UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 74619 / April 1, 2015

ADMINISTRATIVE PROCEEDING
File No. 3-16466

In the Matter of **KBR, Inc.,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against KBR, Inc. ("KBR" or "Respondent").

II.

In anticipation of the institution of these proceedings, KBR has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

<u>Respondent</u>

1. KBR, Inc. is a Delaware corporation headquartered in Houston, Texas. KBR's common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and trades on the New York Stock Exchange. KBR files periodic reports, including reports on Forms 10-K and 10-Q, with the Commission pursuant to Section 13(a) of the Exchange Act and related rules thereunder.

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[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

<u>Facts</u>

A. Statutory and Regulatory Framework Protecting Whistleblowers

2. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010, amended the Exchange Act by adding Section 21F, "Whistleblower Incentives and Protection." The congressional purpose underlying these provisions was "to encourage whistleblowers to report possible violations of the securities laws by providing financial incentives, prohibiting employment-related retaliation, and providing various confidentiality guarantees." *See* "Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934," Release No. 34-64545, at p. 198 (Aug. 12, 2011) (the "Adopting Release").

3. To fulfill this congressional purpose, the Commission adopted Rule 21F-17, which provides in relevant part:

> (a) No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications.

Rule 21F-17 became effective on August 12, 2011.

B. KBR's Confidentiality Statement

4. As part of its compliance program, KBR regularly receives complaints and allegations from its employees of potential illegal or unethical conduct by KBR or its employees, including allegations of potential violations of the federal securities laws. KBR's practice is to conduct internal investigations of these allegations. KBR investigators typically interview KBR employees (including the employees who originally lodged the complaint or allegation) as part of the internal investigations.

5. Prior to the promulgation of Rule 21F-17 and continuing into the time that Rule 21F-17 has been in effect, KBR has used a form confidentiality statement as part of these internal investigations. Although use of the form confidentiality statement is not required by KBR policy, the statement is included as an enclosure to the KBR Code of Business Conduct Investigation Procedures manual, and KBR investigators have had witnesses sign the statement at the start of an interview.

6. The form confidentiality statement that KBR has used before and since the SEC adopted Rule 21F-17 requires witnesses to agree to the following provisions:

> I understand that in order to protect the integrity of this review, I am prohibited from discussing any particulars regarding this interview and the subject matter discussed during the interview, without the prior authorization of the Law Department. I understand that the unauthorized disclosure of information may be grounds for disciplinary action up to and including termination of employment.

7. Though the Commission is unaware of any instances in which (i) a KBR employee was in fact prevented from communicating directly with Commission Staff about potential securities law violations, or (ii) KBR took action to enforce the form confidentiality agreement or otherwise prevent such communications, the language found in the form confidentiality statement impedes such communications by prohibiting employees from discussing the substance of their interview without clearance from KBR's law department under penalty of disciplinary action including termination of employment. This language undermines the purpose of Section 21F and Rule 21F-17(a), which is to "encourage[e] individuals to report to the Commission." Adopting Release at p. 201.

Remedial Steps Taken By KBR

8. KBR has amended its confidentiality statement to include the following statement:

> Nothing in this Confidentiality Statement prohibits me from reporting possible violations of federal law or regulation to any governmental agency or entity, including but not limited to the Department of Justice, the Securities and Exchange Commission, the Congress, and any agency Inspector General, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation. I do not need the prior authorization of the Law Department to make any such reports or disclosures and I am not required to notify the company that I have made such reports or disclosures.

Violation

9. Through its conduct described above, KBR violated Rule 21F-17 under the Exchange Act.

Undertaking

10. KBR has agreed to make reasonable efforts to contact KBR employees in the United States who signed the confidentiality statement from August 21, 2011 to the present, providing them with a copy of this Order and a statement that KBR does not require the employee to seek permission from the General Counsel of KBR before communicating with any governmental agency or entity, including but not limited to the Department of Justice, the Securities and Exchange Commission, the Congress, and any agency Inspector General, regarding possible violations of federal law or regulation. In determining whether to accept the Offer, the Commission has considered this undertaking.

11. KBR has agreed to certify, in writing, compliance with the undertaking set forth above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to David Peavler, Associate Regional Director, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of the completion of the undertakings.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent KBR's Offer.

Accordingly, it is hereby ORDERED that**:**

A. Pursuant to Section 21C of the Exchange Act, Respondent KBR cease and desist from committing or causing any violations and any future violations of Rule 21F-17 of the Exchange Act;

B. Respondent shall, within thirty (30) days of the entry of this Order, pay a civil money penalty in the amount of $130,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury in accordance with Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying KBR as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to David L. Peavler, Associate Regional Director, Fort Worth Regional Office, Division of Enforcement, Securities and Exchange Commission, 801 Cherry Street, Suite 1900, Fort Worth, Texas, 76102.

By the Commission.

Brent J. Fields
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 78141 / June 23, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17312

In the Matter of **MERRILL LYNCH, PIERCE, FENNER & SMITH INCORPORATED AND MERRILL LYNCH PROFESSIONAL CLEARING CORP.** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") and Merrill Lynch Professional Clearing Corp. ("MLPro") (collectively, "ML" or "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have submitted an Offer of Settlement that the Commission has determined to accept. Respondents admit the facts set forth in Sections III.A, III.B., III.D., and III.E. below, acknowledge that their conduct violated the federal securities laws, admit the Commission's jurisdiction over them and the subject matter of these proceedings, and consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-And-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offer of Settlement, the Commission finds[1] that:

Summary

Broker-dealers are required to be diligent stewards of the cash and securities entrusted to them by their customers. This basic principle is embodied in Exchange Act Rule 15c3-3, known as the Customer Protection Rule ("Rule"). The Rule requires broker-dealers to safeguard both the cash and securities of their customers so that customer assets can be quickly returned if the firm fails. In broad strokes, a broker-dealer cannot use customer assets to finance the business activities of the firm, and it cannot place customer assets in locations or accounts that make them vulnerable to claims made against the broker-dealer by third parties.

This matter arises from significant violations of the Customer Protection Rule that began during the Financial Crisis and, in certain respects, continued until this year. The violations were twofold. First, ML used cash belonging to its customers to fund its own business activities through a series of increasingly complex trades. Second, at the same time and continuing for years due to poor oversight and weak controls, MLPF&S allowed certain of its clearing banks to hold general liens over tens of billions of dollars of securities owned by its customers.

The first set of violations concerns trades devised by ML that were known internally as the Leveraged Conversion Trades ("Trades"). From 2009 to 2012, ML used the Trades to reduce the amount of cash it was required to deposit in a customer reserve account that it maintained pursuant to Rule 15c3-3(e). Margin loans extended to finance customer positions can properly reduce the amount a broker-dealer is required to deposit; however, ML made billions of dollars in margin loans to finance riskless trades that lacked defined terms and economic substance which ML structured and then executed with newly-created counterparty entities. Through these trades, ML improperly reduced by billions of dollars the amount it was required to deposit in its customer reserve account. These Trades evolved over time and, in their final iteration, became instantaneous roundtrips structured to provide financing for ML's activities rather than in response to customer trading objectives.

ML used these Trades to remove up to $5 billion of customer cash week over week from its customer reserve account. ML then used these funds to finance its business activities. Had ML failed when the Trades were in use, its customers would have been exposed to a shortfall of customer cash in the customer reserve account.

The second set of violations involved the custody of customer securities from 2009 until this year. Rule 15c3-3(c) requires broker-dealers like MLPF&S to hold customer securities that are not collateralizing margin loans in a segregated account free of liens. The purpose of this requirement is to protect customer securities from claims by a failed broker-dealer's creditors.

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[1] The findings herein are made pursuant to Respondents' Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

From June 2009 to April 2015, MLPF&S held up to $58 billion of customer securities in a clearing account that was subject to a general lien by one of its clearing banks. In addition to this account, until as recently as this year MLPF&S held approximately $1.38 billion in customer securities in 6 other clearing accounts in Europe and Asia as of the end of 2015 that also were subject to liens and approximately $4.8 billion in 48 other accounts in Europe, Asia, and Australia as of the end of 2015 that lacked documentation establishing that they were not subject to liens. Had MLPF&S failed during this period, these liens, and the resultant uncertainty, would have hindered or prevented MLPF&S's customers from retrieving their securities and could have significantly further damaged public confidence in the U.S. brokerage and securities industries during or after the Financial Crisis.

