UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDINGS RULINGS
Release No. 744 / February 1, 2013

ADMINISTRATIVE PROCEEDING
File No. 3-15127

In the Matter of	:	
	:	ORDER REGARDING
J. KENNETH ALDERMAN, CPA,	:	MOTION TO COMPEL AND
ET AL.	:	MOTION TO DISMISS
	:	

On December 10, 2012, the Securities and Exchange Commission (Commission) initiated this proceeding with an Order Instituting Public Administrative and Cease-and-Desist Proceedings (OIP), pursuant to Sections 9(b) and 9(f) of the Investment Company Act of 1940 (Investment Company Act). The hearing is scheduled to commence April 2, 2013.

Pending before me is the Motion to Compel (Motion to Compel) filed on January 8, 2013 by Respondents Jack R. Blair, Albert C. Johnson, CPA, James Stillman R. McFadden, W. Randall Pitman, CPA, Mary S. Stone, CPA, and Archie W. Willis III (collectively, the Independent Directors). The Division of Enforcement (Division) filed an Opposition (filed under seal) (Oppo. to Compel) on January 11, 2013, the Independent Directors filed a Reply (Reply to Compel) on January 14, 2013, and the Division filed a Surreply (Surreply) on January 23, 2013.

Also pending before me is the Motion to Dismiss (Motion to Dismiss) filed on January 3, 2013 by Respondents J. Kenneth Alderman, CPA, and Allen B. Morgan, Jr. (collectively, the Inside Directors), in which the Independent Directors joined. The Division filed an Opposition (Oppo. to Dismiss) on January 8, 2013, to which was attached the Declaration of William P. Hicks (Hicks Declaration), and the Inside Directors filed a Reply (Reply to Dismiss) on January 11, 2013. The Independent Directors filed no separate Reply.

For the reasons discussed below, I GRANT IN PART and DENY IN PART the Motion to Compel, and DENY the Motion to Dismiss.

ALLEGATIONS OF THE OIP

The OIP alleges, in sum and substance, as follows. The eight Inside Directors and Independent Directors (collectively, the Directors) constituted the boards of directors for five

registered investment companies affiliated with Morgan Keegan & Company, Inc. OIP, pp. 1-3. As of March 31, 2007, the five registered investment companies (the Funds) held securities with a combined net asset value (NAV) of approximately $3.85 billion. Id., p. 4. Four of the Funds were closed-end, and one was open-end. Id., p. 3. A substantial portion of the Funds' investments were in subordinated tranches of various securitizations, including mortgage-backed securities, for which market quotations were not readily available between January 2007 and August 2007 (Relevant Period). Id., p. 4. Consequently, a large proportion of the Funds' portfolios had to be periodically valued based on fair value, that is, based on good faith valuation procedures established and overseen by the Directors. Id., pp. 2, 4.

According to Accounting Series Release No. 118, Investment Company Act Release No. 6295 (Dec. 23, 1970) (ASR 118), under such circumstances, the Directors must determine the method of arriving at the fair value of each security, may appoint persons to assist them in that determination and to make the actual calculation, and must continuously review the appropriateness of the method used in valuing each security. OIP, p. 2. The Directors did not so determine a fair valuation method, nor did they continuously review any such method's appropriateness. Id. Instead, they delegated those duties to a fair valuation committee, without providing the committee any meaningful guidance, and did not even bother to learn how fair values were being determined. Id. As a result, the NAVs of the Funds were materially misstated from at least March 31, 2007 to August 9, 2007. Id., p. 9.

MOTION TO COMPEL

There have been multiple investigations involving the Funds, including Morgan Asset Management, A-3042 (A-3042), a resolved proceeding alleging manipulation of prices for Funds securities, Trading in the Securities of Morgan Keegan Select Fund, A-3192 (A-3192), an unresolved proceeding alleging insider trading, and, of course, the investigation leading to the present proceeding. Morgan Asset Management, Exchange Act Release No. 64720 (Jun. 22, 2011), 101 SEC Docket 42608; Oppo. to Compel, pp. 1-2. The Independent Directors state that they provided investigative testimony in A-3192, and allege that the investigation leading to the present proceeding resulted from a tip. Motion to Compel, pp. 1, 3. They now move to compel production of all material in the A-3192 file that "relates or refers in any way to the Independent Directors, to valuation of securities, or to management of the Funds' portfolios, including any information provided to the Division or to [the Office of Compliance, Inspections, and Examinations] by third parties," and "all information relating to supposed misvaluation . . . whether from the Morgan Keegan entities or from other sources." Motion to Compel, p. 3; Reply to Compel, p. 1.

