiencing his first-day return (approximately 67 basis points) compared to the average first-day return for all of his and his clients' purchases (approximately negative 32 basis points) from a "lucky" allocation of trades is less than one in ten million. Similarly, approximately 74% of Myers's trades had a profit on the first day compared to approximately 52% of his clients' trades – the likelihood of observing a difference in profitably this large by chance is less than one in one trillion.

15. Myers realized approximately $138,000 in profits on his trades of SKF (the leveraged and inverse ETF discussed above) while his clients realized a net loss of approximately $2.2 million on their SKF trades. These losses were spread out among approximately 120 clients.

16. Myers's cherry-picking scheme also resulted in significant investment losses for MiddleCove clients to whom Myers allocated shares of SKF. Many of the clients did not know what SKF was or that they had invested in a leveraged ETF, even when their investment in SKF was a significant part of their account value and they experienced significant losses because of it. Many of these clients were retired and/or were using their MiddleCove account as their source of funds for retirement and had limited willingness or ability to accept significant investment risk.

17. Leveraged and inverse ETFs like SKF are generally not designed to be held for more than one day. In June 2009, FINRA issued Notice to Members 09-31 reminding firms of their sales practice obligations relating to leveraged and inverse ETFs. SKF is a leveraged and inverse ETF designed to achieve daily investment results corresponding to twice the inverse (opposite) of the daily performance of the Dow Jones U.S. Financials Index. The FINRA notice described how leveraged and inverse ETFs are designed to achieve their stated objectives on a daily basis, and, "[d]ue to the effect of compounding, their performance over longer periods of time can differ significantly from the performance (or inverse of the performance) of the underlying index or benchmark during the same period of time. . . This effect can be magnified in volatile markets." With an inverse or a leveraged ETF, if the relevant benchmark moves 100 points in one direction on day one and returns to the original level on day two, an investment in the ETF held for both days will be negative even though the benchmark is flat. (If, on the other hand, the benchmark moved in the same direction on both days, an investor in the ETF would have even better performance than shorting the index or investing in the index on margin.) If the ETF is an inverse and leveraged ETF, as is the case with SKF, the loss would be more significant. For these and other reasons, the FINRA notice concluded that "While the customer-specific suitability analysis depends on the investor's particular circumstances, inverse and leveraged ETFs typically are not suitable for retail investors who plan to hold them for more than one trading session, particularly in volatile markets."

18. During the period of his cherry-picking scheme, approximately one-third of Myers's one-day profits were from SKF trades. These profits came at the expense of approximately $2 million in client losses because Myers exposed his clients to the downside of this volatile security so that he could reap the rewards when SKF rose in value on the day of purchase. This scheme meant that Myers held SKF for more than one day in the accounts of

several clients for whom such an investment was inappropriate. Moreover, at times, SKF was a considerable proportion of the holdings of his clients, further magnifying their investment risk. For example, Myers's decision to use SKF as his tool for his cherry-picking scheme extended to:

- Investor A, age 84 and retired, invested all of her savings with MiddleCove. She described herself as conservative investor. Nonetheless, in September 2009, Myers established an $89,727.74 SKF position for this investor, which was 34.3% of her month-end account balance. The investor lost a net of $14,543 on SKF, and she had no idea what this security was.

- Investor B, age 77 and retired, had his retirement savings completely with MiddleCove. He viewed himself as "moderate risk" investor. In September 2009, Myers established a $251,196.95 SKF position for this investor in his only account, representing about 28% of the account. The investor lost a net of $59,483 on SKF.

- Investor C, age 70 and retired, was a client who described himself as unsophisticated. In September 2009, Investor C had approximately $239,288.89 of SKF, or approximately 87.7% of the account's month end value. The investor had no knowledge of what SKF was, and he lost a net of $83,264 on SKF.

The scheme was contrary to MiddleCove's Form ADV.

19. During the relevant time period, MiddleCove filed its Form ADV, Part II on April 29, 2009, and March 29, 2010. Items 12A, 12B, and 13A of the Form ADV, Part II stated, in pertinent part:

> Transactions for each client generally will be effected independently, unless the Adviser decides to purchase or sell the same securities for several clients at approximately the same time. The Adviser may (but is not obligated to) combine or "batch" such orders to obtain best execution, to negotiate more favorable commission rates, or to allocate equitably among the Adviser's clients differences in prices and commissions or other transaction costs that might have been obtained had such orders been placed independently. Under this procedure, transactions will generally be averaged as to price and allocated among the Adviser's clients pro rata to the purchase and sale orders placed for each client on any given day. To the extent that the Adviser determines to aggregate client orders for the purchase or sale of securities, including securities in which the Adviser's Advisory Affiliate(s) may invest, the Adviser shall generally do so in accordance with applicable rules promulgated under the Advisers Act and no-action guidance provided by the staff of the U.S. Securities and Exchange Commission. The Adviser shall not receive any additional compensation or remuneration as a result of the aggregation.

The same items in the ADV went on to list specific circumstances in which allocations may not be *pro rata* among accounts. These statements, taken as a whole, were misleading because the statements conveyed the impression that batched trades would be allocated fairly and not unduly favor Myers or MiddleCove, and, when trades included securities in which the "Adviser's

Advisory Affiliate(s) may invest," there would be extra layer of protection provided by a regulatory framework.

E. VIOLATIONS

20. By knowingly or recklessly allocating profitable trades to Myers's personal and business accounts at the expense of advisory clients, Myers and MiddleCove willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in connection with the purchase or sale of securities. In addition, through this cherry-picking scheme and by failing to disclose the scheme, Myers and MiddleCove willfully violated Sections 206(1) and 206(2) of the Advisers Act, which prohibit fraudulent conduct by an investment adviser with respect to advisory clients or prospective clients.

21. During the relevant period, MiddleCove filed misleading Forms ADV that willfully made material misstatements concerning MiddleCove's trade allocation policies and procedures. Therefore, MiddleCove willfully violated Section 207 of the Advisers Act. By signing and causing to be filed on behalf of MiddleCove these misleading Forms ADV, Myers also willfully violated Section 207 of the Advisers Act.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate and in the public interest that administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II hereof are true and, in connection therewith, to afford Respondents an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Section 15(b) of the Exchange Act including, but not limited to, disgorgement and civil penalties pursuant to Section 21B of the Exchange Act;

C. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Sections 203(e) and 203(f) of the Advisers Act including, but not limited to, disgorgement and civil penalties pursuant to Section 203 of the Advisers Act;

D. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Section 9(b) of the Investment Company Act; and

E. Whether, pursuant to Section 21C of the Exchange Act and Section 203(k) of the Advisers Act Respondents should be ordered to cease and desist from committing or causing violations of and any future violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder and Sections 206(1), 206(2), and 207 of the Advisers Act, whether Respondents should be ordered to pay a civil penalty pursuant to Section 21B(a) of the Exchange Act and Section 203(i) of the Advisers Act, and whether Respondents should be ordered to pay disgorgement pursuant to Sections 21B(e) and 21C(e) of the Exchange Act and Section 203 of the Advisers Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondents shall each file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If either of the Respondents fail to file the directed answer, or fails to appear at a hearing after being duly notified, that Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondents personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary