

## ***INTRODUCTION***

The U.S. Securities and Exchange Commission (SEC) is a civil law enforcement agency. Since its creation in 1934, the SEC's mission has been to administer and enforce the federal securities laws in order to protect investors, and to maintain fair, honest, and efficient markets. Though it is the primary overseer and regulator of the U.S. securities markets, the SEC works closely with many other institutions, including Congress, other federal departments and agencies, the self-regulatory organizations (*e.g.*, the stock exchanges), state securities regulators, and various private sector organizations.

The SEC is pleased to provide this Annual Report for fiscal year 2002. The activities and accomplishments presented on the following pages continue the agency's long tradition of effective enforcement in and regulation of our nation's capital markets.

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## Table of Contents

Commission Members and Principal Staff Officers	vii
Biographies of Commission Members	x
Harvey L. Pitt ♦ Cynthia A. Glassman ♦ Roel C. Campos ♦ Harvey J. Goldschmid ♦ Paul S. Atkins	
Regional and District Offices	xvi
Enforcement	1
International Affairs	12
Investor Education and Assistance	24
Regulation of Securities Markets	32
Investment Management Regulation	51
Compliance Inspections and Examinations	68
Full Disclosure System	77
Accounting and Auditing Matters	85
Other Litigation and Legal Activities	102
Economic Research and Analysis	122
Program Management & Administrative Support	127
Endnotes	132
Appendix	143

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# Commission Members and Principal Staff Officers

(As of November 4, 2002)

Commissioners	Term Expires
<b>Harvey L. Pitt</b> , <i>Chairman</i>	2007
<b>Cynthia A. Glassman</b> , <i>Commissioner</i>	2006
<b>Roel C. Campos</b> , <i>Commissioner</i>	2005
<b>Harvey J. Goldschmid</b> , <i>Commissioner</i>	2004
<b>Paul S. Atkins</b> , <i>Commissioner</i>	2003

**Mark Radke**, *Chief of Staff*

**Lisa Panasiti**, *Deputy Chief of Staff*

**Jonathan G. Katz**, *Secretary of the Commission*

## Principal Staff Officers

**Alan Beller**, *Director, Division of Corporation Finance*

**Martin Dunn**, *Deputy Director*

**James Daly**, *Associate Director*

**Mauri Osheroff**, *Associate Director*

**Shelley E. Parratt**, *Associate Director*

**Carol Stacey**, *Associate Director*

**William Tolbert**, *Associate Director*

**Vacant**, *Associate Director*

**Stephen M. Cutler**, *Director, Division of Enforcement*

**Linda C. Thomsen**, *Deputy Director*

**William Baker**, *Associate Director*

**Paul Berger**, *Associate Director*

**Antonia Chion**, *Associate Director*

**Thomas Newkirk**, *Associate Director*

**Joan McKown**, *Chief Counsel*

**David Kornblau**, *Chief Litigation Counsel*

**Peter H. Bresnan**, *Deputy Chief Litigation Counsel*

**Charles Niemeier**, *Chief Accountant*

**Paul Roye**, *Director, Division of Investment Management*  
**Cynthia Fornelli**, *Deputy Director*  
**Barry D. Miller**, *Associate Director*  
**Susan Nash**, *Associate Director*  
**Robert Plaze**, *Associate Director*  
**Douglas Scheidt**, *Associate Director*  
**David B. Smith**, *Associate Director*

**Annette Nazareth**, *Director, Division of Market Regulation*  
**Robert L.D. Colby**, *Deputy Director*  
**Alden Adkins**, *Associate Director*  
**Larry E. Bergmann**, *Associate Director*  
**Elizabeth King**, *Associate Director*  
**Michael A. Macchiaroli**, *Associate Director*  
**Catherine McGuire**, *Associate Director/Chief Counsel*

**Giovanni Prezioso**, *General Counsel, Office of General Counsel*  
**Meyer Eisenberg**, *Deputy General Counsel*  
**Meridith Mitchell**, *Principal Associate General Counsel*  
**Anne E. Chafer**, *Associate General Counsel*  
**Richard M. Humes**, *Associate General Counsel*  
**Diane Sanger**, *Associate General Counsel*  
**Jacob H. Stillman**, *Solicitor*

**Lori A. Richards**, *Director, Office of Compliance Inspections and Examinations*  
**Karen Burgess**, *Senior Advisor to the Director*  
**Mary Ann Gadziala**, *Associate Director*  
**Gene Gohlke**, *Associate Director*  
**John McCarthy**, *Associate Director*  
**John Walsh**, *Associate Director*

**Robert K. Herdman**, *Chief Accountant, Office of the Chief Accountant*

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

**Lawrence E. Harris**, *Chief Economist, Office of Economic Analysis*

**Brian Gross**, *Director of Communications*

**Jane Cobb**, *Director, Office of Legislative Affairs*

**Christi Harlan**, *Director, Office of Public Affairs*

**Susan Wyderko**, *Director, Office of Investor Education and Assistance*

**Deborah Balducchi**, *Director, Office of Equal Employment Opportunity*

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

**Vacant**, *Associate Executive Director*

**Margaret Carpenter**, *Associate Executive Director*

**Kenneth Fogash**, *Associate Executive Director*

**Jayne Seidman**, *Associate Executive Director*

**Vacant**, *Director, Office of International Affairs*

## Biographies of Commission Members



### **Chairman Harvey L. Pitt**

On August 3, 2001, President Bush appointed Harvey L. Pitt as the twenty-sixth Chairman of the United States Securities and Exchange Commission. Chairman Pitt had previously served as an attorney on the staff of the Commission from 1968 until 1978, the last three years of which he was the Commission's General Counsel.

For nearly a quarter of a century before rejoining the Commission, Chairman Pitt was in the private practice of law. Chairman Pitt also was a founding trustee and the president of the SEC Historical Society, and participated in a wide variety of bar and continuing education activities to further public consideration of significant securities law issues. Chairman Pitt served as an Adjunct Professor of Law at Georgetown University Law Center (1975-84), George Washington University Law School (1974-82) and the University of Pennsylvania School of Law (1983-84).

In his prior service with the Commission, before his appointment as the Commission's General Counsel (1975-78), Chairman Pitt started as a staff attorney in the Commission's Office of General Counsel (1968) and served in the following capacities over the next decade: Legal Assistant to SEC Commissioner Frank M. Wheat (1969); Special Counsel in the Office of General Counsel of the SEC (1970-72); Editor of the SEC's Institutional Investor Study Report (1972); Chief Counsel of the SEC's Division of Market Regulation (1972-73); and Executive Assistant to SEC Chairman Ray Garrett, Jr. (1973-75).

Chairman Pitt received a J.D. degree from St. John's University School of Law (1968), and his B.A. from the City University of



New York (Brooklyn College) (1965). He was awarded an honorary doctorate in law by St. John's University School of Law in June 2002.

### **Commissioner Cynthia A. Glassman, Ph.D.**

Cynthia A. Glassman was appointed by President Bush to the U.S. Securities and Exchange Commission and sworn in on January 28, 2002.



Prior to being appointed Commissioner, Dr. Glassman spent over 30 years in the public and private sectors focusing on financial services regulatory and public policy issues. She spent the first 12 years of her career at the Federal Reserve, first at the Federal Reserve Bank of Philadelphia and subsequently at the Board of Governors, where her positions included Chief of the Financial Reports Section and Special Assistant to Governor Henry C. Wallich. While at the Board of Governors, Dr. Glassman spent one year on assignment to the U.S. Department of the Treasury as Senior Economist in the Office of Capital Markets Legislation during the Carter Administration. Subsequently, she spent two years at Economists Incorporated, eight years at Furash & Company, where she was the Managing Director of the financial services regulatory and public policy practices, and five years at Ernst & Young, in the Risk Management and Regulatory Practice and the Quantitative Economics and Statistics group.

Dr. Glassman taught economics at the University of Cambridge, England, where she remains as a Senior Member of Lucy Cavendish College. She has served on the Boards of the Federal Reserve Board Credit Union, the National Economists Club, Women in Housing and Finance, and the Commission on Savings and Investment in America, and was on the Executive Advisory Committee for the

Bank Administration Institute's Certified Risk Professional Certification Program.

Dr. Glassman received her M.A. and Ph.D. in Economics from the University of Pennsylvania and her B.A. in Economics from Wellesley College.

### **Commissioner Roel C. Campos**



Roel C. Campos was nominated to the Securities and Exchange Commission by President George Bush on July 16, 2002 and confirmed by the Senate on July 25, 2002. He was sworn in as a Commissioner on August 20, 2002.

Prior to being nominated to the Commission, Mr. Campos was one of two principal owners of El Dorado Communications and served as an executive with the radio broadcasting company at its headquarters in Houston, Texas. Mr. Campos began his career, however, with the government, serving as an officer in the U.S. Air Force. For the next 15 years, he worked in Los Angeles, California for major law firms as a corporate transactions/securities lawyer and litigator. Campos served in the government for a second time beginning in 1985 as a federal prosecutor for several years in the U.S. Attorney's Office in Los Angeles. He successfully prosecuted complex and violent narcotics cartels. He also investigated and prosecuted major government contractors for fraudulent conduct. After being in private law practice for several years, he co-founded El Dorado Communications, Inc. Now, he has returned to the public sector.

Mr. Campos earned his J.D. from Harvard Law School (1979), his MBA from UCLA (1972) and his BS from the U.S. Air Force Academy (1971).

Mr. Campos was born in Harlingen, Texas, of Mexican-American parents. He married his high school sweetheart, Mini Villarreal, who now practices medicine in Houston, Texas. They have two boys, David, 16 and Daniel, 12.

### **Commissioner Harvey J. Goldschmid**

Harvey J. Goldschmid is a Commissioner at the United States Securities and Exchange Commission. He is on leave from the Columbia University School of Law, where he serves as Dwight Professor of Law. He has served as Dwight Professor since 1984, and was an Assistant Professor (1970-71), an Associate Professor (1971-73), and a Professor of Law (1973-84) at Columbia. In



1998-99, Professor Goldschmid served as General Counsel (chief legal officer) of the SEC, and from January 1 to July 15, 2000, he was Special Senior Advisor to SEC Chairman Arthur Levitt.

Professor Goldschmid is the author of numerous publications on corporate, securities, and antitrust law. He is a frequent lecturer at national and international legal programs and seminars. He received the 1999 Chairman's Award for Excellence from the SEC, and several teaching awards, including Columbia Law School's Willis L.M. Reese Award for Excellence in Teaching in both 1996 and 1997.

From 1980-93, Professor Goldschmid served as a Reporter for the American Law Institute's Corporate Governance Project. From 2000-01, he served as Chair of the Nominating Committee, and in 1998, completed a term as Treasurer and a member of the Executive Committee (*i.e.*, Board of Directors) of the Association of the Bar of the City of New York, where Professor Goldschmid previously served as Chair of the Executive Committee, Chair of the Committee on Securities Regulation, and Chair of the Committee on Antitrust and Trade Regulation. He also has served as Chair of the Section on Antitrust and Economic Regulation of the Association of

American Law Schools and as Founding Director of Columbia University's Center for Law and Economic Studies. He served in 1997-98 as a consultant to both the Federal Trade Commission and the SEC, and during this period, was a member of the Legal Advisory Committee (and Chair of its Subcommittee on Corporate Governance) of the New York Stock Exchange.

Professor Goldschmid received his J.D., magnum cum laude, from the Columbia University School of Law in 1965 and a B.A., also magna cum laude, from Columbia College in 1962. He was Articles Editor of the *Columbia Law Review* and a member of Phi Beta Kappa. His publications include *Cases and Materials on Trade Regulation* (4<sup>th</sup> ed. 1997) (with Handler, Pitofsky, and Wood); *The Impact of the Modern Corporation* (1984) (with Bock, Millstein, and Scherer); *Business Disclosure: Government's Need to Know* (1979); and *Industrial Concentration: The New Learning* (1974) (with Mann and Weston).

### **Commissioner Paul S. Atkins**

Paul S. Atkins was appointed by President George W. Bush to be a commissioner of the Securities and Exchange Commission on July 29, 2002 and began his service on August 9, 2002.



Commissioner Atkins has a 20-year career focusing on the financial services industry and securities regulation. Before his appointment as commissioner, he assisted financial services firms in improving their compliance with SEC regulations and worked with law enforcement agencies to investigate and rectify situations where investors had been harmed. The largest of these investigations entailed assisting the bankruptcy trustee of the Bennett Funding Group, Inc., a \$1 billion leasing company that was the largest “Ponzi” fraud in U.S. history in which more than 20,000 investors lost much of their investment. In connection with that bankruptcy, he served as crisis president of the sole surviving subsidiary--he

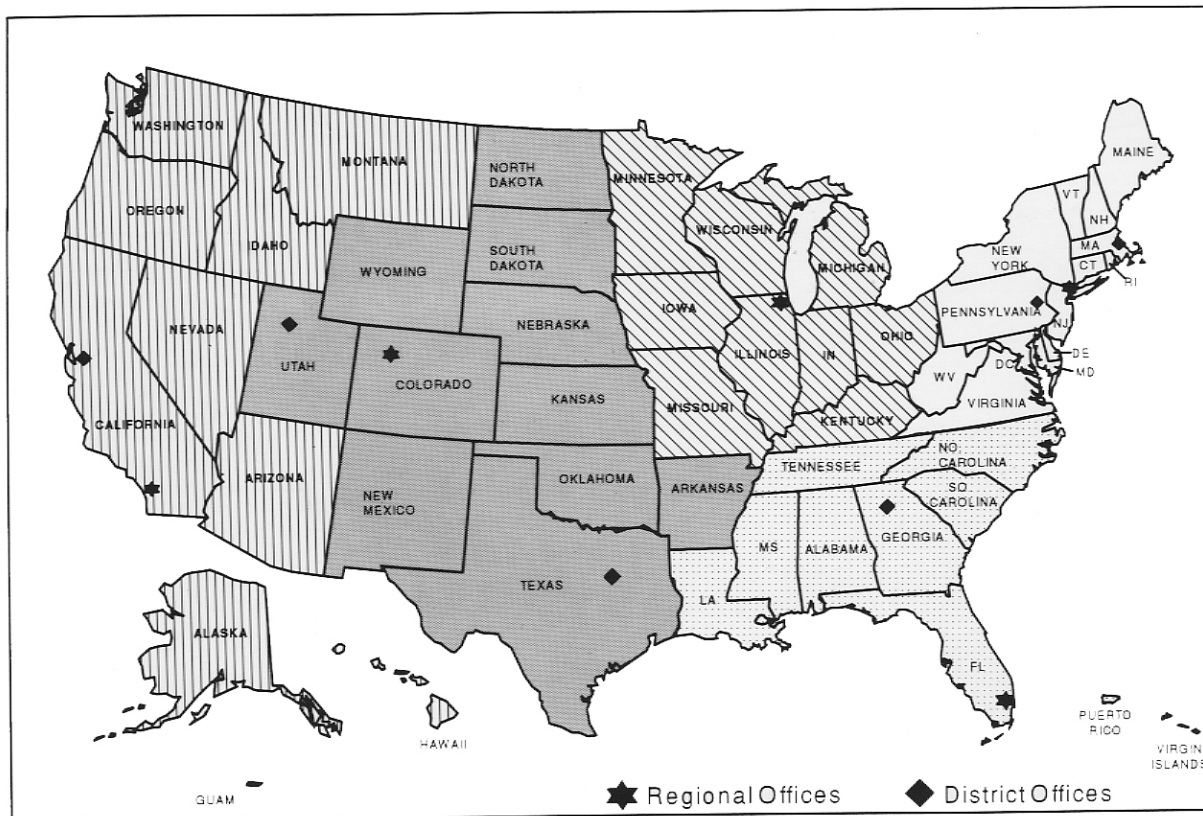
stabilized its finances and operations and rebuilt and expanded its business, increasing its market capitalization by almost 2000%.

From 1990-94, Commissioner Atkins served on the staff of two former chairmen of the SEC, Richard C. Breeden and Arthur Levitt, ultimately as executive assistant and counselor, respectively. Under Chairman Breeden, he assisted in efforts to improve regulations regarding corporate governance, enhance shareholder communications, strengthen management accountability through proxy reform, and decrease barriers to entry for small businesses and middle market companies to the capital markets. Under Chairman Levitt, he was responsible for organizing the SEC's individual investor program, including the first investor town hall meetings, an SEC consumer affairs advisory committee, and other investor education efforts, including the original *Invest Wisely* brochures regarding the fundamentals of the retail brokerage relationship and mutual fund investment.

Commissioner Atkins began his career as a lawyer in New York City, focusing on a wide range of corporate transactions for U.S. and foreign clients, including public and private securities offerings and mergers and acquisitions. He was resident for 2½ years in his firm's Paris office and admitted as *conseil juridique* in France in 1988.

A member of the New York and Florida bars, Commissioner Atkins received his J.D. from Vanderbilt University School of Law in 1983 and was Senior Student Writing Editor of the *Vanderbilt Law Review*. He received his A.B. from Wofford College in 1980 and was a member of Phi Beta Kappa. Originally from Lillington, North Carolina, Commissioner Atkins grew up in Tampa, Florida, where he was graduated as valedictorian from Plant High School in 1976. He is married with three sons, aged 9, 6, and 2.

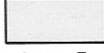
# SEC REGIONAL AND DISTRICT OFFICES




  
Pacific Region  
San Francisco District

  
Central Region  
Fort Worth District  
Salt Lake District

  
Midwest Region

  
Northeast Region  
Boston District  
Philadelphia District

  
Southeast Region  
Atlanta District

**Central Regional Office**

Randall J. Fons, Regional Director  
1801 California Street, Suite 4800  
Denver, Colorado 80202-2648  
(303) 844-1000

**Fort Worth District Office**

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(817) 978-3821

**Salt Lake District Office**

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(801) 524-5796

**Midwest Regional Office**

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175 West Jackson Boulevard  
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**Northeast Regional Office**

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**Boston District Office**

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**Philadelphia District Office**

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**Pacific Regional Office**

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**San Francisco District Office**

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**Southeast Regional Office**

David Nelson, Regional Director  
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Miami, Florida 33131  
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**Atlanta District Office**

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



# Enforcement

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*The SEC's enforcement program seeks to promote the public interest by protecting investors and preserving the integrity and efficiency of the securities markets.*

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## What We Did

- Obtained orders in SEC judicial and administrative proceedings requiring securities law violators to disgorge illegal profits of approximately \$1.293 billion.
- Civil penalties ordered in SEC proceedings totaled approximately \$101 million.
- Sought orders barring 126 defendants from serving as officers or directors of public companies.
- Sought emergency relief from federal courts in the form of temporary restraining orders (TROs) to halt ongoing fraudulent conduct in 48 actions, and sought asset freezes in 63 actions.
- Filed 19 actions to enforce investigative subpoenas.
- Halted trading in securities of 11 issuers about which there was inadequate public disclosure.
- In SEC-related criminal cases, prosecutors filed indictments, informations, or contempts against 259 individuals or entities.

### Enforcement Actions Initiated

	<u>FY98</u>	<u>FY99</u>	<u>FY00</u>	<u>FY01</u>	<u>FY02</u>
Civil Injunctive Actions	214	198	223	205	270
Administrative Proceedings	248	298	244	248	280
Contempt Proceedings	15	29	36	31	47
Reports of Investigation	0	0	0	0	1
Total	477	525	503	484	598

### Significant Enforcement Actions

Most of the SEC's enforcement actions were resolved by settlement with the defendants or respondents, who generally consented to the entry of judicial or administrative orders without admitting or denying the allegations against them. The following is a sampling of the year's significant actions.

#### Financial Fraud and Disclosure

- *SEC v. Dynegey Inc.*<sup>1</sup> The Commission filed and settled a civil action against Dynegey Inc., a Houston-based energy production, distribution, and trading company. The Commission's action arose from (1) Dynegey's improper accounting for and misleading disclosures relating to a \$300 million financing transaction, known as Project Alpha, involving special purpose entities, and (2) Dynegey's

overstatement of its energy-trading activity resulting from “round-trip” or “wash” trades--simultaneous, prearranged buy-sell trades of energy with the same counterparty, at the same price and volume, and over the same term, resulting in neither profit nor loss to either transacting party. Dynegy agreed to pay a \$3 million penalty in the civil action and, simultaneously, consented to the entry of an order in related cease-and-desist proceedings.

- *SEC v. L. Dennis Kozlowski, et al.*<sup>2</sup> The Commission filed an action against three former top executives of Tyco International Ltd., alleging that they failed to disclose the multi-million dollar, low-interest and interest-free loans they took from the company. L. Dennis Kozlowski, the former chief executive officer and chairman of Tyco’s board of directors, and Mark H. Swartz, the former chief financial officer and a director, granted themselves hundreds of millions of dollars in secret low-interest and interest-free loans from the company, and used the proceeds for personal expenses. They then covertly caused the company to forgive tens of millions of dollars of those outstanding loans, again without disclosure to investors as required by the federal securities laws. In addition, they engaged in other undisclosed related party transactions that cost shareholders hundreds of thousands, if not millions, of dollars. Mark A. Belnick, the former chief legal officer, failed to disclose the receipt of more than \$14 million of interest-free loans from the company to acquire two residences, an apartment in New York City and a \$10 million home in Park City, Utah. Kozlowski, Swartz, and Belnick also sold their shares of Tyco stock valued at millions of dollars while their self-dealing remained undisclosed.
- *SEC v. Michael J. Kopper.*<sup>3</sup> The Commission filed and settled a civil action against Michael J. Kopper, a former high-ranking official of Enron Corp., alleging that Kopper and others used complex structures, straw men, hidden payments, and secret loans to create the appearance that certain entities that Kopper and others at Enron funded and controlled were

independent of Enron, thereby allowing Enron to move its interests in these entities off its balance sheet. Kopper agreed to an injunction and an officer and director bar, and, subject to the court's approval, to disgorge and forfeit a total of approximately \$12 million. Kopper also agreed to enter a guilty plea in related criminal proceedings filed by the U.S. Department of Justice.

- *SEC v. Adelphia Communications Corporation, et al.*<sup>4</sup> The Commission filed a civil action against Adelphia Communications Corporation, its founder, John J. Rigas, his three sons, and two senior Adelphia executives. The Commission alleged that Adelphia fraudulently excluded billions of dollars in liabilities from its consolidated financial statements by hiding them in off-balance sheet affiliates; falsified operations statistics and inflated earnings to meet Wall Street's expectations; and concealed rampant self-dealing by the Rigas family, including the undisclosed use of corporate funds for the family's stock purchases and the acquisition of luxury condominiums.
- *SEC v. WorldCom, Inc.*<sup>5</sup> The Commission filed a civil action charging WorldCom, Inc. with a massive accounting fraud totaling more than \$3.8 billion. The Commission's complaint alleges that WorldCom fraudulently overstated its income before interest, taxes, depreciation, and amortization by approximately \$3.055 billion in 2001 and \$797 million during the first quarter of 2002. In a related administrative proceeding, the Commission ordered WorldCom to file with the Commission, under oath, a detailed report of the circumstances and specifics of these matters.
- *SEC v. Frank M. Bergonzi, et al.*<sup>6</sup> The Commission filed accounting fraud charges against three former senior executives of Rite Aid Corporation. The Commission also instituted separate settled cease-and-desist proceedings against Rite Aid and its former president and chief operating officer, Timothy J. Noonan.<sup>7</sup> The Commission alleges that

the executives conducted a wide-ranging accounting fraud scheme that resulted in the significant inflation of Rite Aid's net income in every quarter from May 1997 to May 1999. After the discovery of improper and unsubstantiated accounting transactions, in July and October 2000, Rite Aid restated cumulative pretax income by a massive \$2.3 billion dollars and cumulative net income by \$1.6 billion dollars.

- *In the Matter of Microsoft Corporation.*<sup>8</sup> The Commission instituted and settled administrative proceedings against Microsoft Corporation, finding that, between 1994 and 1998, Microsoft maintained between approximately \$200 million and \$900 million in unsupported and undisclosed reserves, a significant portion of which did not comply with U.S. Generally Accepted Accounting Principles (GAAP), which resulted in material inaccuracies in filings made by Microsoft with the Commission.
- *SEC v. Xerox Corporation.*<sup>9</sup> The Commission filed and settled a civil action alleging that, from at least 1997 through 2000, Xerox Corporation employed a variety of undisclosed accounting actions to meet or exceed Wall Street expectations and disguise its true operating performance from investors. These actions accelerated Xerox's recognition of equipment revenue by over \$3 billion and increased its pre-tax earnings by approximately \$1.5 billion over the four-year period. In addition to an injunction, Xerox agreed to pay a \$10 million penalty, the largest ever levied in a Commission action against a public company for financial fraud.
- *SEC v. Alan K. Anderson.*<sup>10</sup> In the action against Alan K. Anderson of Quintus Corp., the Commission alleged that the defendant personally forged contracts, e-mails, purchase orders, letters, and an audit confirmation in order to boost his company's financial results, creating three fake transactions adding up to \$13.7 million in nonexistent sales.

- *In the Matter of ACLN Limited.*<sup>11</sup> The Commission ordered a temporary suspension in the trading of ACLN Limited, a company located in Cyprus and Belgium, citing serious questions about the accuracy and completeness of the company's financial statements and disclosures. ACLN's shares were traded on the New York Stock Exchange. This was the first trading suspension of an exchange-listed company in more than 20 years.
- *SEC v. Kenneth E. Kurtzman, et al.; In the Matter of Ashford.com, Inc., et al.*<sup>12</sup> The Commission filed a settled civil action against the former chief executive officer and the former vice president for finance of Ashford.com; without admitting or denying the allegations in the Commission's complaint, the defendants agreed to pay civil penalties of \$60,000 and \$25,000, respectively. The Commission also filed and settled cease-and-desist proceedings against those individuals, Ashford.com, and Amazon.com, Inc. Ashford.com improperly deferred \$1.5 million in expenses under a contract with Amazon.com, causing Ashford.com to just beat analysts' pro forma earnings estimates (of a loss of \$0.31 per share) for the quarter ended March 31, 2000. The improper deferral resulted from the settlement of a dispute with Amazon.com using two separate documents prepared by Amazon.com at Ashford.com's request, only one of which was disclosed to auditors.
- *In the Matter of Kimberly-Clark Corporation, et al.*<sup>13</sup> The Commission instituted settled cease-and-desist proceedings against Kimberly-Clark Corporation and its chief financial officer, alleging inaccurate annual financial statements filed by Kimberly-Clark for the years ended December 31, 1995 through December 31, 1998, and quarterly financial statements from March 31, 1996 through the quarter ended March 31, 1999. These inaccuracies arose in connection with a \$1.44 billion charge for restructuring and other unusual charges that Kimberly-Clark recorded after its merger with Scott Paper Company in December 1995. Kimberly-Clark

materially overstated this restructuring charge by accruing \$354 million of merger-related expenses (about 25 percent of the \$1.44 billion charge) that did not constitute restructuring liabilities under GAAP. In 1999, after discussions with the Commission's Division of Corporation Finance, Kimberly-Clark voluntarily restated its financial statements.

- *SEC v. Dean L. Buntrock, et al.*<sup>14</sup> The Commission filed a complaint charging the founder and five other former top officers of Waste Management, Inc. with perpetrating a massive financial fraud, lasting more than five years, in which the company overstated its pre-tax earnings by \$1.7 billion. The Commission alleged that the defendants engaged in a systematic scheme to falsify and misrepresent Waste Management's financial results and to enrich themselves and keep their jobs. The Commission is seeking injunctions; officer and director bars; disgorgement of options, bonuses, performance-based compensation and proceeds from stock sales; and civil penalties.
- *SEC v. Roys Poyiadjis, et al.*<sup>15</sup> The Commission filed a civil action against AremisSoft Corporation and two former officers alleging that they overstated the value of the company's contracts, revenues and recent acquisitions, and that the two former officers engaged in massive insider trading during the period of the reporting fraud. The court ordered a freeze of any funds or assets of the two officers and two relief defendants, and ordered repatriation of all such funds and assets that had been moved offshore. Upon motion of the Commission, \$175 million was frozen by the courts in the Isle of Man in connection with this matter. Subsequently, AremisSoft was permitted by the bankruptcy court to settle this case, consenting to the entry of an injunction and an administrative order revoking the registration of its common stock.

## Auditor Independence

- *PricewaterhouseCoopers LLP, et al.*<sup>16</sup> The Commission filed a settled administrative proceeding against Pricewaterhouse-Coopers LLP (PwC) and its broker-dealer affiliate for violations of the auditor independence rules. The Commission charges that PwC used prohibited contingent fee arrangements with 14 different audit clients for which its broker-dealer affiliate provided investment banking services, and that PwC participated with two other audit clients, Pinnacle Holdings, Inc. and Avon Products, Inc., in the improper accounting of costs that included PwC's own consulting fees. Because of its independence violations, the firm caused these 16 public audit clients to file false and misleading financial statements with the Commission. PwC and its affiliate agreed to pay civil penalties of \$5 million. PwC also agreed to comply with significant remedial undertakings, to cease-and-desist from violating the auditor independence rules and to be censured for engaging in improper professional conduct. In related enforcement actions, settled cease-and-desist orders were entered against Pinnacle Holdings, Inc. and Avon Products, Inc.; the financial statements of both companies were restated.<sup>17</sup>
- *In the Matter of KPMG, LLP.*<sup>18</sup> The Commission instituted settled administrative proceedings censuring KPMG LLP based on its improper professional conduct in conducting an audit of a client in which KPMG had invested through the client's money market fund.
- *In the Matter of Moret Ernst & Young Accountants.*<sup>19</sup> The Commission instituted settled administrative proceedings against Moret Ernst & Young Accountants, an accounting firm based in the Netherlands. Moret audited the financial statements of a major client at a time when consultants affiliated with Moret had joint business relationships with the same client, thus impairing Moret's independence as auditor. The Commission also instituted administrative proceedings against Ernst & Young LLP, alleging that Ernst & Young's



joint business relationships with PeopleSoft Inc. from 1994-2000 violated auditor independence requirements.<sup>20</sup>

### Foreign Payments

- *SEC v. Douglas A. Murphy, et al.*<sup>21</sup> The Commission filed a civil action against two former officers of American Rice, Inc., alleging that they authorized over \$500,000 in bribery payments to Haitian customs officials to reduce American Rice's import taxes by approximately \$1.5 million.
- *In the Matter of BellSouth Corporation; SEC v. BellSouth Corporation.*<sup>22</sup> The Commission instituted settled cease-and-desist proceedings against BellSouth Corp. and obtained an order directing it to pay a \$150,000 penalty based on its improper recordation of payments relating to its expansion into Venezuela and Nicaragua.

### Regulated Entities

- *SEC v. Credit Suisse First Boston Corporation.*<sup>23</sup> The Commission filed a complaint against Credit Suisse First Boston Corporation (CSFB), a New York-based brokerage firm and investment bank, alleging that, in exchange for shares in "hot" initial public offerings (IPOs), CSFB wrongfully extracted from certain customers a large portion of the profits that those customers made by immediately selling their IPO stock. The profits were channeled to CSFB in the form of excessive brokerage commissions generated by the customers in unrelated securities trades that the customers effected solely to share the IPO profits with CSFB. CSFB agreed (1) to pay a total of \$100 million in the Commission's action and in a related action by the National Association of Securities Dealers Regulation, Inc., (2) to be enjoined by a federal court from future violations, and (3) to adopt extensive new policies and procedures.

- *SEC v. Frank D. Gruttadauria, et al.*<sup>24</sup> The Commission filed an action charging Frank D. Gruttadauria, formerly the branch manager for the Cleveland Ohio office of Lehman Bros. Inc., with securities fraud, alleging that over the last six years, while he worked at two different brokerage firms, Gruttadauria stole at least \$40 million in the course of defrauding more than 50 clients. The Commission promptly obtained a temporary restraining order and an asset freeze. A preliminary injunction was subsequently entered against Gruttadauria.
- *In the Matter of iCapital Markets LLC.*<sup>25</sup> The Commission instituted settled administrative proceedings against iCapital Markets LLC (formerly Datek Securities Corporation) finding that Datek had fraudulently misused the Nasdaq Stock Market's Small Order Execution System, an automatic trade execution system for small retail customer orders, by executing millions of proprietary trades, resulting in tens of millions of dollars in illegal trading profits for the firm. The firm was censured and ordered to pay a penalty of \$6.3 million.

### Insider Trading

- *SEC v. Samuel D. Waksal.*<sup>26</sup> The Commission filed an insider trading action against Samuel D. Waksal, the former CEO of ImClone Systems, Inc. The Commission charges that Waksal, having received news that the Food and Drug Administration was about to reject ImClone's pending application to market a cancer treatment, tipped this information to family members who sold more than \$10 million of ImClone stock before the news became public. Waksal also tried to sell \$5 million of his own holdings of ImClone stock, and was unable to do so only because two different broker-dealers would not execute his orders. The Commission's investigation is continuing.

- *SEC v. Hugo Salvador Villa Manzo, et al.*<sup>27</sup> The Commission filed and settled an insider trading action against Hugo Salvador Villa Manzo, a Mexican businessman, and Multinvestments, Inc., a U.S. broker-dealer based in San Antonio, Texas. The Commission's complaint alleged that the defendants engaged in highly lucrative insider trading prior to the June 28, 1999 public announcement that Nalco Chemical Company would be acquired by Suez Lyonnaise des Eaux, a French company. Villa received information about the proposed acquisition from Jose Luis Ballesteros, a director of Nalco, and instructed one of his senior colleagues at Multinvestments to buy Nalco stock for Multinvestments' proprietary account. Multinvestments purchased 50,000 Nalco shares for \$2,015,625. Following the announcement of the acquisition, the defendants realized unlawful profits totaling \$558,750. Without admitting or denying the Commission's allegations, Villa and Multinvestments consented to pay a total of \$1,503,471.83, representing disgorgement of \$558,750, prejudgment interest in the amount of \$106,596.83, and a one and one-half time penalty of \$838,125.

# International Affairs

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*The SEC operates in a global marketplace. The Office of International Affairs works to protect U.S. investors and the integrity of U.S. markets by encouraging international regulatory and enforcement cooperation, negotiating information sharing arrangements for regulatory and enforcement matters, encouraging the adoption of high quality regulatory standards worldwide, and conducting international technical assistance programs.*

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## What We Did

- Worked with foreign authorities to address cross-border fraud, including concluding three new arrangements on information sharing.
  - Promoted the strengthening and implementation of high quality international accounting standards.
  - Worked with foreign authorities to address weaknesses revealed in connection with recent corporate failures and to restore investor confidence. These efforts included the adoption of principles on auditor oversight, auditor independence, and disclosure and transparency.
  - Offered technical assistance to regulators of emerging securities markets.
-

## Enforcement Cooperation

### SEC Actions

The SEC continues to need assistance from foreign authorities to protect U.S. investors from cross-border fraud. To accomplish this, the SEC has developed formal and informal relationships with foreign authorities for enforcement cooperation. To date, the SEC has entered into over 30 formal information-sharing arrangements with foreign counterparts. These arrangements have enabled the Commission to bring significant enforcement actions based on information gathered from abroad.

<b>Fiscal 2002 Enforcement Cooperation Results</b>	
Requests to Foreign Authorities for Enforcement Assistance	448
Requests for Enforcement Assistance from Foreign Authorities	353

The SEC filed a record number of enforcement actions with international elements during the past fiscal year. Several of the actions are described below.

- *SEC v. ACLN*.<sup>28</sup> The Commission filed a civil injunctive action in U.S. District Court against ACLN, Ltd., a Cypriot corporation operating from Antwerp, Belgium that purportedly shipped used vehicles to North and East Africa and sold new cars in that region. The SEC sued three of ACLN's officers and

its Cypriot auditor. The complaint alleged that ACLN was the vehicle for an elaborate financial fraud (overstating assets/revenue, nonexistence of a new car line of business) that resulted in losses of hundreds of millions of dollars to investors in the United States and abroad. The alleged fraud included the falsification of bank records to distort the company's financial picture, and the sale of at least \$80 million of ACLN stock by company principals when they knew the financial disclosures were fraudulent. The Commission received assistance from several foreign government agencies in Belgium, Denmark, Luxembourg, Monaco, the Netherlands, Norway and the United Kingdom to freeze approximately \$45 million in bank accounts. The SEC will seek to have proceeds returned to defrauded investors.

- *SEC v. Millennium Financial, Ltd.*<sup>29</sup> This case involved a sophisticated international boiler-room operation. The SEC filed suit in U.S. District Court alleging that Millennium had contacted investors in at least 20 different countries and fraudulently sold them "pre-IPO" stocks of several private U.S. issuers. Millennium engaged in a variety of practices that were apparently designed to avoid detection and minimize the chances that any single country would have the basis, or the motivation, to bring an enforcement action. For example, Millennium claimed to have offices in several different countries, including Singapore, Mexico, Switzerland, and Brazil. However, these were only "virtual offices" used to circuitously route mail, phone calls, and faxes to other locations. Millennium also routed investor funds through a variety of banks in several different jurisdictions, including Guernsey, the British Virgin Islands, Hong Kong, Nevis, the Seychelles, and the United States. With the cooperation of approximately ten foreign regulatory and law enforcement authorities, the Commission was able to file an action

against Millennium within four months of starting its investigation. In addition, with the assistance of Nevis, over \$1.3 million in investor funds were frozen.