In response, the Division has agreed to produce, or has produced: (1) documents received in A-3192 from Morgan Keegan & Company, Inc. and related entities, (2) the A-3192 investigative testimony of Respondent Alderman, the only Director who testified in A-3192, (3) the A-3042 investigative file, (4) the investigative file for another investigation that has apparently not led to any enforcement actions, (5) all subpoenas issued in A-3192 except for those issued to telecommunications providers, (6) all documents in the Division's possession received in response to said subpoenas, (7) all investigative exhibits marked in A-3192, (8) a recorded conversation between a Morgan Keegan customer and a Morgan Keegan broker, and

(9) all correspondence accompanying the productions referenced in items (6) and (8) above. Oppo. to Compel, pp. 2-3; Surreply, pp. 2-3.[1] The Division represents that all other documents received in A-3192 were provided by third parties, and relate to trading by those parties rather than valuation issues, and that the documents received in A-3192 played no part in the Division's recommendation to institute the present proceeding. Oppo. to Compel, p. 3.

The Division has agreed to produce those portions of the A-3192 investigative file – namely, the documents received from Morgan Keegan and related entities – which presumably contain information pertaining to "valuation of securities" held by the Funds, and I will order that the Division furnish these to the Independent Directors. Motion to Compel, p. 3. I will also order that the Division furnish the other categories of evidence that they have agreed to produce.

The Independent Directors have failed to sufficiently explain why any other documents obtained by the Division in an insider trading investigation would have any relevance to a proceeding alleging misvaluation of the Funds' NAVs. Documents that refer or relate to the Independent Directors, or to management of the Funds' portfolios, and information provided to the Division or to other Commission components by third parties, do not necessarily have any bearing on this proceeding, nor have the Independent Directors adequately explained what bearing they may have. That the investigation leading to this proceeding began with a tip does not necessarily mean that the details of the tip are legally relevant, and to disclose such details may chill future tipsters from providing useful information to the Commission. Respondents argue that the requested documents are relevant to prove estoppel, but I have stricken their estoppel defense. J. Kenneth Alderman, CPA, Administrative Proceedings Rulings Release No. 743 (Feb. 1, 2013).

The Division is reminded of its continuing duty to disclose material exculpatory evidence pursuant to Brady v. Maryland, 373 U.S. 83 (1963), and its progeny. See 17 C.F.R. § 201.230(b)(2).

I note that the Division filed its Opposition and Surreply under seal. Oppo. to Compel, p. 1. It is not obvious why these filings deserve such treatment, and the Division has not filed a motion for a protective order pursuant to the Commission's Rule of Practice 322 (Rules) or otherwise made the showing required by Rule 322(b). See 17 C.F.R. § 201.322. Accordingly, if the Division desires to continue to extend confidential treatment to its Opposition and Surreply, it shall file a motion for protective order pursuant to Rule 322 no later than February 8, 2013.

MOTION TO DISMISS

All Respondents have moved to dismiss this case. The Federal Rules of Civil Procedure (FRCP) provide several avenues for dismissal, including: lack of personal jurisdiction (FRCP 12(b)(2)), improper venue (FRCP 12(b)(3)), insufficient service (FRCP 12(b)(4)), and insufficient service of process (FRCP 12(b)(5)). No analogous provisions appear to apply in

[1] Although the Commission's Rules of Practice do not contemplate or permit the filing of a Surreply, I have considered the Surreply in resolving the Motion to Compel because doing so works entirely to the advantage of the Respondents.

Commission administrative proceedings. The Commission's Rules of Practice permit the Chief Administrative Law Judge to discontinue a proceeding, but only upon motion by the Division and only for reasons not applicable here. See 17 C.F.R. § 200.30-10(a)(8). I have found no other provisions in the Rules even remotely analogous to FRCP 12(b), and the parties have not identified any.

Accordingly, I will construe the Motion to Dismiss as a motion for summary disposition. See Hudson Investors Fund, Inc., Administrative Proceedings Rulings Release No. 557 (Dec. 9, 1997), 66 SEC Docket 199. So construed, the facts of the pleadings of the party against whom the motion is made shall be taken as true, except as modified by stipulations or admissions made by that party, by uncontested affidavits, or by facts officially noticed pursuant to Rule 323. Id.; 17 C.F.R. § 201.323. A motion for summary disposition may be granted if there is no genuine issue with regard to any material fact and the party making the motion is entitled to summary disposition as a matter of law. See 17 C.F.R. § 201.250(b).