The significant penalties and other relief imposed in this Order in connection with ML's violations of the Customer Protection Rule reflect the seriousness with which the Commission views failures to comply with this Rule.

A. Respondents

1. Merrill Lynch, Pierce, Fenner & Smith Incorporated, headquartered in New York, New York, is dually-registered with the Commission as a broker-dealer and investment adviser. It is a wholly-owned subsidiary of Bank of America Corporation.

2. Merrill Lynch Professional Clearing Corp., headquartered in New York, New York, is registered with the Commission as a broker-dealer. It is a direct, wholly-owned subsidiary of MLPF&S.

B. Other Entities and Individuals

3. Bank of America Corporation ("BAC") is a bank holding company incorporated in Delaware and a financial services holding company under the Gramm-Leach-Bliley Act. BAC's common stock is registered with the Commission under Section 12(b) of the Exchange Act and trades on the New York Stock Exchange under the symbol "BAC." BAC's principal offices are located in Charlotte, North Carolina.

4. William Tirrell ("Tirrell"), age 61, is a resident of Lawrenceville, NJ and an associated person of broker-dealer and investment adviser MLPF&S. From 2004 until April 2016, he was the Financial and Operations Principal ("FinOp") and Head of the Regulatory Reporting Department for MLPF&S and in that role oversaw regulatory reporting for MLPF&S and MLPro. Concurrent with that role, Tirrell was the Acting CFO of MLPF&S from August 2014 to April 2016. He holds a Series 27 License.

5. SEFT Trader was a Managing Director at MLPF&S who worked on its Structured Equity Financing & Trading ("SEFT") desk from 2005 to 2012.

Background

C. The Customer Protection Rule

6. Rule 15c3-3 of the Exchange Act is designed to protect broker-dealer customers in the event a broker-dealer becomes insolvent. The intent and objective of the Rule is:

> the elimination of the use by broker-dealers of customer funds and securities to finance firm overhead and such firm activities as trading and underwriting through the separation of customer related activities from other broker-dealer operations.

Rule 15c3-3 Adopting Release, Exch. Rel. No. 9775, 1972 WL 125434, at *1 (Sept. 14, 1972); *see also id.* (one objective of the Rule was to "inhibit the unwarranted expansion of a broker-dealer's business through the use of customers' funds by prohibiting the use of those funds except for designated purposes"); Exch. Act Rel. No. 21651, 50 FR 2690-01 at 2690 (Jan. 18, 1985) (Rule "forbid[s] brokers and dealers from using customer assets to finance any part of their businesses unrelated to servicing securities customers; *e.g.*, a firm is virtually precluded from using customer funds to buy securities for its own account").

7. Rule 15c3-3 requires a broker-dealer that maintains custody of customer securities and cash (a "carrying broker-dealer") to take two primary steps to safeguard these assets. The steps are designed to protect customers by segregating their cash and securities from the broker-dealer's business activities. If the broker-dealer fails financially, the securities and cash should be readily available to be returned to the customers. In addition, if the failed broker-dealer is liquidated in a formal proceeding under the Securities Investor Protection Act, the securities and cash should be isolated and readily identifiable as customer property and, consequently, available to be distributed to customers ahead of other creditors. *See* 15 U.S.C. 78aaa *et seq.*

Customer Protection Rule Requirements for Customer Cash

8. The Rule requires a carrying broker-dealer to maintain a reserve of funds and/or certain qualified securities in an account at a bank ("Reserve Account") that is at least equal in value to the net cash owed to customers. 17 CFR 240.15c3-3(e).

9. The amount of net cash owed to customers is computed pursuant to a formula set forth in Exhibit A to Rule 15c3-3 ("Reserve Formula"), which most carrying broker-dealers calculate on a weekly basis. 17 CFR 240.15c3-3a. Under the Reserve Formula, the carrying broker-dealer adds up customer credit items that it owes its customers (*e.g.*, cash in customer securities accounts) and then subtracts from that amount customer debit items that its customers owe it (*e.g.*, margin loans). *See id.* If credit items exceed debit items, that net amount must be deposited, or already be on deposit, in the Reserve Account in the form of cash and/or qualified securities.[2] 17 CFR 240.15c3-3(e). A broker-dealer generally cannot make a withdrawal from the

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[2] Customer cash is a balance sheet item of the carrying broker-dealer (*i.e.*, the amount of cash received from a customer increases the amount of the carrying broker-dealer's assets and creates a corresponding liability to the customer). The Reserve Formula is designed to isolate these broker-dealer assets so that an amount equal to the net liabilities to customers is held as a reserve in the form of cash or U.S. government securities. The reserve

Reserve Account until the next computation and even then only if the computation shows that the reserve requirement has decreased. *Id.* The broker-dealer must make a deposit into the Reserve Account if the computation shows an increase in the reserve requirement.

10. While the formula itself is somewhat complex, it embodies a simple concept for the responsible stewardship of customer cash: if a broker-dealer owes more to its customers than its customers owe to it, the broker-dealer must set aside at least an amount equal to that difference so that it is readily available to repay customers.

11. FINRA's Interpretations of Financial and Operational Rules handbook includes an update, first issued in 1989, which states that the Commission staff has advised that any "device, window dressing or restructuring of transactions made solely to reduce an excess of credits over debits in the Rule 15c3-3 formula computation and not otherwise a normal business transaction" may be considered a circumvention of the Rule. FINRA Interpretations of Financial and Operational Rules, Rule 15c3-3(e)(2)/02 ("Interp. 15c3-3(e)(2)/02") *formerly* N.Y.S.E. Interpretation Handbook, Vol. II, Interpretation Memo No. 89-10, Aug. 23, 1989 (Commission Staff to NYSE) (No. 89-11, 1989 WL 1169979, Oct. 9, 1989).

12. To facilitate the Commission's oversight of broker-dealers, Rule 15c3-3(i) imposes a self-reporting requirement. If a broker-dealer fails to maintain the minimum required amount in its customer reserve account, it must immediately notify the Commission and FINRA of this failure.

Customer Protection Rule Requirements for Customer Securities

13. Rule 15c3-3 also protects customer securities from the risks broker-dealers take in running their business and from the dangers that would arise if a broker-dealer fails. Specifically, the Customer Protection Rule requires a carrying broker-dealer to promptly obtain and thereafter maintain physical possession or control over customers' fully paid and excess margin securities. 17 CFR 240.15c3-3(b). Physical possession or control generally means that the broker-dealer must hold these securities in one of several locations specified in the Rule and that they be held free of liens or any other interest that could be exercised by a third-party to secure an obligation of the broker-dealer.[3] 17 CFR 240.15c3-3(c). Permissible locations include a bank, as defined in Section 3(a)(6) of the Exchange Act, and a clearing agency. *Id.*

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requirement is designed to prevent the carrying broker-dealer from using customer funds for business activities. The goal is to put the carrying broker-dealer in a position to be able to meet its cash obligations to customers by requiring the firm to make deposits of cash and/or U.S. government securities into the Reserve Account in the amount of the net cash owed to customers.

[3] Customer securities held by the carrying broker-dealer are not assets of the firm. Rather, the carrying broker-dealer holds them in a custodial capacity and the possession and control requirement is designed to ensure that the carrying broker-dealer treats them in a manner that allows for their prompt return.

D. ML Improperly Reduced Its Reserve Account

14. From 2009 to 2012, ML executed a series of trades that reduced the balance of its Reserve Account by billions of dollars and then used those freed-up funds to finance firm inventory and thereby finance its business activities.