- *SEC v. AremisSoft Corp.*<sup>30</sup> The SEC obtained an injunction in the U.S. District Court for the Southern District of New York against AremisSoft Corporation, an international software company with offices in New Jersey, London, England, Cyprus, and India, and its former principal officers. The SEC's action is based on evidence of financial fraud in which the company reported phony acquisitions and phony customers, and made other misrepresentations regarding company revenue. The complaint also alleges that the former AremisSoft principal officers engaged in insider trading by secretly selling millions of shares of AremisSoft stock through various affiliated offshore entities while they had knowledge that the company's public disclosures were materially false. The SEC obtained assistance in securing asset freezes and records from numerous foreign authorities, including authorities in the Isle of Man, Switzerland, United Kingdom, and Cyprus. The SEC also worked closely with the U.S. Attorney's Office that obtained indictments of several former AremisSoft principals.
- *SEC v. Lernout & Hauspie.*<sup>31</sup> The Commission filed a civil injunctive action in the U.S. District Court for the District of Columbia against Lernout & Hauspie Speech Products, N.V., a developer, licensor, and provider of speech and language technologies, headquartered in Ieper, Belgium, and Burlington, Massachusetts. The SEC's complaint alleged that, from 1996 through the second quarter of 2000, while its common stock was listed on the Nasdaq National Market System and Nasdaq Europe, Lernout & Hauspie engaged in a variety of fraudulent schemes to inflate its reported revenue and income. The result of this conduct was an international financial scandal, the

destruction of Lernout & Hauspie as an operating company, and a loss of at least \$8.6 billion dollars in market capitalization, borne by investors in Belgium, the United States and elsewhere. The SEC received assistance from the U.S. Attorney for the Southern District of New York, the Belgian Ministry of Justice, and the Jersey Attorney General. The Commission's investigation is continuing with respect to other persons and entities.

### Information-Sharing Initiatives

The Commission also worked on bilateral and multilateral approaches to strengthen international information sharing and cooperation, thereby enhancing its ability to investigate and prosecute cross-border fraud. These initiatives included the following:

- *International Organization of Securities Commissions' Multilateral Memorandum of Understanding.* In the wake of the events of September 11, 2001, the International Organization of Securities Commissions (IOSCO) undertook to enhance the sharing of information critical to the successful investigation and prosecution of cross-border securities violations. The result was the adoption of a Multilateral Memorandum of Understanding (MOU) in May 2002. The MOU focuses on two aspects of cross-border enforcement cooperation. First, the MOU specifies the particular types of information a signatory must be able to provide, such as bank, brokerage, and client records. Second, the MOU mandates the protection of such information from disclosure, while allowing its use for compliance with the securities laws, investigations and enforcement proceedings, surveillance or enforcement activities of self-regulatory organizations, and assistance in criminal prosecutions. The MOU is open to all IOSCO members that demonstrate their legal authority to comply with its provisions. The SEC was



among the first group of IOSCO members to sign the MOU in the fall of 2002.

- *Statement of Intent with the Japanese Financial Supervisory Authority.* In May 2002, the Commission and the U.S. Commodity Futures Trading Commission (CFTC) signed a Statement of Intent Concerning Cooperation, Consultation and the Exchange of Information (SOI) with the Japanese Financial Supervisory Authority (JFSA). The SOI establishes a framework to facilitate consultation and cooperation between the SEC and the JFSA, and expresses each party's commitment to provide assistance in enforcement matters. It was accompanied by an exchange of diplomatic Notes Verbale concerning the use of information by criminal authorities.
- *Memorandum of Understanding with the Jersey Financial Services Commission.* In May 2002, the Commission and the CFTC completed negotiations and signed an MOU with the Jersey Financial Services Commission. The MOU and new legislation in Jersey should facilitate the process of requesting and obtaining information from this significant offshore financial center.

## **Initiatives to Address Weaknesses in Market Foundations and Strengthen International Standards**

The Commission identified and responded to various regulatory concerns raised by recent large corporate failures. The response included the implementation of the Sarbanes-Oxley Act of 2002 and an evaluation of its international impact, as well as the development of proposals by IOSCO and other organizations relating to auditor oversight, auditor independence, disclosure and transparency, and other areas of importance to the strength of the

infrastructure supporting financial markets. The Commission undertook these initiatives in the following contexts.

### Regulatory Dialogue

The SEC is focusing on implementing the provisions of the Sarbanes-Oxley Act as mandated by Congress. The Act makes no distinction between U.S. issuers and foreign private issuers, and the Commission intends to give the law full effect. Yet the SEC is cognizant of the fact that the requirements of the Sarbanes-Oxley Act may come into conflict with requirements under which foreign private issuers and other market participants are subject in their home jurisdictions.

To this end, the Commission staff established regular dialogue with foreign counterparts in Europe, Asia, and Latin America for the purpose of identifying SEC proposals that conflict with foreign laws or foreign stock exchange requirements, and discussing the manner in which foreign laws and regulations address the same issues as the Sarbanes-Oxley Act. The dialogue will be useful as the Commission seeks to fulfill the mandate of the Act in ways that accommodate foreign requirements and regulatory approaches.

### IOSCO Chairs' Committee

IOSCO created the Chairs' Committee to develop an international response to the concerns relating to accounting, auditing, and disclosure raised by recent corporate failures. The committee, which included representatives from the SEC, was tasked with developing general principles as guidance to regulators undertaking reform in each of these three areas. In October 2002, the Chairs' Committee adopted key principles that are broadly consistent with the Commission's approach in these areas. The principles describe essential features of regulatory systems requiring transparency and disclosure by listed entities, the independence of external auditors, and the need for public oversight of the audit function. The principles serve as a benchmark to which regulators can refer in addressing auditor

independence, auditor oversight, and disclosure and transparency issues.

## International Accounting Standards

For many years, the Commission has been active, both directly and through IOSCO and other international organizations, in encouraging the development and use of a high quality set of global accounting standards that could be used in cross-border capital formation. In May 2002, IOSCO issued a communiqué encouraging the International Accounting Standards Board (IASB) and national standard setters to work cooperatively and expeditiously to achieve convergence in order to facilitate cross-border offerings and listings. It also encouraged regulators to address the broader issues of consistent interpretation, application, and enforcement of international accounting standards. The Commission already allows foreign issuers to use International Accounting Standards Committee standards, subject to reconciliation to U.S. Generally Accepted Accounting Principles (GAAP).

On October 29, 2002, the Financial Accounting Standards Board (FASB) and the IASB announced that they will work together toward greater convergence between GAAP and International Accounting Standards (IAS). The Commission applauded this decision and supported efforts towards convergence on high-quality standards that provide investors consistent, comparable, relevant and reliable information. In noting the need to reduce differences between GAAP and IAS, the Commission staff has encouraged joint projects of the FASB and IASB to accomplish this goal, including reducing many differences in the short-term, over the next two years prior to the European Union's conversion to IAS in 2005. The Commission also noted that an effective infrastructure for interpretation and enforcement of accounting standards, and cooperation among regulators, will be critical to realizing the benefits of convergence.

## IOSCO's Core Principles

In 1998, IOSCO adopted the "Objectives and Principles of Securities Regulation" (the Core Principles), which represent consensus among securities regulators worldwide on sound practices for regulating securities markets. To promote implementation of the Core Principles, the SEC and other IOSCO members are conducting self-assessments regarding their compliance with the Core Principles. In addition, IOSCO is preparing a methodology, which will be used by the international financial institutions (*e.g.*, the International Monetary Fund and the World Bank) in their reform and restructuring work. The methodology also may be used by IOSCO to further assess the degree of members' implementation of the Core Principles.

## Financial Action Task Force

The Financial Action Task Force (FATF), an inter-governmental anti-money laundering organization, first issued its Forty Recommendations on Anti-Money Laundering in 1990 as a set of comprehensive guidelines for governments to follow in combating money laundering. In light of global technological and financial changes, the FATF launched a review of the Forty Recommendations aimed at strengthening, clarifying and refining certain key areas. The revisions would strengthen the standards and extend their scope. Because many of the Forty Recommendations apply to financial institutions, the review has implications for securities firms. The review is also of interest to securities regulators, given that the Recommendations also address cross-border information sharing and cooperation to combat money laundering and predicate offenses, such as securities fraud. The SEC, through the U.S. delegation to the FATF and IOSCO, worked to ensure that the FATF Forty Recommendations take into account the manner in which securities markets operate and are regulated, and the role played by securities regulators in combating money laundering and financial crime. The advice was rendered in the interest of improving the international anti-money laundering regime while

ensuring that legitimate securities businesses are permitted to operate as efficiently as possible.

## Financial Stability Forum

The Commission continues to work together with the U.S. Department of the Treasury and the Federal Reserve Board on Financial Stability Forum projects to address systemic threats to financial stability. In the past year, work focused on issues relating to vulnerabilities in the international financial system and issues raised by recent corporate failures.

## **Regional Initiatives**

### European Union

The U.S. Department of the Treasury is leading a team of high-ranking officials from U.S. financial regulators, including the SEC and the Federal Reserve Board, in a dialogue with representatives of the European Commission on regulatory and legislative matters relating to financial markets. The dialogue has focused on matters relating to access to U.S. and EU capital markets. U.S. interest in the dialogue centers on the Financial Services Action Plan (FSAP) (designed to develop a single European capital market by 2005) and its impact on the regulation of U.S. market participants. The meetings have contributed to greater understanding of the concerns and interests relating to financial markets on both sides of the Atlantic.

### Latin America

Through the Council of Securities Regulators of the Americas (COSRA), a grouping of securities regulators in the western hemisphere, the SEC participated in an examination of the legal, regulatory, and operational structures of members' clearance and settlement systems, focusing specifically on delivery versus payment and settlement assurance. COSRA received wide support for its efforts in this area from other international groups

such as the World Bank, the InterAmerican Development Bank and CEMLA (Centro de Estudios Monetarios Latino Americanos).

## **Technical Assistance**

The Commission's technical assistance program helps emerging securities markets develop regulatory structures that promote investor confidence and capital formation. The program is multifaceted and includes training programs, review of foreign securities laws, and responses to specific inquiries from foreign regulators.

<b>Fiscal 2002 Technical Assistance Results</b>	
Requests for Technical Assistance from Foreign Authorities	234
U.S. Training Provided	191 Officials from 87 Countries
Overseas Training Provided	Over 325 Officials

The cornerstone of the Commission's technical assistance program is the International Institute for Securities Market Development, a two-week, management level training program covering the development and oversight of securities markets. In addition, the Commission conducts a week-long International Institute for Securities Enforcement and Market Oversight,

covering techniques for investigating securities law violations and oversight of market participants.

Commission staff participated in a range of overseas training initiatives including: regional enforcement and market oversight training programs in Bulgaria and Mexico; regional disclosure and corporate governance training programs in Hungary and Lithuania; a regional capital markets training program in Jordan; and bilateral training initiatives in China, India, and Russia.

# Investor Education and Assistance

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*Our investor education and assistance staff serves investors who complain to the SEC about investment fraud or the mishandling of their investments by securities professionals. The staff responds to a broad range of investor contacts, produces and distributes educational materials, and organizes educational events.*

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## What We Did

- Received 82,337 complaints and questions.
  - Launched three new “fake scam” websites to educate potential investors about fraud, released four new publications, and substantially revised two existing brochures for investors.
  - Organized or participated in dozens of investor education events, including town meeting seminars, panel discussions, roundtables, and the SEC’s first-ever Investor Summit.
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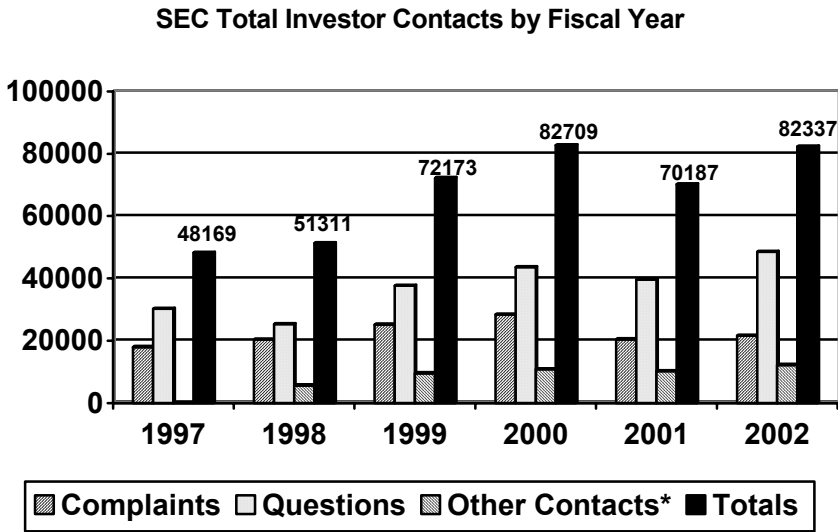
## Investor Complaints and Questions

### Substantial Rise in Investor Contacts

During the year, the SEC’s investor assistance staff received 82,337 complaints and questions, a 17 percent increase compared with fiscal 2001. Nearly 44 percent of these contacts came in electronically through our online investor complaint form or e-mail, a 5 percent increase over last year. Approximately 36 percent of



our investor contacts involved telephone calls, and the remainder included letters, faxes, and personal visits.

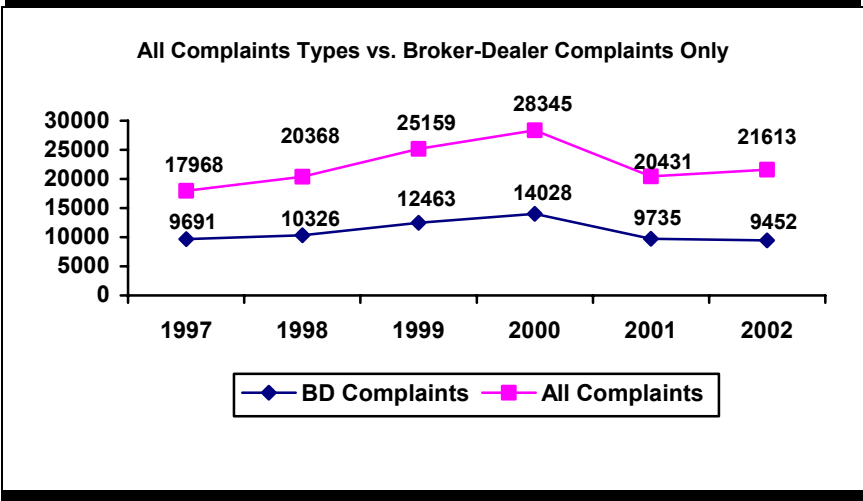


\* Other contacts includes repeat contacts, contacts with insufficient information to process, and contacts not within our jurisdiction.

The overall number of investor contacts has increased by almost 71 percent over the past 5 years.

### Complaint Trends

The SEC received 21,613 complaints during the year, compared with 20,435 in fiscal 2001. Approximately 44 percent of these complaints--a total of 9,452--involved broker-dealers. In a year when overall complaints increased by nearly 6 percent, complaints against broker-dealers fell by almost 3 percent.



During 2002, complaints concerning administrative and other fees became our number one complaint, having increased by 40 percent over 2001. While complaints in most categories generally declined, complaints concerning unsuitable recommendations and failure to follow instructions rose by 16 percent and 37 percent, respectively. In addition, poor investment advice and problems with account liquidations replaced margin position sellouts and errors in processing orders as the leading complaint types.

The ten most common complaints against broker-dealers included:

<b>FY 2002 Ranking</b>	<b>Complaint Type</b>	<b>Total</b>	<b>FY 2001 Ranking</b>	<b>Change</b>
1	Fees, commissions, and administrative costs	806	5	Up 40%
2	Misrepresentations	768	1	Down 11%
3	Unauthorized transactions	678	2	Down 6%
4	Transfer of account problems	658	4	Down 3%
5	Unsuitable recommendations	558	6	Up 16%
6	Failure to follow customer's instructions	331	9	Up 37%
7	Failures to process/delays in executing orders	443	3	Down 35%
8	Errors/omissions in account records	320	7	Down 13%
9	Poor investment advice	272	N/A	N/A
10	Problems with account liquidations	264	N/A	N/A

Approximately 20 percent of all broker-dealer complaints received during the year concerned online brokerage firms, compared with 24 percent last year. Complaints against online broker-dealers fell to 1,867 during 2002, down 20 percent from the 2,320 we received in 2001 and down more than 55 percent from an all-time high of 4,258 in 2000. The top five types of online broker-dealer complaints for 2002 included:

FY 2002 Ranking	Complaint Type	Total	FY 2001 Ranking	Change
1	Fees, commissions, and administrative costs	317	2	Up 19%
2	Failures to process/delays in executing orders	208	1	Down 41%
3	Best execution problems	113	5	Down 1%
4	Errors in processing orders	110	4	Down 14%
5	Difficulty in accessing account/contacting firm	101	N/A	N/A

## Educating Investors

Because a well-educated investor provides one of the most important defenses against securities fraud, we continued our efforts to educate investors. A sampling of our significant accomplishments follows.

### Fake “Scam” Website Initiative

In January and February 2002, we launched three fake “scam” websites that warn investors about fraud *before* they lose their money. Although each website purports to offer a “guaranteed, once-in-a-lifetime” investment opportunity, investors who click on the “invest now” link reach a page that says, “If you responded to an investment idea like this, you could get scammed.” The page also gives tips on how to spot potential frauds and provides links to key regulators. Within weeks of its launch, our first fake scam site--[www.McWhortle.com](http://www.McWhortle.com)--garnered more than 1.5 million hits

and our investor assistance staff received more than 500 e-mails, which were overwhelmingly positive.

### “Fast Answers” Interactive Database

In April 2001, the SEC began a pilot program using new interactive software to answer commonly asked questions through the SEC’s website. By matching incoming questions against a pre-loaded database of questions and answers, the new software allows users to receive instant answers. During the year, the software provided answers to 205,799 questions. In addition, this new service dramatically increased the number of hits the SEC received on its “Investor Information” and “Fast Answers” web pages--from approximately 575,000 in 2000 to more than 1.4 million in 2001 and more than 3.1 million in 2002.

### New Publications

During the year we released the following publications for investors:

<b>Title of Publication</b>	<b>What It Covers</b>
<b>All About Auditors</b>	Helps investors understand the role of the auditor in reviewing a company's financial books and records and provides tips on identifying a company's auditor.
<b>Analyzing Analyst Recommendations (revised)</b>	Describes the role analysts play in the capital formation process and advises investors not to rely solely on analyst recommendations when deciding whether to buy, hold, or sell a security.
<b>High Yields and Hot Air</b>	Gives investors a list of the most common "red flags" we find in many of the recent frauds we've seen.
<b>Holding Your Securities (revised)</b>	Explains the various ways investors can hold their securities--including physical certificate form, "street name" registration, and direct registration--and lays out the advantages and disadvantages of each.
<b>Privacy Choices for Your Personal Financial Information</b>	Describes the rules that govern privacy of personal financial information and lists the steps investors can take to help protect the privacy of their information (a joint publication of the SEC, the Federal Reserve Board, and other federal banking regulators).
<b>"Pro Forma" Financial Information: Tips for Investors</b>	Highlights the differences between "pro forma" financial information and financial statements that have been prepared in accordance with Generally Accepted Accounting Principles.

## Spanish Website

In October 2001, we launched a Spanish language section of the SEC website, which features Spanish translations of our popular brochures on investing wisely and avoiding fraud as well as links to Spanish language investor education resources offered by other government agencies and industry organizations.

## Investor Education Events

During the spring of 2002, we organized three “Roundtables on Accounting and Auditing,” which took place in New York City, Washington, D.C., and Chicago. In May 2002, we held our first-ever Investor Summit in Washington, D.C. To reach the broadest audience possible, we arranged to have all four events simultaneously audio-cast over the Internet and subsequently posted transcripts of each on the SEC’s website. The SEC has used the results of these extremely popular events in crafting rule proposals and setting its regulatory agenda. In June 2002, in cooperation with the U.S. Department of Defense, we organized an Investors Town Meeting in Norfolk, Virginia. In addition, throughout the year, numerous senior SEC officials participated in dozens of educational events, including programs targeted toward the elderly and minorities.

# Regulation of Securities Markets

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*The Division of Market Regulation oversees the operations of the nation's securities markets and market participants. In 2002, the SEC supervised over 8,000 registered broker-dealers with approximately 92,200 branch offices and 675,500 registered representatives. Broker-dealers filing FOCUS reports with the SEC had approximately \$3.4 trillion in total assets and \$204.6 billion in total capital for fiscal 2002. In addition, the average daily trading volume reached 1.4 billion shares on the New York Stock Exchange and over 1.7 billion shares on the Nasdaq Stock Market as of September 30, 2002.*

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## What We Did

- Implemented the Commodity Futures Modernization Act of 2000 (CFMA).
- Approved an amended Options Intermarket Linkage Plan that enhances price protection on customer orders by limiting intermarket trade-throughs across all five national options exchanges.
- Approved Nasdaq Stock Market's SuperMontage trading facility and the National Association of Securities Dealers' (NASD) Alternative Display Facility (ADF).
- Adopted a six-month pilot program that creates a *de minimis* exemption from the trade-through restrictions of the Intermarket Trading System (ITS) Plan for all



market participants trading the three most popular exchange-traded funds (ETFs).

- Began implementing the Sarbanes-Oxley Act of 2002.

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## **Securities Markets, Trading, and Significant Regulatory Issues**

### Analysts

On May 10, 2002, the Commission approved rule changes filed by the New York Stock Exchange (NYSE) and NASD governing analyst conflicts. On August 2, 2002, the Commission proposed Regulation Analyst Certification, which would, among other things, require brokers or dealers issuing research reports to include clear and prominent certifications by the research analysts that the report accurately reflects the analyst's personal views about the subject securities and issuers, and to disclose whether the analyst received compensation for views or specific recommendations in the research report.

On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act. Section 501 of the Act amends the Securities Exchange Act of 1934 (Exchange Act) to require the Commission (or, upon the authorization and direction of the Commission, an SRO) to adopt rules, within a year of enactment, governing analyst conflicts. The Commission currently is working to meet this and other mandates of the Sarbanes-Oxley Act.

### Strengthening Financial Sector Resilience

Late last year, Commission staff began working with other U.S. financial regulators--the Federal Reserve Board, the Office of the Comptroller of the Currency, and the New York State Banking Department--on a project to strengthen the operational resilience

of the financial sector. Specifically, we have been exploring with the private sector the possibility of developing common sound practices that would provide a consistent level of business continuity planning for financial market participants. Ultimately, this project will result in the financial regulators jointly issuing a set of sound practices or other guidance on appropriate levels of business continuity planning. We and the other agencies published for public comment a White Paper on sound practices in September 2002.

### Options Intermarket Linkage Plan

All five national options markets participate in the Options Intermarket Linkage Plan, which the Commission approved in July 2000. In May 2002, the Commission approved amendments to the Linkage Plan requiring any exchange that wishes to withdraw from the Plan to satisfy the Commission that it can achieve, by alternative means, the Linkage Plan's stated goal of limiting intermarket trade-throughs.<sup>32</sup> The exchanges expect to start intermarket testing of the linkage by December 1, 2002, and begin final roll out of the linkage by April 30, 2003.

### Repeal of the Trade-Through Disclosure Rule

In May 2002, the Commission proposed repealing rule 11Ac1-7 under the Exchange Act, the Trade-Through Disclosure Rule.<sup>33</sup> The Trade-Through Disclosure Rule requires a broker-dealer to disclose to its customer when the customer's order for listed options has been executed at a price inferior to a better-published quote (an "intermarket trade-through"), unless the transaction was effected on a market that participates in an intermarket options linkage plan that contains adequate trade-through protections. Under the amended Linkage Plan, discussed above, an options exchange may not withdraw from the Plan unless it can accomplish, by alternative means, the Plan's goal of limiting intermarket trade-throughs. The Commission repealed the Trade-Through Disclosure Rule after fiscal year-end because it believed that it was unnecessary.<sup>34</sup>

## *De Minimis* Exemption to the ITS Plan's Trade-Through Restrictions

In August 2002, the Commission adopted a six-month pilot program that creates a *de minimis* exemption from the trade-through restrictions of the Intermarket Trading System Plan for all market participants trading QQQ, DIA, and SPDR, the three most popular ETFs.<sup>35</sup> The exemption permits market participants to trade the three ETFs at prices that are no more than \$0.03 away from the national best bid or offer. In adopting the pilot program, the Commission sought to facilitate the participation of electronic communications networks (ECNs) and other alternative trading systems (ATSS) in the ITS Plan. The pilot program preserves the core price protection principles of ITS while the Plan's participants work to create a longer-term solution.

## Nasdaq's SuperMontage and the NASD's Alternative Display Facility

In January 2001, the Commission conditionally approved Nasdaq's SuperMontage, a new order display and collection facility for Nasdaq-listed securities.<sup>36</sup> As a condition of the Commission's Nasdaq approval, the NASD developed an ADF. The Commission approved the ADF as a nine-month pilot program in July 2002.<sup>37</sup> The ADF pilot program permits registered market-makers and registered ECNs to display their best-priced quotes or customer limit orders in Nasdaq-listed securities through the NASD. Although market participants are not required to use the ADF or SuperMontage to quote or report trades, the ADF allows market participants to satisfy their order display and execution access obligations under the Order Handling Rules and Regulation ATS. To date, Instinet and NexTrade are actively participating in the ADF.

## **Oversight of Self-Regulatory Organizations**

### **National Securities Exchanges**

As of September 30, 2002, there were nine active securities exchanges registered with the SEC as national securities exchanges: American Stock Exchange (Amex), Boston Stock Exchange (BSE), Chicago Board Options Exchange (CBOE), Cincinnati Stock Exchange (CSE), Chicago Stock Exchange (Chx), International Securities Exchange (ISE), NYSE, Philadelphia Stock Exchange (Phlx), and Pacific Exchange, Inc. (PCX). During fiscal 2002, the Commission granted 244 exchange applications to delist equity issues and 54 applications by issuers seeking withdrawals of their registration and listing on exchanges. The exchanges submitted 508 proposed rule changes and withdrew 63 proposed rules during 2002. The Commission also approved 421 rule proposals.

### **National Association of Securities Dealers**

The NASD is the only national securities association registered with the SEC and includes more than 5,500 member firms. The NASD submitted 164 proposed rule filings to the SEC during the year. The Commission approved 123 rule proposals and 19 were withdrawn.

### **Clearing Agencies**

At the end of fiscal 2002, 13 clearing agencies were registered with the Commission, and five clearing agencies had been granted exemptions from clearing agency registration. Registered clearing agencies submitted 77 proposed rule changes, and the Commission approved 79 new and pending proposed rule changes.

### **Municipal Securities Rulemaking Board**

The Municipal Securities Rulemaking Board (MSRB) is the primary rulemaking authority for municipal securities dealers. In

fiscal 2002, the Commission received 16 new proposed rule changes from the MSRB and approved 12.

### Total SRO Rules Processed

The Division received a total of 768 filings in fiscal 2002. Of these filings, 633 were approved, and 84 were withdrawn after discussions with staff, for a total of 717 closed SRO rule filings.

### **SRO Rule Proposals**

In July 2002, the Commission approved the Amex's proposed rule change to permit side-by-side trading and integrated market-making of certain ETFs and their related options. Historically, the Commission has had concerns regarding side-by-side trading and integrated market-making, including, among other things, the potential that market participants in a side-by-side trading or integrated market-making environment could unfairly use non-public market information to their advantage and the potential for such market participants to engage in manipulative or other improper trading practices. The Commission believed that the Amex proposal was sufficiently limited to address regulatory concerns. Specifically, the Commission believed that, because the prices of ETFs are based on the prices of groups of stocks, a market participant's ability to manipulate the price of the ETF or its related option was limited. Further, the Amex proposal was limited only to side-by-side trading and integrated market making of certain broad-based ETFs that satisfied specific criteria. The Commission believed that limiting the proposal to broad-based ETFs would lessen concerns regarding information advantages about the individual securities. Finally, the proposal required that the limit order books for the ETFs and related options be disclosed to all market participants, which the Commission believed would prevent any market participant from having an unfair competitive advantage over other participants.

## Proxy Fees

In March 2002, the Division of Market Regulation, pursuant to delegated authority, approved the NYSE's proposal to amend its proxy fee reimbursement guidelines, which were then under a pilot program, and to seek permanent approval of the pilot program. Division staff believed that the proposed amendments would help establish a more practical and organized proxy reimbursement structure.

## Alternative Trading Systems

Regulation ATS establishes recordkeeping and reporting requirements for ATSs that choose to register as broker-dealers.<sup>38</sup> In fiscal 2002, the staff reviewed 7 initial operation reports, 38 amendments, 140 quarterly activity reports, and 4 reports of cessation of operations under Regulation ATS.

## Order Handling Rules

In fiscal 2002, the Commission's staff renewed 11 no-action letters that had been issued to ECNs in light of the Commission's 1996 adoption of the Order Handling Rules. In addition, the staff issued a no-action letter to the Track ECN and withdrew a no-action letter from the Market XT ECN. The staff also issued a no-action letter to Instinet to cover Instinet's activities on NASD's ADF.

## Corporate Bond Price Transparency

In July 2002, the NASD began implementing phase I of the TRACE system for reporting and disseminating corporate bond transaction prices.<sup>39</sup> TRACE requires NASD members to report transactions in most U.S. corporate bonds to the NASD, and establishes a facility to collect and redistribute that transaction information. Currently, TRACE disseminates transaction information on investment-grade corporate bonds with original issue size of \$1 billion or more and approximately 50 high yield bonds. The NASD makes this information available to investors

on its website. Subsequent phases of TRACE will further enhance price transparency in the corporate bond market.

### Execution Quality Disclosure Rules

In November 2000, the Commission adopted the execution quality disclosure rules, rules 11Ac1-5 and 11Ac1-6 under the Exchange Act.<sup>40</sup> Rule 11Ac1-5 requires market centers to make available monthly electronic reports that include uniform statistical measures of execution quality. Rule 11Ac1-6 requires broker-dealers to make publicly available quarterly reports describing their order routing practices. The first quarterly reports under the rules were required to be posted in November 2001. The Division of Market Regulation issued Staff Legal Bulletin No. 12R on rule 11Ac1-5 and Staff Legal Bulletin No. 13A on rule 11Ac1-6. In December 2001, the Commission issued a temporary exemption from rule 11Ac1-5 for the Primex Auction System. In June 2002, the Commission issued an exemption from rule 11Ac1-5 to the Nasdaq Stock Market, Inc. for orders received through Nasdaq's SelectNet system and for the initial display of orders in the Order Display System of Nasdaq's SuperMontage system. At the same time, the Division of Market Regulation gave Nasdaq interpretive guidance under rule 11Ac1-5 with respect to orders executed through SuperMontage.

### Options Price Reporting Order--Settlement

In September 2000, the Commission instituted public administrative proceedings against the Amex, the CBOE, the PCX, and the Phlx, and simultaneously accepted settlement offers from each respondent.<sup>41</sup> The settlement order required the respondent exchanges to: (1) amend the Options Price Reporting Order Plan (OPRA) to establish a system for procuring and allocating capacity that eliminates joint action by OPRA participants; (2) adopt rules that substantially enhance incentives to quote competitively; (3) adopt sanctioning guidelines designed to enforce compliance with each respondent exchange's options order handling rules; and (4) adopt rules codifying any practices

whereby market-makers determine by agreement the spreads or prices at which they will trade an option class or the allocation of orders in that class. The respondent exchanges submitted proposed sanctioning guidelines. In March 2002, the Commission approved sanctioning guidelines that each of the respondent exchanges had proposed. The respondent exchanges also have submitted collective action filings to permit specialists or Lead Market Makers (LMMs) to consult with the trading crowd in setting auto-quote parameters, and to permit the specialists or LMMs and members of the crowd to provide collectively a single response to a request for a large order. The Commission approved these filings in March and April 2002.

## **Implementation of the Commodity Futures Modernization Act**

The following is a sampling of the year's significant accomplishments with respect to the implementation of the CFMA. Implementation centered on extensive joint rulemakings with the Commodity Futures Trading Commission (CFTC) to create a regulatory framework for security futures products, including adopting:

- rules that govern trading halts and cash settlement procedures for security futures products,<sup>42</sup>
- rules regarding the collection of customer margin for security futures,<sup>43</sup> and
- rules regarding customer protection and recordkeeping requirements for intermediaries that trade security futures.<sup>44</sup>

Independently, the Commission also:

- Amended its rules to clarify how exchanges and associations should calculate section 31 fees for



security futures transactions and for sales of securities resulting from physical settlement of security futures.<sup>45</sup>

- Adopted amendments to rule 10b-10 under the Exchange Act to provide confirmation requirements for security futures transactions effected in futures accounts.<sup>46</sup>
- Issued to the Chicago Mercantile Exchange, Inc., Nasdaq-Liffe Markets LLC, and OneChicago, LLC acknowledgements of receipt of notice of their registration as national securities exchanges.
- Issued an interpretive release that provided guidance about how certain provisions of the Securities Act of 1933 and the Exchange Act, and certain rules under those Acts, would apply to the trading of security futures products. The release addressed a variety of potential issues that could arise from the trading of securities futures products, including issues related to broker-dealers, trading practices and market supervision. The release also addressed issues administered by the SEC's Division of Corporation Finance.<sup>47</sup>
- Amended rule 10b-10, and promulgated new Rule 11d2-1, to clarify the disclosures that broker-dealers that effect transactions in security futures products in futures accounts must make in the confirmations they send to customers regarding those transactions. Those actions streamlined the rule 10b-10 disclosure requirements applicable to those transactions to better correspond to the confirmation rules applicable to the futures markets.<sup>48</sup> Previously, the Commission had provided an exemption to those broker-dealers pending the adoption of the rule changes.<sup>49</sup>

- Granted interim no-action relief from some broker-dealer requirements to firms that are dually-registered as broker-dealers and futures commission merchants and that provide certain services with respect to non-U.S. security futures held in futures accounts for non-U.S. persons. The request for relief, which was submitted jointly by the Securities Industry Association and the Futures Industry Association, sought to ensure that the firms could clear and carry those foreign security future positions, and engage in related solicitation, order execution, and research activities. The temporary relief will terminate when the Commission and the CFTC issue final rules governing the offer and sale of foreign security futures. The no-action letter was limited in scope, and did not provide relief with respect to certain broker-dealer requirements such as net capital, customer protection, and records requirements.<sup>50</sup>
- Consulted with personnel at the CFTC regarding the CFTC's proposed rules restricting the dual trading of security futures products on contract markets and derivatives transaction execution facilities.
- Adopted rules outlining the applicability of CFTC and SEC customer protection, recordkeeping, reporting, and bankruptcy rules and the Securities Investor Protection Act of 1970 to accounts holding security future products.<sup>51</sup>
- Proposed amendments to the reserve requirement under Exchange Act rule 15c3-3 related to margin for securities futures products.<sup>52</sup>

## Automation Review Policy Program

The Automation Review Policy (ARP) program continued its oversight of the capacity of the automation systems of the

securities markets. The ARP program staff performed 7 on-site inspections and issued 28 recommendations for improvement in information technology resources. In addition, staff attended 8 annual technology briefings presented by the exchanges and tracked systems problems. The ARP staff also monitored the successful re-opening of the securities markets following the September 11 terrorist attack.

### “Soft Dollar” Interpretation

On December 27, 2001, the Commission modified its interpretation of the scope of the “soft dollar” safe harbor provided by section 28(e) of the Exchange Act. Section 28(e) states that money managers who receive research and brokerage services from broker-dealers who execute trades for their advised accounts will not be deemed to have breached a fiduciary duty if they meet certain conditions. The Commission’s modified interpretation states that the safe harbor may apply to riskless principal transactions executed by market-makers in Nasdaq-traded securities. A prior Commission interpretation had excluded all “principal” transactions from the scope of the safe harbor. In modifying its earlier interpretation, the Commission recognized that the NASD had modified its trade reporting rules for certain riskless principal transactions, and concluded that a money manager buying or selling a Nasdaq-traded stock would now have the information necessary to determine whether the transaction fee paid was reasonable in relation to the value of the research and brokerage received.<sup>53</sup>

## **Broker-Dealer Issues**

### Implementation of Title II of Gramm-Leach-Bliley Act of 1999

Title II of the Gramm-Leach-Bliley Act (GLBA) redefined the terms broker and dealer. Under the old definitions, banks were excepted from the definitions for all of their securities activities. Under the new definitions, banks have particular exceptions for specific bank securities activities. In fiscal 2001, the Commission

adopted interim final rules clarifying key terms in the amended definitions of broker and dealer. The interim final rules also provide non-exclusive safe harbors for banks and thrifts from the definitions of broker and dealer.<sup>54</sup> Later in fiscal 2001, the Commission extended the time available for banks to comply with the new GLBA requirements. On May 8, 2002, the Commission further extended temporary exemptions from the definitions of broker and dealer for banks, savings associations, and savings banks. The temporary exemption from the definition of broker was extended until May 12, 2003, and the temporary exemption from the definition of dealer was extended until November 12, 2002. The Commission also gave notice of its intent to amend the interim final rules and, as appropriate, to extend further the temporary exemptions.<sup>55</sup> The Commission staff is carefully considering related comments from industry members and the public.

## **Credit Union Sweep Accounts**

The Commission received an application from the Evangelical Christian Credit Union for exemptive relief under sections 15 and 36 of the Exchange Act to permit it to offer sweep account services to customers without registering as a broker-dealer. In June 2002, the Commission issued a notice regarding the application and requested comment on both the application and related issues, including whether all federally-insured credit unions should be permitted to sweep deposits into no-load money market funds on the same terms and conditions available to banks under the GLBA.<sup>56</sup> The staff is considering comments on the proposal.

## **Consumer Financial Privacy**

The Commission was one of eight federal agencies that jointly sponsored a December 4, 2001 public workshop on improving the privacy notices that the GLBA requires financial institutions to provide to consumers. At the workshop, which was entitled “GETTING NOTICED: Writing Effective Financial Privacy Notices,” government officials, financial institution and industry

association representatives, communications experts, and consumer and privacy advocates discussed how financial privacy notices might be made more effective. Commission staff also responded to inquiries from the public, financial institutions, and members of Congress regarding various interpretive issues relating to the privacy requirements of Regulation S-P. Among other activities, the staff coordinated with other agencies and the NASD to address issues including requirements for delivering privacy notices, transferring customer accounts, posting privacy notices on financial institution websites, and whether customer or consumer relationships exist in particular circumstances. For example, the staff prepared an interagency response to a congressional inquiry on behalf of a state agency that had expressed concern that financial institutions disclosing or agreeing to disclose certain information to the state agency might be subject to liability under the financial privacy provisions of the GLBA.

