

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 BEAR, STEARNS & CO. INC., :  
 :  
 : Defendant. :  
-----X  
-----X

Civil Action No.  
  
03 Civ. 2937 (WHP)

**RESPONSE OF PLAINTIFF  
SEC TO COMMENTARY  
OF THIRD PARTY  
INVESTOR PROTECTION  
TRUST**

SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 JACK BENJAMIN GRUBMAN, :  
 :  
 : Defendant. :  
-----X  
-----X

Civil Action No.  
  
03 Civ. 2938 (WHP)

SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 J.P. MORGAN SECURITIES INC., :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
  
03 Civ. 2939 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : LEHMAN BROTHERS, INC., :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2940 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : MERRILL LYNCH, PIERCE, FENNER & :  
 : SMITH INCORPORATED, :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2941 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : U.S. BANCORP PIPER JAFFRAY, INC., :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2942 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : UBS WARBURG LLC, :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2943 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : GOLDMAN, SACHS & CO., :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2944 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : CITIGROUP GLOBAL MARKETS, INC., F/K/A :  
 : SALOMON SMITH BARNEY INC., :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2945 (WHP)

-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : CREDIT SUISSE FIRST BOSTON LLC, :  
 : F/K/A CREDIT SUISSE FIRST BOSTON :  
 : CORPORATION, :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2946 (WHP)

-----X  
-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : HENRY McKELVEY BLODGET, :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2947 (WHP)

-----X  
-----X  
SECURITIES AND EXCHANGE COMMISSION, :  
 :  
 : Plaintiff, :  
 :  
 : - against - :  
 :  
 : MORGAN STANLEY & CO. INCORPORATED, :  
 :  
 : Defendant. :  
-----X

Civil Action No.  
03 Civ. 2948 (WHP)

-----X	:	
SECURITIES AND EXCHANGE COMMISSION,	:	
	:	Civil Action No.
Plaintiff,	:	
	:	04 Civ. 6909 (WHP)
– against –	:	
	:	
DEUTSCHE BANK SECURITIES INC.,	:	
	:	
Defendant.	:	
-----X	:	

-----X	:	
SECURITIES AND EXCHANGE COMMISSION,	:	
	:	Civil Action No.
Plaintiff,	:	
	:	04 Civ. 6910 (WHP)
– against –	:	
	:	
THOMAS WEISEL PARTNERS LLC,	:	
	:	
Defendant.	:	
-----X	:	

**I. INTRODUCTION**

On May 5, 2005, the SEC submitted for the Court’s consideration a proposed Order approving a new investor education plan. The new plan calls for the dissolution of the current investor education entity and the distribution of the federal portion of investor education funds to the NASD Investor Education Foundation.

On June 3, 2005, the Investor Protection Trust (“IPT”), an entity holding the states’ portion of investor education funds, submitted a “commentary” to the Court regarding the SEC’s new plan. The IPT criticized the SEC and the NASD Foundation and requested a portion of the federal investor education funds. The IPT’s concerns are unfounded and it should not receive any additional funds for investor education.

Given the structure of the settlement between the parties in these cases, the IPT should not receive the federal portion of the investor education funds. The apportionment of investor education funds between the federal and state regulators was the product of negotiations with the defendants. The states received their share of such funds and the IPT cannot now undo the settlement to claim the federal investor education funds.

The distribution of federal investor education funds to the NASD Foundation is consistent with the terms of the settlement, as it will result in the awarding of grants by an established entity with a proven track record and nation-wide scope. The IPT's allegation that the NASD Foundation is too closely aligned with the securities industry is without merit. The NASD Foundation is independent of the NASD, has strict guidelines protecting against industry influence, and also has pledged to have a majority of public board members.

The IPT is not a viable option for the receipt of the funds not only because of the structural limitations of the settlement, but because the IPT is not, as it claims, an established nation-wide investor education entity. Nor is it clear that the IPT "enjoys public confidence," as it claims. Ex. 1, Deborah Solomon, What's the Best Way to Invest in Teaching the U.S. to Invest?, Wall Street Journal, May 26, 2005, at C-1; Ex. 2, Tom Baxter, Jim Galloway, Cox Raises Profile at No Cost to Her or Taxpayers, The Atlanta Journal-Constitution, September 23, 2004, at C-2. Based on publicly available information, there are a number of other questions about the IPT's operation and use of funds that weigh against consideration of the IPT as a recipient of federal investor education funds.

The SEC has submitted a new investor education plan that is consistent with the intent of the settling parties, and will result in an effective, efficient, and expeditious distribution of investor education funds. The SEC respectfully requests that the Court approve the new plan.