15. To efficiently manage the firm's capital, ML requires its trading desks to finance the securities they hold. ML makes capital available to its trading desks so that the desks can purchase securities, but it charges an interest rate on this capital, known as the firm's treasury rate, that typically is higher than the interest that external third parties charge. To avoid being assessed the more expensive internal financing rate, a trading desk can finance its positions externally through a repurchase agreement, stock loan, or other means. Taking a repurchase agreement as an example, a ML trading desk can pledge its securities to another firm as collateral for a loan that is roughly equivalent to the market value of the securities. As part of this repurchase agreement, the ML trading desk pays interest on this loan. The ML trading desk can then use the funds obtained through the repurchase agreement to pay for the firm securities it posted as collateral or use the funds to engage in more trading activity. As described below, the Trades used interest-free funds obtained through reductions to the Reserve Account balance, rather than repurchase agreements, to finance its business activities.

16. In 2008, ML sought to reduce the amount of cash it was required to deposit in the Reserve Account that it maintained for the benefit of MLPF&S's and MLPro's customers. MLPF&S's SEFT desk developed a trade designed to introduce customer debits into the Reserve Formula through soliciting customers to enter into conversion trades that would include margin loans that would decrease dollar-for-dollar the amount ML was required to maintain in the Reserve Account. To ensure that it would operate as desired and did not run afoul of the Rule, the SEFT desk developed the trade in consultation with MLPF&S's Regulatory Reporting Department, which is responsible for performing the Reserve Formula calculation each week and maintaining the minimum required amount in its Reserve Account.

17. SEFT Trader conceived of the trade and was responsible for structuring it. During 2008 to 2012, William Tirrell was the Head of MLPF&S's Regulatory Reporting Department and its FinOp. While developing the trade, the SEFT desk consulted with Tirrell about the Trades' potential impact on the Reserve Formula.

18. In August 2008, the SEFT desk obtained internal approval for Trades, known as the Leveraged Conversion Trades. In their initial form, the Leveraged Conversion Trades were conversion trades that used listed options financed by customers through margin loans extended by MLPF&S or MLPro. This margin loan introduced a customer debit into the Reserve Formula that reduced the minimum amount ML was required to maintain on deposit in ML's Reserve Account.

19. In this listed conversion trade, a customer would buy a put and sell a call on a stock with the same strike price and expiration date. The customer would also purchase on margin the stock to cover the call. Because the options fully hedged the customer's stock purchase, it was insulated from market risk provided that the customer could fully cover the short position created

by his call option. In addition to this stock borrow risk, the trade presented other risks because it was exposed to the market, such as pin risk, dividend risk, and early exercise risk.[4]

20. The original version of the trade, as presented by the SEFT desk to internal reviewers in a one page handout, expressly proposed that the trade be used to provide "synthetic financing" to ML through which the firm's inventory would be used in the Trades and financed through the reductions to the amount deposited into the Reserve Account caused by the extension of the margin loan to a customer. A Leveraged Conversion Trade using listed options cannot finance firm inventory in situations where other market participants on the exchange are able to step in to take the other side of the customer's put and call options. If the customer long position in that scenario is sourced from ML's inventory, ML would lose that inventory when the counterparty to the conversion trade exercised his in-the-money put or call. To avoid that, under the trade proposed by the SEFT desk, ML would ensure that it always was the counterparty to the customer's conversion trade and thereby was guaranteed to retain the inventory it used in a Leveraged Conversion Trade.

21. Through this proposed Trade, the SEFT desk was proposing to finance a customer – through the extension of a margin loan – so that the customer could then use the loan it received to provide that same financing back to ML – through the customer's purchase of ML inventory used to cover the short. While this reciprocal financing cancels itself out, the margin loan extended to the customer would reduce the Reserve Account and those funds could be used – on an interest-free basis – to finance the firm inventory used in the Trade.

22. Internal reviewers rejected this proposal but agreed to a modified one in which firm inventory may be financed incidentally through a customer-driven trade, but cannot be the driver for the conversion trade or the terms or securities used in a trade. As reflected in a revised handout (i) the Trades would be exposed to the market, (ii) ML could take the other side of the Trades, but floor traders could also step in and take all or part of the Trades, and (iii) the customer's long position used to cover the short would be sourced as all customer shorts typically were sourced, through either a borrow from an external lender, firm inventory, or some combination of the two. The following is the handout revised to reflect limitations imposed by internal reviewers:

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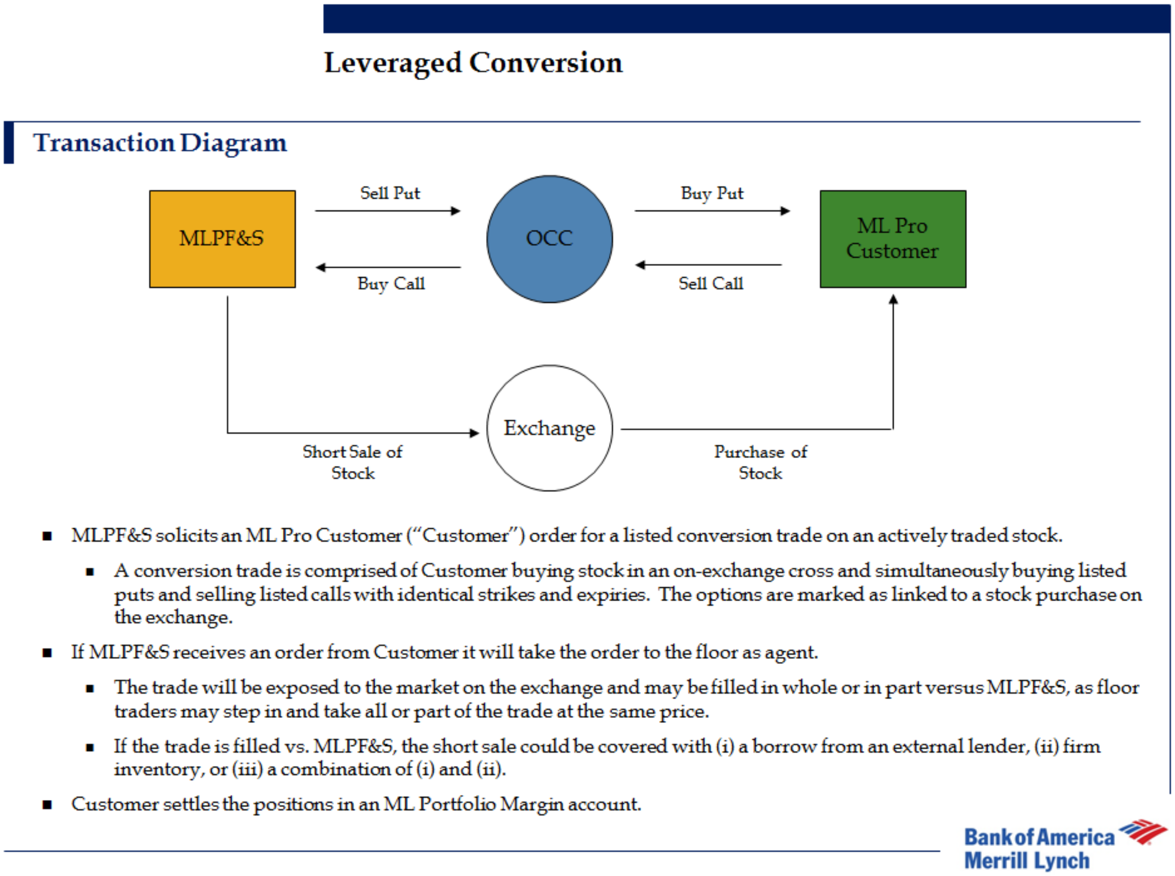
4 Pin risk arises when the market price of the underlying stock at the time of the put and call's expiration is close to the strike price. If this occurs, there is a risk that options may not be exercised and the customer is left with a large, undesired, and unhedged stock position. Dividend risk occurs when a dividend on the underlying stock is unexpectedly cancelled or lowered. Because the pricing of a conversion trade takes into account the anticipated dividend amount, any dividends paid that are less than this anticipated amount will result in a loss to the customer. Early exercise risk materializes when the owner of the call or put option exercises the option prior to its expiration date.