## **Net Capital Developments**

The following highlights the agency's most significant net capital rule developments.

- The staff issued a letter clarifying when a firm is a dealer for net capital purposes.<sup>57</sup>
- The Commission adopted rule amendments that clarified and expanded recordkeeping requirements with respect to purchase and sale documents, customer records, associated person records, customer complaints, and certain other matters. In addition, the amendments expanded the types of records that broker-dealers must maintain and required broker-dealers to maintain or promptly produce certain records at each office to which those records relate.<sup>58</sup>

- The Commission issued an order extending the broker-dealer exemption from sending certain financial information to customers under specified circumstances.<sup>59</sup>
- The Commission proposed an amendment to rule 15c3-3(b)(3) that would increase the categories of collateral broker-dealers could pledge when borrowing fully paid for or excess margin securities from customers.<sup>60</sup>

## **Risk Assessment Program**

As of September 30, 2002, Division staff reviewed filings for 164 broker-dealers and their material affiliates under the Commission's Risk Assessment Program. In addition, the staff reviewed risk management information filed by five firms who voluntarily report their over-the-counter derivatives activities under the Derivatives Policy Group framework.

## **Arbitration and Mediation**

The Commission approved an amendment to NASD rules to simplify and clarify the procedures for parties to obtain injunctive relief in securities industry disputes involving a registered representative's change in employment from one member firm to another.<sup>61</sup> At the same time, the Commission approved an NASD rule prohibiting members from interfering with a customer's request to transfer his or her account in connection with those changes in employment.<sup>62</sup> The Commission also approved an amendment to NASD rules designed to allow claimants in arbitration to more easily obtain awards against defunct parties, which in turn can be enforced in court.<sup>63</sup>

## **National Money Laundering Strategy for 2002**

The staff worked with the U.S. Department of the Treasury on anti-money laundering and anti-terrorist financing regulations called for by the USA PATRIOT Act. Those Treasury Department regulations proposed customer identification requirements, banned financial institutions from maintaining correspondent accounts with foreign shell banks, expanded suspicious activity rules to cover all broker-dealers, and authorized the sharing of information by broker-dealers, other financial institutions, and the government. The staff also worked with the NYSE and the NASD to develop rule changes to help implement the USA PATRIOT Act requirement that broker-dealers establish anti-money laundering compliance programs.<sup>64</sup> Moreover, Division of Market Regulation Director Annette Nazareth testified on January 29, 2002 before the Senate Committee on Banking, Housing and Urban Affairs about the Commission's activities in implementing the USA PATRIOT Act.

On July 23, 2002, the Commission proposed a customer identification rule as required by section 326 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act, Pub. L. 107-56). The Commission and the U.S. Treasury Department jointly issued the proposing release.<sup>65</sup>

### **Letters Related to Broker-Dealer Activities**

#### **Equity Lines of Credit**

In October 2001, the staff released a July 2001 letter granting no-action relief to a fund that sought to invest in equity lines of credit without registering as a broker-dealer. This particular type of line of credit requires an investor to purchase stock from a company at a discount to the market price, and gives the company the

flexibility to choose the timing of those sales. The staff's position was conditioned on a number of representations, including that:

- the fund would not solicit any company to enter into an equity line of credit,
- a broker-dealer that is unaffiliated with the fund would act as placement agent on behalf of any company entering into an equity line of credit,
- the fund effect sales of securities through an unaffiliated broker-dealer other than the placement agent,
- the fund would be restricted in its ability to short sell the company's stock, the fund would not pay finder's fees, the fund would not hire persons who are statutorily disqualified from association with a broker-dealer, and
- that purchases of company stock would not be made contingent upon any measure of market volume.<sup>66</sup>

#### Employee Benefit Plan Staffing Provider

The staff issued a letter granting no-action relief to a firm that, without registering as a broker-dealer, sought to provide employers with short-term staffing to assist the employers in explaining benefit plan details to their employees. The staff noted, among other factors, that:

- the firm would not hold itself out as a broker-dealer;
- the firm would not receive compensation linked to employee contributions, investment selections or compensation earned by plan providers;



- the benefits professionals would not solicit the sale of securities or solicit broker-dealer business; and
- neither the firm nor the benefits professionals would process investment instructions, handle funds and securities, or have any responsibility or control over investment alternatives.<sup>67</sup>

### Website Service and Communications Contractor

The staff issued a letter granting no-action relief to permit a registered broker-dealer to retain an unregistered affiliate to provide website and communications services on behalf of the broker-dealer. As compensation, the broker-dealer would pay per-order communications fees, as well as other fees not based on transactions, to the unregistered affiliate. The relief was predicated on several conditions to prevent the unregistered affiliate from soliciting securities transactions, and to require the broker-dealer to be responsible for the activities performed by the unregistered affiliate. Among other factors, the unregistered affiliate would be precluded from marketing the broker-dealer's services, negotiating agreements involving the broker-dealer, or becoming a party to the broker-dealer's agreements with its customers. Other conditions further precluded the unregistered affiliate's ability to engage in broker-dealer activities through the technical services that it would provide to the broker-dealer.<sup>68</sup>

### Employee Leasing Service Provider

The staff issued a letter granting no-action relief to an unregistered entity that proposed offering employee leasing services, including payroll processing, to registered broker-dealers and their employees without registering as a broker-dealer. The unregistered entity would receive payment from the broker-dealers for salaries, wages, and commissions, which the firm would then pay to the broker-dealers' personnel. The staff noted that although the employees would be placed on the firm's payroll, they would remain employees of its broker-dealer clients for purposes of the securities laws, and the broker-dealer clients

would maintain direction and control over the employees. The unregistered firm also would not engage in any securities-related activities or be associated with a broker-dealer.<sup>69</sup>

#### Request to Handle Securities Commissions for Benefits Purposes

The staff issued a letter denying no-action relief to an unregistered firm that sought, without registering as a broker-dealer, to receive securities commissions earned by employees who also were registered representatives of a broker-dealer. The unregistered firm proposed to receive commissions, deduct the cost of overhead, taxes and benefits, and pay the remainder back to the representative who earned the commission. In denying the request, the staff noted that the unregistered firm appeared to have a professional interest in the securities transactions of those employees, and that the proposed arrangements would be inconsistent with the primacy of the employment relationship between the broker-dealer and its registered representatives.<sup>70</sup>

#### Request to Permit Unregistered Entities to Handle Securities Commissions for Payroll Purposes

The staff issued a letter denying no-action relief to a registered broker-dealer and its unregistered parent related to the handling of securities commissions and profits. The entities proposed to permit affiliated unregistered firms to act as payroll agents that would pay securities commissions to individuals who were dually employed by the unregistered affiliates and by a third-party broker-dealer. They also proposed to permit the parent to receive the broker-dealer subsidiary's profits and distribute them as compensation to employees of the unregistered affiliates. In denying the request, the staff noted that the unregistered parent was supplying the third-party broker-dealer with a sales force as well as a customer base. Moreover, the parties were already engaged in the activities, and as a matter of policy, the staff grants no-action relief only prospectively.<sup>71</sup>

# Investment Management Regulation

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*The Investment Management Division regulates investment companies (which include mutual funds, closed-end funds and unit investment trusts) and investment advisers under two companion statutes, the Investment Company Act of 1940 and the Investment Advisers Act of 1940. The Division also administers the Public Utility Holding Company Act of 1935. The Division's goal is to minimize financial risks to investors from fraud, self-dealing, and misleading or incomplete disclosure.*

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## What We Did

- As part of the Commission's actions to implement the Sarbanes-Oxley Act of 2002, adopted a new rule requiring a mutual fund's principal executive and financial officers to certify the fund's reports on Form N-SAR; and to better implement the intent of the Act, proposed a new form that would be certified by the fund's principal executive and financial officers and would contain shareholder reports, the primary means by which funds provide financial statements to investors.
- With other federal financial regulators, proposed rules to implement the requirements of the USA PATRIOT Act. These rules to prevent money laundering and terrorist financing would require mutual funds to adopt procedures to verify their customers' identities.
- Proposed amendments requiring mutual funds to disclose their proxy votes and voting policies and procedures to enable shareholders to monitor their

funds' involvement in the governance of portfolio companies; and proposed rules requiring investment advisers to adopt written policies and procedures governing how they vote proxies for client securities.

- Proposed amendments to modernize the mutual fund advertising rules, designed to encourage fund advertisements to convey more balanced information to prospective investors, particularly with respect to past performance.
- Approved the first exchange-traded funds (ETFs) based on fixed-income indices, giving investors another option to invest in a basket of fixed-income securities. The Commission also issued a concept release seeking input on actively managed ETFs.
- Adopted new registration Form N-6 for variable life insurance policies.
- Adopted amendments providing greater flexibility for mutual funds to merge without obtaining an exemptive order from the Commission and proposed amendments to permit certain affiliated transactions involving sub-advisers and portfolio affiliates in circumstances under which investor protection would not be compromised.
- Proposed amendments to modernize custody rules for investment companies and investment advisers.

## **Significant Investment Company Act Developments**

Total assets managed by investment companies at the end of fiscal 2002 were \$6.7 trillion, approximately the same amount as a year earlier. A sharp decline in equity assets was offset by increases in fixed income and money market assets. During the fiscal year, stock prices continued to retreat from record highs set

in 2000, with the major stock indices recording declines of between 11 and 19 percent. The technology-oriented Nasdaq Composite index closed at 1,172.06 on September 30, 2002, down more than 75 percent from its March 10, 2000 peak of 5,048.62. Notwithstanding these declines, the \$6.7 trillion managed by investment companies remains almost double the \$3.7 trillion on deposit at commercial banks and roughly equals the \$6.8 trillion of financial assets at commercial banks. At the end of 2002, a total of 31,100 investment company portfolios were managed or sponsored by 995 investment company complexes. Open-end management investment companies, commonly known as mutual funds, are the largest segment of the investment company industry. Approximately 54 million U.S. households, representing 50 percent of total households, own mutual funds.

### Rulemaking

- *Chief Executive Office/Chief Financial Officer Certifications.* The Commission implemented section 302 of the Sarbanes-Oxley Act with respect to registered investment companies by adopting amendments requiring each registered investment company's principal executive and financial officers to certify the information contained in its reports on Form N-SAR, the form designated for registered investment companies to comply with their periodic reporting requirements under the Securities Exchange Act of 1934.<sup>72</sup> In addition, the Commission proposed amendments designed to better implement the intent of section 302 of the Sarbanes-Oxley Act with respect to investment companies, by requiring the principal executive and financial officers of registered management investment companies to certify a new Form N-CSR, which contains shareholder reports.<sup>73</sup>
- *Customer Identification Programs.* The Commission and other federal financial regulators, including the U.S. Department of the Treasury, proposed rules to implement section 326 of the USA PATRIOT Act, which directs the issuance of regulations requiring financial institutions to institute reasonable procedures for (1) verifying the identity of

any person seeking to open an account, to the extent reasonable and practicable; (2) maintaining records of the information used to verify the person's identity; and (3) determining whether the person appears on any list of known or suspected terrorists or terrorist organizations.<sup>74</sup> The proposed rules seek to protect the U.S. financial system from money laundering and terrorist financing activity. Additionally, the identity verification procedures required under the rules may serve to protect consumers against various forms of fraud, including identity theft.

- *Proxy Voting.* The Commission proposed amendments that would require mutual funds and other registered management investment companies to provide disclosure about how they vote proxies relating to portfolio securities they hold.<sup>75</sup> The proposals are designed to enable fund shareholders to monitor their funds' involvement in the governance activities of portfolio companies. The proposals would require registered management investment companies to file with the Commission and to make available to their shareholders the specific proxy votes that they cast in shareholder meetings of issuers of portfolio securities. Under the proposed amendments, registered management investment companies also would be required to disclose the policies and procedures that they use to determine how to vote proxies relating to portfolio securities.
- *Variable Life Insurance Registration Form.* The Commission adopted a new registration form, Form N-6, for variable life insurance policies.<sup>76</sup> The new form focuses prospectus disclosure on essential information that would assist an investor in deciding whether to invest in a particular variable life insurance policy. In particular, Form N-6 requires a uniform, tabular presentation of fees and charges in order to improve disclosure of the often complex charges associated with variable life insurance policies.

- *Mergers of Affiliated Investment Companies.* The Commission adopted amendments to rule 17a-8 under the Investment Company Act.<sup>77</sup> Rule 17a-8 allows affiliated registered investment companies to merge without obtaining a specific exemptive order from the Commission. The amendments expand the rule to permit a greater range of fund mergers consistent with the protection of fund investors.
- *Investment Company Advertising.* The Commission proposed rule amendments that are designed to encourage mutual fund advertisements to convey more balanced information to prospective investors, particularly with respect to past performance.<sup>78</sup> The proposed amendments would, among other things, require funds that advertise performance to make available returns that are current to the most recent month-end by a toll-free or collect telephone number. The proposals also implement a provision of the National Securities Markets Improvement Act of 1996 by eliminating the requirement in rule 482 under the Securities Act of 1933 that investment company advertisements under that rule contain only information the substance of which is included in the investment company's statutory prospectus.
- *Transactions of Investment Companies with Portfolio and Subadviser Affiliates.* The Commission proposed a new rule and several amendments governing exemptions for transactions between investment companies and their affiliated persons.<sup>79</sup> The Investment Company Act contains a number of provisions that prevent persons who may be in a position to take advantage of an investment company from entering into transactions or arrangements with the investment company. These include prohibitions on "affiliated transactions" and "joint transactions" with affiliated persons. The rule and amendments would eliminate the need for funds to obtain individual exemptive orders in circumstances that are not likely to raise investor protection concerns.

- *Acquisition of Securities During the Existence of an Underwriting or Selling Syndicate.* The Commission adopted amendments to rule 10f-3, which allows a fund that has certain affiliations with an underwriting participant to purchase securities during an offering.<sup>80</sup> The amendments expand the exemption provided by the rule to permit a fund to purchase U.S. government securities (including securities issued by government-sponsored entities) in a syndicated offering.
- *Custody of Investment Company Assets with a Securities Depository.* The Commission proposed amendments to rule 17f-4 under the Investment Company Act.<sup>81</sup> The proposed amendments would permit additional types of organizations to operate as depositories under the rule, allow depositories to perform additional functions, and expand the types of investment companies that can rely on the rule.

## Exemptive Orders

The Commission issued 309 orders based on applications reviewed by the Office of Investment Company Regulation seeking relief from various provisions of the Investment Company Act. The Commission also issued 46 exemptive orders based on applications reviewed by the Office of Insurance Products.

Some of the significant orders and related releases that the Commission issued in fiscal 2002 are discussed below.

- *ETFs.* The Commission issued a concept release seeking comment on actively managed ETFs.<sup>82</sup> Comments received in response to this concept release are intended to inform the Commission's review of any future exemptive applications to introduce actively managed ETFs. The Commission also issued two orders permitting the first ETFs based on fixed income securities indices.<sup>83</sup> In addition, the Commission



issued an order to allow dealers to sell shares of certain existing and future ETFs in the secondary market without delivering a prospectus under certain circumstances.<sup>84</sup>

- *Closed-End Interval Fund.* The Commission issued an order permitting an exchange traded closed-end investment company to conduct periodic repurchase offers in compliance with rule 23c-3 under the Investment Company Act, but with additional flexibility to set the amount of each repurchase offer and the periodic intervals between repurchase offers, as well as to pay the proceeds in-kind.<sup>85</sup>
- *Affiliated Transactions.* The Commission issued an order permitting certain investment companies to engage in securities transactions involving a broker-dealer or a bank that is an affiliated person of an affiliated person of the investment companies.<sup>86</sup> The Commission also issued a statement concerning reimbursement of proxy solicitation expenses of an affiliated shareholder by registered investment companies under section 17(d) of the Investment Company Act and rule 17d-1.<sup>87</sup>
- *Status Under the Investment Company Act.* The Commission issued an order exempting a company from all provisions of the Investment Company Act for a period no longer than four years.<sup>88</sup> The Commission also issued an order exempting an escrow account from all provisions of the Investment Company Act except section 9 and sections 36 through 53.<sup>89</sup>
- *Relief for Arthur Andersen LLP Auditing Clients.* To minimize any potential disruptions that may have occurred as a result of the indictment of Arthur Andersen LLP, the Commission issued an order under the Investment Company Act and Investment Advisers Act that, among other things, provided for an extension of time in obtaining and filing financial statements and other reports from an independent accountant other than Arthur Andersen.<sup>90</sup> The order also

provided relief for investment company audit committees in selecting new independent auditors.

## Interpretive and No-Action Letters

Some of the most significant Investment Company Act guidance that the Division issued in 2002 is discussed below.

- *Status of Certain Legal Counsel to Independent Fund Directors as Non-Interested Persons.* The staff provided interpretive guidance to investment companies, stating that a person would not be an interested person, as defined in section 2(a)(19)(A)(iv) of the Investment Company Act, of a registered investment company solely because the person acts as legal counsel for the fund's independent directors. The staff further noted that a fund's payment of fund-related legal expenses of the independent directors' legal counsel would not, by itself, mean that such counsel is acting as the fund's legal counsel for purposes of that section.<sup>91</sup>
- *Internet-based Auction Program Offers Capital to Help Mutual Funds Meet Redemption Needs.* The staff issued a letter to a fund in which the staff agreed not to recommend enforcement action to the Commission under sections 18(f) or 22(d) of the Investment Company Act or rules 12b-1 or 22c-1 thereunder in connection with an Internet-based auction program. Specifically, the letter addressed instances in which a fund proposes to make capital available to certain open-end registered investment companies to help them meet their redemption needs.<sup>92</sup>
- *Reporting and Recordkeeping Requirements Relating to Certain Canadian Mutual Funds.* The staff agreed not to recommend enforcement action to the Commission under section 17(j) of the Investment Company Act and rule 17j-1 thereunder if access persons of a registered investment company do not report their personal transactions in and holdings of shares of certain Canadian mutual funds.

Similarly, the staff agreed not to recommend enforcement action to the Commission under section 204 of the Investment Advisers Act and rule 204-2(a)(12) if registered investment advisers do not make and keep records of advisory representatives' personal trading transactions in shares of certain Canadian mutual funds.<sup>93</sup>

- *Master and Feeder Funds.* The staff stated that it would not recommend enforcement action to the Commission under section 12(d)(1) of the Investment Company Act if a feeder fund engages in certain foreign currency hedging contracts in addition to investing in a master fund. Under the Investment Company Act, feeder funds generally are prohibited from holding any investment securities other than shares of the master fund.<sup>94</sup>
- *Private Investment Companies.* The staff stated that it would not recommend enforcement action to the Commission under section 7 of the Investment Company Act if a conduit does not register as an investment company under the Act. The conduit will privately offer its short-term paper in the United States while simultaneously publicly offering its short-term paper outside of the United States.<sup>95</sup>
- *Money Market Funds.* The staff stated that it would not recommend enforcement action to the Commission under sections 34(b) or 35(d) of the Investment Company Act or rule 22c-1 against funds that hold themselves out as money market funds in reliance on rule 2a-7 under the Act. Specifically, staff will not recommend action if such money market funds purchase certain preferred stock, provided that they otherwise comply with the conditions of rule 2a-7.<sup>96</sup>
- *Independent Directors.* The staff concluded that mutual funds can pay their independent directors' membership dues in a mutual fund directors organization, without violating the Investment Company Act's prohibitions against affiliated joint transactions. The mutual fund directors organization is a

non-profit corporation dedicated to improving fund governance by offering continuing education and outreach programs to fund directors.<sup>97</sup>

- *Affiliated Transactions.* The staff stated that it would not recommend enforcement action to the Commission under section 17(a) of the Investment Company Act with respect to certain issues raised in connection with the merger of two banking institutions. The letter permits one of the banking institutions, which is affiliated with certain funds, to sell its securities to, and purchase the other institution's securities from, the funds involved in the merger without obtaining an exemptive order from the Commission under the affiliated transaction prohibitions of the Investment Company Act.<sup>98</sup>
- *Funds Organized as Limited Partnerships.* The staff concluded that under certain circumstances the corporate general partner of a fund organized as a limited partnership, as well as the natural persons through which the general partner acts, would not be considered directors of the fund, as that term is defined in section 2(a)(12) of the Investment Company Act.<sup>99</sup>
- *Reimbursement of Proxy Expenses.* The staff stated that it would not recommend enforcement action to the Commission under section 17(d) of the Investment Company Act and rule 17d-1 if a fund reimburses an affiliated shareholder for the proxy solicitation expenses that he incurred in connection with the annual shareholder meeting at which he was elected an independent director of the fund.<sup>100</sup>
- *Securities Depositories.* The staff agreed that the Government Securities Clearing Corporation acts as a securities depository, as defined in rule 17f-4 under the Investment Company Act, in connection with its clearance and settlement of U.S. government securities through a mechanism that allows its member dealers to engage in

general collateral repurchase agreements with dealers that use different clearing banks.<sup>101</sup>

- *Independent Fund Counsel.* The staff provided guidance to fund directors regarding questions that have arisen concerning the independent legal counsel provision in the fund governance rule amendments that the Commission adopted in 2001. In particular, the staff provided guidance regarding a fund director's determination that certain legal counsel to the fund is independent.<sup>102</sup>

## Other

- *Fund Names--Frequently Asked Questions (FAQs).* The staff issued responses to FAQs about Investment Company Act rule 35d-1, which addresses certain broad categories of investment company names that are likely to mislead investors about an investment company's investments and risks. The staff's responses addressed the following topics: adoption of an 80 percent investment policy; application of the rule to tax-exempt funds; specific terms commonly used in fund names; notices to shareholders of changes in investment policies; and compliance dates.<sup>103</sup>
- *After-Tax Returns--FAQs.* The staff issued responses to FAQs about the Commission's mutual fund after-tax return rule amendments.<sup>104</sup> These amendments require mutual funds to disclose in their prospectuses after-tax returns based on standardized formulas. The amendments also require funds to include standardized after-tax returns in certain advertisements and sales materials.<sup>105</sup>
- *Electronic-Only Variable Annuity.* The Commission accelerated the effectiveness of a registration statement for an electronic-only variable annuity offered by the American Life Insurance Company of New York--the first product of its kind.<sup>106</sup> The annuity contract is offered and sold over the Internet. Before an investor may purchase the contract, he or

she must consent to electronic delivery of all documents relating to the contract. American Life will treat a contract owner's revocation of consent to electronic delivery as a surrender of the contract. In declaring the registration statement effective, the Commission stated that its decision to do so reflected the particular facts and circumstances of the registration statement.

## **Significant Investment Advisers Act Developments**

As of September 30, 2002, 7,700 investment advisers were registered with the Commission. These advisers had assets under management of approximately \$21 trillion.

### Rulemaking

- *Proxy Voting.* As a companion to its mutual fund proxy voting rule proposal, the Commission proposed new rules under the Investment Advisers Act that would address proxy voting by investment advisers.<sup>107</sup> The proposed rules would require an investment adviser that votes client securities to (1) establish proxy voting policies and procedures designed to ensure the adviser addresses material conflicts of interest that may arise between the adviser and its client and (2) vote proxies in the best interest of the client. The proposal would also require the adviser to disclose information about these policies and procedures and how clients may obtain information on how their proxies are voted.
- *Custody of Funds and Securities.* The Commission proposed amendments to modernize the Investment Advisers Act rule governing investment advisers' custody of client funds and securities.<sup>108</sup> The proposal is designed to harmonize the custody rule with current custodial practices and enhance the protections afforded to clients' assets. The proposed amendments would require an investment adviser with custody of client assets to maintain those assets with a

qualified custodian, such as a broker-dealer or bank. If the qualified custodian sends monthly account statements directly to the clients, the adviser would no longer be obligated to prepare and deliver quarterly account statements to the client or undergo an annual surprise examination of the client funds and securities in its custody. The proposed amendments would also clarify when an investment adviser has custody subjecting it to the rule's requirements.

- *Commission Registration of Investment Advisers Operating Through the Internet.* The Commission proposed a new rule that would exempt certain investment advisers that advise their clients through the Internet from the prohibition against Commission registration under the Investment Advisers Act.<sup>109</sup> The only Internet investment advisers that would be eligible for the exemption are those that advise substantially all of their clients through interactive websites. Clients of these advisers submit personal information on-line through the adviser's website and the adviser's computer-based application generates personalized investment advice that is communicated to the client through the website. The effect of the proposed exemption would be to permit these Internet investment advisers, whose clients can come from any state at any time, to register with the Commission rather than with multiple state securities authorities.

#### Interpretive and No-Action Letters

- *Performance Fees.* The staff stated that it would not recommend enforcement action to the Commission if a registered investment adviser operates under an agreement with a registered investment company that provides for a performance fee notwithstanding certain transfers of fund shares to persons to whom the investment adviser could not directly charge a performance fee.<sup>110</sup>
- *Information Provided Through Password-Protected Websites.* The staff stated that it would not recommend enforcement

action to the Commission under section 203(a) of the Investment Advisers Act if, under certain circumstances, unregistered investment advisers provide information about themselves to a website operator for inclusion on password-protected websites. The staff emphasized that the websites would be available exclusively to the institutional sales and trading desks of registered broker-dealers to streamline their communication with institutional investors for brokerage services and to fund managers to monitor their competition. The staff also emphasized that the website operator would implement procedures that would effectively prevent persons who may be seeking advisory services from gaining access to the websites.<sup>111</sup>

- *Investment Adviser Status.* The staff concluded that the National Football League Players Association would not be an investment adviser as defined in section 202(a)(11) of the Investment Advisers Act as a result of its operation of a program in which the Association provides its members with a list of financial advisers that have passed certain screening requirements established by the Association. The staff also stated that it would not recommend enforcement action to the Commission under section 206(4) of the Investment Advisers Act and rule 206(4)-3 against the Association and investment advisers participating in the Association's program if those investment advisers make cash payments to the Association and do not treat the Association as a solicitor.<sup>112</sup>

## **Significant Public Utility Holding Company Act Developments**

### Developments in Holding Company Regulation

The trend towards consolidation of utility company systems slowed but still resulted in an increase in the number of proposed mergers and acquisitions considered by the Commission in fiscal 2002. The Commission approved four new registered holding companies in fiscal 2002. In addition, utility holding company



systems continued to show interest in investments in nonutility activities on both domestic and foreign fronts.

### Registered Holding Companies

As of September 30, 2002, there were 64 public utility holding companies comprising 28 public utility holding company systems registered under the Holding Company Act. The registered systems were comprised of 132 public utility subsidiaries, 186 exempt wholesale generators, 114 foreign utility companies, 5,018 nonutility subsidiaries and 599 inactive subsidiaries, for a total of 6,113 companies and systems with utility operations in 44 states. These holding company systems had aggregate assets of approximately \$601 billion and operating revenues of approximately \$142 billion for the six-month period ending June 30, 2002.

### Financing Authorizations

The Commission authorized registered holding company systems to issue approximately \$163 billion of securities, an increase of approximately 107 percent from last year. The total financing authorizations included approximately \$102.5 billion for investments in exempt wholesale generators and foreign utility companies.

### Examinations

The staff conducted examinations of 6 service companies, 6 parent holding companies and 18 nonutility companies. The examinations focused on the methods of allocating costs of services and goods shared by associate companies, internal controls, cost determination procedures, accounting and billing policies, and quarterly and annual reports of the registered holding company systems. By identifying misallocated expenses and inefficiencies through the examination process, the Commission's activities resulted in savings to consumers of approximately \$31.8 million.

## Orders

The Commission issued numerous orders under the Holding Company Act. Some of the more significant orders are described below.

- *Relief for Arthur Andersen LLP Public Utility Clients.* The Commission issued an order to minimize any potential disruptions that may have occurred as a result of the indictment of Arthur Andersen LLP.<sup>113</sup> The order provided for an extension of time for registered public utility holding companies to obtain and file financial statements and other reports from an independent accountant other than Arthur Andersen.
- *Xcel Energy, Inc.* The Commission authorized Xcel Energy, Inc. (Xcel), a public utility holding company, to purchase the outstanding common stock of NRG Energy, Inc., a partially-owned nonutility subsidiary of Xcel, by means of a tender or exchange offer. The order also denied a request for a hearing.<sup>114</sup>
- *E.ON AG.* The Commission issued an order approving the application by E.ON AG (E.ON), a German corporation that was a utility holding company exempt by rule 5 under the Holding Company Act, to acquire Powergen plc, a British corporation that is a registered holding company, because of its ownership of Louisville Gas & Electric and Kentucky Utilities, two utility subsidiaries that operate primarily in Kentucky. The acquisition involved novel issues including,
  - permitting a registered holding company with foreign utility operations to retain ownership of a foreign water utility,
  - permitting E.ON to invest additional money in businesses that the Holding Company Act requires

them to divest in order to maximize the value at which those businesses will likely be sold,

- requiring a registered holding company to divest nonconforming companies within five years rather than the typical two or three years, and
- permitting E.ON to invest in equity securities of third parties in an amount designed to allow it to meet future pension liabilities and nuclear decommissioning costs without making those investments through a separate entity.<sup>115</sup>
- *Reliant Energy, Incorporated.* The Commission authorized Reliant Energy, Incorporated (REI), a Texas corporation engaged in various electric, gas and nonutility businesses to restructure its operations. REI operated an electric utility in Texas through its HL&P division, owned a gas utility that, through three divisions, operated in Texas, Louisiana, Arkansas, Oklahoma, Mississippi and Minnesota, and owned an 83 percent interest in Reliant Resources, a merchant generation and energy trading company. Specifically, REI sought authority to spin-off its remaining stake in Reliant Resources to its existing shareholders, and reorganize its remaining utility operations. As a result of this reorganization, REI (now renamed CenterPoint Energy) was required to register under the Holding Company Act.<sup>116</sup>

# Compliance Inspections and Examinations

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*The Office of Compliance Inspections and Examinations manages the SEC's examination program. Inspections and examinations are authorized by the Securities Exchange Act of 1934, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. Entities subject to this oversight include brokers, dealers, municipal securities dealers, self-regulatory organizations, transfer agents, clearing agencies, investment companies, and investment advisers.*

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## What We Did

- Inspected 278 investment company complexes, 1,570 investment advisers, 24 insurance company complexes, 626 broker-dealers, 138 transfer agents, and 3 clearing agencies. We also conducted 32 inspections of specific self-regulatory organization (SRO) programs, including at least one program at each of the 11 SROs.
- Continued to increase interaction among SEC examiners responsible for different types of regulated entities to increase effectiveness and productivity and enhance investor protection. We also enhanced cooperation with foreign, federal, and state regulators, as well as with the SROs. The staff conducted joint examinations and a number of significant examination sweeps with the SROs. The staff also conducted coordinated examinations with staff from Mexico and the United Kingdom's Financial Services Authority.

- Expanded our review of internal controls at several large broker-dealers, and focused on money laundering, comprehensive compliance, analysts' conflicts of interest, allocation of hot initial public offerings (IPOs), and hedge funds in both routine and special purpose examinations.
  - Conducted, for the first time, joint examination sweeps, one with SROs and state securities regulators and one with state insurance regulators. The first sweep covered 30 offices of a large broker-dealer giving a comprehensive picture of supervision. The sweep focused on large financial complexes containing both insurance and securities firms. The sweep enabled the Office of Compliance Inspections and Examinations and state regulators to take a consolidated look at complexes' compliance with and internal controls for privacy and the safeguarding of customer records and information.
  - Conducted six limited scope examinations of investment companies that invest in bank loan participation agreements (BLPs). These examinations focused primarily on the manner in which BLPs were being valued and whether the open-end investment companies maintain sufficient liquidity to meet emergency redemption demands.
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## **Investment Company and Investment Adviser Inspections**

### Investment Companies

SEC examiners inspected 278 investment company complexes, including 19 fund administrators. The average frequency of inspections for investment company complexes was 4.5 years. The complexes inspected managed \$1.3 trillion in 3,037 portfolios, which represented approximately 9 percent of the 34,423 variable insurance products, unit investment trust, and mutual and closed-end fund portfolios in existence at the beginning of 2002. The complexes inspected represented a mix of large and small complexes. Ten of the inspections were done on a “for cause” basis, which means the staff had some reason to believe that a problem existed.

Many investment company examinations focused on the role of the fund’s board of directors in reviewing and approving the advisory contract and the fund’s distribution plan. We also focused on personal trading, allocation of portfolio securities, the fund’s use of brokerage, and valuation procedures for illiquid securities.

The staff identified deficiencies or control weaknesses that resulted in a deficiency letter in 213--or 76 percent--of investment company examinations. Most frequent deficiencies or weaknesses resulting in deficiency letters were inadequate internal control procedures, conflicts of interest, inadequate oversight by board of directors, errors and omissions in registration and SEC filings, and books and records problems.

Serious deficiencies found during 14--or 5 percent--of the examinations warranted referrals for further investigation by the Division of Enforcement. The most common deficiencies resulting in referrals involved fraud; failure to disclose material information, including conflicts of interest; disproportionate

allocation of IPOs; failure to properly value illiquid privately-placed securities; misleading registration filings; and breach of fiduciary duty.

## Investment Advisers

The staff completed 1,570 inspections of investment advisers. The average frequency of inspections for the 7,347 registered investment advisers was 4.7 years. The non-investment company assets managed by the advisers inspected totaled \$3.3 trillion. The staff inspected 65 investment advisers for cause.

Many investment adviser examinations focused on adviser marketing and performance advertising, personal trading, suitability of recommendations, policies and procedures adopted in response to Regulation S-P, and disaster recovery procedures. We also continued focusing closely on how advisers fulfill their duty of best execution in client securities transactions. In addition, we participated in a fact-finding review of the activities of hedge fund and hedge fund managers as part of the Commission's investigation of the role of hedge funds in the securities markets and investor protection implications of hedge fund growth.

The staff identified deficiencies or control weakness resulting in a deficiency letter in 1,407--or 90 percent--of investment adviser examinations. Most frequent deficiencies were inadequate internal control procedures, errors and omissions in Form ADV or the brochure, books and records problems, custody, conflicts of interest, and inadequate marketing and performance practices.

Serious deficiencies warranting enforcement referrals were uncovered in 48--or 3 percent--of the examinations. The most common deficiencies resulting in referrals involved fraud; failure to disclose material information, including conflicts of interest; brokerage and execution practices; custody; misleading marketing materials; and books and records problems.

## Mutual Fund Administrators

Many mutual fund complexes use third party administrators to perform their accounting and administrative functions. During 2002, 16 of 19 fund administrator inspections resulted in deficiency letters, 2 in no further action, and one in an enforcement referral.

## Variable Insurance Products

In response to the rapid growth in variable insurance product assets and the emergence of new channels of distribution, specially trained insurance product teams conducted examinations in this area. These teams identified and examined variable life and annuity contract separate accounts. Deficiency letters were issued to each of the 24 insurance company complexes that were examined. Deficiencies included internal control weaknesses and failure to properly process contract holder transactions.

## **Broker-Dealer, Transfer Agent, and Clearing Agency Examinations**

### Broker-Dealers

In fiscal 2002, the staff conducted 626 oversight, cause, and surveillance examinations of broker-dealers, government securities broker-dealers, and municipal securities dealers. These examinations included 96 branch office examinations. Deficiency letters were sent to 529 broker-dealers, representing 84 percent of those examined. Serious deficiencies discovered in 76--or 12 percent--of the examinations warranted referrals to the Division of Enforcement for further investigation. An additional 80 examination findings--or 13 percent--were referred to SROs for appropriate action. The most common deficiencies found were recordkeeping deficiencies, net capital computation errors, unsuitable recommendations to customers, and inadequate written supervisory procedures.



Examination staff continued to conduct reviews of selected larger broker-dealers' internal controls, involving risk management, funding and liquidity, credit, and operations. Broker-dealer examinations also focused on a variety of sales practices, including sales of variable annuity products and mutual fund switching.

In addition to the routine exam work that is so critical to the success of our program, we undertook a number of initiatives this past year, including: an investigation of analysts' conflicts of interest jointly with the National Association of Securities Dealers (NASD) and New York Stock Exchange (NYSE), which resulted in significant enforcement actions; a review of stock borrow/loan arrangements; financial disclosure relating to registrants whose parents are paying the subsidiaries' expenses; private investments in public entities; contingency planning; best execution exams; and broker-dealer comprehensive compliance examinations. We also completed a coordinated exam of a large broker-dealer, working closely with the NASD, NYSE, Chicago Board Options Exchange (CBOE), and 11 states. Through this joint initiative that included exams of 30 offices, and use of a common exam module, we were able to comprehensively examine this registrant and explore the benefits of a coordinated exam approach.

In addition, the staff began a coordinated examination sweep with the NASD and NYSE to assess how broker-dealers are complying with various anti-money laundering rules and regulations. Specifically, we focused on how firms are detecting suspicious activity that could be indicative of money laundering. We also conducted several reviews of registrants' programs for dealing with the privacy rules outlined in Regulation S-P.

Examination staff continued initiatives to enhance cooperation with foreign, federal, and state regulators, as well as with SROs. Examiners worked through National Summit Meetings, Regional Summit Meetings, and other coordinated mechanisms to enhance

cooperation and reduce any duplication of effort in broker-dealer examinations.

### Transfer Agents and Clearing Agencies

In 2002, our staff conducted 138 examinations of registered transfer agents, including 34 federally-regulated banks. The program resulted in 107 deficiency letters, 8 cancellations or withdrawals of registrations, 7 referrals to the Division of Enforcement, 31 referrals to bank regulators, and one staff conference with a registrant. The examinations discovered 50 registrants with deficiencies in compliance with the Lost Securities Rule. In addition, the staff completed 3 routine inspections of clearing agencies, and conducted a series of on-site briefings regarding securities/futures cross-margining programs with staff from the Commodity Futures Trading Commission.

### **Self-Regulatory Organization Inspections**

In fiscal 2002, the staff completed 32 inspections of SROs and Alternative Trading Systems (ATSS). The completed inspections included at least one program at the following SROs:

- American Stock Exchange,
- Boston Stock Exchange,
- Chicago Board Options Exchange,
- Chicago Stock Exchange,
- Cincinnati Stock Exchange,
- International Securities Exchange,
- Municipal Securities Rulemaking Board,
- National Association of Securities Dealers,
- New York Stock Exchange
- Pacific Exchange, and
- Philadelphia Stock Exchange.