## **II. DISCUSSION**

### **A. The Settlement Structure Precludes Giving The IPT Any Portion Of The Federal Investor Education Funds**

The \$55 million in federal investor education funds is the result of the Global Research Analyst Settlement between the SEC, NASD, the New York Stock Exchange and defendants. The NASD and NYSE authorized the federal investor education funds to be paid into the above-captioned actions, subject to a plan to be submitted to the Court by the SEC. The \$55 million includes \$25 million paid by Merrill Lynch for investor education purposes. Previously, the states settled with Merrill Lynch and obtained a \$100 million penalty with no funds earmarked for remedial purposes.

As part of the Global Research Analyst Settlement, the defendants also settled with state regulators and agreed to pay \$30 million to the states for investor education purposes. The states' portion of investor education funds is held by the IPT. The trustees of IPT are state securities regulators. The funds are allocated for investor education purposes on a state-by-state basis by population.

The apportionment of investor education funds between the federal and state regulators was the product of negotiations between the regulators and the defendants. Given this structured settlement, the federal portion of the investor education funds should not be distributed to the states, via the IPT. That was not the intent of the parties to the settlement, then or now. Evidently, the states recognize this fundamental fact, as they have recently sought to distance themselves from IPT's public campaign attacking the SEC. Ex. 3, Letter to the Editor, The Wall Street Journal, from North American Securities Administrators Association, Inc., May 27, 2005.

**B. The SEC Properly Exercised Its Discretion In Submitting A New Investor Education Plan Consistent With The Intent Of The Settling Parties**

In this governmental enforcement action it is for the SEC, not the IPT, to represent the investing public. As this Court has recognized, “the SEC, in its role as *parens patriae*, is presumed to represent the interests of the investing public aggressively and adequately.” SEC v. Bear Stearns & Co. Inc., 2003 U.S. Dist. LEXIS 14611 at \*9 (SDNY Aug. 25, 2003) (italics in original). The SEC has dutifully served the interests of the investing public in these cases. The IPT’s proposal would result not only in usurping the SEC’s recognized investor-protection role, but it would lead to confusion and delay. As this Court noted in a different context, in denying a motion by investors to intervene in this case, “opening the door to intervention by some self-proclaimed interested parties with views as to the best way to structure the settlements” would inevitably lead to further interventions and “would cause incalculable confusion, add unmanageable complexity, and bring this Court’s review and administration of the underlying actions to a halt.” Id. at \*13-14. While the IPT has not sought to intervene, the same concerns expressed by the Court should apply to IPT’s efforts to change the SEC’s new investor education plan.

The terms of the settlement required the SEC to submit a plan for the use of the federal investor education funds. While the final judgments called for the creation of a new non-profit grant administration entity, the SEC’s new plan is consistent with the idea of distributing grants through a comparable entity, in this case the NASD Foundation. The parties to these actions have not objected to the SEC’s new plan.

In crafting the new investor education plan, the SEC relied on its Office of Investor Education and Assistance. The SEC confirmed that the NASD Foundation is an independent



investor education entity that is nation-wide in scope and not funded by individual financial services companies or their trade associations.

The IPT's criticisms of the NASD Foundation are without merit. In addition to the independent nature of the NASD Foundation, and its pledge to have a majority of public members, the guidelines, procedures, and focus of the NASD Foundation are compatible with the Court's Orders regarding the use of investor education funds. The SEC has a good working relationship with the NASD Foundation. The NASD Foundation's mission is investor education, not the broader goal of financial education. The NASD Foundation publicly discloses, via its website, all grants made, the purpose of each grant, and the recipient of each grant. Such transparency is very important when disbursing public funds. Further, the NASD Foundation's agreement to work within the terms of the Court's Orders regarding investor education will permit sufficient SEC and Court oversight.

**C. The Focus Of The Investor Protection Trust Is Not Nation-Wide Investor Education**

The structure of the IPT does not lend itself to nation-wide investor education programs. The states' portion of the investor education funds is held in separate accounts for each participating state. Each state's securities administrator has a say in the funding of particular projects to use that state's money. In light of this structure, multiple states would have to agree to pool their portions in order to fund national or multi-state projects. Thus far, there is no indication of a plan for all of the states to work together to advance common nation-wide investor education programs. As the IPT concedes, "its broader purpose is to nurture programs in one state, that can be replicated in others." IPT Commentary at 8. The allocation of funds to an individual state program with the faint hope that 49 other states will adopt the very same

program is not a national program. The SEC considers this a fatal flaw to consideration of the IPT as a viable option for investor education funds.