23. After executing Leveraged Conversion Trades according to the limitations imposed by internal reviewers, the SEFT desk in early 2009 renewed their request to use the Trades to finance firm inventory. The SEFT desk also requested to scale the Trades up so that they could reduce the minimum amount required to be maintained in the Reserve Account by a greater amount.

24. ML, which by that time had recently been acquired by BAC, sought to discuss the Leveraged Conversion Trades with securities regulators for two reasons. First, because this sizeable decrease in the Reserve Account balance would be observable in monthly reports submitted to the Financial Industry Regulatory Authority ("FINRA"), ML requested to meet with staff from FINRA and the Commission's Division of Trading and Markets ("T&M") to discuss the Trades. Second, it was perceived within ML that using customer money to finance firm inventory moved the Trades into an area of regulatory uncertainty. As stated above, one of the primary objectives of the Reserve Account requirement in Rule 15c3-3 is to prevent broker-dealers from using customer assets to finance firm activities.

ML Presented an Early Iteration of the Leveraged Conversion Trades to Its Regulators

25. Tirrell and SEFT Trader presented the Trades at a meeting with FINRA and T&M in August 2009. Despite being an impetus for the meeting, ML did not inform FINRA and T&M, either at the August 2009 meeting or subsequently, that the primary purpose of the Leveraged

Conversion Trades was to finance firm inventory. Tirrell, using the revised handout shown above, presented the Trades to regulators. In addition to explaining the bullets on the slide concerning market exposure and the use of only actively traded large cap stocks, Tirrell told regulators that ML's customers took on real risk, which in Tirrell's view made the Trades like any other conversion trade. Based on the revised handout and the discussions at the meeting concerning the presence of real risk, the fact that these were standard conversion trades – which were to be customer and not firm driven – and the perceived economic substance of all of the trade components, the regulators did not object to the version of the Leveraged Conversion Trades that was presented. While they did not object to the Trade as presented, the regulators limited them by advising ML that the Trades collectively could not exceed a notional value of $3 billion for any given calculation period.

26. Over the next year, the Leveraged Conversion Trades would lose each of the key attributes that had been presented to regulators.

27. Shortly after ML met with regulators, it began using the Leveraged Conversion Trades to finance firm inventory. ML chose stocks that it had in inventory and that it otherwise would be seeking to finance through a more costly repurchase agreement or other means. ML then advised floor traders that it intended to take the other side of the trade and that they need not locate counterparties on the exchange. The margin loan extended to customers in each trade created a debit that reduced the required amount to be deposited into the Reserve Account by hundreds of millions and, collectively, billions of dollars. The cash freed from ML's Reserve Account through this debit was used to finance the security sold to the Leveraged Conversion Trade customers as part of the Trades.

28. ML considered the difference between the cost of financing the position through traditional means and through a Leveraged Conversion Trade as profit. The SEFT desk was credited with approximately half of the profit generated by the Leveraged Conversion Trades, and the trading desk that supplied the inventory was credited with the residual.

ML Did Not Keep Regulators Apprised in Regular Reports

29. At the August 2009 meeting with FINRA and T&M, and in a subsequent email confirming the takeaways from that meeting, ML agreed to provide details on executed Leveraged Conversion Trades in its Financial and Operational Combined Uniform Single ("FOCUS") Reports that MLPF&S and MLPro each submit monthly to FINRA, which in turn provides them to the Commission.

30. MLPF&S did not, however, provide details relating to its Leveraged Conversion Trade activity in any monthly FOCUS Reports filed in 2009, 2010, or 2011. And, aside from one FOCUS Report filed in September 2009, MLPro similarly failed to provide this information from 2009 to 2012.

Leveraged Conversion Trade Counterparties

31. Once ML began using the Leveraged Conversion Trades to finance firm inventory, ML's financing needs wholly dictated the terms of the Trades. As a result, the customer debits

created by the Trades became purely firm driven. A significant portion of the Leveraged Conversion Trades were done with limited liability companies ("LLCs") that were set up at ML's behest, were told they would receive fixed profits, and had no meaningful input into the Trades.

32. In mid-2010, SEFT Trader solicited three former options traders who, at the time, were not ML customers, to participate in the Trades. SEFT Trader advised them to create LLCs to execute Leveraged Conversion Trades, from which they would earn a fixed rate of return of up to 15% on the total amount they deposited to capitalize the LLC. Specifically, SEFT Trader advised each of them to open portfolio margin accounts at MLPF&S in the name of the newly-created LLC and to deposit at least $5 million in cash or securities into the account. The LLCs were offered significant leverage; for every dollar in cash or securities an LLC deposited into a portfolio margin account, ML allowed the LLC to purchase on margin up to $100 of securities. Although a fixed 1% margin rate was ostensibly applied to the margin loans extended, the Leveraged Conversion Trades would generate fixed profits sufficient to pay all interest owed in addition to the pre-determined return.

33. SEFT Trader advised the prospective counterparties that ML would take the other side of these Trades, *i.e.*, that the put and the call for the conversion trade would be between the LLC and ML, and that ML would sell the LLC the underlying stock needed, and that as a result the trades were virtually riskless.

34. In a typical conversion trade, a customer attempts to profit from pricing inefficiencies in the options market, and as part of the trade, purchases stock on margin. However, the Leveraged Conversion Trades designed by ML did not generate potential profits from a traditional leverage conversion strategy, but instead provided a fixed rate of return on cash or securities held in the LLC's account. If one leaves aside the gains ML made from reducing the balance in its Reserve Account, the trades themselves, which were not with the market but with ML, were zero sum: customers made money on the trades in the exact amount by which ML lost money.

35. The prospective counterparties did not question why ML would effectively pay them to engage in trades in which ML would lose money every time. Presented with an offer of a virtually riskless return on their capital, they agreed to create LLCs. They each then opened portfolio margin accounts at ML in the name of their respective LLCs and transferred stocks they were holding at other broker-dealers into the accounts.

36. For each Leveraged Conversion Trade executed by an LLC, ML devised the terms of the trade, and the LLC offered no meaningful input. ML chose when to do the trades, the underlying stock to be used and its purchase price as well as the price, strike price, and expiration date of the options. ML did not negotiate these terms with the LLC, but requested that the LLC give ML an order for this pre-packaged trade. After receiving an order, ML would execute the trade.

37. SEFT Trader made a similar solicitation to an options trading firm, which also engaged in a significant number of Leveraged Conversion Trades with ML as its counterparty from

2010 through 2012. Like the LLCs, this entity did not question the rationale for the Trades and had little input into the terms and structure of the Trades.

38. The purported customer debits generated by the Leveraged Conversion Trades were tracked in internal reports under the heading, “non-client debit.” Also, internally ML referred to the net amount a counterparty received for completing a Leveraged Conversion Trade not as its profit, but as a fee that ML paid the counterparty.

The Trades Morphed

39. Any unexpected loss in a Leveraged Conversion Trade would result in the counterparty receiving an amount that fell short of the fixed rate of return it was advised it would receive. Any unexpected gain would result in a windfall to the counterparty that ML would be required to pay. In 2009, an unexpected dividend resulted in a windfall to an LLC. The LLC’s principal offered to return the windfall to ML. SEFT Trader declined to accept it, but resolved to avoid dividend and all other risks going forward.

40. Following this unexpected loss, SEFT Trader sought to modify the Leveraged Conversion Trades so that the SEFT desk had total control over each leg of each trade. By exclusively using firm inventory, ML eliminated the risk relating to the acquisition of the underlying stock.

41. To achieve this, the SEFT desk sought to use unlisted, over-the-counter (“OTC”) options. OTC options, which are bilateral contracts directly between the LLC and ML, eliminate exposure to the listed option market and the risks that come with it. Because the prices used for OTC options are not reported and are not exposed to the market, ML could depart from the prevailing market price of the securities and reverse engineer prices that yielded the precise “fee” owed to the customer participating in the Trades. ML also drafted the OTC contracts to remove dividend risk. Because this iteration of the Leveraged Conversion Trades was effectively riskless, ML removed the Leveraged Conversion Trades from its risk monitoring systems.