The NASD inspections included review of the regulatory programs administered by the NASD's 14 district offices. The staff also inspected the Securities Investor Protection Corporation.

The SRO inspections focused on programs dealing with arbitration, initial and continued listing of securities for trading, financial and operational surveillance and examinations of member firms, market surveillance, investigations, disciplinary actions, and the detection of and sanctioning for sales practice abuses. The inspections resulted in recommendations to improve each SRO's or ATS's effectiveness and efficiency.

### SRO Final Disciplinary Actions

Section 19(d)(1) of the Securities Exchange Act of 1934 and rule 19d-1 require all SROs to file reports with the SEC of all final disciplinary actions. In fiscal 2002, a total of 2,507 reports were filed with the SEC, as reflected in the following table.

**SRO Reports of  
Final Disciplinary Action**

American Stock Exchange	30
Boston Stock Exchange	0
Chicago Board Options Exchange	112
Chicago Stock Exchange	414
Cincinnati Stock Exchange	0
National Association of Securities Dealers	1,317
Nasdaq	10*
National Securities Clearing Corporation	0
New York Stock Exchange	528
Options Clearing Corporation	0
Philadelphia Stock Exchange	25
Pacific Exchange	68
International Securities Exchange	<u>3</u>
 Total	 2,507

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\* This number represents 19d-1 reports filed regarding Nasdaq delisting.

# Full Disclosure System

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*The Full Disclosure System's goals are to:*

- *foster investor confidence;*
- *provide investors with material information;*
- *improve the quality and timeliness of disclosure to investors;*
- *contribute to the maintenance of fair and orderly markets;*
- *reduce the costs of capital raising; and*
- *inhibit fraud in the public offering, trading, voting, and tendering of securities.*

*The Division of Corporation Finance achieves these goals by reviewing the financial and non-financial disclosure made by companies in their periodic reports and transactional filings. The Division also achieves its goal by making and interpreting rules that facilitate and enhance corporate disclosure.*

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## What We Did

- Monitored the annual reports of all Fortune 500 companies to identify information that may be unclear or conflict with accepted accounting principles or SEC rules, and completed reviews of the year-end financial disclosure of 2,570 reporting issuers and approximately 950 new issuers.
- Implemented the Commission's order under section 21(a) of the Securities Exchange Act of 1934 (Exchange Act) requiring chief executive officers

(CEOs) and chief financial officers (CFOs) of the 947 largest U.S. companies to certify past disclosure.

- Adopted amendments requiring certification of annual and quarterly reports by CEOs and CFOs.
  - Adopted amendments to accelerate the filing of quarterly and annual reports under the Exchange Act by certain domestic reporting companies.
  - Adopted rule and form amendments that require foreign private issuers and foreign governments to file electronically their securities documents through our Electronic Data Gathering, Analysis and Retrieval (EDGAR) system.
  - Adopted amendments to accelerate filing of Exchange Act section 16 beneficial ownership reports filed by officers, directors, and principal security holders.
  - Proposed amendments to increase current disclosure by requiring a company to file a current report on Form 8-K to disclose the occurrence of 11 new events including material impairments, write-offs, and restructuring charges.
  - Adopted amendments to improve the transparency of financial disclosure by requiring companies to disclose their critical accounting estimates and the initial adoption of accounting policies that have a material impact on their financial presentation.
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## Review of Filings

The following table summarizes the principal filings reviewed during the last five years.

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	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>
<b>Full Disclosure Reviews</b>					
Major Filing Reviews					
Securities Act filings					
Initial Public Offerings	1,320	1,010	1,350	745	610
Repeat Issuers	720	510	270	620	715
P/E Amdts. <u>a/</u>	28	10	10	25	15
Regulation A	81	65	70	50	30
Exchange Act					
Initial Registrations	338	680	1,015	400	310
Annual Report Reviews					
Full <u>b/</u>	1,527	1,375	595	880	1,220
Full Financial	997	960	550	1,400	1,440
Tender Offers (14D-1)	259	355	300	225	210
Going Private Schedules	115	180	115	145	90
Contested Proxy					
Solicitations	59	70	90	58	66
Proxy Statements					
Merger/Going Private	219	195	75	65	45
Others w/Financials	257	190	150	90	125
Reporting Issuer Reviews <u>c/</u>	2,828	2,550	1,535	2,400	2,570
New Issuer Reviews <u>d/</u>	1,739	1,755	2,435	1,195	950
Total Issuer Reviews	4,567	4,305	3,970	3,595	3,520

a/ Post-effective amendments with new financial statements.

b/ Includes annual reports reviewed in connection with the review of other filings that incorporated financial statements by reference.

c/ Includes companies subject to Exchange Act reporting whose financial statements were reviewed during the year.

d/ Includes reviews of Securities Act of 1933 registration statements and Exchange Act registrations by non-Exchange Act reporting companies. Includes reviews of Regulation A filings.

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Companies filed registration statements covering \$2.0 trillion in proposed securities offerings during the year, approximately 13 percent less than the amount registered in 2001. With the continuing decline in corporate merger activity and initial filings by new companies, the Division again focused its resources on reviewing Exchange Act reports and away from transactional filings (Securities Act of 1933 registration statements and Exchange Act proxy statements). In fiscal 2001, we reviewed 1,595 transactional filings and 2,280 Exchange Act reports. During fiscal 2002, we reviewed 1,540 transaction filings, 3 percent less than last year, and 2,660 Exchange Act reports, nearly 17 percent more than last year.

## **Sarbanes-Oxley Act of 2002**

The SEC began implementing the provisions of the Sarbanes-Oxley Act, which was adopted late in the fiscal year. The Act provides the SEC with additional significant review and rulemaking responsibilities, including the requirement to refine its review process in light of specified criteria and to review each reporting issuer at least once every three years. The Act also imposes new requirements on officers of domestic and foreign companies, expedites the filing of beneficial ownership reports, expands disclosure requirements of off-balance sheet transactions, and sets fixed time frames for a number of studies and rulemaking projects.

## **International Activities**

Large numbers of foreign companies continued to access the United States public securities markets in 2002. During the year, approximately 70 foreign companies from 25 countries entered the U.S. public markets for the first time. At year-end, there were over 1,300 foreign companies from 59 countries filing reports with us. Public offerings filed by foreign companies in 2002 totaled over \$147 billion.



## **Recent Rulemaking, Interpretive, and Related Matters**

Rulemaking is undertaken to protect investors, facilitate capital formation, improve and simplify disclosure, establish uniform requirements, and eliminate unnecessary regulation. The objective in rulemaking is to define regulatory requirements on a cost-effective basis. The SEC provides general interpretive and accounting advice through interpretive releases, staff legal bulletins, staff accounting bulletins, no-action and interpretive letters, the current issues outline, and responses to telephone inquiries.

### **Certification of Disclosure in Companies' Quarterly and Annual Reports**

On August 28, 2002, the Commission adopted rules under the Exchange Act to require an issuer's principal executive officer and principal financial officer to certify the contents of the issuer's quarterly and annual reports.<sup>117</sup> The rules, which implemented section 302 of the Sarbanes-Oxley Act, superseded the certification proposal included in our June 14, 2002 release.<sup>118</sup>

### **Acceleration of Periodic Report Filing**

On September 5, 2002, the Commission adopted amendments originally proposed in April 2002 that would accelerate the filing of quarterly reports and annual reports under the Exchange Act by domestic reporting companies.<sup>119</sup> The amendments shorten the filing deadlines for the affected companies from 45 to 30 calendar days after period-end for quarterly reports and from 90 to 60 calendar days after year-end for annual reports.

### **Accelerated Filing of Beneficial Ownership Reports**

On August 27, 2002, the Commission adopted rule and form amendments to implement the accelerated filing deadline applicable to change of beneficial ownership reports. Officers,

directors, and principal security holders are required to file these reports under section 16(a) of the Exchange Act.<sup>120</sup> The amendments are intended to facilitate the statutory changes required by the Sarbanes-Oxley Act.

### Mandated EDGAR Filing For Foreign Issuers

On May 14, 2002, the Commission adopted amendments that require foreign private issuers and foreign governments to file electronically their securities documents through our EDGAR system.<sup>121</sup>

### Disclosure of Equity Compensation Plan Information

On December 21, 2001, the Commission adopted amendments that require companies to disclose, at least annually, information about the total number of securities that have been authorized for issuance under their equity compensation plans, regardless of whether or not security holders approved the plans.<sup>122</sup> The amendments address investors' concerns about companies' increased use of stock options as compensation, the potential dilutive effect of these options, and the absence of information regarding plans adopted without shareholder approval.

### Requirements for Arthur Andersen LLP Audit Clients

On March 18, 2002, the Commission adopted rules to assure a continuing and orderly flow of information to investors and the U.S. capital markets, and to minimize any potential disruptions occurring as a result of the Arthur Andersen LLP indictment.<sup>123</sup> The Commission also modified the requirements for inclusion of audited financial statements in Securities Act registration statements and in Trust Indenture Act of 1939 filings from registrants unable or electing not to have Andersen issue a manually signed audit report.

## Additional Form 8-K Disclosure Requirements and Acceleration of Filing Date

On June 17, 2002, SEC staff proposed amendments to require a company to file a current report on Form 8-K to disclose the occurrence of 11 new extraordinary corporate events, including material impairments, write-offs, and restructuring charges.<sup>124</sup> The amendments also would accelerate the filing deadline for Form 8-K to require filing within two business days after the occurrence of an event requiring disclosure.

## Disclosure in Management's Discussion and Analysis About the Application of Critical Accounting Policies

On May 10, 2002, the Commission proposed amendments to improve the transparency of financial disclosure by requiring companies to disclose their critical accounting estimates and the initial adoption of accounting policies that have a material impact on their financial presentations.<sup>125</sup>

## Commission Order

On June 27, 2002, the Commission issued an order under section 21(a) of the Exchange Act requiring the CEOs and CFOs of the 947 largest U.S. companies to certify their most recent annual reports and subsequent Exchange Act filings. SEC staff reviewed certifications and related filings to ensure compliance with the order. The staff also established a location on the Commission's website where investors could monitor and review certifications. In August and September 2002, there were over 628,000 total "hits" on this location, nearly 12 times the number of the next most popular page on the Commission's website.

## **Conferences**

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

The SEC conducted the 19th Annual Federal/State Uniformity Conference in April 2002 in Washington, D.C. Approximately 60 Commission officials met with nearly 60 representatives of the North American Securities Administrators Association, Inc. to discuss methods of achieving greater uniformity in federal and state securities matters. After the conference, a final report summarizing the discussions was prepared and distributed to interested persons and participants.

### **SEC Government-Business Forum on Small Business Capital Formation**

In September 2002, we conducted the 21st Annual Government-Business Forum on Small Business Capital Formation in Washington, D.C. This forum is the only government-sponsored national gathering related to the securities industry that is geared toward small business. It offers small businesses the opportunity to inform government officials how the laws, rules, and regulations affect their ability to raise capital.

# Accounting and Auditing Matters

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*The Chief Accountant is the principal adviser to the Commission on accounting and auditing matters arising from the administration of the federal securities laws. Activities designed to achieve compliance with the accounting, financial disclosure, and auditor independence requirements of the securities laws include:*

- *rulemaking and interpretation initiatives that supplement private sector accounting standards and implement financial disclosure requirements;*
- *a review and comment process for agency filings to improve disclosures in filings, identify emerging accounting issues (which may result in rulemaking or private-sector standard setting), and identify problems that may warrant enforcement actions;*
- *oversight of U.S. private sector efforts, principally by the Financial Accounting Standards Board (FASB), the Public Company Accounting Oversight Board (PCAOB), and the American Institute of Certified Public Accountants (AICPA); and*
- *monitoring of various international bodies, which establish accounting, auditing, and independence standards designed to improve financial accounting and reporting and the quality of audit practice, including standards applicable to multinational offerings.*

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## What We Did

- Played a proactive role in responding to a turbulent financial reporting environment through issuance of guidance to company management, auditors, audit

committees, and investors on various topical financial reporting matters emerging from this environment.

- Proposed rules which would have established a Public Accountability Board (PAB) to improve investor confidence in the quality of reporting.
  - Began implementing numerous provisions of the Sarbanes-Oxley Act of 2002.
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## **Accounting-Related Rules and Interpretations**

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

SEC staff identified several deficiencies in our current financial reporting system and undertook the initiatives described below to address these deficiencies. Among the most significant of these deficiencies was the failure of the accounting profession's self-regulatory system.

### **Pro Forma Financial Information**

On December 4, 2001, the Commission issued a cautionary release in response to an increase in the use of measures of earnings and results of operations calculated using methodologies other than U.S. Generally Accepted Accounting Principles (GAAP).<sup>126</sup> This information is presented in earnings releases and often is referred to as "pro forma" financial information. The release cautions public companies that the use of "pro forma" information entails certain risks and alerts investors to the potential dangers in relying on such information. Shortly after

fiscal year-end, as directed by section 401(b) of the Sarbanes-Oxley Act, the Commission issued proposed rules to govern the presentation of non-GAAP financial information.<sup>127</sup>

### Disclosure of Critical Accounting Policies

The Commission issued a second cautionary release to remind company management, auditors, audit committees, and other advisors that the selection and application of the company's critical accounting policies and practices must be appropriately reasoned.<sup>128</sup> The release emphasized the demands by investors for transparent disclosure of accounting policies and their effect. As a follow up action, the Commission subsequently proposed rules to require that public companies provide disclosures about the selection of critical accounting policies within Management's Discussion and Analysis (MD&A).<sup>129</sup>

### Commission Statement Regarding MD&A

In response to a rulemaking petition submitted by certain major accounting firms and the AICPA, the Commission issued a statement regarding disclosures that should be considered by registrants in preparing MD&A disclosures.<sup>130</sup> The release focuses on the need to provide disclosures on (1) liquidity and capital resources, including dependence on off-balance sheet arrangements, (2) trading activities involving non-exchange trading contracts, and (3) related-party transactions.

### Requirements for Arthur Andersen LLP Audit Clients

The Commission adopted certain temporary and final rules to ensure a continuing and orderly flow of information to investors and U.S. capital markets and to minimize potential disruptions resulting from the indictment of Arthur Andersen LLP.<sup>131</sup>

### Improved Oversight and Accountability of Auditors

In June, the Commission proposed rules that would have established a framework for enhancing the quality of financial

information through needed improvements in oversight of the auditing process.<sup>132</sup> The rule proposal was designed to restore investors' confidence in the financial information being relied upon to make investment decisions. As emphasized by Chairman Pitt in congressional testimony of March 21, 2002, concerning accounting and investor protection issues raised by Enron and other public companies, "[t]he number of sudden and dramatic reversals of public companies' financial statements calls into question the regulatory system currently used to oversee the quality of audits of public company financial statements."<sup>133</sup>

Under the proposed rules, a registrant's financial statements would not have complied with the requirements of the securities laws and Commission rules unless the registrant's independent accountant was a member of a PAB. The proposed rules also would have required that the registrant engaging an accountant to audit or review financial statements that are filed with the Commission be an adjunct member of the same PAB to which the independent accountant belongs.

The proposed rules set forth a number of specified conditions and functional performance requirements that must be met before the Commission would recognize a PAB. Examples included:

- the PAB must be committed to improving the quality of financial statements and the professional conduct of accountants by (1) directing periodic reviews of accounting firms' quality controls over their accounting and auditing practices, (2) disciplining accountants when appropriate, and (3) performing other related functions;
- a majority of the PAB's membership must be persons who are not members of the accounting profession;
- the PAB must be subject to SEC oversight; and



- the PAB has the authority to establish audit, quality control, and ethics standards, or to designate and oversee other private sector bodies that would establish such standards.

The PAB was intended as a replacement for the then-current system of self regulation to which the accounting profession was subject. There was general consensus among affected parties that this system of oversight (involving firm-on-firm peer reviews overseen by the Public Oversight Board under the aegis of the AICPA) had not produced a credible result. Longstanding deficiencies in the regulatory system to oversee the quality of audits and reviews of financial statements filed with the Commission have contributed to a decline in investor confidence and provided the impetus for the Commission's proposal. This policy initiative was superseded by the Sarbanes-Oxley legislation.

### Implementation of the Sarbanes-Oxley Act

In addition to the sudden bankruptcy of Enron Corporation and the indictment and collapse of Arthur Andersen LLP described earlier, reports that WorldCom would restate its financial statements with respect to billions of dollars in operating expenses further eroded investor confidence in the integrity of reported information. In response, Congress passed the Sarbanes-Oxley Act.

The Sarbanes-Oxley Act established the PCAOB and addressed issues related to auditor independence, corporate responsibility, full disclosure, analysts' conflicts of interest, criminal sanctions, and other matters. The staff provided input during consideration of the bills that formed the Act and is participating in drafting several of the rules mandated by the Act. These rules relate to, among other things:

- the formation of the PCAOB;

- preventing an issuer’s officers, directors, and persons acting under the director of an officer or director from fraudulently influencing, coercing, manipulating, or misleading an auditor of the issuer’s financial statements for the purpose of rendering the financial statements materially misleading;
- auditor independence, including prohibited non-audit services, an audit committee’s pre-approval of services provided by the auditor, and limitations on certain audit firm partners becoming officers of audit clients;
- management and auditor reports on an issuer’s internal controls for financial reporting;
- disclosure of material off-balance sheet transactions;
- disclosure of “pro forma” financial information;
- recognition as “generally accepted” the accounting standards promulgated by the Financial Accounting Standards Board; and
- the retention of relevant audit records.

Also, pursuant to section 108(d) of the Act, the staff has initiated a study on the adoption in the United States of a system of principles-based accounting standards.

## **Oversight of Private Sector Standard Setting**

### Accounting Standards

#### *Financial Accounting Standards Board*

The Commission oversees the FASB process to determine whether the process is operating in an open, fair, and impartial

manner and whether each standard is within an acceptable range of alternatives that serves the public interest and protects investors. The Commission and its staff work with the FASB to improve the standard-setting process, including the need to respond to various regulatory, legal, and business changes in a timely and appropriate manner. The FASB process involves constant, active participation by all interested parties in the financial reporting process.

The staff attended meetings of the FASB and its Emerging Issues Task Force (EITF), observed FASB task force meetings, and held quarterly discussions with the FASB staff. The Commission's Office of the Chief Accountant observed the quarterly meetings of the Financial Accounting Standards Advisory Council, which consults with the FASB on major policy and agenda issues.

### Special Purpose Entities

During 2002, the FASB resumed work on a project to specify when entities with specific limits on their powers, also referred to as special purpose entities (SPE), should be included within consolidated financial statements. In previous SEC annual reports, we noted that the existing standards do not adequately address circumstances involving SPEs and urged the FASB to continue its efforts to provide consolidation guidance for these entities.

The FASB issued a proposed interpretation that would establish standards for consolidation of SPEs that do not have sufficient equity interest to finance their own activities without additional financial support.<sup>134</sup> Under the proposed interpretation, an enterprise that provides significant financial support to a SPE would be required to consolidate the SPE if it provides either significantly more financial support than any other party or a majority of the financial support.

At fiscal year-end, the FASB was evaluating comment letters received on the proposed interpretation along with input from participants at a public roundtable conducted on September 30 to

discuss issues relevant to this project. The FASB plans to issue a final interpretation in early 2003.

### Recognizing Expense for Stock-Based Compensation Arrangements

During 2002, several prominent public companies announced plans to adopt the provisions of FASB Statement 123 in recognizing expense for stock-based compensation arrangements.<sup>135</sup> In response to these actions, the FASB reached a number of decisions intended to ease the transition for companies that voluntarily adopt the fair value method of recording expenses related to employee stock options as prescribed by the FASB standard. The FASB issued an exposure draft of a proposed amendment to Statement 123<sup>136</sup> that would permit three alternative methods of transition for companies choosing to adopt the preferable method of accounting for stock-based compensation arrangements. The exposure draft also would amend Statement 123 to require expanded disclosures about the costs of stock-based compensation and to require disclosures in interim financial statements.

### Revenue Recognition

The FASB added to its agenda a project to develop a comprehensive standard on revenue recognition applicable to business entities generally. The scope of the project will include a reconsideration of the guidance on revenue recognition set forth in the FASB's Concepts Statements on revenue recognition and measurement. From the SEC's perspective, this project should be given high priority in view of the substantial number of financial frauds involving improper revenue recognition by public companies.

During 2002, the FASB's EITF reached consensus on several significant issues relating to the appropriate method of revenue recognition for certain specific types of transactions. The EITF also devoted significant resources to addressing a related issue of how an arrangement involving multiple deliverables should be divided into units for accounting purposes.<sup>137</sup>

## Principles-Based Accounting Standards

Also during 2002, the FASB initiated a project to address concerns about an increase in the detail and complexity of U.S. accounting standards. The project entailed issuance of a proposal for a principles-based approach to accounting standards setting, which the FASB intends to pursue. As presently contemplated, the accounting standards developed under a principles-based approach focus on establishing general principles derived from the conceptual framework concerning the recognition, measurement, and reporting requirements for the transactions covered by the standards. The major differences envisioned between existing accounting standards and standards developed under a principles-based approach relate to exceptions and the level and nature of additional guidance.

Under the principles-based approach being contemplated, accounting standards would provide few, if any, exceptions to the general principles. Furthermore, additional guidance would be restricted to the transactions typically covered by the relevant standard; the exercise of professional judgment would be necessary in applying the general principles to other transactions.

As discussed earlier, the Sarbanes-Oxley legislation directs the SEC to conduct a study of principles-based accounting standards. Compliance with the legislation will require that a report of such a study be made to Congress no later than July 30, 2003.

## Other

The FASB completed a project on the financial reporting for costs associated with exit or disposal activities.<sup>138</sup> The standard resolved a conflict between guidance previously issued by the EITF and the FASB's conceptual definition of a liability.<sup>139</sup>

The FASB also worked on a project to amend its existing requirements for applying the purchase method in acquisitions for financial institutions. The amendments would conform these requirements with newly adopted Statements No. 141, *Business Combinations* and No. 142, *Goodwill and Intangible Assets*. The

FASB issued a final standard conforming these requirements in October 2002.<sup>140</sup>

### *Accounting Standards Executive Committee (AcSEC)*

The Commission's accounting staff oversaw various accounting-standard setting activities conducted through the AcSEC. The AICPA established AcSEC to provide guidance through its issuance of statements of position and practice bulletins. AcSEC continued work on various projects, including one concerning the accounting for certain costs and activities related to property, plant, and equipment.<sup>141</sup>

### *Panel on Audit Effectiveness of the Public Oversight Board*

In August 2000, the Panel on Audit Effectiveness (Panel) issued its report, which included recommendations to the accounting profession, standard setters, regulators and others.<sup>142</sup>

Organizations are implementing the Panel's recommendations voluntarily. In the course of carrying out its oversight responsibilities, SEC staff has monitored the implementation of the Panel's recommendations, including the Auditing Standards Board's responses to the Panel's recommendation (described below).

In addition to the staff's activities, the Transition Oversight Staff (TOS) (formerly the staff of the Public Oversight Board) periodically monitored and reported on the actions taken by those organizations necessary to respond to the Panel's recommendations. The TOS completed its most recent analysis early in 2002. The TOS, SEC staff or PCAOB staff may complete future analyses.

### *Public Company Accounting Oversight Board (PCAOB)*

The Sarbanes-Oxley Act established the PCAOB to oversee the audits of public companies and related matters, to protect investors, and to further the public interest in the preparation of informative, accurate, and independent audit reports. The PCAOB is expected

to accomplish these goals through registration, standard setting, inspection, and disciplinary programs. Under the Act, the Commission, among other things, is to approve the PCAOB's rules, hear appeals from the PCAOB's disciplinary process, and oversee the PCAOB's inspection program. At fiscal year-end, the PCAOB was in the formative stages. SEC staff will work closely with the Board as it develops its programs and begins operations.

## Auditing Standards

### *Auditing Standards Board (ASB)*

The staff continued to oversee activities of the ASB, including its efforts to enhance the effectiveness of the audit process. The staff monitored the ASB's progress in addressing the recommendations in the report of the Panel on Audit Effectiveness. During 2002, the ASB issued new auditing standards regarding audit documentation,<sup>143</sup> the hierarchy of Generally Accepted Auditing Standards,<sup>144</sup> and consideration of fraud in a financial statement audit.<sup>145</sup> The ASB also issued guidance on the appropriate reporting of restated financial statements previously audited by Arthur Andersen<sup>146</sup> and amended its existing guidance to eliminate auditors reporting on hypothetical transactions.<sup>147</sup>

## Quality Controls and Peer Reviews

### *SEC Practice Section (SECPS)*

The Commission's accounting staff oversaw the processes of the SECPS, established by the AICPA to improve the quality of audit practice by member accounting firms that audit the financial statements of public companies. Two programs administered by the SECPS are intended to evaluate whether the financial statements of SEC registrants are audited by accounting firms that have adequate quality control systems. The peer review program requires a review of member firms by other accountants every three years, and the Quality Control Inquiry Committee (QCIC) reviews on a more timely basis the quality control implications of

litigation against member firms that involves public company clients.

Significantly, in January of this year, the Public Oversight Board voted to cease operations after the Commission proposed establishing a new Public Accountability Board. The staff of the POB was reconstituted as the TOS and will perform an oversight role over the peer review and QCIC processes until the PCAOB is operational next year.

During the year, the Commission's staff selected a random sample of peer reviews, evaluated selected working papers and related POB oversight files, and reviewed QCIC closed case summaries and related POB oversight files. The SEC staff provided the POB staff (currently the TOS) with comments on certain peer reviews with the goal of achieving more understandable communications to the public of the peer review findings.

The SECPS issued a new membership requirement that sets standards for member firms' quality control systems for monitoring auditor's independence in U.S. firms. The largest firms in the SECPS agreed with the SEC staff to conduct a voluntary "look-back" program to assess each firm's compliance with specified independence criteria. The agreement requires firms to upgrade their quality control systems that monitor compliance with auditor independence rules. Pursuant to the terms of the look-back program, participating firms also are required to permit the POB to oversee the design and implementation of the new quality control systems. The look-back phase of the review was completed. The second phase of the program, under which the TOS is to test the firms' quality controls, is in the final stages. SEC staff will continue to consult with the TOS and the accounting firms during this phase of the review.



## International Accounting and Auditing

Transparency in financial reporting and the impartial assurance provided through audits of public company financial statements by independent accountants are critical to the capital formation provided in all investing activities. It is especially valuable in international investing, where great distances and substantial differences in business and economic conditions may be involved.

Investors need high quality information on the performance and financial position of the companies that look to attract their investments. Companies seeking funds for growth are obligated to produce reliable and useful financial information, in accordance with GAAP and SEC requirements, to supply the full and fair disclosure that will aid investor decision-making.

### International Accounting Standards

International accounting standards have been a subject of interest in the global financial community for some time. The SEC, the International Organization of Securities Commissions (IOSCO), and other international financial institutions and professional bodies have noted the benefit that could be provided to investors if a single set of high quality global accounting standards could be developed and applied in such a way as to become widely accepted and recognized for use in cross-border investing activities. The International Accounting Standards Board (IASB) and its predecessor, the International Accounting Standards Committee, have been working to develop and improve such a set of global accounting standards for more than 25 years. Such work has become more prominent in recent years, in part due to the decision of the European Union to adopt International Accounting Standards (IAS) as its official body of accounting standards in 2005 and similar actions announced or being considered in several other countries. SEC staff regularly monitored the accounting standards development work of the IASB and communicated with the IASB on areas of concern, either directly or through staff involvement in IOSCO.

The IASB established an agenda of significant accounting projects soon after its reorganization into a full-time, independent private sector accounting standards-setting body in 2001. During 2002, several additional projects were added to address current matters of concern in financial reporting, and the IASB also established the International Financial Reporting Interpretations Committee (IFRIC). The SEC staff attended the meetings of IFRIC as one of the IOSCO observers of the process, and also sends an SEC representative to the meetings of the IASB Standards Advisory Council. The SEC staff also observes the work of IFRIC and encourages the development of guidance that will promote the consistent interpretation and application of IAS.

### Convergence of Accounting Standards

U.S. GAAP has long been recognized as the most comprehensive and robust body of accounting guidance in the world. GAAP has been widely accepted for financial reporting by U.S. companies listing in markets outside the U.S., and for use in some instances by non-U.S. companies. At the same time, participants in cross-border investing activities, regulators with oversight responsibilities, and others in the international financial reporting community have noted the desirability of achieving a single set of high quality global accounting standards that could be used in cross-border offerings of securities.

In 2000, the SEC issued a concept release seeking public comment on experiences using IAS issued by the International Accounting Standards Committee, the predecessor to the IASB, and also raised a number of questions regarding current and potential use of IAS by foreign private issuers listing in the U.S. markets.<sup>148</sup> A significant topic in the release involved the SEC's requirement for reconciliation of financial statements of foreign issuers prepared under IAS to net income and equity prepared under U.S. GAAP.

Also in 2000, IOSCO completed an assessment of the IAS then in existence and issued a recommendation that IOSCO members accept IAS in incoming filings of cross-border issuers, subject to

additional requirements for interpretation, disclosure or reconciliation that might be needed to meet national concerns in member jurisdictions.

The SEC staff continued consideration of potential actions with respect to use of IAS by foreign issuers in the U.S. Staff activities included identification and consideration of the accounting differences that are being encountered in the reconciliations from IAS to U.S. GAAP in foreign issuer filings under SEC Form 20-F, as well as attention to other differences that exist in the two bodies of accounting standards.

In discussions of accounting differences between IAS and U.S. GAAP, the SEC staff encouraged the FASB and the IASB to work together to achieve greater convergence in accounting standards. The two standards-setting boards responded by agreeing to work toward reducing the differences in IAS and U.S. GAAP as they work to improve accounting principles and address issues in financial reporting.

### Consistency in International Financial Reporting

A set of high quality international accounting standards is a critical foundation for international financial reporting, but other elements of a global financial reporting infrastructure are needed to support their consistent use. Other elements of a global financial reporting infrastructure include:

- high quality auditing and auditing standards;
- consistent interpretation of accounting standards;
- effective oversight of standards setters and auditors;
- independence of auditors;
- ethics and competence on the part of preparers, auditors, and others;

- corporate governance over financial reporting;
- quality controls within accounting firms; and
- reviews and enforcement of financial reporting by authorities.

The SEC staff works with regulators within the IOSCO to promote consistent interpretation and application of IAS across jurisdictions, to enhance international financial reporting in other ways, and to promote cooperation in regulatory oversight, review, and enforcement activities. During 2002, the staff participated in a number of IOSCO initiatives to curb abuses in the use of non-GAAP performance measures, and to establish general principles for auditor oversight, auditor independence, and transparency and disclosure. These efforts resulted in the IOSCO issuance of a “Cautionary Statement on Non-GAAP Results Measures” and also in issuance of three IOSCO statements of principles to guide securities regulators in dealing with critical areas necessary for investor confidence in securities markets. The principles describe essential features of regulatory systems requiring transparency and disclosure by listed entities, the independence of external auditors, and the need for public oversight of the audit function.

The staff is engaged in ongoing dialogues with other countries’ regulators regarding ways to promote consistent interpretation of IAS across jurisdictions as well as ways to communicate on other accounting and reporting matters of concern. The staff met this year with representatives of the European Commission and authorities from jurisdictions around the world to discuss ways in which regulators can promote high quality financial reporting and auditing.

### International Audit Quality

It has been noted that the quality and amount of effort associated with audits of public company financial statements varies

significantly around the world. The SEC staff has been working, through IOSCO and directly, with public and private sector bodies that are concerned with international auditing. During 2002, the staff participated in an ongoing assessment of the International Standards on Auditing issued by the International Federation of Accountants. The staff met with representatives of the European Commission, regulators in other countries, and audit firms and professional groups to discuss ways to improve international auditing through auditor oversight, internal and external reviews, and audit firm quality controls.

## Other Litigation and Legal Activity

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*The Office of General Counsel provides legal services to the Commission concerning its law enforcement, regulatory, legislative, and adjudicatory activities. The office represents the Commission in appeals and in defense of civil litigation, and provides technical assistance to Congress on legislative initiatives.*

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### What We Did

- Played a lead role in coordinating the agency's implementation of the landmark Sarbanes-Oxley Act of 2002.
  - Played a significant role in crafting the Commission's proposal to create a private sector oversight board for the accounting profession and advised the Commission on other, novel measures taken to enhance investor confidence, including the Commission's order requiring the 947 largest public companies to certify the accuracy and completeness of their filings.
  - Litigated *SEC v. Zanford*, in which the Supreme Court issued an important decision upholding the Commission's longstanding interpretation of the antifraud provisions that assures broad protection for investors.
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## Significant Litigation Developments

Fraud “in connection with the purchase or sale of any security”

In *SEC v. Zandford*,<sup>149</sup> the United States Supreme Court agreed with the Commission’s argument that, contrary to the view of the court of appeals,<sup>150</sup> a stockbroker’s fraud was committed “in connection with the \* \* \* sale of any security,” and therefore violated Securities Exchange Act of 1934 (Exchange Act) section 10(b), when he sold his customer’s securities for his own benefit and used the proceeds for himself, without authorization and disclosure to his customer. The Supreme Court rejected the view that only a misrepresentation about a particular securities value can constitute a violation.

Stock Manipulation Under Section 10(b) of the Exchange Act

In *Markowski v. SEC*,<sup>151</sup> the court of appeals agreed with the Commission that “manipulation can be illegal solely because of the actor’s purpose” and that, accordingly, a stock price support scheme that involved real rather than fictitious trades constituted unlawful manipulation under section 10(b) because of the manipulators’ purpose to affect the stock price. Markowski’s petition for Supreme Court review was denied.<sup>152</sup>

Insider Trading

In *SEC v. Lipson*,<sup>153</sup> the court of appeals upheld an insider trading judgment against a corporate president who sold stock in his company based on confidential adverse information about the company’s financial performance. On appeal, the defendant argued that the jury instructions improperly shifted to him the burden of persuasion on whether he used the information. The court agreed that such an instruction would be improper, but held that the instruction in this case did not shift the burden of persuasion. It held that the instruction properly told the jury that where a defendant possesses inside information, the jury may infer that his contemporaneous trades were influenced by the information. The court stated that the inference “is sufficiently

compelling" to shift to the defendant "the burden of presenting some rebuttal evidence, on pain of suffering an adverse judgment as a matter of law if he does not." The court also rejected the defendant's argument that a legitimate purpose for the trade proves that the defendant was not influenced by the inside information. The court held that a person might have two purposes and "[t]he existence of the legitimate purpose would not sanitize the illegitimate one."

In *SEC v. Yun*,<sup>154</sup> a case involving the tipping of non-public material information by the spouse of a corporate insider and trading by the tippee, the Commission argued that the appellants' contention that severe recklessness is not sufficient to satisfy the scienter requirement for insider trading is contrary to law, and also that there is no requirement of a "tipper benefit" in cases brought under the misappropriation theory of insider trading. The appeal is pending.

#### Securities Act of 1933 (Securities Act) Registration

In a friend of the court brief filed in *DeMaria v. Anderson*,<sup>155</sup> the Commission took the position that an issuer whose prospectus is subject to rule 3-12 of Regulation S-X, which provides that no interim financial results are required from an issuer that has filed a registration statement containing an audited financial statement as of a date within 135 days, must nevertheless report interim financial results if the failure to do so would amount to a material omission rendering what has been disclosed false or misleading. The Commission further urged that, under rule 304(b)(2) of Regulation S-T, the determination whether a registrant has made a "good faith effort" to describe graphic material not included in an electronically filed EDGAR prospectus requires the court to look at the nature of: (1) the graphic material being described, (2) the discrepancy and the degree to which it is evident, and (3) the steps that the registrant took to check the accuracy of the electronic filing. The appeal is pending.



Definition of a Security; Reliance by Private Section 10(b)  
Plaintiffs on Oral Misrepresentations that Vary from Written  
Disclosures

In *Caiola v. Citibank, N.A., New York*<sup>156</sup>, the court of appeals agreed with the position taken by the Commission in a friend of the court brief that the term “option” in the Exchange Act’s definition of “security” includes both physically-settled and cash-settled options, rejecting the district court’s conclusion<sup>157</sup> that only physically-settled options are included. The court of appeals also agreed with the Commission and rejected the district court’s interpretation of the Commodity Futures Modernization Act of 2000 (CFMA) as providing that cash-settled options are “security based swap agreements” under the CFMA and excluded from the definition of security. The court of appeals also followed the reasoning urged by the Commission in questioning the correctness of the district court’s holding that oral misrepresentations are not actionable by a private plaintiff under section 10(b) as a matter of law when they are contradicted by written disclosures.

In *SEC v. ETS Payphones, Inc.*,<sup>158</sup> the court of appeals held that payphone sale/lease/buyback agreements were not investment contracts, and thus not securities, under the test in *SEC v. W.J. Howe, Co.*,<sup>159</sup> which described an investment contract as “a contract, transaction, or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter” or a third party. The court ruled that the fixed lease payments did not constitute “profits” as contemplated by *United Housing Found. v. Forman*,<sup>160</sup> because they represented neither capital appreciation nor a participation in the issuer’s earnings. The court further held that even if the fixed payments were profits for purposes of the investment contract test, the interests at issue failed to meet another element of the test--the lease payments were not derived from the efforts of others because they were “contractually guaranteed.”

In its petition for rehearing in the *ETS Payphones* case, the Commission argued that the panel’s holding on fixed returns

conflicts with the *Howey* decision itself, which specifically refers to “income” as being a form of “profits” and with the decisions of two other courts of appeals expressly holding that fixed returns are profits under the investment contract test. In addition, the Commission argued that the alternative holding--that any profits involved were not derived from the efforts of others because they were “contractually guaranteed”--conflicts with numerous Supreme Court and court of appeals decisions holding that the “efforts of others” element turns on whether, as represented to potential investors, it is promoters or the investors themselves who are to manage the enterprise expected to generate the profits, not on whether the profits are provided for by contract. Finally, the Commission argued that even if the court of appeals were correct that the payphone interests at issue are not investment contracts, they are securities because they are “notes,” “evidences of indebtedness,” or interests “commonly known as a security.” The rehearing petition was denied.