**D. The IPT's Use Of The States' Investor Education Funds Raises Issues**

The IPT's operations and use of funds raise questions regarding whether they would be an appropriate entity to entrust with public funds. For example, the IPT has not wisely invested its funds. According to the IPT's unaudited financial statements for the first four months of 2005, IPT has suffered losses of \$74,892 on its investments. IPT Financial Statements, April 30, 2005 at 2, [www.investorprotection.org/pdfs/04-30-05\\_IPT\\_Financial\\_Statements.pdf](http://www.investorprotection.org/pdfs/04-30-05_IPT_Financial_Statements.pdf). The realized losses for the first three months of 2005 were approximately \$80,000. The IPT's website indicates that it invests its funds in a "mix" that includes equities, an investment strategy that the SEC is not comfortable with for the investment of public funds by a 501(c) non-profit entity.

The IPT's disbursement of funds also raises questions. Apparently, based on news reports, a portion of the settlement proceeds allocated to Georgia were used to aid the political ambitions of the secretary of state, by featuring her in a \$3 million, prime-time advertising campaign. Tom Baxter, Jim Galloway, Cox Raises Profile at No Cost to Her or Taxpayers, The Atlanta Journal-Constitution, September 23, 2004, at C-2. Ex. 2.

There is also a lack of transparency to IPT's disclosures regarding the expenditure of investor education funds. The portion of the IPT's website captioned "grant award updates" does not disclose any grants awarded by the IPT. The IPT's financial statements for the first three months of 2005 list several instances of large expenditures of investor education funds from the accounts of various states with no explanation of the use of funds. IPT Financial Statements, April 30, 2005, at 7 and state entries for California, Florida, Georgia, New York, and Pennsylvania, [www.investorprotection.org/pdfs/04-30-05\\_IPT\\_Financial\\_Statements.pdf](http://www.investorprotection.org/pdfs/04-30-05_IPT_Financial_Statements.pdf). Many

of the amounts are categorized on the financial statements as “program expenses” with no details.

Id. Although the IPT states in its Commentary that it is funding projects “with regional and national applications,” it is impossible to tell from IPT’s website or its financial statements just what those projects might be.

Expenditures by IPT from prior years raise the same concerns. According to IPT Forms 990 filed with the Internal Revenue Service, from 1999 through 2003, the IPT paid over \$1 million dollars to The Hastings Group, a consulting firm owned by Scott Stapf and Maureen Thompson, who the IPT identified in its 1999 Form 990 as “co-directors” of IPT. Exs. 4-5.<sup>1</sup> In 2000 and 2001, the payments to Hastings accounted for over 50% of IPT’s program expenses. Ex. 5; [http://www.investorprotection.org/pdfs/ipt\\_990\\_2001.pdf](http://www.investorprotection.org/pdfs/ipt_990_2001.pdf).

These examples raise questions regarding IPT’s operations and use of the states’ portion of investor education funds that weigh against consideration of IPT as a recipient of the federal portion of investor education funds.

### **III. CONCLUSION**

Based on the foregoing, the IPT’s concerns regarding the SEC’s new investor education plan are unfounded, and the IPT should not receive the federal portion of investor education funds. The SEC believes that its new investor education plan, that provides for grants to be

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<sup>1</sup> The SEC did not wish to burden the Court with attaching a hard copy of all of the lengthy Forms 990. The links to the available on-line Form 990s for 2001, 2002, and 2003 are:

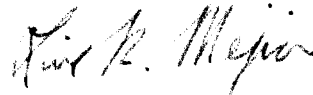
[http://www.investorprotection.org/pdfs/ipt\\_990\\_2003.pdf](http://www.investorprotection.org/pdfs/ipt_990_2003.pdf);  
[http://www.investorprotection.org/pdfs/ipt\\_990\\_2002.pdf](http://www.investorprotection.org/pdfs/ipt_990_2002.pdf);  
[http://www.investorprotection.org/pdfs/ipt\\_990\\_2001.pdf](http://www.investorprotection.org/pdfs/ipt_990_2001.pdf)

awarded by the NASD Foundation, will result in the efficient, cost-effective, and expeditious distribution of investor education funds. The SEC respectfully requests that the Court enter the proposed Order as the new investor education plan.

Date: June 7, 2005

Linda Chatman Thomsen, Director  
Antonia Chion, Associate Director  
Division of Enforcement  
Securities and Exchange Commission

Respectfully submitted,



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