42. In addition, by moving to OTC options, which can be written on any security, ML diverged from its presentation to regulators that ML would use only actively traded stocks. As discussed below, using OTC options allowed ML to use customer money to finance certain of its less liquid positions, the financing costs for which were higher than those associated with large cap stocks.

43. In December 2009, Tirrell emailed FINRA staff to advise them that the SEFT desk “would like to [] use unlisted options as it provides greater flexibility.” “I don’t see this as a material change to the current arraingement [sic],” Tirrell stated in the email, “but wanted to ensure you are in agreement.” In January 2010, FINRA staff communicated to Tirrell that the regulators’ non-objection did not extend to unlisted options and requested that ML describe, in writing, the difference in transaction structure, the regulatory impacts, and the rationale for why this version of the Leveraged Conversion Trades should be allowed to have a similar impact on the Reserve Formula.

44. Tirrell did not provide the requested information. The SEFT desk obtained internal approval from Tirrell and others for Leveraged Conversion Trades using OTC options. However, it is not apparent that, at the time, anyone within ML other than Tirrell knew about FINRA staff's questions posed in the January 2010 email.

45. Later in January 2010, the regulators granted ML's request to expand the size of the Leveraged Conversion Trades, as they understood them based on the August 2009 meeting, from $3 billion to $5 billion.

46. In September 2010, the SEFT desk began executing Leveraged Conversion Trades using OTC options. The SEFT desk used the counterparties described above to execute these trades.

47. The following is an example of an OTC Leveraged Conversion Trade:

a. In February 2011, ML identified a block of 310,000 shares of Google common stock in firm inventory that at the time were worth approximately $189 million. ML determined that cost savings could be achieved through a Leveraged Conversion Trade because the fee paid to an LLC to obtain customer money from the Reserve Account was much less than the interest that would be charged in a repurchase agreement or other means of financing.

b. The SEFT desk informed the LLC's principal that it intended to do a Leveraged Conversion Trade using 310,000 Google shares in the LLC's name. ML set all of the terms of the trade, and the LLC offered no input.

c. On February 7, 2011, the SEFT desk executed a Leverage Conversion Trade in which (i) the LLC purchased 310,000 shares of Google, (ii) simultaneously sold them back at $612 with a delayed settlement date of April 6, 2011, and (iii) and purchased from ML an OTC put on the Google shares and sold to ML an OTC call for these shares that both had the same strike price, $612, and expired that day.[5] The effect of this delayed settlement was to keep the margin loan for this one day trade – and the resulting customer debit in the Reserve Formula – open for months. Because the LLC sold the shares back to ML at the same moment it purchased them, the put and the call between the LLC and ML were not necessary to hedge market risk once the trade was put on and, in fact, there is no evidence that ML or the LLC accomplished the instantaneous sale and repurchase through the exercise of the in-the-money put or call. Moreover, as described below, ML and the LLC did not execute an OTC contract for these one-day options until over a year after they expired.

[5] Due to systems limitations, ML was unable to execute a Leveraged Conversion Trade using OTC options that expired past the trade date. To account for this limitation, SEFT Trader considered a trade structure that simply involved a sale and simultaneous repurchase of stock with a delayed settlement of the repurchase, but he recognized that an instantaneous roundtrip would be inappropriate from a regulatory perspective. The SEFT desk, with the involvement and approval of Tirrell and others at ML, settled on a trade structure that involved these same components but also included a put and a call that expired on the trade date.

d. To finance the LLC's purchase of the Google shares, ML extended a portfolio margin loan to the LLC in the amount of approximately $189 million. Other than the securities transferred into the LLC's portfolio margin account against which ML extended margin, the LLC did not contribute any funds toward this trade. The rate on the margin loan was 1%. This margin loan introduced a customer debit in the Reserve Formula and reduced the amount of customer money to be deposited into that account by the same amount. ML would then use the money it otherwise would have been required to deposit into the Reserve Account to finance the Google shares. The trading desk that controlled these Google shares could then use these funds in its trading activities.

e. Although the price of Google shares on the trade date ranged from $613 to $625, the SEFT desk reverse engineered the $610.98 purchase price and the $612 strike price to yield a total profit to the LLC that was equal to the sum of the LLC's costs to do the trade and the fixed rate of return the LLC's principal was told he would receive. The SEFT desk calculated the cost of the purchase of the stock and the OTC put, the profit from the sale of the OTC call, the total interest that would be charged on the margin loan, and the cost of regulatory fees and then chose a strike price that ensured the total profits were sufficient to cover the sum of these costs and the rate of return the LLC expected on the value of the stock it deposited into its portfolio margin account.

f. The April 6 settlement date was a placeholder, and the SEFT desk had no expectation that the trade would be settled then. If ML could benefit from financing its Google shares through this trade past April 6, it would delay the settlement to an even later date by requesting that the LLC agree to a new settlement date that ML unilaterally determined. With this trade, after receiving approval from the LLC, ML extended the settlement date to May 4, 2011. This further extended the time that the margin loan would be open and the accompanying customer debit would stay in the Reserve Formula.

g. Extending the settlement date altered the economics of the trade. ML would continue to charge a margin interest rate of 1% until the trade was settled, and the interest charged from the original settlement date of April 6 to the new settlement date of May 4 would have eliminated the customer profit on the trade. To avoid this, ML changed the economics of the trade. Although the trade had been fully completed months before, ML went into the closed trade and increased the strike price of the expired put and the expired call from $612 to $612.499. While this could have no effect on the trade because it happened months before, ML used it as a justification to increase the buyback price of the Google shares to $612.499 and thereby increase the customer's profits. ML arrived at this new strike price for these expired options by reverse engineering the amount of profits needed for this Leveraged Conversion Trade taking into account all of the items previously mentioned as well as the additional margin interest charged as a result of the new delayed settlement date. ML informed the LLC of this modification and requested an order from it, which the LLC provided.

h. From March to October 2011, ML modified the February 7, 2011 Google trade ten times. Through these modifications, ML extended the settlement date to December 7, 2011 and increased the buyback price from $612.499 to $616.3934. During this period, however, the actual share price of Google common stock was declining and fell to as low as $474.40.

i. In late October, ML sought to unwind the trade before the December 7 extended settlement date that it had set just a few weeks before. On October 31, 2011, ML revised the trade by shortening the settlement date to the next day and decreasing the buyback price from $616.3934 to $615.745.

j. On November 1, 2011, the Google shares settled in ML's account. ML applied the cash it paid for the shares to the LLC's margin loan, which closed it out. The total gross profits from this trade to the customer were approximately $1.8 million and the net amount ML paid to the LLC, after taking into account its margin interest and other costs, was $71,585. This fee offered the fixed return on the value of the stock the LLC held with ML and was much less than the interest payments ML would have been required to make if it had financed these shares through other means.

48. ML's systems recognized this version of the Leveraged Conversion Trades as a nullity and automatically cancelled them. To avoid these cancellations, ML personnel manually overrode these systems.

49. Like the early version of the Trade that used actively traded large cap stocks, the OTC version of the Trade was used to finance large cap equity securities. However, unlike the listed version, the OTC version also was used to finance less liquid positions, such as convertible bonds and stock warrants that were more difficult and more expensive to finance than large cap equities. This shift to illiquid securities departed from the trade structure presented to regulators.

50. In the OTC iteration of the Trades, which lasted from approximately September 2010 to April 2012, ML reduced the minimum amount required in its Reserve Account by up to $5 billion per week through Leveraged Conversion Trades. During this period, ML's Reserve Account balance ranged from approximately $7.6 to $12.8 billion; therefore, although no customers were harmed, ML put them at risk by reducing the customer money it was required to deposit into its Reserve Account by approximately 28% to 40%.

ML Halted All Leveraged Conversion Trades

51. In early 2012, a new co-head of the business unit that included the SEFT desk learned of the Leveraged Conversion Trades and became concerned about whether they complied with the Customer Protection Rule. After he discussed the OTC version of the Trades with the SEFT desk and others within ML, the firm retained external counsel to conduct a review of the Leveraged Conversion Trades.