### Broker-Dealer Regulation

In *SEC v. Tuschner*,<sup>161</sup> the court of appeals reversed a district court decision that held that the owner of a broker-dealer violated the federal securities laws by allowing a former registered representative, who had been barred by the Commission from associating with any broker-dealer, to become an associated person of his firm. The former representative was located in Greece, opened accounts for Greek customers at the American firm, sold them securities for which the firm was an underwriter and market maker, and was compensated by the firm for the sales. The court of appeals held by a 2-1 vote that on the facts of the case the firm did not sufficiently control the former representative’s activities to make him an associated person within the meaning of the Exchange Act. By a 5-4 vote, the full court denied the Commission’s petition for rehearing, which argued that the former representative was controlled to the same extent as independent contractors who are recognized as associated persons of brokerage firms.

## Foreign Corrupt Practices Act

In *United States v. Kay*,<sup>162</sup> the Commission argued in a friend of the court brief that, contrary to the district court's decision, the antibribery provision of Exchange Act section 30A (part of the Foreign Corrupt Practices Act) (which prohibits publicly held companies from making payments to foreign officials "for purposes of" inducing them to misuse their office "in order to assist such [company] in obtaining or retaining business for or with, or directing business to, any person....") encompasses payments to reduce taxes and duties. In its brief, the Commission urged the court of appeals to hold that, read in context, the "in order to assist such issuer in obtaining or retaining business" language covers all cases in which a payor's objective is to *assist* an issuer's efforts to obtain or retain business with any person. Accordingly, prohibited bribes are not limited to those seeking official action that, *in itself, directly* results in an issuer's obtaining or retaining specific contracts or business arrangements but also include bribes seeking official action which, *in turn*, will *assist* an issuer in obtaining or retaining business. The Commission therefore urged that, as a matter of common understanding and basic economic principles, the prohibition broadly covers bribes made to induce official action favorable to an issuer's carrying on its business enterprise, such as tax reduction. The appeal is pending.

## Cease-and-Desist Authority

In *KPMG, LLP v. SEC*,<sup>163</sup> the court of appeals upheld a Commission cease-and-desist order against KPMG. The court held, in a manner consistent with the Commission's appellate argument, that:

- the Commission properly determined that, under the cease-and-desist provisions of the Exchange Act, negligence is sufficient to establish liability of any person, including a professional, who causes violations of the federal securities laws;

- the Commission can reasonably interpret its cease-and-desist authority as authorizing it to issue orders prohibiting violations of the provisions of law or regulations found to have been violated and not as restricting it to prohibiting only the specific types of violations of those provisions found;
- a cease-and-desist order that prohibits future independence-related violations of certain statutes and rules is not vague even though independence standards may be complex and reasonable professionals may differ as to the application of those standards to discrete sets of facts; and
- the Commission may proceed, in a cease-and-desist proceeding, on the basis of a lower risk of future violation than is required for an injunction.

#### Arbitrations Conducted by Self-Regulatory Organizations

In *Howsam v. Dean Witter Reynolds, Inc.*,<sup>164</sup> the Commission filed a friend of the court brief urging that arbitrators, rather than courts, should initially apply the National Association of Securities Dealer's (NASD) six-year eligibility requirement for arbitrations conducted under its Code of Arbitration Procedure. The case is pending.

In *NASD Dispute Resolution, Inc. v. Judicial Council of California*,<sup>165</sup> the Commission filed a friend of the court brief, which argued that California's recently adopted disclosure requirements for arbitrators, and companion rules providing for disqualification of arbitrators and vacation of an arbitral award if those requirements are not met, cannot be applied to securities arbitrations conducted by securities industry self-regulatory organizations. The Commission argued that, in light of the Commission's comprehensive oversight of the self-regulatory organizations (SROs) under the Exchange Act, only the Commission can decide what disclosure and disqualification

standards are appropriate for the protection of investors in SRO arbitration, and can ensure that those standards are part of an effective national system. Thus, the California requirements, as applied to SRO arbitration, are preempted by federal law. The Commission also argued that the California requirements are preempted by the Federal Arbitration Act. The case was decided on other grounds in an opinion that did not address issues briefed by the Commission.

#### Private Right of Action Under Contract-Voiding Provision of the Investment Company Act

In *Olmstead v. Pruco Life Insurance Co.*,<sup>166</sup> the Commission filed a friend of the court brief urging that excessive charges imposed on purchasers of variable annuities could be recovered by means of a private action under section 47(b) of the Investment Company Act of 1940 for rescission and restitution of the amount of the overcharge, and that it was therefore not necessary for the court of appeals to decide whether an implied right of action for damages was created by section 26(f) or section 27(i) of that Act. Because the plaintiffs had not raised this argument, the court of appeals decision did not address the applicability of section 47(b).

#### Private Right of Action under Section 11 of the Securities Act

In *Lee v. Ernst & Young, LLP*,<sup>167</sup> the court of appeals agreed with the Commission's friend of the court brief that standing to sue under section 11 of the Securities Act for misrepresentations in a registration statement is not limited to those who purchased in the offering, but extends to all who bought securities issued pursuant to the registration statement containing material misrepresentations. It thus became the third court of appeals to agree with the Commission's position, and to reject the argument that section 11 standing should be so limited to initial purchasers in light of the Supreme Court's decision in *Gustafson v. Alloyd Holdings, Inc.*<sup>168</sup> No court of appeals has accepted this interpretation of *Gustafson*.

## Litigation Under the Private Securities Litigation Reform Act

In *Florida State Board of Administration v. Green Tree Financial Corp.*,<sup>169</sup> the court of appeals agreed with the Commission's interpretation in a friend of the court brief of the state of mind pleading standard under the Private Securities Litigation Reform Act of 1995 (PSLRA). Consistent with the position it has urged in briefs in other circuits, the Commission argued that the pleading standard does not eliminate recklessness as a basis for liability and that, in interpreting the pleading standard, courts should rely upon the pre-PSLRA Second Circuit tests, under which a plaintiff may allege facts that constitute strong circumstantial evidence of conscious misbehavior or recklessness or facts that show that the defendant had both a motive and an opportunity to commit fraud.

The Commission addressed the PSLRA's lead plaintiff provisions in friend of the court briefs in two appeals in securities fraud class actions, *In re Cavanaugh*<sup>170</sup> and *State of Wisconsin Investment Board v. Ruttenberg*.<sup>171</sup> In *Cavanaugh*, the Commission argued that a lead plaintiff applicant's conduct in dealing with counsel, including a failure to make a meaningful effort to negotiate the counsel fee, could be a basis for a finding that the applicant would not adequately represent the class under Federal Rule of Civil Procedure 23, and thus would not qualify as the lead plaintiff under the PSLRA. The Commission also argued that in awarding class counsel fees at the conclusion of a case a district court could rely on the lead plaintiff's fee agreement with its counsel, but only if the court had carefully reviewed that plaintiff's selection and retention of counsel and had determined that the plaintiff had shown the active, effective involvement and oversight of a "model" PSLRA lead plaintiff. Finally, the Commission argued that the PSLRA does not preclude a district court from conducting an auction to select and set a fee schedule for class counsel when the lead plaintiff is unwilling or unable to perform the selection, retention, and monitoring functions envisioned by Congress.

In its decision in *Cavanaugh*, the court of appeals agreed in principle that a lead plaintiff applicant's dealings with counsel could be evidence that the applicant is not adequate under Rule 23, although two of the judges appeared to take a narrower view of the circumstances in which this might happen than did the Commission and the third judge on the panel. As to the other issues, the court acknowledged that the lead plaintiff's fee agreement might be used by the district court to set a cap on class counsel fees, and viewed a counsel auction as "not generally permissible in a [PSLRA] case, at least as a matter of first resort," but did not rule out the use of auctions in appropriate circumstances in PSLRA cases.

In *Ruttenberg*, the Commission argued that the PSLRA does not permit the appointment of competing lead plaintiff applicants as co-lead plaintiffs when one of the applicants satisfies all of the statute's lead plaintiff criteria. The Commission further argued that it is contrary to the PSLRA for a district court to override that applicant's selection of counsel and to set class counsel fees without regard to that applicant's fee agreement with its chosen counsel simply because: (1) the court had erroneously appointed co-lead plaintiffs, (2) the other co-lead plaintiffs selected other counsel and refused to negotiate fees, and (3) class counsel fees have not traditionally been set by reference to fee agreements. The appeal is pending.

### Motions to Vacate Permanent Injunctions

In *SEC v. Walsh*,<sup>172</sup> the district court commuted Walsh's permanent injunction to a temporary injunction to be served in full as of the filing of the motion seeking relief from the injunction. The district court found that Walsh had satisfied the standard for obtaining modification of an injunction. He noted that the evidence that Walsh had violated the securities laws was somewhat weak and that during settlement negotiations the parties did not anticipate that the permanent injunction would interfere with Walsh's ability to satisfy state registration requirements.

## Plans of Distribution of Disgorged Assets

In *SEC v. Credit Bancorp Ltd.*,<sup>173</sup> the court of appeals affirmed the *pro rata* distribution of assets seized from a ponzi scheme to its defrauded investors. The appellant had argued that it was entitled to the return of securities that it had transferred to the ponzi scheme because the securities were identifiable and purportedly held in trust. In rejecting this argument, the court noted that while the investor may have intended to enter into a trust arrangement, the documents it had executed caused an outright transfer of share ownership. The court then noted that all of the investors' assets were commingled, so the fact that one investor's assets might have been comparatively undisturbed was the "result of the merely fortuitous fact that the defrauders spent the money of the other victims first." In such situations, the court held, the law favors *pro rata* distributions.

## Appeals of Interlocutory Commission Orders

In *Abel v. SEC*,<sup>174</sup> the court of appeals denied the request for interlocutory review challenging a Commission order disqualifying an attorney from representing both the respondent and witnesses the Division of Enforcement was calling to testify against the respondent. The court held that it lacked jurisdiction over the appeal as appellants sought review of an interlocutory, non-final Commission order. The court also held the decision was not appealable under the collateral order exception to the rule against interlocutory appeals, noting that Abel could appeal the order following completion of the Commission proceedings against him. It also ruled that because the witnesses faced no liability in the Commission proceedings, they lacked standing to appeal to the court.

## Actions to Enforce NASD Restitution Orders

Pursuant to section 21(e)(1) of the Exchange Act, the Commission, working with the NASD, obtained district court orders requiring payments of fines and restitution imposed as NASD disciplinary sanctions. Respondents in two actions, *SEC*



*v. McCarthy and Blodgett*,<sup>175</sup> and *SEC v. Vittor*,<sup>176</sup> appealed and questioned the Commission's authority to apply to a district court for an order commanding compliance with a Commission order affirming NASD sanctions. The Commission responded that section 21(e)(1) specifically provides that the Commission can apply to district courts for orders commanding compliance with Commission orders. The appeals are pending.

### Equal Access to Justice Cases

In *Adams v. SEC*,<sup>177</sup> the court of appeals held that a respondent in a Commission administrative action had filed a timely claim for attorneys' fees under the Equal Access to Justice Act (EAJA) even though he did not file within 30 days of the Commission order dismissing the claims against him. The court explained that the 30-day period for filing the claim did not start until the Commission order was "not appealable." The Commission had contended the order was not appealable when it was issued because the respondent had obtained the relief he sought. The court rejected that argument and explained that when the "governing statute relevant to the underlying agency proceeding allows an appeal generally, the underlying order is considered 'appealable,'" regardless whether the specific order could be appealed.

### Application of the Work Product Doctrine to Work Product Shared with the Commission

The Commission filed friend of the court briefs in three private actions in state court and in a federal criminal action to explain that disclosure of attorney work product to the Commission pursuant to a confidentiality agreement does not waive work product protection. The Commission stated that the work product doctrine should not be waived because the Commission's ability to obtain work product pursuant to confidentiality agreements plays an important role in the Commission's enforcement of the securities laws. In all three state court actions, the courts held work product protection was not waived. The criminal action is pending.

## Requests for Access to Commission Records

The Commission received 96 subpoenas for documents and testimony. In certain of the cases, the Commission declined to produce the requested documents or testimony because the information sought was privileged.

The Commission received 3,570 requests under the Freedom of Information Act (FOIA) for access to agency records and 14,150 confidential treatment requests from persons who had submitted information to the Commission. There were 85 appeals to the Office of the General Counsel from initial denials from the FOIA officer. Several of these appeals resulted in district court litigation challenging the decisions.

In *American Legal Media, Inc. & Michael Ravnitzky v. SEC*,<sup>178</sup> the district court largely granted the Commission's motion for summary judgment on a FOIA complaint seeking disclosure of those portions of the *SEC Freedom of Information Training Manual* that the Commission had withheld. The district court ordered the SEC to disclose limited parts of the *Manual* to the extent they provide instruction on how particular FOIA exemptions apply to different types of SEC records. In all other respects, the court upheld the SEC's decision to withhold portions of the *Manual* under Exemption 2.

## Significant Adjudication Developments

During fiscal 2002, the Commission issued 28 opinions and 18 orders, and the staff resolved an additional 50 motions. Highlighted are some of the significant opinions and orders issued by the Commission during the year.

### Cease-and-Desist Proceedings

The Commission ordered Herbert Moskowitz to cease-and-desist from violations of the Commission's reporting requirements.<sup>179</sup> Under these requirements, the beneficial owner of more than 5

percent of any class of equity securities registered under the Exchange Act must report that beneficial ownership on a Schedule 13D. The owner must also report any material change in beneficial ownership.

The Commission concluded that Moskowitz had investment power over, and therefore beneficially owned, shares of Ferrofluidics Corporation held in the account of Kamrooz Abir, his son-in-law. Moskowitz made certain filings on Schedule 13D but failed to include Abir's shares in those filings and failed to report, as required, the disposition of those shares.

The Commission concluded that a cease-and-desist order was appropriate. The Commission recognized that the complained-of conduct occurred in 1991. While the Commission noted that part of this delay was attributable to a stay for related criminal proceedings, it recognized that this was not the sole cause of the delay and that the passage of time militated against issuing a cease-and-desist order. However, the Commission found that Moskowitz's repeated violations of the reporting requirements provided a compelling reason for imposing a cease-and-desist order. The Commission considered the lateness of both the incomplete Schedule 13D and the subsequent amendment that Moskowitz filed with respect to Ferrofluidics. The Commission also found that, after the period at issue, Moskowitz failed on various occasions to file timely and complete Schedules 13D with respect to his holdings in other public companies

The Commission rejected Moskowitz's argument that the proceeding was barred by the general five-year statute of limitations imposed by 28 U.S.C. §2462. Section 2462 imposes a five-year limitation on any proceeding for enforcement of a civil fine, penalty, or forfeiture. The Commission held that a cease-and-desist order is not subject to section 2462. A cease-and-desist order focuses on a respondent's future conduct and is prospective. The Commission concluded that this remedy does not resemble a penalty within the meaning of section 2462. The Commission further found that the Division of Enforcement had demonstrated Moskowitz's present risk to the public by (1) his

continued failures to file and his incomplete and untimely filings on Schedules 13D, (2) his continued promotion of public companies, and (3) his lack of appreciation of the importance of the reporting requirements.

### Summary Disposition in Broker-Dealer Proceeding

The Commission barred John Brownson<sup>180</sup> from association with a broker or dealer. Brownson was statutorily disqualified because he pleaded guilty to one count of conspiracy to commit securities fraud, mail fraud, and wire fraud. He was sentenced to five months imprisonment followed by three years supervised release, during which he is prohibited from engaging in the securities industry, and ordered to pay restitution. The indictment alleged that Brownson and others conspired with a stock promoter to recommend certain stocks to customers in return for payments from the promoter that were not disclosed to the customers.

The Division of Enforcement brought an administrative proceeding to bar Brownson. An administrative law judge granted summary disposition in favor of the Division, finding that there was no dispute as to any material fact. The law judge accepted as true Brownson's assertions that he was a minor player in the conspiracy and cooperated with the investigation. The law judge nonetheless concluded that there were no extraordinary circumstances that warranted a sanction other than a bar.

Upon Brownson's appeal, the Commission upheld the law judge's grant of the Division's motion. The Commission noted that summary disposition may be granted where there is no genuine issue of material fact and the party is entitled to summary disposition as a matter of law. The Commission held that summary disposition was particularly appropriate where, as here, the respondent had been convicted of securities fraud. Brownson failed to challenge any of the law judge's evidentiary findings. He also failed to state what evidence he would have presented at an oral hearing or explain how such evidence would establish factors that would counter a determination that it was in the public interest to bar him.

In imposing a bar, the Commission found Brownson engaged in serious misconduct over an extended period of time for personal gain. The Commission also weighed the fact that Brownson is prohibited from engaging in the securities business during his supervised release.

### Disqualification of Counsel

The Commission disqualified counsel for a respondent in a pending administrative proceeding.<sup>181</sup> The attorney represented two respondents, Rudolph Abel and Donald C. Berry, who had served successively as chief investment officers of an investment adviser. Berry and four other respondents settled or defaulted. The proceeding was continuing as to Abel. Abel's counsel sought also to represent Berry and four other prospective witnesses in the proceeding. The law judge denied the Division of Enforcement's motion to disqualify counsel, stating that she did not have the authority to disqualify counsel.

The Commission accepted interlocutory review of the law judge's ruling. The Commission stated that Rule of Practice 111(d) granted the law judge the power to regulate a proceeding and the conduct of the parties and counsel. The Commission concluded that the rule authorized disqualification of counsel if the conflict of interest was of sufficient magnitude to render the proceeding unjust.

The Commission concluded that the potential for conflict could not be addressed by the consent of the clients. An attorney before any tribunal must advocate his client's position forcefully in order to preserve the integrity of the proceeding. The Commission found that counsel's representation of Abel with respect to subjects that were substantially related to counsel's representation of the witness clients could result in divided loyalty that would prevent counsel from fulfilling his duty to act in good faith.

The Commission concluded that it did not need to wait until an actual conflict tainted the proceeding where the nature of the

multiple representation presented such a serious potential for conflict. The Commission stated that the right to counsel of one's choice is outweighed by the necessity of ensuring the propriety and integrity of its processes.

## **Legal Policy**

The General Counsel's responsibilities include providing legal and policy advice on SEC enforcement and regulatory initiatives before they are presented to the Commission for a vote. The General Counsel also advises the Commission on administrative law matters, and has substantial responsibility for carrying out the Commission's legislative program, including drafting testimony, developing the Commission's position on pending bills in Congress, and providing technical assistance to Congress on legislative matters.

Following enactment of the Sarbanes-Oxley Act, the General Counsel took the lead in coordinating the agency's implementation of this landmark legislation. The General Counsel also played a significant role in the Commission's efforts to respond to investor concerns in the wake of events at Enron and other public companies. This included advising the Commission on its order requiring the 947 largest public companies to certify the accuracy and completeness of their filings and on the Commission's immediate regulatory actions to minimize any potential disruptions to the capital markets that may have occurred due to the indictment and subsequent conviction of Arthur Andersen LLP.

On the regulatory front, the General Counsel was significantly involved in the development of the Commission's proposed Public Accountability Board, which would have ended the self-regulation of the accounting profession by creating an independent overseer for the accounting profession with mandatory funding. The office also assisted in the development of several rulemakings to implement the Commission's disclosure initiatives and begin implementation of the Sarbanes-Oxley Act.

## Significant Legislative Developments

In fiscal 2002, Congress passed the USA PATRIOT Act and the Sarbanes-Oxley Act. The USA PATRIOT Act was enacted in response to the terrorist attacks of September 11, 2001 and included electronic surveillance and money laundering provisions of relevance to the Commission's work. The Act specifically directed the Commission to engage jointly in or to be consulted by the U.S. Department of the Treasury on several rulemakings and studies relating to the anti-money laundering efforts of entities regulated by the SEC. The Sarbanes-Oxley Act, among other things, created a new oversight board for the accounting profession, mandated new measures intended to promote auditor independence, added new disclosure requirements for public companies, and strengthened the criminal penalties for securities fraud. The Act contains numerous directives to the Commission to promulgate rules and complete studies. Several other bills that would affect the work of the SEC received significant attention during the year, including accounting, bankruptcy, derivatives, energy, and other measures.

### Commission Congressional Testimony

The Commission testified at congressional hearings on the following matters during fiscal 2002:

- events relating to Enron Corp.;
- financial aspects of the war on terrorism and implementation of the USA PATRIOT Act;
- financial literacy;
- the adequacy of current financial accounting standards and roles of the SEC and the Financial Accounting Standards Board in setting generally accepted accounting principles;

- proposals to repeal the Public Utility Holding Company Act of 1935 (PUHCA), and the relationship of PUHCA to the Enron bankruptcy and the energy crisis in California;
- legislative proposals to respond to crises at Enron and other public companies;
- appropriations for the SEC in fiscal 2003 and resource and staffing issues facing the agency;
- telecommunications accounting issues;
- the role of credit rating agencies in the U.S. securities markets;
- pending proposals by the European Commission;
- issues raised by the Frank Gruttadauria matter; and
- legislative proposals to require the SEC to prepare audited financial statements.

## **Corporate Reorganizations**

The Commission, as a statutory adviser in cases under Chapter 11 of the Bankruptcy Code, seeks to assure that the interests of public investors in companies undergoing bankruptcy reorganization are protected. During the past year, the Commission entered a formal appearance in 32 Chapter 11 cases with significant public investor interest. The Commission also monitored 120 new cases involving large public companies and brokerage firm liquidation proceedings under the Securities Investor Protection Act of 1970.

The Commission formally supported a motion for the appointment of an official committee to represent shareholders in



one case. Official committees negotiate with debtors on the formulation of reorganization plans and participate in all aspects of a Chapter 11 case. The Bankruptcy Code provides for the appointment of official committees for stockholders where necessary to assure adequate representation of their interests.

A Chapter 11 disclosure statement is a combination proxy and offering statement used to solicit acceptances for a reorganization plan. The bankruptcy staff commented on 182 of the 268 disclosure statements it reviewed during 2002. Recurring problems with disclosure statements included inadequate financial information, lack of disclosure on the issuance of unregistered securities and insider transactions, and plan provisions that contravene the Bankruptcy Code. Most of the staff's comments to debtors or plan proponents were adopted; formal Commission objections were filed in 8 cases.

The Commission was successful in persuading companies to eliminate provisions in 48 plans that improperly attempted to release officers, directors, and other related persons from liability. This is a significant issue for investors because in many cases debtors improperly seek to use the bankruptcy discharge to protect officers and directors from personal liability for various kinds of claims, including liability under the federal securities laws. In 12 cases, the Commission successfully blocked plan provisions that would have resulted in shell companies that could have been used for stock manipulation purposes. Also in 12 cases, the Commission prevented improper use of the Bankruptcy Code exemption from Securities Act registration.

# Economic Research and Analysis

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*The Office of Economic Analysis is the primary adviser to the Commission on the economics of securities markets and the economic impact of Commission actions. The economic analysis program provides technical and analytical support necessary to understand and evaluate the economic effects of Commission regulatory policy, including the costs and benefits of rulemaking initiatives. The staff also reviews all rule proposals to assess their potential impacts on small businesses, competition within the securities industry and across markets, and efficiency, competition, and capital formation.*

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## What We Did

- Prepared various reports on market developments surrounding the September 11 terrorist attack, including the effects of issuer buybacks and short-selling activity.
- Monitored the economic effects of policy initiatives, such as decimalization, the execution quality disclosure rule, and bond market transparency via the Trade Reporting and Compliance Engine.
- Provided economic advice and guidance for various rule proposals required by the Sarbanes-Oxley Act of 2002. Also provided various reports and analyses of recent market developments including: accelerated disclosure of 10-K and 10-Q filings, accelerated disclosure of insider trades, proposed corporate governance reforms, auditor independence, the growth

of exchange-traded funds (ETFs) and intensified competition in the market for trading listed options.

- Developed statistical methods for forecasting securities registrations and transactions to set fee rates in accordance with the Investor and Capital Markets Fee Relief Act of 2002.
- Provided advice and technical assistance in a variety of compliance inspections and enforcement actions, applied financial economics and statistical techniques to examine evidence, and estimated the amount of disgorgement to be sought in insider trading cases.

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## **Economic Analysis and Technical Assistance**

The economic analysis staff provided substantial quantitative economic evidence on 67 regulatory and market initiatives impacting the securities industry and markets.

### **Market Structure and Trading Practices**

- Provided economic advice and support for the Commission's exploration of market structure principles and issues, particularly for the October 2002 market structure hearings.
- Monitored the implementation of decimal pricing on Nasdaq and exchanges and reviewed decimalization studies submitted by the self-regulatory organizations (SROs). Prepared studies of decimalization's effects on penny jumping, transparency, inter-exchange competition, and short selling.

- Monitored the implementation of the execution quality disclosures and analyzed the disclosures for various market centers. Sought feedback from the industry and academia, and responded to their analyses.
- Provided economic advice and empirical analysis on the effects of policies and rules governing market operations, trading structures, and SRO initiatives, including: SuperMontage, exchange registration, primary market maker standards, and linkages in the equity and options markets.
- Analyzed the impact of requests for relief from short sale rules.
- Provided economic analysis and technical advice on issues pertaining to electronic communications networks such as access fees, quote display, and the impact of Regulation ATS obligations.
- Assessed the likely effects of single stock futures trading rules and evaluated proposed customer margin requirements.

#### Disclosure and Accounting Standards

- Monitored the economic effects of Regulation FD and evaluated related surveys and empirical studies.
- Continued to provide advice and technical assistance to the Division of Corporation Finance in conjunction with a Division study of compliance with the new audit committee requirements.
- Provided economic advice and technical assistance to the Division of Corporation Finance on the

acceleration of reporting deadlines for Forms 10-K and 10-Q.

- Provided economic advice and technical assistance on issues pertaining to road show communications, faster insider trading reporting, EDGAR foreign filings, and critical accounting policies.

## Mutual Funds

- Analyzed the costs and benefits of rule changes impacting mutual funds and investment advisers. In particular, provided support for rules governing investment company mergers, Internet investment advisers, the custody of investment company securities, proxy voting of investment advisers, and the disclosure of proxy policies.
- Provided support to the Division of Investment Management regarding changes to the frequency of disclosure requirements.
- Prepared reports on issues relating to the economic effects of ETFs and the evaluation of applications for new types of ETFs. For example, the staff provided assistance in the evaluation of ETFs based on bonds, and provided assistance in the evaluation of actively-managed ETFs.
- Provided support to the Division of Investment Management on the economic implications of exemptive relief applications.

## International and Cross-Border Issues

- Helped determine the agenda for the International Organization of Securities Commissions' Standing Committee 3 and papers for the Technical Committee

that provide guidance and establish principles to be followed by both securities regulators and financial intermediaries worldwide.

- Participated in the new Joint Forum (JF) Working Group on enhanced disclosure by securities firms, banks, insurance companies and hedge funds. Provided input on the JF Working Group's mandate and work plan and contributed to its deliberations and discussions with industry representatives from both the suppliers and users of financial information.

## **Inspections and Examinations**

Our economic analysis staff provided advice and technical assistance to the SEC's Office of Compliance Inspections and Examinations in reviewing the first phase of the new Consolidated Options Audit Trail, as well as broker-dealer and exchange order execution practices in the equity and option markets.

## **Enforcement Issues**

Our economic analysis staff provided assistance in approximately 96 investigations and other enforcement actions involving insider trading, fraudulent fund trade allocation, market manipulation, deceptive financial reporting, and other violations of securities laws. The staff applied financial economics and statistical techniques to determine whether the elements of fraud were present and to estimate the amount of disgorgement to be sought. The economics staff also assisted in evaluating the testimony of experts hired by other parties.

# Policy Management & Administrative Support

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*The policy management and administrative support staff provide the Commission and operating divisions with the necessary services to accomplish the agency's mission. Their responsibilities and activities include developing and executing management policies, formulating and communicating program policy, overseeing the allocation and expenditure of agency funds, maintaining liaison with Congress, disseminating information to the press, and facilitating Commission meetings. Administrative support services include information technology, financial, space and facilities, and human resources management.*

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## What We Did

- Held 83 Commission meetings, during which 907 matters were considered.
- Acted on 331 staff recommendations by seriatim vote.
- Implemented provisions of the Investor and Capital Markets Fee Relief Act, including reducing certain fee rates under the Securities Act of 1933 (Securities Act) and the Securities Exchange Act of 1934 (Exchange Act) and establishing a pay parity system to improve employee retention.
- Negotiated a collective bargaining agreement with the National Treasury Employees Union (NTEU).

- Enhanced the Commission’s website and Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system to allow for extended filing hours, electronic filings by foreign securities issuers, real-time access, and improved search capabilities.
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## **Policy Management**

### Commission Activities

During the 83 Commission meetings held in 2002, the Commission considered 907 matters, including the proposal and adoption of Commission rules, enforcement actions, and other items that affect the nation’s capital markets and the economy. The Commission also acted on 331 staff recommendations by seriatim vote.

## **Administrative Support**

### Financial Management

The SEC deposited \$1.013 billion in fees in the U.S. Treasury, of which \$109.5 million was used to directly fund the agency in 2002. Of the \$1.013 billion in total fees collected, 32 percent was from securities registrations; 67 percent was from securities transactions; and 1 percent was from tender offer, merger, and other filings.

The fee rate for securities registrations was established in the Securities Act of 1933 at 1/50 of 1 percent. Between 1990 and 1996, Congress annually increased this fee rate to partially offset the costs of funding the agency. In October 1996, Congress enacted Title IV of the National Securities Market Improvement



Act (NSMIA), reducing the fee rate for fiscal 1997 to 1/33 of 1 percent and providing future annual reductions in the fee rate. The transaction fee rate on exchange-listed securities was established in the Exchange Act at 1/300 of 1 percent of the total dollar value of all trades. To equalize the costs of trading across markets, NSMIA extended these transaction fees to the over-the-counter market at the same rate of 1/300 of 1 percent. On January 16, 2002, the President signed the Investor and Capital Markets Fee Relief Act (Fee Relief Act). The Fee Relief Act reduced the fee rates applicable under section 6(b) of the Securities Act for all of fiscal 2002 and sections 13(e), 14(g), 31(b) and 31(c) of the Exchange Act for the rest of fiscal 2002. The Fee Relief Act also amended these sections to require the Commission to make annual adjustments to the fee rates applicable under these sections for fiscal years 2003 through 2011, and one final adjustment to fix the fee rates under these sections for fiscal 2012 and beyond.

## Human Resources Management

During the year, the SEC:

- Successfully implemented the new pay parity system and converted the agency's payroll operations on May 19, 2002.
- Established a new Executive Program and Compensation System for members of the agency's Senior Officers Program.
- Negotiated a collective bargaining agreement with the NTEU, which covers all bargaining unit members of the SEC.
- Established a comprehensive Work/Life Plus Program for all SEC employees, including a referral service, brochure, and intranet site.

- Established an agency-wide Reasonable Accommodation Program, working with the Offices of Information Technology and Equal Employment Opportunity.
- Implemented a Mentor Program for the Summer Honors Program.

## EDGAR

The SEC enhanced the EDGAR system to allow for Commission-mandated electronic filing by foreign securities issuers. The most significant changes made to the system were the introduction of new form type changes and the updating of the country codes. The enhancements also permit the EDGAR system to support an earlier morning opening to provide for the business work times of our foreign securities issuers.

EDGAR continued to receive recognition for its innovative information technology. *Computerworld* awarded EDGAR its Honors Laureate for Innovations in Technology Achievement Award. *Post Newsweek* awarded EDGAR its Excellence in Government Award for Innovative IT Accomplishments. EDGAR also received the Enterprise Value Award from *CIO Magazine* for 2003 for its modernization efforts.

[www.sec.gov](http://www.sec.gov)

The Commission upgraded its website to provide the public and SEC staff with real-time access to the EDGAR filings database of historical and recently filed information. Thus, the agency eliminated the 24-hour delay the public and staff previously had experienced. The Commission also implemented new or enhanced search capabilities, allowing individuals to search the EDGAR database by company name, CIK number, or SIC number via the website.

## Information Technology Security

The SEC initiated a certification and accreditation program for reviewing the security of agency systems. The agency also adopted a policy governing agency practices with respect to certifying and accrediting SEC systems.

## Shared Access to Examination Reports

Working in collaboration with the self-regulatory organizations, the agency established a secure facility for accessing examination and inspection reports from other oversight bodies. The secure data exchange facility dramatically reduced the length of time spent identifying, requesting, and transferring information between parties.

## Space and Facilities Management

During the year, the SEC:

- Reestablished the Commission's Northeast Regional Office in the Woolworth Building. The office had been located at 7 World Trade Center, which was destroyed on September 11, 2001.
- Oversaw and coordinated the moves of the Chicago, Denver, and Miami offices to new space and installed new telephone systems in each.
- Successfully managed mail operations during the anthrax crisis.

## Endnotes

<sup>1</sup>*SEC v. Dynegy Inc.*, Release No. AAER-1632 (Sept. 25, 2002).

<sup>2</sup>*SEC v. L. Dennis Kozlowski, et al.*, Release No. AAER-1627 (Sept. 12, 2002).

<sup>3</sup>*SEC v. Michael J. Kopper*, Release No. AAER-1617 (Aug. 21, 2002).

<sup>4</sup>*SEC v. Adelfia Communications Corporation, et al.*, Release No. AAER-1599 (July 24, 2002).

<sup>5</sup>*SEC v. WorldCom, Inc.*, Release No. AAER-1585 (June 26, 2002).

<sup>6</sup>*SEC v. Frank M. Bergonzi, et al.*, Release No. AAER-1581 (June 21, 2002).

<sup>7</sup>*In the Matter of Rite Aid Corporation*, Release No. AAER-1579 (June 21, 2002); *In the Matter of Timothy J. Noonan*, Release No. AAER-1580 (June 21, 2002).

<sup>8</sup>*In the Matter of Microsoft Corporation*, Release No. AAER-1563 (June 3, 2002).

<sup>9</sup>*SEC v. Xerox Corporation*, Release No. AAER-1542 (Apr. 11, 2002).

<sup>10</sup>*SEC v. Alan K. Anderson*, Release No. AAER-1560 (May 20, 2002).

<sup>11</sup>*In the Matter of ACLN Limited*, Release No. 34-45579 (Mar. 18, 2002).

<sup>12</sup>*SEC v. Kenneth E. Kurtzman, et al.; In the Matter of Ashford.com, Inc., et al.*, Release No. AAER-1574 (June 10, 2002).

<sup>13</sup>*In the Matter of Kimberly-Clark Corporation, et al.*, Release No. AAER-1533 (Mar. 27, 2002).

<sup>14</sup>*SEC v. Dean L. Buntrock, et al.*, Release No. AAER-1532 (Mar. 26, 2002).

<sup>15</sup>*SEC v. Roys Poyiadjis, et al.*, Release No. AAER-1465 (Oct. 4, 2001).

<sup>16</sup>*PricewaterhouseCoopers LLP, et al.*, Release No. AAER-1596 (July 17, 2002).

<sup>17</sup>*In the Matter of Avon Products, Inc.*, Release No. AAER-1595 (July 17, 2002); *In the Matter of Pinnacle Holdings, Inc.*, Release No. AAER-1476 (Dec. 6, 2001).

- <sup>18</sup>*In the Matter of KPMG, LLP*, Release No. AAER-1491 (Jan. 14, 2002).
- <sup>19</sup>*In the Matter of Moret Ernst & Young Accountants*, Release No. AAER-1584 (June 27, 2002).
- <sup>20</sup>*In the Matter of Ernst & Young LLP*, Release No. 34-45964 (May 20, 2002).
- <sup>21</sup>*SEC v. Douglas A. Murphy, et al.*, Release No. LR-17651 (Aug. 1, 2002).
- <sup>22</sup>*In the Matter of BellSouth Corporation*, Release No. AAER-1494 (Jan. 15, 2002); *SEC v. BellSouth Corporation*, Release No. LR-17310 (Jan. 15, 2002).
- <sup>23</sup>*SEC v. Credit Suisse First Boston Corporation*, Release No. LR-17327 (Jan. 22, 2002).
- <sup>24</sup>*SEC v. Frank D. Gruttadauria, et al.*, Release No. LR-17418 (Feb. 27, 2002).
- <sup>25</sup>*In the Matter of iCapital Markets LLC*, Release No. 34-45328 (Jan. 24, 2002).
- <sup>26</sup>*SEC v. Samuel D. Waksal*, Release No. LR-17559 (June 12, 2002).
- <sup>27</sup>*SEC v. Hugo Salvador Villa Manzo, et al.*, Release No. LR-17395 (Mar. 6, 2002).
- <sup>28</sup>*SEC v. A.C.L.N., Ltd; Abderrazak "Aldo" Labiad; Joseph J.H. Bisschops; Alex de Ridder; Pearlrose Holdings International S.A.; Emerald Sea Marine, Inc.; Scott Investments S.A.; BDO International (Cyprus); Minas Ioannou; and Christakis Iannou (Defendants); and Scandinavian Car Carriers A/S; Pandora Shipping, S.A.; Sergui, Ltd; Westbound Development Corp.; Maverick Commercial, Inc.; and DCC Limited (Relief Defendants)*, Litigation Release No. 17776 (Oct. 8, 2002).
- <sup>29</sup>*SEC v. Millennium Financial, Ltd., and Newpont Fiduciaries & Nominees, S.A.*, Litigation Release No. 17528 (May 22, 2002).
- <sup>30</sup>*SEC v. Roys Poyiadjis, Lycourgos Kyprianou and AremisSoft Corp.*, Litigation Release No. 17172 (Oct. 4, 2001).
- <sup>31</sup>*SEC v. Lernout & Hauspie Speech Products, N.V.*, Litigation Release No. 17782 (Oct. 10, 2002).
- <sup>32</sup>Release No. 34-46001 (May 30, 2002), 67 FR 38687 (June 5, 2002).