As the Division correctly notes, the Rules require my leave before filing a motion for summary disposition. 17 C.F.R. § 201.250; Oppo. to Dismiss, p. 1, n.1. However, the issues presented are straightforward and it is judicially efficient to decide the Motion to Dismiss now rather than later, so I will not deny the Motion to Dismiss on that basis.

Respondents present three arguments: the statute of limitations bars this proceeding, the Division failed to comply with Section 929U of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), and fairness and equity require dismissal. I consider each argument in turn.

A. Statute of Limitations

It is undisputed that Respondents agreed to toll the five-year statute of limitations for five months, in effect extending the statute of limitations period back to July 10, 2007. Motion to Dismiss, p. 1; Oppo. to Dismiss, pp. 4-5. The OIP alleges – and I take as true for present purposes – that fair valuation procedures were required, but not complied with, from January 2007 until some date in August 2007, and that the Funds' NAVs were materially misstated from March 31, 2007 until August 9, 2007. OIP, pp. 4, 9. The OIP further alleges that the failure to implement fair valuation procedures constituted a violation of Rule 38a-1 under the Investment Company Act (Rule 38a-1), and that the sale, redemption, or repurchase of redeemable securities at a price that is not the current NAV of such securities constituted a violation of Rule 22c-1 under the Investment Company Act (Rule 22c-1) as to the open-end Fund. Id., p. 9.

As alleged, the Rule 38a-1 violations were continuous for at least three weeks, from July 10, 2007 until the first day of August 2007. ASR 118, p. 3 (noting that there must be "continuous review" of fair valuation methodologies). Additionally, although no party has offered specific evidence on this point, it seems highly likely that the open-end Fund would have sold, redeemed, or repurchased at least some shares in the 30 days between July 10 and August 9, 2007, in violation of Rule 22c-1. A violation of either Rule is sufficient to warrant issuance of a cease-and-desist order. Central Capital Venture Corp., Exchange Act Release No. 67098 (Jun. 4, 2012), 103 SEC Docket 54781, 54784 (Rule 38a-1); Parnassus Investments, Initial Decision

Release No. 131 (Sep. 3, 1998), 67 SEC Docket 2760, 2788-89 (Rule 22c-1); Morgan Asset Management, 101 SEC Docket at 42623 (both). A violation of either Rule is also sufficient to warrant imposition of civil penalties. Morgan Asset Management, 101 SEC Docket at 42625; UBS Global Asset Management (Americas) Inc., Investment Company Act Release No. 29920 (Jan. 17, 2012), 102 SEC Docket 50276, 50281.

In view of the tolling agreements, therefore, the statute of limitations does not bar the present action. Respondents nonetheless argue that the entire OIP should be dismissed as time-barred. I am not persuaded.

Construing the OIP in the light most favorable to the Division, and taking its allegations as true, at least the claims for violations of Rules 38a-1 and 22c-1 did not accrue until the violations actually took place. As to Rule 38a-1, a violation occurred every day the Directors failed to implement fair valuation procedures, and as to Rule 22c-1, a violation occurred each time the open-end Fund's shares were sold, redeemed, or repurchased. That identical violations may have occurred prior to July 10, 2007, with the Commission's knowledge but without the Commission filing any responsive enforcement action, is not relevant to a determination of when the instant claims accrued. Because I have found that at least the claims which accrued between July 10, 2007 and August 2007 are not time-barred, I need not address the applicability of the continuing violations doctrine, whereby a claim is deemed to have accrued on the date a course of violative conduct ended. SEC v. Brown, 740 F. Supp. 2d 148, 158 (D.D.C. 2010); see also SEC v. Huff, 758 F. Supp. 2d 1288, 1339 (S.D. Fla. 2010) ("the 'continuing violations' doctrine tolls the statute of limitations for a claim that otherwise would be time-barred").