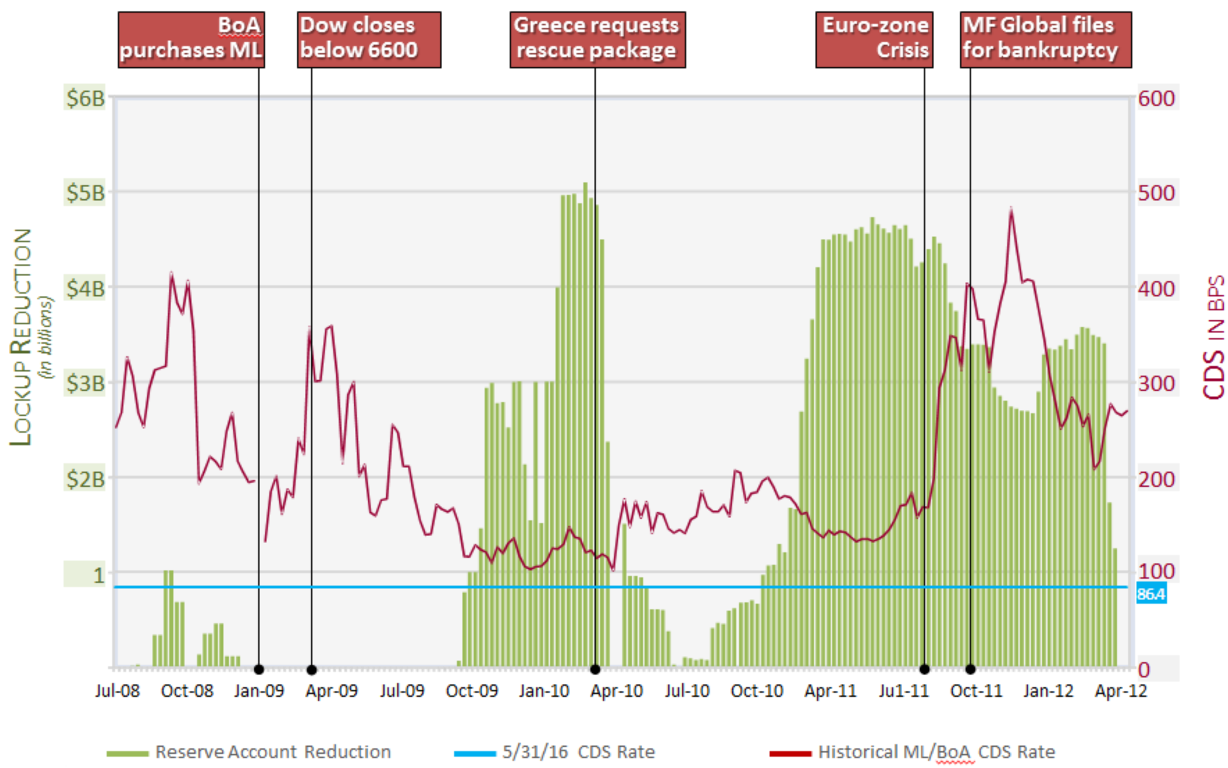
52. ML thereafter changed two practices associated with the Trades. First, ML had the LLCs sign OTC contracts for all of their OTC Leveraged Conversion Trades that attempted to

retroactively create the OTC options that had expired many months ago and that were used in Trades that had already been fully executed. Second, after years of failing to report Leveraged Conversion Trades in FOCUS Reports, both MLPF&S and MLPro began submitting the required information in their respective FOCUS Reports for the months January 2012 through April 2012.

53. In April 2012, ML prohibited the SEFT desk from executing any new Leveraged Conversion Trades. ML did not provide any information relating to the circumstances of its discontinuation of the Leveraged Conversion Trades in 2012 to the regulators.

The Effect of the Leveraged Conversion Trades

54. ML conceived of and executed the Leveraged Conversion Trades during an extremely precarious period of time in the financial markets. Several months after ML began the trades, Lehman Brothers collapsed, and ML was sold to BAC. Based on the market's assessment of ML's risk of default, as reflected in the spread of credit default swaps referencing ML or, following the date of the merger announcement, BAC, the risk of a ML or BAC default remained heightened throughout the life of the Trades.



55. Had ML or its parent failed, the funds ML set aside in its Reserve Account would have been distributed to customers in a liquidation administered by the Securities Investor Protection Corporation ("SIPC"). By improperly reducing its Reserve Account by up to $5 billion to finance its business activities, ML failed to maintain the required minimum amount in its Reserve Account. During this period, the SIPC Fund, which SIPC maintains to cover shortfalls,

was less than $2 billion, and prior to the adoption of the Dodd-Frank Act, SIPC, through the Commission, was authorized to obtain a loan from Treasury of only an additional $1 billion.

56. Taking the Leveraged Conversion Trade using Google shares summarized above, ML reduced the minimum amount it was required to maintain in its Reserve Account by approximately $189 million in a trade that involved 310,000 shares of Google common stock. Given that these LLCs had under $15 million in cash and/or securities in their respective accounts, they could not have repaid the portfolio margin loans extended to them. If ML failed financially, the Reserve Account it maintained to make customers whole would be underfunded. The underlying long (in this example, the 310,000 shares of Google common stock) may be used to reduce that shortfall, but these efforts would not fully protect customers. Even assuming that these shares could be liquidated and applied toward the customer debits introduced by the margin loan to the counterparty, ML's customers would be exposed to significant market risk if ML failed. Indeed, these Google shares dropped in value during this trade and at one point were worth approximately $33 million less than the margin loan. In addition, market conditions during the failure of a large broker-dealer typically are poor. Selling these shares in the midst of those conditions likely would have exposed customers to potential losses much greater than $33 million.

57. The Leveraged Conversion Trades involving convertible bonds further increased the market risk to which ML's other customers were exposed. During this period, the convertible bond market was especially illiquid. Liquidating these securities would have taken a period of time during which customers would not have been able to access their accounts. Also, a liquidation of a large amount of convertible bonds into an already illiquid market would likely be achieved only by selling them at a significant discount.

58. By using customer cash to finance firm inventory, ML made approximately $50 million in profits through the Leveraged Conversion Trades, which represents the amount the firm saved by using customer money to finance its inventory rather than doing so through other means such as repurchase agreements.

E. MLPF&S Improperly Allowed Liens on Customer Securities

59. From June 2009 to April 2015, MLPF&S allowed tens of billions of dollars' worth of its customers' fully paid and excess margin securities to be held in a clearing account subject to a general lien by its domestic clearing bank (the "Clearing Bank"). These customer securities were held in an account at the Clearing Bank for securities that can be transferred through the Federal Reserve Fedwire Funds Transfer System and consisted of Treasuries and mortgage backed securities (collectively, "Fedwire securities"). The total market value of the Fedwire securities in this account during this period ranged from approximately $30 to $60 billion; approximately 98% of the securities in the account were customer securities, and the remainder was firm securities. Pursuant to the Clearing Bank's lien, if MLPF&S went bankrupt or defaulted on any debt it owed to the Clearing Bank, the Clearing Bank had the legal right to assert a security interest in those customers' securities.

MLPF&S – Clearing Bank September 2008 Clearing Agreement

60. In September 2008, MLPF&S and the Clearing Bank executed a securities clearing agreement which provided the Clearing Bank with a general lien on what would become MLPF&S's Fedwire clearing account ("Fedwire Clearing Account"). The lien was established pursuant to the following provision (with MLPF&S being the "Customer" of the Clearing Bank "Bank"):

> Section 3.04 Collateral Security. As security for the repayment of Loans and for the payment of interest thereon and *all other Customer obligations to Bank*, Customer hereby grants Bank a security interest in any and *all Securities* which may now or hereafter be held in the Account…" (emphasis added)

61. Under these terms, the Clearing Bank's lien provided the Clearing Bank with a broad security interest against the repayment of any obligations of MLPF&S to the Clearing Bank, whether or not arising from the Fedwire clearing relationship. Furthermore, the lien applied to any security – whether owned by MLPF&S or not – that was held in the relevant clearing account. Other provisions of the agreement allowed MLPF&S to transfer securities from the Fedwire Clearing Account to a separate segregated account, free of this lien, if MLPF&S met certain conditions.