- <sup>33</sup>Release No. 34-46002 (May 30, 2002), 67 FR 38610 (June 5, 2002).
- <sup>34</sup>Release No. 34-47013 (Dec. 17, 2002).
- <sup>35</sup>Release No. 34-46428 (Aug. 28, 2002), 67 FR 56607 (Sept. 4, 2002).
- <sup>36</sup>Release No. 34-43863 (Jan. 19, 2001), 66 FR 8020 (Jan. 26, 2001).
- <sup>37</sup>Release No. 34-46249 (July 24, 2002), 67 FR 49822 (July 31, 2002).
- <sup>38</sup>17 CFR 242.300 *et seq.*
- <sup>39</sup>*See* Release No. 34-43873 (Jan. 23, 2001), 66 FR 8131 (Jan. 29, 2001); 34-44039 (Mar. 5, 2001), 66 FR 14234 (March 9, 2001); 34-45229 (Jan. 3, 2002), 67 FR 1255 (Jan. 9, 2002); 34-46144 (June 28, 2002) 67 FR 44907 (July 5, 2002); and 34-46145 (June 28, 2002), 67 FR 44911 (July 5, 2002).
- <sup>40</sup>Release No. 34-43590 (Nov. 17, 2000), 65 FR 75414 (Dec. 1, 2000).
- <sup>41</sup>*See* Release No. 34-43268 (Sept. 11, 2000), Administrative Proceedings File No. 3-10282 (Order Instituting Public Administrative Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions) (Settlement Order).
- <sup>42</sup>Release No. 34-45956 (May 17, 2002), 67 FR 36740 (May 24, 2002).
- <sup>43</sup>Release No. 34-46292 (Aug. 1, 2002), 67 FR 53146 (Aug. 14, 2002).
- <sup>44</sup>Release No. 34-46473 (Sept. 9, 2002), 67 FR 58284 (Sept. 13, 2002).
- <sup>45</sup>Release No. 34-46169 (July 8, 2002), 67 FR 46104 (July 12, 2002).
- <sup>46</sup>Release No. 34-46471 (Sept. 6, 2002), 67 FR 58302 (Sept. 13, 2002).
- <sup>47</sup>Release No. 33-8107, 34-46101 (June 21, 2002), 67 FR 43234 (June 27, 2002).
- <sup>48</sup>Release No. 34-46471 (Sept. 6, 2002) 67 FR 58302 (Sept. 13, 2002).
- <sup>49</sup>Release No. 34-46015 (May 31, 2002). 67 FR 39752 (June 10, 2002).

- <sup>50</sup>Letter regarding Interim Relief Related to the Trading of Foreign Security Futures (Aug. 20, 2002).
- <sup>51</sup>Release No. 34-46473 (Sept. 9, 2002), 67 FR 58284 (Sept. 13, 2002).
- <sup>52</sup>Release No. 34-46492 (Sept. 12, 2002), 67 FR 59748 (Sept. 23, 2002).
- <sup>53</sup>Release No. 34-45194 (Dec. 27, 2001), 67 FR 6 (Jan. 2, 2002).
- <sup>54</sup>Release No. 34-44291 (May 11, 2001), 66 FR 27760 (May 18, 2001).
- <sup>55</sup>Release No. 34-45897 (May 8, 2002).
- <sup>56</sup>Release No. 34-46069 (June 12, 2002), 67 FR 41545 (June 18, 2002).
- <sup>57</sup>Letter regarding Minimum Net Capital Requirements for Dealers (Apr. 15, 2002).
- <sup>58</sup>Release No. 34-44992 (Oct. 26, 2001), 66 FR 55818 (Nov. 2, 2001).
- <sup>59</sup>Release No. 34-45170 (Dec. 20, 2001).
- <sup>60</sup>Release No. 34-46019 (June 3, 2002), 67 FR 39642 (June 10, 2002).
- <sup>61</sup>Release No. 34-45261 (Jan. 9, 2002), 67 FR 2258 (Jan. 16, 2002).
- <sup>62</sup>Release No. 34-45239 (Jan. 4, 2002), 67FR 1790 (Jan. 14, 2002).
- <sup>63</sup>Release No. 34-46221 (July 17, 2002), 67 FR 48237 (July 23, 2002).
- <sup>64</sup>Release No. 34-45798 (Apr. 22, 2002), 67 FR 20854 (Apr. 26, 2002).
- <sup>65</sup>Release No. 34-46192 (July 12, 2002), 67 FR 48306 (July 23, 2002).
- <sup>66</sup>Letter regarding Acqua Wellington North American Equities Fund, Ltd. (July 22, 2001, pub. avail. Oct. 11, 2001).
- <sup>67</sup>Letter regarding Total Benefit Communications, Inc. (pub. avail. Nov. 6, 2001).
- <sup>68</sup>Letter regarding Swiss American Securities, Inc. (pub. avail. May 28, 2002).
- <sup>69</sup>Letter regarding Headway Corporate Staff Administration (pub. avail. Aug. 14, 2002).

- <sup>70</sup>Letter regarding Herbruck Alder & Co. (pub. avail. May 3, 2002).
- <sup>71</sup>Letter regarding Century Business Services, Inc. (pub. avail. Mar. 1, 2002).
- <sup>72</sup>Release No. IC-25722 (Aug. 28, 2002), 67 FR 57276 (Sept. 9, 2002).
- <sup>73</sup>Release No. IC-25723 (Aug. 30, 2002), 67 FR 57298 (Sept. 9, 2002).
- <sup>74</sup>Release No. IC-25657 (July 12, 2002), 67 FR 48318 (July 23, 2002).
- <sup>75</sup>Release No. IC-25739 (Sept. 20, 2002), 67 FR 60828 (Sept. 26, 2002).
- <sup>76</sup>Release No. IC-23066 (Mar. 13, 1998), 63 FR 13988 (Mar. 23, 1998); Release No. IC-25522 (Apr. 12, 2002), 67 FR 19848 (Apr. 23, 2002).
- <sup>77</sup>Release No. IC-25259 (Nov. 8, 2001), 66 FR 57602 (Nov. 15, 2001); Release No. IC-25666 (July 18, 2002), 67 FR 48512 (July 24, 2002).
- <sup>78</sup>Release No. IC-25575 (May 17, 2002), 67 FR 36712 (May 24, 2002).
- <sup>79</sup>Release No. IC-25557 (Apr. 30, 2002), 67 FR 31081 (May 8, 2002).
- <sup>80</sup>Release No. IC-24775 (Nov. 29, 2000), 65 FR 76189 (Dec. 6, 2000); Release No. IC-25560 (Apr. 30, 2002), 67 FR 31076 (May 8, 2002).
- <sup>81</sup>Release No. IC-25266 (Nov. 15, 2001), 66 FR 58412 (Nov. 21, 2001).
- <sup>82</sup>Release No. IC-25258 (Nov. 8, 2001), 66 FR 57614 (Nov. 15, 2001).
- <sup>83</sup>Barclays Global Fund Advisors, *et al.*, Release Nos. IC-25594 (May 29, 2002) (notice) and IC-25622 (June 25, 2002) (order); ETF Advisors Trust, *et al.*, Release Nos. IC-25725 (Sept. 3, 2002) (notice) and IC-25759 (Sept. 27, 2002) (order).
- <sup>84</sup>iShares, Inc., *et al.*, Release Nos. IC-25595 (May 29, 2002) (notice) and IC-25623 (June 25, 2002) (order).
- <sup>85</sup>The Mexico Fund, Inc., Release Nos. IC- 25729 (Sept. 13, 2002) (notice) and IC-25764 (Oct. 7, 2002) (order).



- <sup>86</sup>American Century Companies, *et al.*, Release Nos. IC-25449 (Mar. 1, 2002) (notice) and IC-25501 (Mar. 27, 2002) (order).
- <sup>87</sup>The Mexico Fund, Inc., Release No. IC-25729 (Sept. 13, 2002) (Commission Statement).
- <sup>88</sup>Price Communications Corporation, *et al.*, Release Nos. IC-25533 (Apr. 23, 2002) (notice) and IC-25579 (May 22, 2002) (order).
- <sup>89</sup>Blue Cross and Blue Shield of Kansas, Inc., Release Nos. IC-25316 (Dec. 11, 2001) (notice) and IC-25358 (Jan. 8, 2002) (order).
- <sup>90</sup>Release Nos. IC-25463 and IA-2017 (Mar. 18, 2002).
- <sup>91</sup>Ballard Spahr Andrews & Ingersoll, LLP (pub. avail. Apr. 3, 2002).
- <sup>92</sup>ReFlow Fund, LLC (pub. avail. July 15, 2002).
- <sup>93</sup>Manufacturers Adviser Corp. (pub. avail. Sept. 10, 2002).
- <sup>94</sup>PIMCO Funds (pub. avail. July 9, 2002).
- <sup>95</sup>ING Bank, N.V. (pub. avail. July 8, 2002).
- <sup>96</sup>Merrill Lynch Investment Managers (pub. avail. May 10, 2002).
- <sup>97</sup>Mutual Fund Directors Forum (pub. avail. May 9, 2002).
- <sup>98</sup>Evergreen Investment Management Company, LLC (pub. avail. Feb. 13, 2002).
- <sup>99</sup>Federated Core Trust II, L.P. (pub. avail. Feb. 6, 2002).
- <sup>100</sup>The Mexico Equity and Income Fund (pub. avail. Nov. 15, 2001).
- <sup>101</sup>Government Securities Clearing Corporation (pub. avail. Oct. 19, 2001).
- <sup>102</sup>Investment Company Institute (pub. avail. Feb. 12, 2002).
- <sup>103</sup>Frequently Asked Questions about Rule 35d-1 (Investment Company Names) (Dec. 4, 2001), at <http://www.sec.gov/divisions/investment/guidance/rule35d-1faq.htm>.
- <sup>104</sup>Release No. IC-24832 (Jan. 18, 2001), 66 FR 9002 (Feb. 5, 2001).
- <sup>105</sup>Frequently Asked Questions about Mutual Fund After-Tax Return Requirements (Jan. 14, 2002), at <http://www.sec.gov/divisions/investment/guidance/mutualqa.htm>.
- <sup>106</sup>Release No. IC-25243 (Oct. 25, 2001).

<sup>107</sup>Release No. IA-2059 (Sept. 20, 2002), 67 FR 60841 (Sept. 26, 2002).

<sup>108</sup>Release No. IA-2044 (July 18, 2002), 67 FR 48579 (July 25, 2002).

<sup>109</sup>Release No. IA-2028 (Apr. 12, 2002), 67 FR 19500 (Apr. 19, 2002).

<sup>110</sup>Seligman New Technologies Fund II, Inc. (pub. avail. Feb. 7, 2002).

<sup>111</sup>Thomson Financial Inc. (pub. avail. July 10, 2002).

<sup>112</sup>National Football League Players Association (pub. avail. Jan. 25, 2002).

<sup>113</sup>Release No. 35-27502 (Mar. 18, 2002).

<sup>114</sup>Release No. 35-27533 (May 30, 2002).

<sup>115</sup>Release No. 35-27539 (June 14, 2002).

<sup>116</sup>Release No. 35-27548 (July 5, 2002).

<sup>117</sup>Release No. 33-8124 (Aug. 28, 2002), 67 FR 57276 (Sept. 9, 2002).

<sup>118</sup>Release No. 34-46079 (June 14, 2002), 67 FR 41877 (June 20, 2002).

<sup>119</sup>Release No. 33-8128 (Sept. 5, 2002), 67 FR 58480 (Sept. 16, 2002); and Release No. 33-8089 (Apr. 12, 2002), 67 FR 19896 (Apr. 23, 2002).

<sup>120</sup>Release No. 34-46421 (Aug. 27, 2002), 67 FR 56462 (Sept. 3, 2002).

<sup>121</sup>Release No. 33-8099 (May 14, 2002), 67 FR 36678 (May 24, 2002).

<sup>122</sup>Release No. 33-8048 (Dec. 21, 2001), 67 FR 232 (Jan. 2, 2002).

<sup>123</sup>Release No. 33-8070 (Mar. 18, 2002), 67 FR 13518 (Mar. 22, 2002).

<sup>124</sup>Release No. 33-8106 (June 17, 2002), 67 FR 42914 (June 25, 2002).

<sup>125</sup>Release No. 33-8098 (May 10, 2002), 67 FR 35620 (May 20, 2002).

<sup>126</sup>Financial Reporting Release No. 59 (Dec. 4, 2001), 66 FR 63731 (Dec. 10, 2001).

<sup>127</sup>Release No. 33-8145 (Nov. 5, 2002), 67 FR 68790 (Nov. 13, 2002).

<sup>128</sup>Financial Reporting Release No. 60 (Dec. 12, 2001), 66 FR 65013 (Dec. 17, 2001).

<sup>129</sup>Release No. 33-8098 (May 10, 2002), 67 FR 35620 (May 20, 2002).

<sup>130</sup>Financial Reporting Release No. 61 (Jan. 22, 2002), 67 FR 3746 (Jan. 25, 2002).

<sup>131</sup>Release No. 33-8070 (Mar. 18, 2002), 67 FR 13517 (Mar. 22, 2002).

<sup>132</sup>Release No. 33-8109 (June 26, 2002), 67 FR 44963 (July 5, 2002).

<sup>133</sup>Oral testimony by Harvey L. Pitt, Chairman, U.S. Securities and Exchange Commission, before the Senate Committee on Banking, Housing, and Urban Affairs, March 21, 2002.

<sup>134</sup>Exposure Draft of Proposed Interpretation, *Consolidation of Certain Special Purpose Entities* (July 2002).

<sup>135</sup>Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (Oct. 1995).

<sup>136</sup>Exposure Draft of Proposed Statement of Financial Accounting Standards, *Accounting for Stock-Based Compensation--Transition and Disclosure* (Oct. 4, 2002).

<sup>137</sup>EITF Issue No. 00-21, *Accounting for Revenue Arrangements with Multiple Deliverables*.

<sup>138</sup>Statement of Financial Accounting Standards No. 146, *Accounting for Exit or Disposal Activities* (June 2002).

<sup>139</sup>FASB Concepts Statement No. 6, *Elements of Financial Statements* (Dec. 1985).

<sup>140</sup>Statement of Financial Accounting Standards No. 147, *Acquisitions of Certain Financial Institutions--An Amendment of FASB Statements No. 72 and 144 and FASB Interpretation No. 9* (Oct. 2002).

<sup>141</sup>Exposure Draft of Proposed Statement of Position, *Accounting for Certain Costs and Activities Related to Property, Plant, and Equipment* (June 29, 2001).

<sup>142</sup>The Panel on Audit Effectiveness, *Report and Recommendations* (Aug. 31, 2000).

<sup>143</sup>Statement on Auditing Standards No. 96, *Audit Documentation* (Jan. 2002).

<sup>144</sup>Statement on Auditing Standards No. 95, *Generally Accepted Auditing Standards* (Dec. 2001).

<sup>145</sup>Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit* (Sept. 2002).

<sup>146</sup>Interpretation of SAS No. 58 (AU Section 508), *Reporting as Successor Auditor When Prior-Period Audited Financial Statements were Audited by a Predecessor Auditor that Ceased Operations*.

<sup>147</sup>Statement on Auditing Standards No. 97, *Reports on the Application of Accounting Principles* (July 2002).

<sup>148</sup>Release No. 33-7801 (Feb. 16, 2000) 65 FR 889 (Feb. 23, 2000).

<sup>149</sup>22 S. Ct. 1899 (2002).

<sup>150</sup>238 F.3d 559 (4<sup>th</sup> Cir. 2001).

<sup>151</sup>274 F.3d 525 (D.C. Cir. 2002).

<sup>152</sup>No. 01-1749, \_\_\_ S. Ct. \_\_\_ (Oct. 7, 2002).

<sup>153</sup>278 F.3d 656 (7<sup>th</sup> Cir. 2002).

<sup>154</sup>No. 01-1490-HH (11<sup>th</sup> Cir.).

<sup>155</sup>No. 01-7505 (2d Cir.).

<sup>156</sup>295 F.3d 312 (2d Cir. 2002).

<sup>157</sup>137 F. Supp.2d 362 (S.D.N.Y. 2001).

<sup>158</sup>300 F.3d 1281 (11<sup>th</sup> Cir. 2002).

<sup>159</sup>328 U.S. 293 (1946).

<sup>160</sup>421 U.S. 837 (1975).

<sup>161</sup>272 F.3d 1102 (8<sup>th</sup> Cir. 2001).

<sup>162</sup>No. 02-20588 (5<sup>th</sup> Cir.).

<sup>163</sup>289 F.3d 109 (D.C. Cir. 2002).

<sup>164</sup>No. 01-800 (S. Ct.).

<sup>165</sup>No. 02-3486 (N.D. Cal.).

<sup>166</sup>283 F.3d 429 (2d Cir. 2002).

<sup>167</sup>294 F.3d 969 (8<sup>th</sup> Cir. 2002).

<sup>168</sup>513 U.S. 561 (1995).

<sup>169</sup>270 F.3d 645 (8<sup>th</sup> Cir. 2001).

<sup>170</sup>No. 01-70772, 2002 WL 31051543 (9<sup>th</sup> Cir. 2002).

<sup>171</sup>No. 02-11818 (11<sup>th</sup> Cir.).

<sup>172</sup>Civ. No. 3:CV-97-0001 (M.D. Pa. Feb. 19, 2002 (unpublished opinion)).

<sup>173</sup>290 F.3d 80 (2d Cir. 2002).

Table 1  
 ENFORCEMENT CASES INITIATED BY THE COMMISSION  
 DURING FISCAL YEAR 2002 IN VARIOUS PROGRAM AREAS

(Each case initiated has been included in only one category listed below, even though many cases involve multiple allegations and may fall under more than one category. The number of defendants and respondents is noted parenthetically.)

Primary Classification	Civil Actions	Administrative Proceedings	Total	% of Total Actions
Securities Offering Actions	79 (417)	40 (52)	119 (469)	20%
Broker-dealer Actions				
(a) Fraud Against Customer	12 (28)	37 (55)	49 (83)	8%
(b) Failure to Supervise	0 (0)	7 (14)	7 (14)	1%
(c) Government/Municipal Securities	0 (0)	3 (3)	3 (3)	1%
(d) Books & Records	0 (0)	1 (1)	1 (1)	0%
(e) Other	5 (8)	17 (20)	22 (28)	4%
Total Broker-dealer Actions	<u>17 (36)</u>	<u>65 (93)</u>	<u>82 (129)</u>	<u>14%</u>
Issuer Financial Statement and Reporting Actions				
(a) Issuer Financial Disclosure	59 (156)	82 (109)	141 (265)	23%
(b) Issuer Reporting Other	10 (31)	12 (13)	22 (44)	4%
Total Issuer Financial Statement and Reporting Actions	<u>69 (187)</u>	<u>94 (122)</u>	<u>163 (309)</u>	<u>27%</u>
Other Regulated Entity Actions				
(a) Investment Advisers	13 (38)	35 (53)	48 (91)	8%
(b) Investment Companies	2 (5)	2 (5)	4 (10)	.5%
(c) Transfer Agents	0 (0)	2 (4)	2 (4)	.5%
Total Other Regulated Entity Actions	<u>15 (43)</u>	<u>39 (62)</u>	<u>54 (105)</u>	<u>9%</u>
Insider Trading Actions	53 (138)	6 (6)	59 (144)	10%
Market Manipulation Actions	27 (83)	15 (27)	42 (210)	7%
Delinquent Filing Actions	0 (0)	10 (11)	10 (11)	2%
Contempt Proceedings	47 (93)	0 (0)	47 (93)	8%
Touting	5 (12)	8 (11)	13 (23)	2%
Corporate Control Actions	1 (2)	1 (6)	2 (8)	0%
Miscellaneous Actions	4 (13)	3 (4)	7 (17)	1%
GRAND TOTAL	<u>317(1124)</u>	<u>281 (394)</u>	<u>598 (1518)</u>	<u>100%</u>

**Table 2**  
**FISCAL 2002 ENFORCEMENT CASES**  
**LISTED BY PROGRAM AREA**

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
<b>Broker-Dealer: Books &amp; Records</b>		
In the Matter of iCapital Markets LLC	34-45328	01/24/02
<b>Broker-Dealer: Fraud Against Customer</b>		
In the Matter of Brett L. Bouchy, et al.	34-44977	10/24/01
SEC v. Daniel Patrick O'Connell	LR-17209	10/26/01
In the Matter of Richard M. Eisenmenger	34-45055	11/07/01
In the Matter of Leroy K. Messenger	34-45042	11/07/01
SEC v. Dunyasha M. Yetts, et al.	LR-17286	12/20/01
In the Matter of Daniel Patrick O'Connell	34-45298	01/17/02
SEC v. Credit Suisse First Boston Corporation	LR-17327	01/22/02
In the Matter of Gregory F. Mazzeo	33-8060	01/24/02
SEC v. Enrique E. Perusquia	LR-17348	01/30/02
In the Matter of Garri Zhigun	34-45381	02/01/02
In the Matter of Craig Wiginton	34-45445	02/14/02
In the Matter of Robert Shane Jones	34-45446	02/14/02
In the Matter of John Adams, Jr., et al.	34-45455	02/15/02
In the Matter of Russell C. Turek	34-45459	02/20/02
In the Matter of Nigel A. Ramsay	34-45463	02/20/02
SEC v. R. Christopher Hanna	LR-17368	02/20/02
In the Matter of Mark McDermott	34-45461	02/20/02
SEC v. Frank D. Gruttadauria, et al.	LR-17418	02/27/02
In the Matter of Frank Lee Harris III	34-45485	02/28/02
In the Matter of Oleg Feldman	34-45610	03/21/02
In the Matter of Joao P. Santos	34-45690	04/04/02
In the Matter of Wayne Miller	33-8085	04/11/02
In the Matter of H. Dalton Davlin	34-45776	04/18/02
In the Matter of J.W. Barclay & Co., Inc., et al.	33-8094	04/24/02
SEC v. William M. Ucherek	LR-17488	04/24/02
In the Matter of Andrew P. Bodnar	34-46142	04/29/02
In the Matter of Joseph E. Erwin	34-46171	05/15/02
In the Matter of Kfir Barzilay, et al.	34-45961	05/20/02
In the Matter of Jeffrey Dene Leader	34-46080	06/17/02
SEC v. Gregory P. Waldon	LR-17591	06/26/02
In the Matter of James A. Nies	34-46200	07/15/02
SEC v. Gregory A. Hinkson	LR-17621	07/17/02
SEC v. Quest Capital Strategies, Inc., et al.	LR-17644	07/31/02
In the Matter of Joseph Orlando, et al.	34-46358	08/15/02
In the Matter of Gregory A. Hinkson	34-46387	08/20/02
In the Matter of William M. Ucherek	34-46408	08/23/02
In the Matter Chimneyville Investments Group, Inc.	34-46424	08/28/02
In the Matter of Joseph Randolph Belew	34-46426	08/28/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
In the Matter of Michael J. Christie	34-46423	08/28/02
In the Matter of Monica Lynn Coleman	34-46431	08/29/02
SEC v. J. Scott Eskind, et al.	LR-17725	09/03/02
In the Matter of Enrique E. Perusquia	34-46500	09/16/02
In the Matter of Robert F. Curley	34-46510	09/18/02

**Broker-Dealer: Government / Municipal Securities**

In the Matter of David E. Fitzgerald	34-45599	03/20/02
In the Matter of Fifth Third Securities, Inc.	34-46087	06/18/02
In the Matter of RBC Dain Rauscher Incorporated, et al.	33-8121	08/13/02

**Broker-Dealer: Other**

In the Matter of Mark Steven Snader, et al.	34-45002	10/30/01
In the Matter of Bruce E. Straughn	34-45058	11/15/01
In the Matter of Republic New York Securities Corp.	34-45157	12/17/01
In the Matter of W.J. Nolan & Co., Inc.	34-45208	12/28/01
In the Matter of Thomas J. Palazzolo	33-8051	01/02/02
SEC v. W.J. Nolan & Co., Inc.	LR-17324	01/08/02
In the Matter of Robert E. Duke	34-45491	03/01/02
SEC v. Millennium Financial, Ltd., et al.	LR-17528	05/22/02
SEC v. Bruce D. LeDuc	LR-17545	05/30/02
SEC v. J.W. Barclay & Co., Inc., et al.	LR-17765	07/01/02
In the Matter of David Rubinov	34-46158	07/02/02
In the Matter of William S. Killeen	34-46201	07/15/02
In the Matter of Thomas Beck	34-46202	07/15/02
In the Matter of Edward J. Mueger	34-46203	07/15/02
In the Matter of Thomas Cavallino, et al.	34-46204	07/15/02
In the Matter of Knight Securities, L.P.	34-46226	07/18/02
In the Matter of Mark R. Savarese	34-46277	07/29/02
In the Matter of John J. Savarese	34-46278	07/29/02
SEC v. James Vincent O'Brien, et al.	LR-17655	07/31/02
In the Matter of Keith J. Mauney	33-8125	09/03/02
In the Matter of Leslie A. Arouh	33-8127	09/03/02
In the Matter of Bruce D. LeDuc	34-46565	09/27/02

**Contempt Proceedings**

SEC v. Colin Smith, et al.	NONE	10/02/01
SEC v. Cary S. Greene	LR-17224	11/02/01
SEC v. Vestron Financial Corp., et al.	NONE	11/06/01
SEC v. Steven E. Thorn, et al.	NONE	11/09/01
Devin A. Danehy	NONE	11/16/01
SEC v. Anthony P. Caliendo, Jr.	LR-17341	12/05/01
SEC v. Paul R. Johnson, et al.	NONE	01/15/02
SEC v. Richard Onorato, et al.	NONE	01/17/02
SEC v. Robert Schlotterbeck, et al.	NONE	01/23/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. Paul J. Montle	NONE	01/30/02
SEC v. Kenneth G. Mason	NONE	02/07/02
SEC v. Terry L. Dowdell, et al.	NONE	02/07/02
SEC v. John Collins	NONE	02/11/02
SEC v. Robert R. Dillie, et al.	NONE	02/11/02
SEC v. Carl T. Johnson, et al.	NONE	03/13/02
SEC v. Carl T. Johnson, et al.	NONE	03/13/02
SEC v. Marada Global Corporation, et al.	NONE	03/26/02
SEC v. Edward M. Harris	NONE	03/27/02
SEC v. Resource Development International, LLC, et al.	NONE	03/27/02
SEC v. Anthony Burges, et al.	NONE	03/27/02
SEC v. James Edwards	NONE	03/28/02
SEC v. David Edwards	NONE	04/03/02
SEC v. Authorized Auto Service, Inc.	NONE	04/05/02
SEC v. Roc Hatfield, et al.	NONE	04/10/02
SEC v. Roc Hatfield, et al.	NONE	04/18/02
SEC v. Alan Clagg, et al.	NONE	04/25/02
SEC v. Bonnie Couch, et al.	NONE	04/30/02
SEC v. Hanh Truong, et al.	NONE	05/09/02
SEC v. David J. Dambro, et al.	NONE	05/15/02
SEC v. Edward R. Showalter	NONE	05/21/02
SEC v. Kevin Lynds, et al.	NONE	06/12/02
SEC v. Starcash, Inc., et al.	NONE	06/17/02
SEC v. Kenneth G. Mason	NONE	06/20/02
SEC v. Jean Leclercq., et al.	LR-17751	06/24/02
SEC v. David Cluff	NONE	07/12/02
SEC v. Steven E. Thorn	NONE	07/24/02
SEC v. Composite Holdings, Inc., et al.	NONE	07/29/02
SEC v. Investco, Inc., et al.	NONE	07/30/02
SEC v. Alfred M. Lemcke, et al.	NONE	08/01/02
SEC v. Dennis S. Herula, et al.	NONE	08/09/02
SEC v. Birgit Mechlenberg	NONE	08/16/02
SEC v. Marlen V. Johnson	LR-17717	09/10/02
SEC v. Richard Mann	NONE	09/27/02
SEC v. David H. Siegel	NONE	09/27/02
SEC v. Claude Lefebvre, et al.	LR-17759	09/30/02
SEC v. RMO Assets Management SA	NONE	09/30/02
SEC v. Jamie P. Piromalli, et al.	NONE	09/30/02

### **Corporate Control**

In the Matter of Basic Capital Management, Inc., et al.	34-46538	09/24/02
SEC v. Basic Capital Management, Inc., et al.	LR-17740	09/24/02



<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
<b>Delinquent Filings</b>		
In the Matter of Arete Industries, Inc.	34-44911	10/05/01
In the Matter of WSF Corporation	34-45222	01/03/02
In the Matter of First Florida Communications, Inc.	34-45635	03/25/02
In the Matter of The S.I.N.C.L.A.R.E Group, Inc.	34-45821	04/15/02
In the Matter of Hightec, Inc.	34-45822	04/15/02
In the Matter of ANICOM, Inc.	34-45880	05/06/02
In the Matter of NewCom, Inc.	34-46283	07/30/02
In the Matter of Ives Health Company, Inc.	34-46420	08/27/02
In the Matter of Adrien Arpel, Inc.	34-46497	09/13/02
In the Matter of Ambassador Eyewear Group, Inc.	34-46558	09/26/02
<b>Failure To Supervise</b>		
In the Matter of Norwest Investment Services, Inc.	34-45460	02/20/02
In the Matter of Delta Equity Services Corporation, et al.	34-45465	02/21/02
In the Matter of Harvest Financial Corporation, Inc., et al.	33-8077	03/25/02
In the Matter of Roundhill Securities, Inc., et al.	33-8080	04/08/02
In the Matter of Josephthal & Co., Inc.	34-46039	06/06/02
In the Matter of Donna N. Morehead	34-46121	06/26/02
In the Matter of Roger Fan	34-46359	08/15/02
<b>Insider Trading</b>		
SEC v. Alan E. Wesa	LR-17168	10/01/01
SEC v. Sol Berg, et al.	LR-17170	10/04/01
In the Matter of Ryan Campbell Doersam	34-44939	10/16/01
SEC v. Rodolfo Luzardo, et al.	LR-17197	10/18/01
SEC v. William A. Rothrock, IV, et al.	LR-17213	10/31/01
SEC v. Joseph F. Doody IV, et al.	LR-17225	11/08/01
SEC v. Ken C. Chow, et al.	LR-17243	11/19/01
SEC v. Mark Apton, et al.	LR-17243	11/19/01
SEC v. Robert J. Prevette, et al.	LR-17243	11/19/01
SEC v. Geoffrey Chang, et al.	LR-17243	11/19/01
SEC v. David Chang, et al.	LR-17243	11/19/01
SEC v. Evan K. Lau, et al.	LR-17243	11/19/01
SEC v. Atul Bhagat, et al.	LR-17243	11/19/01
SEC v. George P. Matus, et al.	LR-17259	12/04/01
SEC v. Patricia A. Burgenhagen, et al.	LR-17278	12/18/01
SEC v. Sean R. Price, et al.,	LR-17279	12/19/01
SEC v. Douglas M. Gloff	LR-17282	12/19/01
In the Matter of Benjamin J. Maldonado, III	34-45198	12/27/01
SEC v. Felix Litvinsky, et al.	LR-17306	01/14/02
SEC v. Robert C. Lowes	LR-17320	01/16/02
SEC v. Daniel J. Wooten III	LR-17330	01/22/02
SEC v. Ryan D. Evans, et al.	LR-17340	01/24/02
SEC v. Thomas T. Johnson, et al.	LR-17347	01/30/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. Pablo Escandon Cusi, et al.	LR-17356	02/07/02
SEC v. John S. Kramer, et al.	LR-17391	02/19/02
SEC v. John Patrick Fitzgerald	LR-17370	02/21/02
SEC v. Robert Bartzoff	LR-17384	02/21/02
SEC v. John J. Cassese	LR-17378	02/25/02
SEC v. Hugo Salvador Villa Manzo, et al.	LR-17395	03/06/02
SEC v. Ronald K. Mahabir, et al.	LR-17401	03/07/02
SEC v. Andrew W. Sachs	LR-17402	03/07/02
SEC v. Anthony Chrysikos, et al.	LR-17404	03/07/02
SEC v. John Harbottle	LR-17424	03/20/02
SEC v. Geoffrey Etherington II, et al.	LR-17467	04/11/02
SEC v. George Kline, et al.	LR-17475	04/17/02
In the Matter of Hugo Salvador Villa Manzo	34-45806	04/24/02
SEC v. Eric Patton, et al.	LR-17495	04/30/02
SEC v. Edward Fruchtenbaum	LR-17499	05/02/02
In the Matter of Erich A. Kline	34-45878	05/03/02
SEC v. Steven S. Goldberg	LR-17505	05/07/02
In the Matter of Steven S. Goldberg	34-45888	05/07/02
SEC v. Josephine Anne Pagano	LR-17543	06/05/02
SEC v. Sitestar Corporation, et al.	LR-17541	06/05/02
SEC v. John Wesley Straub, et al.	LR-17549	06/10/02
SEC v. Jean-Jacques Degroof, et al.	LR-17554	06/11/02
SEC v. Samuel D. Waksal	LR-17559	06/12/02
SEC v. Janice A. Loeff	LR-17599	06/28/02
SEC v. Ja y S. Laveson	LR-17596	07/02/02
SEC v. Barry L. Saffer	LR-17597	07/02/02
In the Matter of Ronald K. Mahabir	34-46217	07/17/02
SEC v. Joseph Sidoryk, et al.	LR-17628	07/23/02
SEC v. Edward J. Smith, et al.	LR-17629	07/24/02
SEC v. Michael A. Ofstedahl, et al.	LR-17645	07/31/02
SEC v. Timothy P. Horne	LR-17680	08/15/02
SEC v. Genentech, Inc., et al.	LR-17684	08/15/02
SEC v. John Gomersall and Barry McGriff	LR-17699	08/22/02
SEC v. Michael W. Foti	LR-17700	08/27/02
SEC v. Harvey R. Dobrow, et al.	LR-17733	09/18/02

### **Investment Adviser**

In the Matter of Tiffany Capital Advisors, Inc.	IA-1988	10/03/01
In the Matter of F.X.C. Investors Corp., et al.	IA-1991	10/18/01
SEC v. Don D. Lukens, et al.	LR-17218	11/02/01
In the Matter of Felix Anthony Berry	IA-2000	12/03/01
SEC v. Yehuda Shiv, et al.	LR-17264	12/10/01
In the Matter of Cambridge Equity Advisors, Inc., et al.	IA-2001	12/12/01
In the Matter of Zion Capital Management LLC, et al.	33-8046	12/20/01
In the Matter of James D. Cooper, III	34-45186	12/21/01
In the Matter of Lawrence B. Irwin, et al.	33-8047	12/21/01
In the Matter of Reed E. Slatkin	IA-2006	01/02/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
In the Matter of Financial Asset Management, Inc., et al.	AAER-1485	01/03/02
In the Matter of United Custodial Corporation	IA-2011	01/24/02
In the Matter of Rupay-Barrington Capital Management, Inc.	IA-2012	01/30/02
In the Matter of Craig P. Scanlon	IA-2014	02/13/02
In the Matter of Eugene B. Deveney	IA-2015	02/22/02
SEC v. Saint James Asset Management, Inc., et al.	LR-17429	03/11/02
In the Matter of Henry Weingarten	IA-2019	03/19/02
SEC v. James Oh	LR-17428	03/21/02
In the Matter of Stan D. Kiefer & Associates, et al.	IA-2023	03/22/02
In the Matter of Edward Thomas Jung, et al.	34-45669	03/28/02
SEC v. Dennis Herula, et al.	LR-17461	04/01/02
In the Matter of Thomas J. Kearns	IA-2026	04/01/02
In the Matter of James Oh	IA-2029	04/18/02
In the Matter of Alexis A. Arlett	IA-2034	05/30/02
SEC v. Roger A. Householder, et al.	LR-17565	06/10/02
SEC v. Edward Gobora	LR-17555	06/11/02
In the Matter of DePrince, Race & Zollo, Inc., et al.	IA-2035	06/12/02
In the Matter of Performance Analytics, Inc., et al.	IA-2036	06/17/02
In the Matter of Peter P. Tarangelo	34-46094	06/20/02
In the Matter of PortFolio Advisory Services, LLC, et al.	IA-2038	06/20/02
In the Matter of William F. Branstor	IA-2040	06/26/02
In the Matter of Terrance Michael O'Donohue	34-46150	07/01/02
In the Matter of Edward F. Gobora	IA-2042	07/10/02
In the Matter of Schwendiman Partners, LLC, et al.	33-8111	07/11/02
In the Matter of Consortium Investment, Ltd., et al.	33-8117	07/30/02
SEC v. Steven M. Bolla, et al.	LR-17642	07/31/02
SEC v. Thomas M. Durkin, et al.	LR-17650	08/01/02
In the Matter of Michael L. Smirlock	IA-2046	08/12/02
SEC v. Slocum, Gordon & Co., et al.	LR-17688	08/20/02
In the Matter of Market Timing Systems, Inc., et al.	IA-2048	08/28/02
In the Matter of Thomas M. Durkin	IA-2051	08/30/02
In the Matter of John E. Orin, Jr.	IA-2050	08/30/02
In the Matter of Harvey I. Rubinstein	33-8126	09/03/02
In the Matter of Vanderbilt Capital Advisors LLC	IA-2053	09/03/02
SEC v. Fred Albert Schluep	LR-17711	09/04/02
In the Matter of John Raymond Linney Clain	IA-2057	09/17/02
SEC v. Isaac Sofair, et al.	LR-17730	09/17/02
In the Matter of Donald D. Lukens	34-46526	09/20/02
In the Matter of Oxford Capital Management, Inc., et al.	IA-2061	09/23/02
In the Matter of Alfred M. Lemcke	34-46574	09/30/02
SEC v. Alfred Lemcke	LR-17237	11/16/01