This analysis plainly applies with equal force both to any civil penalties, which the Division does not dispute are covered by the five-year statute of limitations established by 28 U.S.C. § 2462, and to any cease-and-desist order. Oppo. to Dismiss, pp. 4-5. It would plainly also apply to any other authorized sanction not addressed by the parties, such as an associational bar. Respondents' argument that a cease-and-desist order would operate as a penalty and is time-barred is thus beside the point; any cease-and-desist order could be based solely on conduct occurring within the limitations period, and dismissal based on the statute of limitations is not warranted.[2]

[2] Because Respondents argue that the OIP should be dismissed in its entirety, and only that it should be dismissed, I need not address the admissibility of evidence pertaining to conduct predating July 10, 2007, or whether and in what manner such evidence may be considered in evaluating liability and any potential sanctions. As one example, I need not address the appropriateness of a civil penalty for a securities sale violative of Rule 22c-1 and predating July 10, 2007. See Guy P. Riordan, Initial Decision Release No. 353 (Jul. 28, 2008), 93 SEC Docket 8408, 8425 (rejecting the continuing violations doctrine and relying only on violations occurring within the limitations period in evaluating civil penalties). Nor need I address whether the alleged Investment Company Act Rule 30a-3(a) violation and the alleged false registration statement violation are barred by the statute of limitations, because the parties do not argue each alleged violation separately. OIP, p. 9.

B. Dodd-Frank

Section 929U of Dodd-Frank, codified in Section 4E of the Securities Exchange Act of 1934, provides that "[n]ot later than 180 days after the date on which Commission staff provide a written Wells notification to any person, the Commission staff shall either file an action against such person or provide notice to the Director of the Division of Enforcement of its intent to not file an action." 15 U.S.C. § 78d-5(a)(1). However, Section 929U of Dodd-Frank also permits, in certain complex actions, the Director of the Division of Enforcement (Division Director), or his designee, to authorize a 180-day extension to the deadline upon notice to the Chairman of the Commission. See 15 U.S.C. § 78d-5(a)(2).

Respondents assert that the Division failed to institute this action within the 180-day time limit set forth in Dodd-Frank, and requests that the OIP be dismissed in its entirety. See 15 U.S.C. § 78d-5; Motion to Dismiss, pp. 11-13. Specifically, Respondents assert that the 180-day period expired because the written Wells notice was provided to them on May 2, 2012, seven months before the Commission issued this OIP. Motion to Dismiss, p. 12.

The Division contends that its Director authorized a 90-day extension to the deadline, and provided notice to the Chairman of the Commission, on October 12, 2012. Oppo. to Dismiss, p. 6; Hicks Declaration. The Hicks Declaration establishes that the Division Director complied with the notification and approval requirements set forth in Section 929U of Dodd-Frank, and that the deadline was extended until January 20, 2013. Hicks Declaration, p. 2. Respondents do not address this argument in their Reply. Reply to Dismiss.

I conclude that that there is no genuine issue of material fact, and that the Division Director properly authorized the extension of the deadline to bring this proceeding until January 20, 2013. Therefore, the proceeding was instituted within the period authorized by Dodd-Frank.

C. Fairness and Equity

Respondents argue that the Division "faces a difficult challenge in proving the equity of seeking injunctive relief against Respondents for alleged misconduct that concluded in August of 2007 and for which the Division's claims for civil penalties are time-barred." Motion to Dismiss, p. 11. Assuming that such a defense is available and is distinguishable from the defense of laches, and taking the facts pled by the Division as true, there exists a genuine issue of material fact as to whether it is fair and equitable to maintain this action. Summary disposition on this basis is therefore not appropriate.

ORDER

It is ORDERED that the Independent Directors' Motion to Compel is GRANTED IN PART AND DENIED IN PART as discussed above. The Division of Enforcement shall, no later than February 1, 2013, make available for inspection and copying the following categories of documents and exhibits: (1) documents received in A-3192 from Morgan Keegan & Company, Inc., and related entities, (2) the A-3192 investigative testimony of Respondent Alderman, (3) the A-3042 investigative file, (4) the investigative file for another investigation

that has apparently not led to any enforcement actions, (5) all subpoenas issued in A-3192 except for those issued to telecommunications providers, (6) all documents in the Division's possession received in response to said subpoenas, (7) all investigative exhibits marked in A-3192, (8) a recorded conversation between a Morgan Keegan customer and a Morgan Keegan broker, and (9) all correspondence accompanying the productions referenced in items (6) and (8) above.

It is further ORDERED that the Division of Enforcement shall, no later than February 8, 2013, file a motion for protective order pertaining to any filings it has made under seal in this proceeding. Failure to so file a motion for protective order will result in any sealed filings being unsealed.

It is further ORDERED that Respondents' Motion to Dismiss is DENIED.

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Cameron Elliot
Administrative Law Judge