62. One of the services provided by the Clearing Bank is to extend its clearing clients intraday loans to facilitate the daily purchase of securities into the account. If MLPF&S or one of its customers seeks to purchase a security, and if there is not sufficient cash in the clearing account to cover that purchase, the Clearing Bank will extend a loan to enable that transaction. Particularly if the securities purchases on a given day exceed securities sales, the balance of these loans from the Clearing Bank can rise into the billions or even tens of billions of dollars. The loan is typically paid back by the clearing customer at the end of the trading day.

63. Given the credit risk inherent in making loans to a clearing client, the Clearing Bank required a lien on any "street-facing account," – *i.e.*, any account for which securities can be freely delivered out to or in from third-parties without the Clearing Bank's review – for which it extends intraday credit. However, under the September 2008 securities clearing agreement, MLPF&S could have instructed the Clearing Bank to transfer customer fully-paid and excess margin securities from the Fedwire Clearing Account to a lien-free account if MLPF&S met certain conditions.

MLPF&S Moved Fedwire Clearing Account to the Clearing Bank

64. In late 2008, around the time of the acquisition of MLPF&S by BAC, MLPF&S decided to migrate its Fedwire Clearing Account from a different clearing bank, where it had not been subject to a lien, to the Clearing Bank.

65. Pursuant to the clearing agreement reached months earlier, the Clearing Bank would have a lien on all securities held in a street-facing, non-segregated account such as the Fedwire Clearing Account. MLPF&S, however, did not then have the capability to segregate Fedwire securities from the Fedwire Clearing Account by transferring them into a separate, lien-

free account after they had cleared. Operations personnel recognized that using an account with a lien to hold customers' fully paid and excess margin securities without the ability to transfer them to a no-lien account, or to otherwise resolve the lien, was a violation of Rule 15c3-3's possession and control requirement.

66. To address this problem, operations personnel drafted a proposal to create information technology systems within MLPF&S that would allow it to transfer customer fully paid and excess margin securities to a segregated no-lien account at the close of every trading day. As of the end of May 2009, it was estimated that this project could only be completed by October 2009.

67. Due to insufficient processes concerning the identification, escalation and resolution of potential violations of Rule 15c3-3, MLPF&S failed to identify that proceeding with the migration to the Fedwire Clearing Account despite the existence of a lien without first implementing systems to segregate customer securities would violate Rule 15c3-3. Although the Rule 15c3-3 concern was raised internally, managers in MLPF&S's operations group did not correctly understand how the Clearing Bank lien would work. One manager, for instance, wrongly believed that the Clearing Bank lien would only apply up to the amount of net intraday debt MLPF&S had to the Clearing Bank. Based on this misunderstanding, which the manager discussed with many others in his department and other departments, that manager and others erroneously concluded that the Clearing Bank's lien would not extend to customer Fedwire securities, particularly if MLPF&S prefunded the account and paid back all loans at the end of each trading day.

68. On June 22, 2009, MLPF&S migrated its Fedwire securities to the Fedwire Clearing Account at the Clearing Bank without having implemented a process to segregate customer fully-paid and excess margin securities after clearing. Shortly after this migration, MLPF&S terminated the project to create systems capable of handling the segregation of customer fully paid and excess margin securities. At the time these actions were taken, MLPF&S had failed to identify the fact that the Fedwire Clearing Account did not comply with the possession or control requirements of Rule 15c3-3 because of the Clearing Bank's lien.

69. MLPF&S held customer securities in the Fedwire Clearing Account subject to the Clearing Bank's lien from June 2009 until SEC Enforcement staff informed MLPF&S of the issue in March 2015. MLPF&S resolved the issue in the following weeks. No customers suffered any losses or other harm as a result of the lien.

Additional Segregation Violations

70. After remedying the Clearing Bank's lien, MLPF&S conducted a comprehensive review of all its third-party custodial accounts containing customer fully-paid securities and excess margin securities. Based on that review, MLPF&S identified certain additional instances of non-compliance with the "no-lien" requirements of Rule 15c3-3(c) involving foreign custodians, which it reported to the Commission staff. These additional instances of failures to properly maintain possession and control of customer securities involved 6 accounts in Europe and Asia. The aggregate value of securities subject to a lien in these accounts was approximately $1.38 billion as

of the end of 2015. In addition, MLPF&S identified 48 other accounts in Europe, Asia, and Australia for which it could not locate contemporaneous documentation affirmatively establishing that the accounts satisfied the "no-lien" requirements of Rule 15c3-3(c). The aggregate value of securities in these accounts without such documentation was approximately $4.8 billion as of the end of 2015. In each instance, MLPF&S promptly resolved any question of compliance.

F. MLPF&S's Improper Confidentiality Provisions

71. On August 12, 2011, the Commission adopted Rule 21F-17, which provides in relevant part, that "[n]o person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications."

72. After the Commission adopted this Rule, MLPF&S used language in certain of its policies, procedures, and agreements with employees that unduly limited the disclosure of confidential information. For example, MLPF&S used language in a severance agreement for certain departing employees based on a standard template that prohibited them from disclosing any aspect of the confidential information or trade secrets of MLPF&S or any of its subsidiaries or affiliates to any person or entity outside these entities except pursuant to formal legal process or unless the former employee first obtained the written approval of an authorized MLPF&S representative. While the agreement expressly permitted an individual to disclose confidential information pursuant to an order or other requirement of a court, administrative agency, or other authority, it did not permit an individual to voluntarily disclose confidential information to such bodies.

73. Further, in 2014, MLPF&S added a clause to its form severance agreement advising the departing employee that the severance agreement did not prohibit initiating communications directly with the Commission or other authorities, but limiting the types of information that could be conveyed to information relating to the severance agreement itself or "its underlying facts and circumstances."

74. Though we are unaware of any instances in which (i) an MLPF&S employee was in fact prevented from communicating directly with the Commission about potential securities law violations, or (ii) MLPF&S took action to enforce the form confidentiality agreement to prevent such communications with the Commission, the language found in certain of the MLPF&S policies, procedures, and agreements operated to impede such communications by prohibiting employees from voluntarily providing information to the Commission without prior approval from MLPF&S.

G. Cooperation and Remedial Actions

Customer Protection Rule

75. In determining to accept ML's Offer, the Commission considered remedial acts promptly undertaken by ML and substantial cooperation afforded the Commission staff during the course of its investigation. Prior to the entry of this Order, ML retained an independent consultant

(the “IC”) to (i) evaluate ML’s review of each third-party custodial account containing fully paid and excess margin customer securities to ensure that it is not subject to a lien, (ii) review controls relating to Rule 15c3-3, and (iii) review regulatory reporting to the Commission and FINRA regarding Rule 15c3-3. The IC has provided ML and the Commission staff with its preliminary findings and recommendations, and ML has implemented or is in the process of implementing such recommendations. In accordance with the terms of the IC’s engagement, the IC will submit, once per year for two years following the issuance of his final report, a report to the Commission staff concerning the status of ML’s implementation of the recommendations set forth in the final report and whether changes in the law or ML’s business operations requires the updating or amendment of those recommendations. The terms of the IC’s engagement require ML to cooperate fully with the IC and give him reasonable access to files, books and records, and personnel as reasonably requested and required.

Rule 21F-17

76. In determining to accept ML’s Offer, the Commission considered the substantial remedial acts promptly undertaken by ML to address the Rule 21F-17 violation arising from ML’s policies, procedures and agreements, and the substantial cooperation afforded the Commission staff during the course of its investigation. MLPF&S has agreed to modify the confidentiality provision contained in its policies, procedures, and agreements. For example, the language in its form severance agreements has been revised so that information beyond the underlying facts and circumstances of those agreements can be conveyed to the Commission and other regulatory authorities. This updated language, which MLPF&S as well as its parent, BAC and other BAC subsidiaries (“BAC Entities”) have used since January 2016, states that, with the exception of information that is protected from disclosure by any applicable law or privilege, nothing in the agreement prohibits or limits the employee or his counsel from initiating communications directly with, responding to any inquiry from, volunteering information to, or providing testimony before, among others, the Commission in connection with any reporting of, investigation into, or proceeding regarding suspected violations of law. The language also makes clear that the employee is not required to advise or seek permission from any of the BAC Entities before engaging in any such activity.