### **Investment Company**

In the Matter of ND Money Management, Inc., et al.	IA-2027	04/12/02
SEC v. National Presto Industries, Inc.	LR-17647	07/16/02
SEC v. IBF Collateralized Finance Corporation, et al.	LR-17625	07/23/02
In the Matter of Davis Selected Advisers-NY, Inc.	IA-2055	09/04/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
<b>Issuer Financial Disclosure</b>		
In the Matter of Chiquita Brands International, Inc.	AAER-1463	10/03/01
In the Matter of NexPub, Inc.	AAER-1469	10/18/01
In the Matter of Gisela de Leon-Meredith	AAER-1471	10/23/01
In the Matter of Seaboard Corporation	AAER-1470	10/23/01
SEC v. Roys Poyiadjis, et al.	AAER-1473	10/29/01
SEC v. Chiquita Brands International, Inc.	AAER-1464	10/31/01
In the Matter of a Registration Statement of Toks Inc.	33-8032	11/13/01
In the Matter of Pinnacle Holdings, Inc.	AAER-1476	12/06/01
In the Matter of Timothy Tuttle	AAER-1479	12/14/01
In the Matter of Corrine Davies	AAER-1478	12/14/01
SEC v. R. Bruce Acacio	LR-17308	12/18/01
In the Matter of Jeffrey Bacsik, CPA	AAER-1482	12/27/01
In the Matter of Rachel Eckhaus, CPA	AAER-1481	12/27/01
In the Matter of Barbara Horvath, CPA	AAER-1483	12/27/01
SEC v. Nelson Barber	LR-17291	12/27/01
In the Matter of California Software Corporation	AAER-1486	01/07/02
In the Matter of Carol Conway Dewees	AAER-1487	01/07/02
In the Matter of James E. Slayton, CPA	AAER-1566	01/07/02
SEC v. David C. Guenther, et al.	LR-17297	01/08/02
SEC v. Michael A. Porter	AAER-1493	01/14/02
In the Matter of KPMG, LLP	AAER-1491	01/14/02
In the Matter of BellSouth Corporation	AAER-1494	01/15/02
SEC v. BellSouth Corporation	LR-17310	01/15/02
In the Matter of Nelson Barber, CPA	AAER-1496	01/15/02
SEC v. Thomas W. Lambasch	LR-17319	01/16/02
In the Matter of Trump Hotels & Casino Resorts, Inc.	AAER-1499	01/16/02
SEC v. Patrick O. Wheeler, et al.	LR-17346	01/30/02
In the Matter of Cyberguard Corporation, et al.	AAER-1501	01/30/02
In the Matter of Critical Path, Inc.	AAER-1503	02/05/02
SEC v. David A. Thatcher, et al.	LR-17353	02/05/02
In the Matter of William H. Warner, et al.	AAER-1501	02/13/02
SEC v. International Thoroughbred Breeders, Inc., et al.	AAER-1506	02/13/02
SEC v. J. Donald Nichols, et al.	LR-17366	02/20/02
In the Matter of JDN Realty Corporation	AAER-1507	02/20/02
SEC v. Eagle Building Technologies, Inc., et al.	LR-17389	03/01/02
In the Matter of Kevin R. Andersen, CPA	AAER-1510	03/05/02
In the Matter of Telxon Corporation, et al.	AAER-1511	03/05/02
SEC v. Kenneth W. Haver	LR-17394	03/05/02
SEC v. Raece Richardson, et al.	LR-17397	03/06/02
In the Matter of James E. Slayton, CPA	AAER-1567	03/06/02
In the Matter of Donald J. MacPhee	AAER-1519	03/12/02
In the Matter of William A. Dickson, et al.	AAER-1518	03/12/02
In the Matter of IGI, Inc.	AAER-1520	03/12/02
In the Matter of Frederick W. Kolling III, CPA	34-45550	03/12/02
SEC v. Paul Skulsky, et al.	LR-17404	03/12/02
SEC v. Lawrence N. Zitto	LR-17410	03/13/02
SEC v. John P. Gallo	LR-17410	03/13/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. Donald J. MacPhee	LR-17410	03/13/02
In the Matter of Timothy S. Heyerdahl, CPA	AAER-1522	03/18/02
In the Matter of Elaine A. Decker, CPA	AAER-1524	03/18/02
In the Matter of David Held, CPA	AAER-1523	03/18/02
SEC v. First Florida Communications, Inc., et al.	LR-17437	03/21/02
SEC v. Harold J. Macsata	LR-17426	03/21/02
In the Matter of Keith Spero	AAER-1526	03/21/02
In the Matter of Frank Valdez	AAER-1527	03/21/02
In the Matter of Harlan Schier	AAER-1528	03/21/02
In the Matter of Daniel Parker	AAER-1529	03/21/02
In the Matter of Uri Evan, et al.	AAER-1530	03/21/02
In the Matter of Douglas E. Costa	33-8076	03/25/02
SEC v. Dale Peterson, et al.	AAER-1535	03/26/02
SEC v. Dean L. Buntrock, et al.	AAER-1532	03/26/02
In the Matter of Signal Technology Corporation	AAER-1534	03/27/02
In the Matter of Kimberly-Clark Corporation, et al.	AAER-1533	03/27/02
In the Matter of PictureTel Corp., et al.	AAER-1536	03/28/02
In the Matter of David T. Dodge	AAER-1537	03/28/02
SEC v. Leonard J. Guida	LR-17448	03/28/02
SEC v. Les B. Strauss	LR-17448	03/28/02
In the Matter of David A. Thatcher	AAER-1539	04/02/02
SEC v. Michael Paloma, et al.	LR-17462	04/08/02
SEC v. Xerox Corporation	AAER-1542	04/11/02
In the Matter of Michael R. Drogin, CPA	34-45797	04/22/02
SEC v. Byron Robert Lerner	LR-17481	04/22/02
In the Matter of Teltran International Group, Ltd.	AAER-1543	04/22/02
SEC v. Patrick Quinlan, et al.	AAER-1546	04/23/02
In the Matter of Kenneth W. Haver, CPA	AAER-1547	04/24/02
SEC v. G. Matthias Heinzelmann, III	AAER-1549	04/25/02
In the Matter of Surety Capital Corporation	AAER-1550	04/25/02
In the Matter of Serologicals Corporation, Inc.	AAER-1551	05/01/02
In the Matter of Michael A. Kolberg, et al.	AAER-1552	05/01/02
SEC v. Carl E. Putnam, et al.	AAER-1554	05/06/02
In the Matter of Edison Schools, Inc.	AAER-1555	05/14/02
In the Matter of Ernst & Young LLP	34-45964	05/20/02
SEC v. David Malmstedt, et al.	AAER-1561	05/20/02
In the Matter of Legato Systems, Inc., et al.	AAER-1557	05/20/02
SEC v. Reza Mikaili, et al.	LR-17522	05/20/02
SEC v. Alan K. Anderson	AAER-1560	05/20/02
In the Matter of Microsoft Corporation	AAER-1563	06/03/02
SEC v. John F. Mortell, et al.	AAER 1569	06/05/02
In the Matter of John K. Bradley	AAER-1568	06/05/02
In the Matter of Advanced Technical Products, Inc., et al.	AAER-1564	06/05/02
In the Matter of Katrina Krug, CPA	AAER-1565	06/05/02
In the Matter of Gerald S. Papazian	AAER-1572	06/07/02
In the Matter of Korea Data Systems USA, Inc., et al.	AAER-1571	06/07/02
SEC v. Kenneth E. Kurtzman, et al.	AAER 1574	06/10/02
In the Matter of Ashford.Com, Inc., et al.	AAER-1573	06/10/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. Aura Systems, Inc., et al.	AAER-1575	06/11/02
SEC v. Gerald S. Papazian	AAER-1575	06/11/02
In the Matter of Rite Aid Corporation	AAER-1579	06/11/02
SEC v. Bruce Hill, et al.	AAER-1582	06/21/02
SEC v. Richard P. Vatcher	AAER-1582	06/21/02
SEC v. Frank M. Bergonzi, et al.	AAER-1581	06/21/02
In the Matter of Timothy J. Noonan	AAER-1580	06/21/02
SEC v. WorldCom, Inc.	AAER-1585	06/26/02
In the Matter of Moret Ernst & Young Accountants	AAER-1584	06/27/02
In the Matter of Peter D. Stewart, C.A., et al.	AAER-1587	07/02/02
In the Matter of Gregory D. Norton, CPA	AAER-1589	07/09/02
In the Matter of Glen P. Duffy, CPA	AAER-1590	07/09/02
In the Matter of Thomas F. Wraback, CPA	AAER-1588	07/09/02
In the Matter of Steven C. Veen, CPA	AAER-1591	07/10/02
SEC v. Intelliquis International, Inc., et al.	AAER-1592	07/12/02
In the Matter of Avon Products, Inc.	AAER-1595	07/17/02
In the Matter of PriceWaterHouseCoopers LLP, et al.	AAER-1596	07/17/02
In the Matter of The PNC Financial Services Group, Inc.	AAER-1597	07/18/02
SEC v. Adelphia Communications Corporation, et al.	AAER-1599	07/24/02
SEC v. Oxford Health Plans, Inc.	AAER-1601	07/25/02
In the Matter of Oxford Health Plans, Inc., et al.	AAER-1600	07/25/02
In the Matter of Eric C. Brown	AAER-1602	07/29/02
In the Matter of Aremissoft Corporation	34-46285	07/31/02
SEC v. Douglas A. Murphy, et al.	AAER-1607	08/01/02
SEC v. John R. Boyd, et al.	AAER-1605	08/01/02
In the Matter of David Friend, CPA	AAER-1603	08/01/02
In the Matter of Richard P. Bellinger, et al.	AAER-1604	08/01/02
In the Matter of Gas and Oil Technologies, Inc., et al	AAER-1608	08/02/02
In the Matter of Edward T. Creevy	AAER-1612	08/08/02
SEC v. Kevin J. Morrison, et al.	AAER-1616	08/16/02
In the Matter of Kurt D. Saliger, CPA	AAER-1615	08/16/02
SEC v. Michael J. Kopper	AAER-1617	08/21/02
SEC v. William H. Rinehart, et al.	AAER-1619	08/27/02
In the Matter of James Muphy, CPA	AAER-1620	08/30/02
In the Matter of SCB Computer Technology, Inc.	AAER-1622	08/30/02
SEC v. Yervant David Lepejian	AAER-1625	09/10/02
SEC v. Motorcar Parts & Accessories, Inc., et al.	AAER-1629	09/19/02
In the Matter of Dynege Inc.	AAER-1631	09/24/02
SEC v. Asthma Disease Management, Inc., et al.	AAER-1630	09/24/02
SEC v. Dynege Inc.	AAER-1632	09/25/02
SEC v. John Giesecke, Jr., et al.	LR-17745	09/25/02
SEC v. David F. Myers	AAER-1635	09/26/02
SEC v. Barry M. Budilov, et al.	AAER-1634	09/26/02
SEC v. Arthur A. Goodwin, et al.	AAER-1638	09/30/02
SEC v. J. Kenneth Stringer, III, et al.	AAER-1639	09/30/02
In the Matter of FLIR Systems, Inc.	AAER-1637	09/30/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
<b>Issuer Reporting: Other</b>		
In the Matter of Thomas P. Raabe	34-44912	10/05/01
SEC v. Millionaire.Com, et al.	AAER-1468	10/17/01
In the Matter of The Classica Group, Inc.	34-45057	11/15/01
In the Matter of Disease Sciences, Inc.	34-45056	11/15/01
In the Matter of R-Tec Technologies, Inc.	34-45055	11/15/01
SEC v. Hitsgalore.com, Inc., et al.	LR-17249	11/28/01
In the Matter of Zila, Inc., et al.	34-45169	12/19/01
SEC v. Save the World Air, Inc., et al.	LR-17283	12/19/01
SEC v. Global DataTel, Inc., et al.	LR-17300	12/26/01
SEC v. Turbodyne Technologies, Inc., et al.	LR-17339	01/24/02
In the Matter of David B. Gosse	34-45474	02/25/02
In the Matter of Fonecash, Inc.	33-8079	04/08/02
SEC v. FoneCash, Inc., et al.	LR-17464	04/10/02
In The Matter of Registration Statements of Investment Technology, Inc.	33-8092	04/22/02
SEC v. Pinnacle Business Management, Inc., et al.	LR-17507	05/08/02
In the Matter of Tradamax Group, Inc.	34-46271	07/26/02
In the Matter of NetAir.Com, Inc.	34-46286	07/31/02
SEC v. COI Solutions, Inc., et al.	LR-17685	08/15/02
SEC v. Rhino Ecosystems, Inc., et al.	LR-17685	08/15/02
SEC v. Uncommon Media Group, et al.	LR-17685	08/15/02
In the Matter of NorthStar Network, Inc.	34-46388	08/21/02
SEC v. Northstar Network, Inc., et al.	LR-17695	08/21/02
In the Matter of R&RX Group, Inc., formerly known as Neoteric Group, Inc.	34-46470	09/06/02
SEC v. L. Dennis Kozlowski, et al.	AAER-1627	09/12/02

### **Market Manipulation**

SEC v. AbsoluteFuture.Com, et al.	LR-17180	10/11/01
SEC v. U.N. Dollar Corp., et al.	LR-17177	10/11/01
SEC v. Ramoil Management Ltd., et al.	LR-17179	10/11/01
SEC v. Wamex Holdings, Inc., et al.	LR-17178	10/11/01
In the Matter of Hunter Adams, et al.	34-8026	10/18/01
SEC v. Leonid Shipilsky, et al.	LR-17221	11/05/01
In the Matter of Israel M. Shenker	33-8029	11/05/01
SEC v. Israel M. Shenker	LR-17221	11/05/01
In the Matter of Joseph R. Blackwell, et al.	33-8030	11/05/01
SEC v. Joseph Ronald Blackwell, et al.	LR-17221	11/05/01
SEC v. Alexander M. Pomper	LR-17221	11/05/01
SEC v. Stephen J. Fischer	LR-17254	11/29/01
In the Matter of Lee E. Gahr	34-45140	12/07/01
SEC v. Spectrum Brands Corp., et al.	LR-17265	12/11/01
SEC v. Ned C. Sneiderman	LR-17294	01/03/02
SEC v. James E. Franklin, et al.	LR-17311	01/14/02
SEC v. Max C. Tanner, et al.	LR-17305	01/14/02
SEC v. Tel-One, Inc., et al.	LR-17337	01/22/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. New Energy Corp., et al.	LR-17446	02/01/02
In the Matter of Richard Silverman	34-45407	02/06/02
In the Matter of Alefheim Prodani	34-45408	02/06/02
SEC v. Mark E. Rice, et al.	LR-17414	02/27/02
SEC v. David Allen Lester	LR-17396	03/06/02
In the Matter of Edward J. Muller	34-45646	03/26/02
SEC v. Surgilight, Inc., et al.	LR-17469	04/11/02
In the Matter of Bruce E. Straughn	33-8100	05/15/02
SEC v. Investco, Inc., et al.	LR-17525	05/20/02
SEC v. Kin H. Lee	LR-17579	06/24/02
In the Matter of Michael Anthony Lester	34-46107	06/24/02
In the Matter of Benjamin C. Snyder	34-46108	06/25/02
SEC v. Camilo Pereira a/k/a Camilo Agasim-Pereira	LR-17616	07/15/02
In the Matter of George LaFauci	34-46242	07/22/02
In the Matter of Alan S. Lipstein	34-46241	07/22/02
In the Matter of George Carapella	34-46240	07/22/02
SEC v. Andrew L. Pope	LR-17637	07/30/02
SEC v. Environmental Solutions Worldwide, Inc., et al.	LR-17673A	08/07/02
SEC v. eConnect, et al.	LR-17670	08/07/02
In the Matter of Mark A. Taylor, Sr., et al.	34-46342	08/13/02
SEC v. Jeffrey R. Senger, et al.	LR-17685	08/15/02
In the Matter of Gary Salter	34-46550	09/25/02
SEC v. Allen Z. Wolfson, et al.	LR-17756	09/30/02

### **Miscellaneous**

In the Matter of Eric John Watson	34-44934	10/15/01
SEC v. Vito Valentini	LR-17215	10/31/01
In the Matter of Henry Salzhauer, et al.	34-45005	10/31/01
In the Matter of John W. Cruickshank, Jr.	34-45510	03/06/02
SEC v. Patrick J. Rooney, et al.	LR-17425	03/20/02
SEC v. Von Christopher Cummings, et al.	LR-17581	06/24/02
SEC v. Gardere Wynne Sewell LLP	LR-17584	06/25/02
SEC v. Ira J. Gaines, et al.	LR-17703	08/29/02

### **Touting**

In the Matter of Millennium Group of New York, LLC, et al.	33-8023	10/11/01
In the Matter of Dennis M. Wilson	33-8042	12/19/01
SEC v. Christina Skousen, et al.	LR-17379	02/22/02
In the Matter of Edward Alexander	34-45473	02/25/02
SEC v. David S. Heredia, et al.	LR-17390	02/27/02
In the Matter of Mark W. Lancaster	34-45735	04/11/02
In the Matter of Delores Easthom	33-8086	04/11/02
In the Matter of Christina Skousen	34-45856	05/01/02
In the Matter of James W. Spratt III	34-46083	06/17/02
In the Matter of Rodona Garst	33-8113	07/24/02



<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. G. Christopher Scoggin	LR-17690	08/20/02
SEC v. Paul A. Spray, et al.	LR-17721	09/05/02
In the Matter of Martin P. Joswick	33-8133	09/24/02

### **Offering Violations**

In the Matter of PriorityAccess, Inc., et al.	33-8021	10/03/01
SEC v. Nueworld.com Commerce, Inc., et al.	LR-17171	10/04/01
SEC v. The Balancer Company, Inc., et al.	LR-17174	10/05/01
In the Matter of Philip A. Sharpton	34-44926	10/12/01
In the Matter of Joseph F. Denson, Jr.	34-44925	10/12/01
SEC v. Gerard Chiarella, et al.	LR-17182	10/12/01
SEC v. Mark Steven Snader, et al.	LR-17187	10/12/01
SEC v. Vestron Financial Corp., et al.	LR-17200	10/22/01
SEC v. Steven Goldsborough, et al.	LR-17207	10/25/01
In the Matter of Roger J. Walstra	34-45006	10/31/01
SEC v. Michael E. Hill, et al.	LR-17217	11/01/01
SEC v. Robert L. Bentley, et al.	LR-17228	11/13/01
SEC v. Peter W. Chabot, et al.	LR-17276	11/13/01
SEC v. Texon Energy Corporation, et al.	LR-17231	11/14/01
In the Matter of Joseph M. Blumenthal	34-45070	11/16/01
In the Matter of George W. Guttman	34-45069	11/16/01
SEC v. Terry L. Dowdell, et al.	LR-17242	11/19/01
In the Matter of The State Bank of India, et al.	33-8036	11/19/01
In the Matter of Bernadette Stevens a/k/a Bernadette Stevens Bell	34-45092	11/21/01
In the Matter of Wayne L. Prichason	34-45091	11/21/01
SEC v. BJI Financial Services, et al.	LR-17257	12/03/01
SEC v. C-Tech, LLP, et al.	LR-17251	12/03/01
SEC v. World Class Limousines, Inc., et al.	LR-17261	12/05/01
SEC v. John C. Willy, Jr.	LR-17256	12/05/01
In the Matter of Nolan W. Wade	34-45143	12/10/01
In the Matter of Kenneth R. Grossfeld	34-45142	12/10/01
SEC v. Invest Better 2001, et al.	LR-17296	12/13/01
In the Matter of Robert C. Ellenburg	34-45168	12/19/01
SEC v. Lytle E. Fogelson, et al.	LR-17281	12/19/01
SEC v. Richard T. Taylor, et al.	LR-17288	12/20/01
SEC v. Robert R. Dillie, et al.	LR-17290	12/20/01
SEC v. Genesis Leasing IX, Inc., et al.	LR-17332	12/27/01
SEC v. Jean Baptiste Jean Pierre, et al.	LR-17303	01/10/02
In the Matter of Art H. Beroff	33-8054	01/14/02
SEC v. Louis M. Lazorwitz, et al.	LR-17317	01/15/02
SEC v. Art H. Beroff	LR-17312	01/15/02
SEC v. Merrill Scott & Associates, Ltd., et al.	LR-17342	01/15/02
In the Matter of Robert Alen Blackburn	34-45292	01/16/02
In the Matter of Kurtis Keith Lowe	34-45293	01/16/02
In the Matter of Woody Keith Lowe	34-45294	01/16/02
In the Matter Jerry Lynn Ruyle	34-45296	01/16/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
SEC v. Lewis J. McConnell, Jr., et al.	LR-17322	01/16/02
In the Matter of Eric V. Schultz	33-8058	01/24/02
SEC v. Emsanet Internet Services, Inc., et al.	LR-17336	01/24/02
SEC v. Paul R. Johnson, et al.	LR-17375	01/29/02
SEC v. Alexander Naujoks, et al.	LR-17357	02/05/02
SEC v. Gary L. Moody, et al.	LR-17416	02/06/02
SEC v. Larry W. Tyler, et al.	LR-17376	02/11/02
SEC v. Clif Goldstein, et al.	LR-17362	02/14/02
SEC v. Health Maintenance Centers, Inc., et al.	LR-17372	02/15/02
SEC v. Anthony Burges, et al.	LR-17367	02/20/02
SEC v. Make It Reel Productions, Inc., et al.	LR-17393	02/21/02
SEC v. CDH & Affiliates, Inc., et al.	LR-17386	02/25/02
SEC v. Victor Industries, Inc., et al.	LR-17383	02/26/02
SEC v. Harral Dunbar, Jr., et al.	LR-17411	03/04/02
SEC v. Joseph Lloyd Norris, et al.	LR-17403	03/07/02
In the Matter of Victor R. Grauaug	34-45549	03/12/02
SEC v. Discovery Capital Group, et al.	LR-17420	03/14/02
SEC v. Anamar Communications, Inc., et al.	LR-17419	03/15/02
In the Matter of Mark E. Rice	34-45564	03/15/02
In the Matter of Ronald N. Pellett, et al.	34-45565	03/15/02
SEC v. J.T. Wallenbrock & Associates, et al.	LR-17343	03/18/02
SEC v. ACE Payday Plus, LLC, et al.	LR-17422	03/19/02
SEC v. Big Country Ags, Inc., et al.	LR-17434	03/22/02
SEC v. Larry Grabarnick, et al.	LR-17430	03/22/02
SEC v. Resource Development International, LLC, et al.	LR-17438	03/25/02
SEC v. Frederick J. Gilliland, et al.	LR-17474	03/27/02
SEC v. Stand-By Systems, Inc., et al.	LR-17463	03/27/02
SEC v. U.S. Reservation Bank & Trust, et al.	LR-17459	04/03/02
SEC v. Joao P. Santos, et al.	LR-17457	04/04/02
In the Matter of Darrell Flanders, et al.	33-8083	04/10/02
In the Matter of Ronald Nelson Weems	33-8084	04/12/02
SEC v. The Gaming Factory, Inc., et al.	LR-17472	04/15/02
SEC v. Sebastian Corriere, et al.	LR-17506	04/18/02
In the Matter of William L. Haynes	34-45820	04/25/02
SEC v. Larry A. Stockett	LR-17494	04/26/02
SEC v. 4NExchange, LLC, et al.	LR-17500	05/02/02
SEC v. U.S. Funding Corporatiion, et al.	LR-17503	05/03/02
SEC v. Jean Leclerq., et al.	LR-17526	05/16/02
SEC v. American-Inc.com, Inc., et al.	LR-17526	05/16/02
SEC v. Dennis Watts, et al.	LR-17527	05/21/02
SEC v. Southern Financial Group, Inc., et al.	LR-17535	05/24/02
SEC v. Gold-Ventures Club, et al.	LR-17537	05/28/02
In the Matter of Edward Neel Cox, et al.	34-46051	06/10/02
In the Matter of Douglas C. Brandon, Esq.	34-46068	06/12/02
In the Matter of Sara Gomez de Ferro	34-46074	06/13/02
SEC v. Terrance Michael O'Donohue, et al.	LR-17572	06/17/02
In the Matter of Seth Miller	34-46089	06/18/02
SEC v. House Asset Management, LLC, et al.	LR-17583	06/20/02

<u>Name of Case</u>	<u>Release Number</u>	<u>Date Filed</u>
In the Matter of Steven Shane Nichols	34-46118	06/25/02
In the Matter of Charles Edward Dickerson	34-46151	07/01/02
In the Matter of Scott Schoenbauer	34-46156	07/02/02
In the Matter of Raphael "Ray" Levy	34-46173	07/09/02
In the Matter of Gerald Cohn	33-8110	07/09/02
SEC v. Church Extension of the Church of God, Inc., et al.	AAER-1598	07/22/02
In the Matter of Richard Mann	34-46499	07/24/02
SEC v. American Financial Group of Aventura, Inc., et al.	LR-17638	07/24/02
In the Matter of Michael D. Richmond	34-46276	07/29/02
In the Matter of Johann M. Smith	34-46279	07/29/02
SEC v. Claude Lefebvre, et al.	LR-17652	07/31/02
SEC v. Jeffrey D. Chandler, et al.	LR-17674	07/31/02
SEC v. Platinum Investment Corporation, et al.	LR-17643	07/31/02
SEC v. America In-Line Corporation, et al.	LR-17661	08/06/02
SEC v. Heritage Film Group, LLC, et al.	LR-17658	08/06/02
SEC v. Ephone, Inc., et al.	LR-17660	08/06/02
SEC v. Intracom Corporation, et al.	LR-17659	08/06/02
SEC v. Ardian Finance Group, et al.	LR-17663	08/06/02
SEC v. William P. Sauer, et al.	LR-17687	08/07/02
SEC v. Gary Stephen Joiner, et al.	AAER-1611	08/07/02
In the Matter of Arthur Lee Kunes	33-8120	08/09/02
SEC v. American Prometheus Corp., et al.	LR-17682	08/15/02
SEC v. The Strategies Group, Inc., et al.	LR-17681	08/15/02
SEC v. Gary A. Eisenberg	LR-17691	08/20/02
SEC v. Fidelity Petroleum Corp., et al.	LR-17698	08/23/02
SEC v. Shoreline Development Company, et al.	LR-17702	08/27/02
In the Matter of John Cook	34-46447	09/03/02
SEC v. Financial Warfare Club, Inc., et al.	LR-17714	09/05/02
In the Matter of Shawn F. Hackman, Esq.	34-46478	09/10/02
SEC v. Donne Corporation, et al.	AAER-1626	09/11/02
In the Matter of Louis M. Lazowitz	34-46504	09/17/02
In the Matter of Brett R. Mallory	34-46570	09/30/02

### **Transfer Agents**

In the Matter of Gemisys Corporation, et al.	34-45874	05/03/02
In the Matter of Lone Star Transfer, Inc., et al.	34-45870	05/03/02

Table 3  
 INVESTIGATIONS OF POSSIBLE VIOLATIONS OF THE ACTS  
 ADMINISTERED BY THE COMMISSION

Pending as of October 1, 2001 .....	2,401
Opened in Fiscal Year 2002 .....	479
Total .....	2,880
Closed in Fiscal Year 2002 .....	578
Pending as of September 30, 2002 .....	2,302
Formal Orders of Investigation	
Issued in Fiscal Year 2002 .....	300

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### Right to Financial Privacy

Section 21(h) of the Securities Exchange Act of 1934 [15 U.S.C. 78u(h)(6)] requires that the Commission “compile an annual tabulation of the occasions on which the Commission used each separate subparagraph or clause of [Section 21(h)(2)] or the provisions of the Right to Financial Privacy Act of 1978 [12 U.S.C. 3401-22 (the RFPA)] to obtain access to financial records of a customer and include it in its annual report to the Congress.” During the fiscal year, the Commission issued 13 subpoenas based upon Sections 21(h)(2)(A)(ii), (iv) and (v), one subpoena based upon Section 21(h)(2)(A)(iv), and one subpoena based upon Section 21(h)(2)(B), to obtain access to customer financial records. Set forth below are the number of occasions on which the Commission obtained customer records pursuant to the provisions of the RFPA:

Section 1104 (Customer Authorizations)	41
Section 1105 (Administrative Subpoenas)	382
Section 1107 (Judicial Subpoenas)	26
Section 1109 (Delayed Customer Notice)	1

## Corporate Reorganizations

During 2002, the Commission entered its appearance in 32 new reorganization cases filed under Chapter 11 of the Bankruptcy Code involving companies with approximately \$269 billion in assets and 350,000 public investors. Adding these new cases, the Commission was a party in a total of 169 Chapter 11 cases during the year, involving companies with approximately \$374 billion in assets and about 1 million public investors. During the year, 60 cases were concluded through confirmation of a plan, dismissal, or liquidation, leaving 109 cases in which the Commission was a party at year-end.

Table 4  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District		FY Opened	FY Closed
2Xtreme Performance, Inc.3/	D.	CO	1999	2002
Acme Metals Inc.	D.	DE	2001	
Action Auto Rental, Inc.1/	D.	OH	1993	2002
Adelphia Communications	S.D.	NY	2002	
Aileen, Inc.	S.D.	NY	1994	
Alliance Entertainment Corp.	D.	NY	1997	
Allied Products Corp.	N.D.	IL	2001	
American Homestar Corp.1/	S.D.	TX	2001	2002
American Microtel, Inc.3/	D.	NV	1995	2002
American Pad & Paper Co.	D.	DE	2000	
American Rice, Inc.1/	S.D.	TX	1998	2002
AMRESCO, Inc.	N.D.	TX	2001	
Angeion Corporation	D.	MN	2002	

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Apparel America, Inc.	S.D. NY	1998	
APS Holdings, Inc.1/	D. DE	1998	2002
Armstrong World Industries, Inc.	D. DE	2001	
Autoinfo, Inc.	S.D. NY	2000	
Autolend Group, Inc.1/	D. NM	1997	2002
Baldwin Piano & Organ Co.	S.D. OH	2001	
B-E Holdings, Inc.1/	E.D. WI	1994	2002
Ben Franklin Retail Stores, Inc.2/	N.D. IL	1996	2002
BK Entertainment, Inc.	D. M	2001	
Bradlees, Inc.	S.D. NY	1996	
Breed Technologies, Inc.	D. DE	1999	
BroadbandWireless Inter. Corp.	W.D. OK	2002	
Brunos, Inc.	D. DE	1998	
Cable & Co. Worldwide, Inc.	S.D. NY	1998	
Carter Hawley Hale Stores, Inc.1/	C.D. CA	1991	2002
Chester Holdings, LTD.3/	D. SC	2002	2002
Chimneyville Invest. Group, Inc.2/	S.D. MS	1998	2002
Chiquita Brands International, Inc.	S.D. OH	2002	
CinemaStar Luxury Theaters, Inc.1/	S.D. CA	2001	2002
Circuit Systems, Inc.1/	N.D. IL	2000	2002
Cityscape Financial Corp.	S.D. NY	1999	
CML Group, Inc.	D. DE	2001	
Coho Energy, Inc.1/	N.D. TX	1999	2002

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Coho Energy, Inc.1/	S.D. TX	2002	
Cold Metal Products, Inc.	N.D. OH	2002	
Comdisco, Inc.	N.D. IL	2001	
Concord Energy, Inc.	D. DE	1999	
Cooker Restaurant Corp.	S. D. OH	2001	
Costilla Energy, Inc.	W.D. TX	1999	
County Seat Stores, Inc.	S.D. NY	1999	
Coyote Energy, Inc.2/	D. CO	1999	2002
Craig Consumer Electronics, Inc.3/	C.D. CA	1997	2002
Decision Link, Inc.	D. NV	2002	
DeVlieg-Bullard, Inc.1/	N.D. OH	1999	2002
Diagnostic Health Services, Inc.	N.D. TX	2000	2002
Digital Lighthouse Corp.	D. CO	2001	
Drug Emporium, Inc.1/	N.D. OH	2001	2002
Drypers Corp.1/	S.D. OH	2001	2002
Elektryon1/	D. NV	2002	2002
Enron Corporation	S.D. NY	2002	
ERLY Industries, Inc.1/	S.D. TX	1999	2002
Excelsior-Henderson Motorcycle Manufacturing	D. MN	2000	
Factory Card Outlet, Inc.	D. DE	1999	

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Flooring America, Inc.	N.D. GA	2000	
Florsheim Group, Inc.	N.D. IL	2002	
Friede Goldman Halter, Inc.	S.D. MS	2001	
Fruit of the Loom, Ltd.1/	D. DE	2000	2002
Futurenet, Inc.	C.D. CA	2001	
FWT, Inc.	N.D. TX	1999	
Gander Mountain, Inc.1/	E.D. WI	1996	2002
Garden Botanika, Inc.	W.D. WA	1999	
Genesis Worldwide, Inc.	S.D. OH	2002	
Global Crossing, LTD.	S.D. NY	2002	
Graham-Field Health Prod., Inc.	D. DE	2000	
Great American Recreation, Inc.	D. NJ	1996	
Guy F. Atkinson Co. of Calif.1/	N.D. CA	1998	2002
Harnischfeger Industries, Inc.1/	S.D. DE	1999	2002
Health Risk Management, Inc.2/	D. MN	2002	2002
Heilig-Meyers Company	E.D. VA	2000	
Homeland Holding Corp.	W.D. OK	2001	
Horizon Pharmacies, Inc.	N.D. TX	2001	
ICO Global Communications (Holdings) Limited 1/	D. DE	1999	2002
Imperial Sugar Co.1/	D. DE	2001	2002
Integrated Health Services, Inc.	D. DE	2000	
Internet Commerce and Communications, Inc.2/	D. CO	2002	2002
Intile Designs, Inc.3/	S.D. TX	1999	2002
Jacobson Stores, Inc.	E.D. MI	2002	



Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Kevco, Inc.	N.D. TX	2001	
Key Plastics, LLC1/	E.D. MI	2000	2002
Kitty Hawk, Inc.	N.D. TX	2000	
Kmart Corp.	N.D. IL	2002	
KNF Corp.	M.D PA	2001	
Lifeone, Inc.3/	W.D LA	1998	2002
Linc. Capitol, Inc.	N.D IL	2002	
Livent, Inc.	S.D. NY	1999	
L.L. Knickerbocker Co., Inc.1/	C.D. CA	2002	2002
Loehmann's, Inc.	D. DE	1999	
Loewen Group, Inc.	D. DE	1999	
LTV Steel Co.,	N.D. OH	2001	
Manhattan Bagel Co., Inc.	D. NJ	1998	
Mariner Post Acute Network, Inc.1/	D. DE	2000	2002
Marker International 1/	D. DE	1999	2002
Marketing Specialists Corp.	E.D. TX	2001	
Media Vision Technology, Inc.1/	N.D. CA	1994	2002
Metals USA, Inc.	S.D. TX	2002	
Michael Petroleum Corp.	W.D. TX	2000	
MicroAge, Inc.	D. AZ	2001	
Molten Metals Technology, Inc.	D. MA	2001	
Nantucket Industries, Inc.1/	S.D. NY	2001	2002
National Energy Group, Inc.	N.D. TX	1999	
National Steel Corp.	N.D. IL	2002	

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District		FY Opened	FY Closed
Northwestern Steel and Wire Co.	N.D.	IL	2001	
Omega Environmental, Inc.3/	W.D.	WA	1997	2002
Owens Corning Corp.	D.	DE	2001	
Pacific Gas and Electric Co.	N.D.	CA	2001	
Pacific Northwest Housing, Inc.1/	D.	OR	1998	2002
Panaco Inc.	S.D.	TX	2002	
Paracelsus Healthcare Corp.	S.D.	TX	2001	
Paul Harris Stores, Inc.	S.D.	IN	2001	
Payless Cashways, Inc.	W.D.	MO	2001	
PCA Industries, Inc.3/	E.D.	WI	1997	2002
Penn Pacific Corp.1/	E.D.	OK	1994	2002
Philip Services, Inc.	D.	DE	1999	
PHP Healthcare Corp.	D.	DE	1999	
Pillowtex Corporation1/	D.	DE	2001	2002
Pioneer Companies, Inc.1/	S.D.	TX	2001	2002
Ponder Industries Inc.	S.D.	TX	1999	
Precept Business Services, Inc.	N.D.	TX	2001	
President Casinos, Inc.	S.D.	MS	2002	
Pride Companies, L.P.	N.D.	TX	2001	
ProMedCo Management Co.	N.D.	TX	2001	
Rankin Automotive Group, Inc.	S.D.	TX	2001	
RDM Sports Group, Inc. 1/	N.D.	GA	1997	2002
Reddie Brake Supply Co., Inc.1/	D.	CA	1998	2002
Roberds, Inc.	D.	DE	2000	

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Rymer Foods, Inc.1/ Safety-Kleen Corp.	N.D. IL D. DE	1993 2000	2002
Salant Corp.	S.D. NY	1999	
Shaman Pharmaceuticals, Inc.2/	N.D. CA	2001	2002
SmarTalk Teleservices, Inc.	D. DE	1999	
Spinnaker Industries, Inc.	S.D. OH	2002	
Stage Stores, Inc.1/	S.D. TX	2000	2002
Sterling Chemicals Holdings, Inc.	SD TX	2002	
Sterling Optical Corp.	S.D. NY	1992	
Stone & Webster, Inc.	D. DE	2000	
Styling Technology Corp.	D. AZ	2001	
Sun Healthcare Group, Inc.1/	D. DE	2000	2002
Sunterra Corp.1/	D. MD	2000	2002
Telehub Communications Corp.	N.D. IL	2000	
Thermadyne Holdings Corp.	E.D. MO	2002	
Tradetech Americas, Inc.1/	N.D. IL	1998	2002
Transportation Components, Inc.	S.D. TX	2001	
Trans World Airlines, Inc.	D. DE	2001	
Trism Inc.	W.D. MO	2002	
Uniprime Capitol Acceptance, Inc.	D. AZ	2001	
United Artist Theatre Company	D. DE	2001	
United Companies Financial Corp.	D. DE	1999	
United Video, Inc.1/	D. DE	2000	2002
Universal Broadband Networks, Inc.1/	C.D. CA	2002	2002

Table 4 (cont'd)  
REORGANIZATION PROCEEDINGS UNDER CHAPTER 11  
OF THE BANKRUPTCY CODE IN WHICH  
THE SEC ENTERED APPEARANCE

Debtor	District	FY Opened	FY Closed
Universal Seismic Assoc., Inc.	S.D. TX	1999	
US Airways Group, Inc.	E.D. VA	2002	
USG Corp.	D. DE	2001	
USinternetworking, Inc.1/	D. MD	2002	2002
Venturi Technologies, Inc.1/	S.D. TX	2002	2002
Viatel, Inc.1/	D. DE	2001	2002
Vitech America, Inc.2/	S.D. FL	2001	2002
Waste Systems, Int'l. Inc.	D. DE	2001	
Weblink Wirelss, Inc.	N.D. TX	2001	
Winco Corp.	C.D. CA	1998	
World Access, Inc.	N.D. IL	2001	
WorldCom, Inc.	S.D. NY	2002	
Worldtex, Inc.1/	D. DE	2001	2002
Worldwide Xceed Group, Inc.	N.D. IL	2001	
W.R. Grace & Co.	D. DE	2001	
WRT Energy Corp.	W.D. LA	1996	
Xpeditior, Inc.	N.D. IL	2001	
Total Cases Opened (FY 2002)		32	
Total Cases Closed (FY 2002)			60

1/ Chapter 11 plan confirmed.

2/ Debtor liquidated under Chapter 7.

3/ Case dismissed.

**Table 5**  
**UNCONSOLIDATED FINANCIAL INFORMATION FOR BROKER-DEALERS**  
**1997 – 2001** <sup>1/</sup>  
**(\$ in Millions)**

	1997	1998	1999	2000	2001
<b>Revenues</b>					
Securities Commissions	\$ 32,662.2	\$ 36,695.9	\$ 45,937.4	\$ 54,106.7	\$ 44,763.8
Gains (Losses) in Trading and Investment Accounts	35,957.7	32,754.0	55,464.3	70,777.7	38,950.3
Profits (Losses) from Underwriting and Selling Groups	14,611.0	16,237.1	17,781.5	18,717.6	16,941.1
Margin Interest	10,630.4	12,732.5	15,246.7	24,546.9	13,911.5
Revenues from Sale of Investment Company Shares	12,422.1	14,845.0	16,687.6	19,394.9	16,396.4
All Other Revenues	100,961.2	121,699.9	115,692.0	161,949.4	149,132.8
<b>Total Revenues</b>	<b>\$ 207,244.7</b>	<b>\$ 234,964.4</b>	<b>\$ 266,809.4</b>	<b>\$ 349,493.3</b>	<b>\$ 280,095.8</b>
<b>Expenses</b>					
Registered Representatives' Compensation (Part II Only) <sup>2/</sup>	\$ 22,132.0	\$ 24,974.1	\$ 29,048.7	\$ 33,191.0	\$ 29,950.8
Other Employee Compensation and Benefits	31,404.9	34,954.5	47,950.6	55,307.3	48,311.6
Compensation to Partners and Voting Stockholder Officers	5,020.6	5,098.0	4,737.7	6,707.8	5,247.4
Commissions and Clearance Paid to Other Brokers	8,864.1	10,326.5	13,488.3	15,522.7	14,043.4
Interest Expenses	80,659.4	98,095.4	87,508.3	131,877.2	98,947.2
Regulatory Fees and Expenses	828.5	896.3	1,040.8	1,366.7	1,550.9
All Other Expenses <sup>2/</sup>	38,371.2	43,435.4	53,918.6	66,417.3	62,647.7
<b>Total Expenses</b>	<b>\$ 187,280.7</b>	<b>\$ 217,780.2</b>	<b>\$ 237,693.1</b>	<b>\$ 310,390.0</b>	<b>\$ 260,698.9</b>
<b>Income and Profitability</b>					
Pre-tax Income	\$ 19,964.0	\$ 17,184.2	\$ 29,116.3	\$ 39,103.3	\$ 19,396.9
Pre-tax Profit Margin	9.6%	7.3%	10.9%	11.2%	6.9%
Pre-tax Return on Equity	27.1%	19.4%	27.8%	31.1%	13.8%
<b>Assets, Liabilities and Capital</b>					
Total Assets	\$2,078,740.1	\$2,186,942.5	\$ 2,536,616.6	\$2,865,721.0	\$3,371,298.1
<b>Liabilities</b>					
(a) Unsubordinated Liabilities	1,949,026.3	2,037,162.4	2,363,222.6	2,663,758.3	3,158,257.2
(b) Subordinated Liabilities	47,877.6	54,447.1	59,425.0	64,362.3	68,693.6
(c) Total Liabilities	1,996,904.0	2,091,609.5	2,422,647.6	2,728,120.6	3,226,950.8
Ownership Equity	\$ 81,836.1	\$ 95,333.0	\$ 113,969.1	\$ 137,600.4	\$ 144,347.2
Number of Firms	7,796	7,685	7,461	7,258	7,002

Figures may not add due to rounding.

<sup>1/</sup> Calendar, rather than fiscal, year data is reported in this table.

<sup>2/</sup> Registered representatives' compensation for firms that neither carry nor clear is included in "other expenses" as this expense item is not reported separately on Part IIA of the FOCUS Report.

Source: FOCUS Report

Table 6  
**UNCONSOLIDATED ANNUAL REVENUES AND EXPENSES FOR BROKER-DEALERS  
DOING A PUBLIC BUSINESS**  
1997 – 2001 <sup>1/</sup>  
(\$ in Millions)

	1997	1998	1999	2000	2001
<u>Revenues</u>					
Securities Commissions	\$ 31,858.6	\$ 35,847.4	\$45,094.5	\$ 53,160.6	\$43,798.5
Gains (Losses) in Trading and Investment Accounts	31,802.8	28,978.9	48,917.9	60,720.3	33,566.5
Profits (Losses) from Underwriting and Selling Groups	14,612.2	16,237.1	17,780.7	18,718.0	16,941.2
Margin Interest	10,497.9	12,552.0	15,032.8	24,274.0	13,749.1
Revenues from Sale of Investment Company Shares	12,423.7	14,844.2	16,687.6	19,394.9	16,396.4
All Other Revenues	99,581.2	119,143.6	113,101.7	154,836.1	144,758.2
<b>Total Revenues</b>	<b>\$200,776.4</b>	<b>\$227,603.3</b>	<b>\$256,615.2</b>	<b>\$331,103.9</b>	<b>\$269,210.0</b>
<u>Expenses</u>					
Registered Representatives' Compensation (Part II only) <sup>2/</sup>	\$22,046.4	\$ 24,872.2	\$ 29,007.2	\$ 33,162.0	\$29,948.6
Other Employee Compensation and Benefits	30,798.8	34,180.3	46,856.4	53,356.7	46,967.1
Compensation to Partners and Voting Stockholder Officers	4,730.8	4,841.5	4,369.0	5,450.3	4,976.9
Commissions and Clearance Paid to Other Brokers	8,421.0	9,831.7	12,899.7	14,719.0	13,422.4
Interest Expenses	78,689.2	95,627.0	84,713.8	127,211.5	96,120.5
Regulatory Fees and Expenses	771.7	835.8	945.0	1,204.6	1,343.7
All Other Expenses <sup>2/</sup>	37,477.0	42,359.8	52,486.8	64,429.5	60,747.1
<b>Total Expenses</b>	<b>\$182,934.8</b>	<b>\$212,548.4</b>	<b>\$231,277.9</b>	<b>\$299,533.6</b>	<b>\$253,526.4</b>
<u>Income and Profitability</u>					
Pre-tax Income	\$ 17,841.6	\$ 15,054.9	\$ 25,337.3	\$ 31,570.3	\$ 15,683.6
Pre-tax Profit Margin	8.9%	6.6%	9.9%	9.5%	5.8%
Pre-tax Return on Equity	25.7%	18.2%	26.1%	27.5%	12.3%
Number of Firms	5,465	5,453	5,480	5,568	5,493

Figures may not add due to rounding.

<sup>1/</sup> Calendar, rather than fiscal, year data is reported in this table.

<sup>2/</sup> Registered representatives' compensation for firms that neither carry nor clear is included in "other expenses" as this expense item is not reported separately on Part IIA of the FOCUS Report.

Source: FOCUS Report

Table 7  
**UNCONSOLIDATED BALANCE SHEET FOR BROKER-DEALERS  
DOING A PUBLIC BUSINESS**  
**YEAR-END, 1997 – 2001 1/**  
(\$ in Millions)

	1997	1998	1999	2000	2001
<b>Assets</b>					
Cash	\$ 23,309.3	\$ 27,219.1	\$ 30,915.7	\$ 33,472.4	\$ 50,722.9
Receivables from Other					
Broker-dealers	590,731.7	713,732.3	828,208.0	974,675.6	1,115,382.5
Receivables from Customers	118,185.0	135,249.8	205,904.5	203,704.3	177,944.3
Receivables from Non-customers	11,852.2	16,814.2	21,277.9	31,411.0	15,392.7
Long Positions in Securities and Commodities	495,217.4	469,526.9	529,931.2	614,927.6	775,941.9
Securities and Investments not Readily Marketable	8,026.5	8,651.0	10,566.6	9,845.9	10,486.6
Securities Purchased Under Agreements to Resell (Part II only) 2/	715,948.9	638,655.5	682,466.4	724,666.3	855,539.3
Exchange Membership	541.5	562.1	580.8	588.6	664.6
Other Assets 2/	46,786.7	84,060.9	79,596.8	120,788.9	212,798.3
<b>Total Assets</b>	<b>\$2,010,599.3</b>	<b>\$2,094,471.8</b>	<b>\$2,389,447.9</b>	<b>\$2,714,080.5</b>	<b>\$3,214,873.2</b>
<b>Liabilities and Equity Capital</b>					
Bank Loans Payable	\$ 38,298.1	\$ 46,524.7	\$ 58,190.5	\$ 80,745.4	\$ 75,897.2
Payables to Other Broker-dealers	263,879.7	314,940.5	415,101.0	473,215.1	562,210.8
Payables to Non-customers	26,334.0	36,306.8	40,916.5	50,748.0	56,710.4
Payables to Customers	187,839.5	238,677.3	282,996.0	359,818.6	391,358.5
Short Positions in Securities and Commodities	246,437.4	222,526.7	287,946.6	286,545.8	342,189.9
Securities Sold Under Repurchase Agreements (Part II only) 2/	991,752.6	923,300.4	973,524.9	1,092,436.3	1,282,754.8
Other Non-subordinated Liabilities 2/	132,295.6	169,472.6	166,699.4	182,476.9	306,860.4
Subordinated Liabilities	47,422.6	53,913.5	58,813.2	63,436.1	67,304.5
<b>Total Liabilities</b>	<b>\$1,934,259.4</b>	<b>\$2,005,662.4</b>	<b>\$2,284,188.2</b>	<b>\$2,589,422.2</b>	<b>\$3,085,286.3</b>
<b>Equity Capital</b>	<b>\$ 76,339.9</b>	<b>\$ 88,809.4</b>	<b>\$ 105,259.7</b>	<b>\$ 124,658.3</b>	<b>\$ 129,586.9</b>
<b>Number of firms</b>	<b>5,465</b>	<b>5,453</b>	<b>5,480</b>	<b>5,568</b>	<b>5,493</b>

Figures may not add due to rounding.

1/ Calendar, rather than fiscal, year data is reported in this table.

2/ Resale agreements and repurchase agreements for firms that neither carry nor clear are included in "other assets" and "other non-subordinated liabilities," respectively, as these items are not reported separately on Part IIA of the FOCUS Report.

Source: FOCUS Report

**Table 8**  
**UNCONSOLIDATED REVENUES AND EXPENSES FOR**  
**CARRYING/CLEARING BROKER-DEALERS 1/**  
**(\$ in Millions)**

	2000		2001		Percent Change 2000-2001
	Dollars	Percent of Total Revenues	Dollars	Percent of Total Revenues	
<u>Revenues</u>					
Securities Commissions	\$ 36,814.6	13.5%	\$ 30,408.7	13.6%	-17.4%
Gains (Losses) in Trading and Investment Accounts	50,172.3	18.3	28,447.0	12.8	-43.3
Profits (Losses) from Under- writing and Selling Groups	17,406.0	6.4	16,209.3	7.3	-6.9
Margin Interest	24,274.0	8.9	13,749.1	6.2	-43.4
Revenues from Sale of Invest- ment Company Shares	10,810.3	4.0	8,672.7	3.9	-19.8
Miscellaneous Fees	16,770.7	6.1	14,087.1	6.3	-16.0
Revenues from Research	252.9	0.1	171.1	0.1	-32.3
Other Securities Related Revenues	109,888.7	40.2	88,622.3	39.8	-19.4
Commodities Revenues	- 8,912.2	-3.3	5,652.2	2.5	NA
All Other Revenues	16,161.4	5.9	16,849.7	7.6	4.3
<b>Total Revenues</b>	<b>\$273,638.7</b>	<b>100.0%</b>	<b>\$222,869.2</b>	<b>100.0%</b>	<b>-18.6%</b>
<u>Expenses</u>					
Registered Representatives' Compensation	\$ 33,162.0	12.1%	\$ 29,948.6	13.4%	-9.7%
Other Employee Compensation and Benefits	40,755.3	14.9	35,750.2	16.0	-12.3
Compensation to Partners and Voting Stockholder Officers	2,587.5	0.9	2,349.8	1.1	-9.2
Commissions and Clearance Paid to Other Brokers	6,441.7	2.4	5,899.0	2.6	-8.4
Communications	5,891.9	2.2	5,851.6	2.6	-0.7
Occupancy and Equipment Costs	7,441.7	2.7	8,371.6	3.8	12.5
Data Processing Costs	3,664.4	1.3	3,573.6	1.6	-2.5
Interest Expenses	124,453.3	45.5	94,365.3	42.3	-24.2
Regulatory Fees and Expenses	907.0	0.3	1,039.1	0.5	14.6
Losses in Error Accounts and Bad Debts	923.9	0.3	699.3	0.3	-24.3
All Other Expenses	25,041.2	9.2	22,876.9	10.3	-8.6
<b>Total Expenses</b>	<b>\$251,269.9</b>	<b>91.8%</b>	<b>\$210,725.0</b>	<b>94.6%</b>	<b>-16.1%</b>
<u>Income and Profitability</u>					
Pre-tax Income	\$ 22,368.9	8.2%	\$ 12,144.2	5.4%	-45.7%
Pre-tax Profit Margin	8.2%		5.4%		
Pre-tax Return on Equity	25.0%		12.4%		
Number of Firms	660		634		

Figures may not add due to rounding.

1/ Calendar, rather than fiscal, year data is reported in this table.

Note: Includes information for firms doing a public business that carry customer accounts or clear securities transactions.

Source: FOCUS Report



**Table 9**  
**UNCONSOLIDATED BALANCE SHEET FOR CARRYING/CLEARING**  
**BROKER-DEALERS 1/**  
**(\$ in Millions)**

	2000		2001		Percent Change 2000-2001
	Dollars	Percent of Total Assets	Dollars	Percent of Total Assets	
<b>Assets</b>					
Cash	\$ 30,180.4	1.2%	\$ 46,931.2	1.5%	55.5%
Receivables from Other Broker-dealers	943,974.2	36.1	1,091,721.0	34.9	15.7
(a) Securities Failed to Deliver	19,228.4	0.7	94,031.3	3.0	389.0
(b) Securities Borrowed	876,204.6	33.5	949,334.2	30.3	8.3
(c) Other	48,541.2	1.9	48,355.5	1.5	-0.4
Receivables from Customers	203,704.3	7.8	177,944.3	5.7	-12.6
Receivables from Non-customers	30,422.0	1.2	14,568.5	0.5	-52.1
Long Positions in Securities and Commodities	563,132.6	21.5	737,335.1	23.6	30.9
(a) Bankers Acceptances, Certificates of Deposit and Commercial Paper	38,015.0	1.5	46,767.5	1.5	23.0
(b) U.S. and Canadian Government Obligations	296,305.5	11.3	411,970.5	13.2	39.0
(c) State and Municipal Government Obligations	11,287.8	0.4	19,009.3	0.6	68.4
(d) Corporate Obligations	96,972.4	3.7	137,466.3	4.4	41.8
(e) Stocks and Warrants	74,400.9	2.8	81,395.3	2.6	9.4
(f) Options	15,747.1	0.6	9,474.9	0.3	-39.8
(g) Arbitrage	22,817.6	0.9	15,763.9	0.5	-30.9
(h) Other Securities	7,578.3	0.3	15,483.8	0.5	104.3
(i) Spot Commodities	8.1	0.0	3.7	0.0	-54.3
Securities and Investments Not Readily Marketable	8,687.6	0.3	9,306.9	0.3	7.1
Securities Purchased Under Agreements to Resell	724,666.3	27.7	855,539.3	27.3	18.1
Exchange Membership	504.5	0.0	573.0	0.0	13.6
Other Assets	109,060.2	4.2	196,591.6	6.3	80.3
<b>Total Assets</b>	<b>\$2,614,332.1</b>	<b>100.0%</b>	<b>\$3,130,511.0</b>	<b>100.0%</b>	<b>19.7%</b>
<b>Liabilities and Equity Capital</b>					
Bank Loans Payable	\$ 80,639.8	3.1%	\$ 75,740.7	2.4%	-6.1%
Payables to Other Broker-dealers	448,502.6	17.2	536,412.7	17.1	19.6
(a) Securities Failed to Receive	17,570.6	0.7	93,124.9	3.0	430.0
(b) Securities Loaned	395,508.1	15.1	409,737.6	13.1	3.6
(c) Other	35,424.2	1.4	33,550.1	1.1	-5.3
Payables to Non-customers	49,835.4	1.9	55,551.8	1.8	11.5
Payables to Customers	359,818.6	13.8	391,358.5	12.5	8.8
Short Positions in Securities and Commodities	249,676.0	9.6	324,947.7	10.4	30.1
Securities Sold Under Repurchase Agreements	1,092,436.3	41.8	1,282,754.8	41.0	17.4
Other Non-subordinated Liabilities	177,031.1	6.8	297,442.1	9.5	68.0
Subordinated Liabilities	61,015.0	2.3	65,228.5	2.1	6.9
<b>Total Liabilities</b>	<b>\$2,518,955.1</b>	<b>96.4%</b>	<b>\$3,029,436.8</b>	<b>96.8%</b>	<b>20.3%</b>
Equity Capital	\$ 95,377.0	3.6%	\$ 101,074.20	3.2%	6.0%
Number of Firms	660		634		

Figures may not add due to rounding.

1/ Calendar, rather than fiscal, year data is reported in this table.

Note: Includes information for firms doing a public business that carry customer accounts or clear securities transactions.

Source: FOCUS Report

**Table 10**  
**MARKET VALUE OF EQUITY/OPTIONS SALES ON U.S. EXCHANGES <sup>1/</sup>**  
**(\$ in Thousands)**

	Total Market Value	Stocks <sup>2/</sup>	Warrants	Rights	Equity Options		Non-Equity Options <sup>3/</sup>	
					Traded	Exercised		
All Registered Exchanges for Past Six Years								
Calendar Year:	1996	4,719,336,203	4,510,874,989	869,986	34,861	67,861,575	59,451,448	80,243,345
	1997	6,855,461,663	6,559,348,106	616,256	27,363	104,535,151	76,475,307	114,459,480
	1998	8,662,523,260	8,307,341,289	740,879	73,341	140,260,828	85,290,488	128,816,435
	1999	11,131,739,431	10,680,428,325	677,469	256,984	260,293,772	56,857,793	133,225,088
	2000	14,341,711,034	13,690,731,156	488,103	122,822	481,440,134	23,268,706	145,660,113
	2001	13,126,460,534	12,749,906,857	208,824	118,689	258,885,410	6,399,858	110,940,896
Breakdown of 2001 Data by Registered Exchanges								
All Registered Exchanges								
Exchanges:	AMEX	883,734,490	806,618,941	9,327	3,897	71,275,085	3,148,657	2,678,583
	BSE	222,192,612	222,192,612	0	0	0	0	0
	CHX	702,250,513	702,250,513	0	0	0	0	0
	CSE	158,373,257	158,373,257	0	0	0	0	0
	NYSE	10,737,513,380	10,737,199,475	199,112	114,792	0	0	0
	PSE	95,629,315	46,394,051	374	0	48,677,247	557,642	0
	PHLX	129,799,279	76,878,006	10	0	47,234,030	739,759	4,947,474
	CBOE	196,967,687	0	0	0	91,699,048	1,953,800	103,314,839

Figures may not sum due to rounding.

<sup>1/</sup> Data on the value and volume of equity security sales is reported in connection with fees paid under Section 31 of the Securities Exchange Act of 1934 as amended by the Securities Acts Amendments of 1975. It covers odd-lot as well as round-lot transactions.

<sup>2/</sup> Includes voting trust certificates, certificate of deposit for stocks, and American Depositary Receipts for stocks but excludes rights and warrants.

<sup>3/</sup> Includes all exchange trades of call and put options in stock indices, interest rates, and foreign currencies.

Source: SEC Form R-31 and Options Clearing Corporation Statistical Report.

Table 11  
**VOLUME OF EQUITY/OPTIONS SALES ON U.S. SECURITIES EXCHANGES 1/**  
 (Data in Thousands)

		Stocks 2/ (Shares)	Warrants (Units)	Rights (Units)	Equity Options		Non-Equity Options 3/ (Contracts)
					Traded (Contracts)	Exercised (Contracts)	
All Registered Exchanges for Past Six Years							
Calendar Year:	1996	125,746,598	136,314	39,666	199,117	12,446	95,680
	1997	159,712,233	87,153	57,288	272,999	15,901	80,824
	1998	206,425,002	66,041	329,502	329,642	14,603	76,701
	1999	244,137,857	52,485	30,610	444,765	12,219	63,126
	2000	317,698,364	28,204	21,377	665,306	4,597	53,856
	2001	371,677,356	27,102	49,779	657,326	1,613	58,582
Breakdown of 2001 Data by Registered Exchanges							
All Registered Exchanges							
Exchanges:	AMEX*	15,329,445	15,650	918	203,942	666	1,221
	BSE*	7,294,456	0	0	0	0	0
	CHX	27,307,093	0	0	0	0	0
	CSE*	4,456,293	0	0	0	0	0
	NYSE*	313,357,994	11,417	48,861	0	0	0
	PSE	1,530,193	34	0	102,702	194	0
	PHLX*	2,401,882	1	0	96,360	251	5,015
	CBOE*	0	0	0	254,322	503	52,346

Figures may not sum due to rounding.

\* Data of those exchanges marked with asterisk covers transactions cleared during the calendar month; clearance usually occurs within five days of the execution of a trade. Data of other exchanges covers transactions effected on trade dates falling within the reporting month.

1/ Data on the value and volume of equity security sales is reported in connection with fees paid under Section 31 of the Securities Exchange Act of 1934 as amended by the Securities Acts Amendments of 1975. It covers odd-lot as well as round-lot transactions.

2/ Includes voting trust certificates, certificate of deposit for stocks, and American Depositary Receipts for stocks but excludes rights and warrants.

3/ Includes all exchange trades of call and put options in stock indices, interest rates, and foreign currencies.

Source: SEC Form R-31 and Options Clearing Corporation Statistical Report.

Table 12  
**SHARE VOLUME BY EXCHANGES <sup>1/</sup>**  
**(In Percentages)**

Year	Total Share Volume (in Thousands)	NYSE	AMEX	CHX	PSE	PHLX	BSE	CSE	Others <sup>2/</sup>
1945	769,018	65.87	21.31	1.77	2.98	1.06	0.66	0.05	6.30
1950	893,320	76.32	13.54	2.16	3.11	0.97	0.65	0.09	3.16
1955	1,321,401	68.85	19.19	2.09	3.08	0.85	0.48	0.05	5.41
1960	1,441,120	68.47	22.27	2.20	3.11	0.88	0.38	0.04	2.65
1965	2,671,012	69.90	22.53	2.63	2.33	0.81	0.26	0.05	1.49
1970	4,834,887	71.28	19.03	3.16	3.68	1.63	0.51	0.02	0.69
1975	6,376,094	80.99	8.97	3.97	3.26	1.54	0.85	0.13	0.29
1980	15,587,986	79.94	10.78	3.84	2.80	1.54	0.57	0.32	0.21
1985	37,187,567	81.52	5.78	6.12	3.66	1.47	1.27	0.15	0.03
1990	53,746,087	81.86	6.23	4.68	3.16	1.82	1.71	0.53	0.01
1991	58,290,641	82.01	5.52	4.66	3.59	1.60	1.77	0.86	0.01
1992	65,705,037	81.34	5.74	4.62	3.19	1.72	1.57	1.83	0.01
1993	83,056,237	82.90	5.53	4.57	2.81	1.55	1.47	1.17	0.00
1994	90,786,603	84.55	4.96	3.88	2.37	1.42	1.39	1.42	0.01
1995	107,069,656	84.49	4.78	3.67	2.56	1.39	1.45	1.66	0.00
1996	125,922,577	85.95	4.29	3.37	2.40	1.28	1.29	1.42	0.00
1997	159,856,674	86.85	3.88	3.75	2.01	1.09	1.24	1.18	0.00
1998	206,820,545	86.67	3.71	4.57	1.92	0.79	1.52	0.82	0.00
1999	244,220,952	85.07	3.55	5.89	2.01	0.72	1.80	0.96	0.00
2000	317,747,944	83.64	3.76	7.58	1.28	0.70	1.78	1.27	0.00
2001	371,754,237	84.31	4.13	7.35	0.41	0.65	1.96	1.20	0.00

<sup>1/</sup> Share volume for exchanges includes stocks, rights, and warrants; calendar, rather than fiscal, year data is reported in this table.

<sup>2/</sup> Includes all exchanges not listed individually.

Source: SEC Form R-31

**Table 13**  
**DOLLAR VOLUME BY EXCHANGES 1/**  
**(In Percentages)**

Year	Total Dollar Volume (in Thousands)	NYSE	AMEX	CHX	PSE	PHLX	BSE	CSE	Others 2/
1945	\$ 16,284,552	82.75	0.81	2.00	1.78	0.96	1.16	0.06	0.48
1950	21,808,284	85.91	6.85	2.35	2.19	1.03	1.12	0.11	0.44
1955	38,039,107	86.31	6.98	2.44	1.90	1.03	0.78	0.09	0.47
1960	45,309,825	83.80	9.35	2.72	1.94	1.03	0.60	0.07	0.49
1965	89,549,093	81.78	9.91	3.44	2.43	1.12	0.42	0.08	0.82
1970	131,707,946	78.44	11.11	3.76	3.81	1.99	0.67	0.03	0.19
1975	157,256,676	85.20	3.67	4.64	3.26	1.73	1.19	0.17	0.14
1980	476,500,688	83.53	7.33	4.33	2.27	1.61	0.52	0.40	0.01
1985	1,200,127,848	85.25	2.23	6.59	3.06	1.49	1.20	0.18	0.00
1990	1,616,798,075	86.15	2.33	4.58	2.77	1.79	1.63	0.74	0.00
1991	1,778,154,074	86.20	2.31	4.34	3.05	1.54	1.72	0.83	0.01
1992	2,032,684,135	86.47	2.07	4.28	2.87	1.70	1.52	1.09	0.00
1993	2,610,504,390	87.21	2.08	4.10	2.38	1.52	1.35	1.37	0.00
1994	2,817,671,150	88.08	2.01	3.49	2.09	1.34	1.31	1.68	0.00
1995	3,507,991,171	87.71	2.10	3.26	2.24	1.27	1.43	1.99	0.00
1996	4,511,779,836	88.91	1.91	3.01	2.03	1.19	1.32	1.63	0.00
1997	6,559,991,725	89.13	2.13	3.25	1.87	1.01	1.23	1.38	0.00
1998	8,308,155,509	87.57	3.37	3.93	1.79	0.79	1.58	0.98	0.00
1999	10,681,362,778	85.08	4.18	5.06	1.93	0.65	2.04	1.06	0.00
2000	13,691,342,081	81.93	5.53	7.58	1.19	0.62	1.87	1.26	0.01
2001	12,750,234,370	84.20	6.30	5.50	0.40	0.60	1.74	1.24	0.00

1/ Dollar volume for exchanges includes stocks, rights, and warrants; calendar, rather than fiscal, year data is reported in this table.

2/ Includes all exchanges not listed individually.

Source: SEC Form R-31

Table 14  
SECURITIES LISTED ON EXCHANGES 1/  
December 31, 2001

EXCHANGE	COMMON		PREFERRED		BONDS		TOTAL SECURITIES	
	Market Value Number	(in Millions)	Market Value Number	(in Millions)	Value 2/ Number	(in Millions)	Value Number	(in Millions)
Registered:								
Domestic Securities								
American	652	77,416	79	5,448	530	0	1,261	82,864
Boston	64	5,317	0	0	0	0	64	5,317
Cincinnati	0	0	0	0	0	0	0	0
Chicago	6	183	0	0	0	0	6	183
New York	2,050	11,102,124	361	24,083	1,251	2	3,662	11,126,209
Pacific	23	3,640	2	74	2	45	27	3,759
Philadelphia	2	157	11	65	0	0	13	222
Total	2,797	11,188,837	453	29,670	1,783	47	5,033	11,218,554
Includes Foreign Stocks:								
New York	461	564,054	56	23,446	196	65,387	713	652,887
American	50	20,145	0	0	1	0	51	20,145
Boston	6	93	0	0	0	0	6	93
Chicago	0	0	0	0	0	0	0	0
Pacific	3	105	0	0	0	0	3	105
Philadelphia	0	0	0	0	0	0	0	0
Total	520	584,397	56	23,446	197	65,387	773	673,230

Figures may not sum due to rounding

1/ Excludes securities that were suspended from trading at the end of the year and securities that, because of inactivity, had no available quotes.

2/ Principal value for all exchanges, except Philadelphia (PHLX). PHLX could provide only market value. The American and New York exchanges no longer can provide market values for bonds.

Source: SEC Form 1392

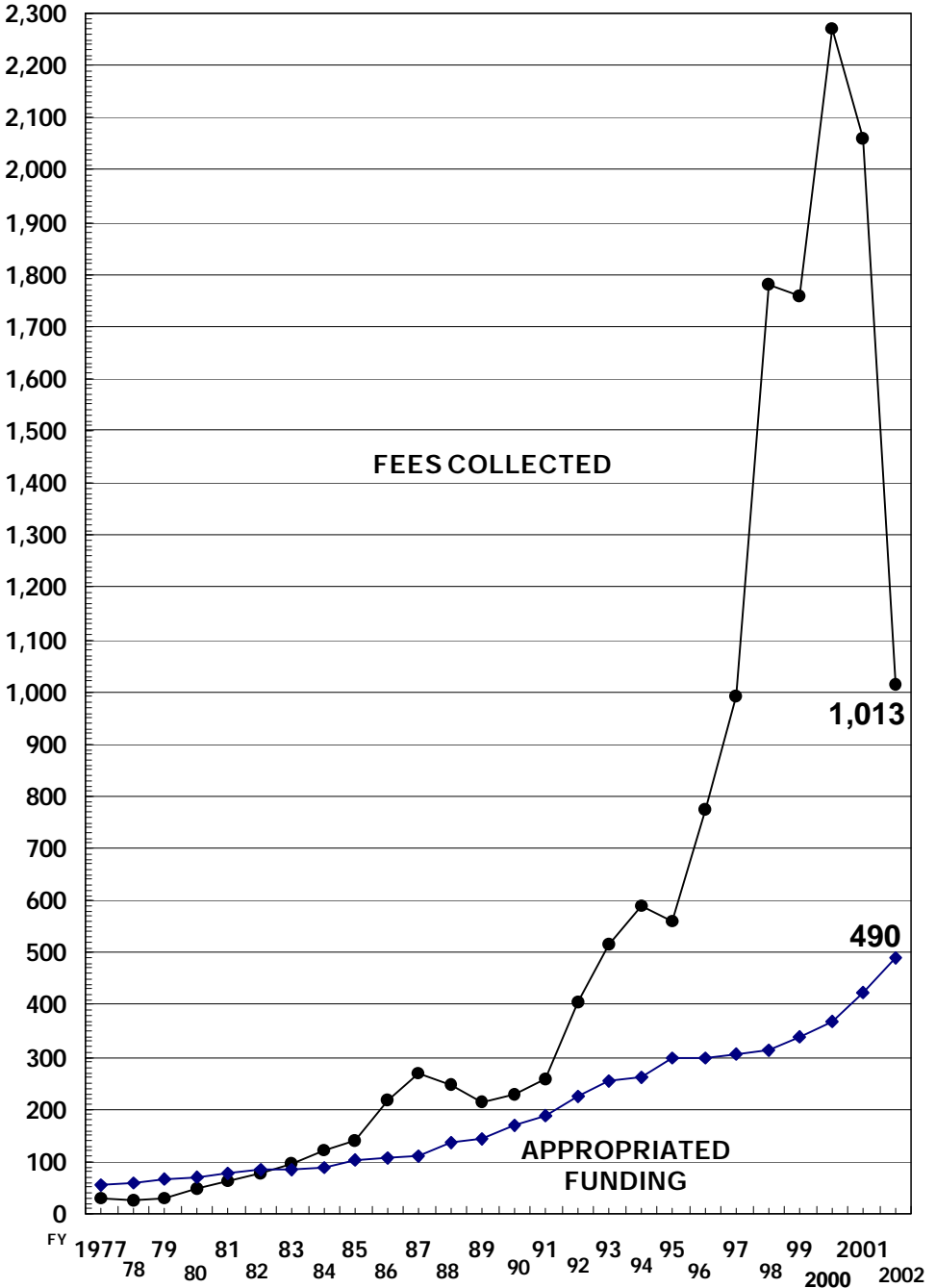
Table 15  
 VALUE OF STOCKS LISTED ON EXCHANGES  
 (\$ in Billions)

As of Dec 31	New York Stock Exchange	American Stock Exchange	Exclusively On Other Exchanges	Total
1940	\$ 46.5	\$ 10.1	\$ .....	\$ 56.6
1945	73.8	14.4	.....	88.2
1950	93.8	13.9	3.3	111.0
1955	207.7	27.1	4.0	238.8
1960	307.0	24.2	4.1	335.3
1965	537.5	30.9	4.7	573.1
1970	636.4	39.5	4.8	680.7
1975	685.1	29.3	4.3	718.7
1980	1,242.8	103.5	2.9	1,349.2
1985	1,882.7	63.2	5.9	1,951.8
1990	2,692.1	69.9	3.9	2,765.9
1991	3,547.5	90.3	4.3	3,642.1
1992	3,877.9	86.4	5.9	3,970.2
1993	4,314.9	98.1	7.2	4,420.2
1994	4,240.8	86.5	4.7	4,332.0
1995	5,755.5	113.3	6.8	5,875.6
1996	6,947.7	106.2	5.7	7,059.6
1997	9,413.1	131.3	3.6	9,548.0
1998r	10,384.8	149.7	4.7	10,539.2
1999	11,556.2	82.5	6.7	11,645.4
2000	11,633.0	94.4	4.7	11,732.1
2001	11,126.2	82.9	9.4	11,218.6

Source: SEC Form 1392

Table 16  
 APPROPRIATED FUNDS vs FEES\* COLLECTED

\$ Millions



\* Excludes disgorgements from fraud actions.



Table 17  
BUDGET ESTIMATES AND APPROPRIATIONS

Action	Fiscal 1998		Fiscal 1999		Fiscal 2000		Fiscal 2001		Fiscal 2002	
	Positions	\$000	Positions	\$000	Positions	\$000	Positions	\$000	Positions	\$000
Estimate Submitted to the Office of Management and Budget	3,039	\$317,412	2,827	\$339,098	2,946	\$367,800	3,296	\$430,600	3,540	\$563,063
Action by the Office of Management and Budget	...	...	...	+2,000	+197	-7,000	-11	-7,800	-312	-125,163
President's Request	3,039	\$317,412	2,827	\$341,098	3,143	\$360,800	3,285	\$422,800	3,228	\$437,900
Action by the House of Representatives	...	-2,412	...	-17,098	...	-36,800	-50	-30,176	...	...
Subtotal	3,039	315,000	2,827	324,000	3,143	324,000	3,235	392,624	3,228	437,900
Action by the Senate	...	+2,412	+274	+17,098	...	+46,800	+50	+97,028	+57	+76,147
Subtotal	3,039	317,412	3,101	341,098	3,143	370,800	3,285	489,652	3,285	514,047
Action by Conferees	...	-2,412	...	-11,098	+50	-3,000	...	-66,852	-57	-76,147
Annual Appropriation	3,039	315,000	3,101	330,000	3,193	367,800	3,285	422,800	3,228	437,900
Supplemental Appropriation	...	...	...	+8,175	...	+500	...	...	+125	+51,605 <sup>4/</sup>
Sequestration / Other	...	...	...	-458	...	...	...	...	...	-336
Use of Prior Year Unobligated Balances	...	+5,100 <sup>1/</sup>	...	+18,357 <sup>2/</sup>	+42	+14,100 <sup>3/</sup>	...	+4,472 <sup>1/</sup>	...	+25,943 <sup>5/</sup>
Total Funding Level	3,039	320,100	3,101	356,074	3,235	382,400	3,285	427,272	3,353	515,112

<sup>1/</sup> Represents spending authority for EDGAR modernization.

<sup>2/</sup> Includes \$14,500 for 3-year EDGAR modernization and \$3,857 from prior year recoveries.

<sup>3/</sup> Includes \$5,400 for EDGAR modernization and \$8,700 reprogramming.

<sup>4/</sup> Includes \$20,705 for 9-11 disaster recovery and \$30,900 supplemental.

<sup>5/</sup> Includes \$1,123 for EDGAR modernization and \$24,820 reprogramming.

# U.S. Securities and Exchange Commission