77. In addition, as of January 2016, the BAC Entities now provide all employees with mandatory yearly trainings that includes a summary of and link to a document entitled, “Notice Concerning Your Rights to Report Possible Violations of Law” (“21F-17 Notice”). The 21F-17 Notice sets forth an employee’s rights to (i) report potential violations of law to the Commission or other government or self-regulatory authorities without permission from or notice to his or her employer, (ii) report possible violations anonymously and to provide disclosures that are protected or required under whistleblower laws, and (iii) cooperate voluntarily with or respond to any inquiry from the Commission or other federal or state agencies or self-regulatory organizations. The 21F-17 Notice also summarizes several of the rights the employee possesses under the Commission’s Whistleblower Program and states that employees have the right to not be retaliated against for reporting possible securities law violations.

78. The BAC Entities have updated their Code of Conduct as well as other relevant agreements, policies, and procedures to ensure that employees understand that there is no restriction on their rights under Rule 21F-17.

IV.

Violations

79. As a result of the conduct described above, MLPF&S and MLPro willfully[6] violated Section 15(c)(3) of the Exchange Act and Rule 15c3-3 thereunder which, *inter alia*, require carrying broker-dealers to maintain a reserve of funds or qualified securities in an account at a bank that is at least equal in value to the net cash owed to customers, and MLPF&S further violated Section 15(c)(3) of the Exchange Act and Rule 15c3-3 thereunder, which also requires that carrying broker-dealers maintain physical possession or control over customers' fully paid and excess margin securities.

80. As a result of the conduct described above, MLPF&S and MLPro willfully violated Section 17(a)(1) of the Exchange Act and Rule 17a-3(a)(10) thereunder which, *inter alia*, require a broker or dealer to maintain and keep accurate records, including records relating to all puts or calls in which the broker or dealer has any interest.

81. As a result of the conduct described above, MLPF&S and MLPro willfully violated Section 17(a)(1) of the Exchange Act and Rule 17a-5(a) thereunder, which, *inter alia*, require certain brokers or dealers to file monthly FOCUS Reports.

82. As a result of the conduct described above, MLPF&S willfully violated Section 17(a)(1) of the Exchange Act and Rules 17a-5(d)(3) (as it existed prior to amendments to Rule 17a-5 in 2014), 17a-5(d)(2)(ii), 17a-5(d)(3), and 17a-11(e) thereunder which, *inter alia*, require certain brokers or dealers to file compliance and other reports and supporting schedules with the Commission and to notify the Commission of material weaknesses relating to compliance with the Customer Protection Rule.

83. As a result of the conduct described above, MLPF&S willfully violated Exchange Act Rule 21F-17, which prohibits any action impeding an individual from communicating directly with Commission staff about a possible securities law violation.

V.

In view of the foregoing, the Commission deems it appropriate, in the public interest, and for the protection of investors to impose the sanctions agreed to in Respondents' Offer.

[6] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "'also be aware that he is violating one of the Rules or Acts.'" *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that:

A. MLPF&S cease and desist from committing or causing any violations and any future violations of Sections 15(c)(3) and 17(a)(1) of the Exchange Act and Rules 15c3-3, 17a-3(a)(10), 17a-5(a), 17a-5(d)(2)(ii), 17a-5(d)(3), 17a-11(e), and 21F-17 thereunder; and MLPro cease and desist from committing or causing any violations and any future violations of Sections 15(c)(3) and 17(a)(1) of the Exchange Act and Rules 15c3-3, 17a-3(a)(10) and 17a-5(a) thereunder.

B. MLPF&S and MLPro are censured.

C. MLPF&S and MLPro shall, within 14 days of the entry of this Order, pay, jointly and severally, disgorgement of $50,000,000 and prejudgment interest of $7,000,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600.

D. MLPF&S shall, within 14 days of the entry of this Order, pay a civil money penalty in the amount of $358,000,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717.

Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the Commission website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying MLPF&S and MLPro as Respondents in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Michael Osnato, Unit Chief, Complex Financial Instruments Unit, Division of Enforcement, Securities and Exchange Commission, Brookfield Place, 200 Vesey Street, Suite 400, New York, NY 10281.

E. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, MLPF&S agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of its payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, MLPF&S agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against MLPF&S by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 79804 / January 17, 2017

ADMINISTRATIVE PROCEEDING
File No. 3-17786

In the Matter of **BlackRock, Inc.,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against BlackRock, Inc. ("BlackRock" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Respondent

1. BlackRock, Inc. is a Delaware corporation headquartered in New York, New York. BlackRock's common stock is registered with the Commission pursuant to Section 12(b) of the

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Exchange Act and trades on the New York Stock Exchange. BlackRock files periodic reports, including reports on Forms 10-K and 10-Q, with the Commission pursuant to Section 13(a) of the Exchange Act and related rules thereunder. As of December 31, 2015, BlackRock and its subsidiaries had approximately 13,000 employees.

Facts

A. Statutory and Regulatory Framework Protecting Whistleblowers

2. The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), enacted on July 21, 2010, amended the Exchange Act by adding Section 21F, "Whistleblower Incentives and Protection." The purpose of these provisions was to encourage whistleblowers to report possible securities law violations by providing, among other things, financial incentives and various confidentiality guarantees.

3. Congress explicitly noted the critical importance of providing financial incentives to promote whistleblowing to the SEC as it determined that "a critical component of the Whistleblower Program is the minimum payout that any individual could look towards in determining whether to take the enormous risk of blowing the whistle in calling attention to fraud." *See* "The Restoring American Financial Stability Act of 2010" report from the Committee on Banking, Housing, and Urban Affairs (April 30, 2010).

4. To fulfill this Congressional purpose, the Commission adopted Rule 21F-17, which provides in relevant part:

> (a) No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications.

Rule 21F-17 became effective on August 12, 2011.

B. BlackRock's Separation Agreements

5. Historically, BlackRock has entered into voluntary separation agreements with many employees who leave the company. A separation agreement is a contract between an employer and a former employee documenting the rights and responsibilities of both parties incidental to the employee's departure.

6. On October 14, 2011 – after the Commission adopted Rule 21F-17 – BlackRock revised its form separation agreement to include language requiring a departing employee to waive recovery of incentives for reporting misconduct available under, among other things, the Dodd-Frank Act in exchange for receiving monetary separation payments and other voluntarily provided consideration from BlackRock. That agreement did not, however, prohibit former employees from communicating directly with the Commission or any other governmental agency regarding potential violations of law.

7. Specifically, Paragraph 5 of BlackRock's separation agreement in use from October 14, 2011 through March 31, 2016 stated in relevant part:

> To the fullest extent permitted by applicable law, you hereby release and forever discharge, BlackRock, as defined above, from all claims for, and you waive any right to recovery of, incentives for reporting of misconduct, including, without limitation, under the Dodd-Frank Wall Street Reform and Consumer Protection Act and the Sarbanes-Oxley Act of 2002, relating to conduct occurring prior to the date of this Agreement.

8. One thousand sixty seven (1067) departing employees signed agreements that contained the above language.

9. On March 31, 2016, before being contacted by the Commission staff in this matter, BlackRock voluntarily revised its separation agreement as part of a regular periodic review and update of its agreements. The revised agreement does not require a separating employee to waive his or her right to recovery of incentives available under the Dodd-Frank Act.

10. Though the Commission is unaware of any instances in which (i) a former employee of BlackRock who executed the above-noted agreement did not communicate directly with Commission staff about potential securities law violations or (ii) BlackRock took action to enforce those provisions or otherwise prevent such communications, BlackRock – from October 2011 through March 2016 – directly targeted the SEC's whistleblower program by removing the critically important financial incentives that are intended to encourage persons to communicate directly with the Commission staff about possible securities law violations. Such restrictions on accepting financial awards for providing information regarding possible securities law violations to the Commission undermine the purpose of Section 21F and Rule 21F-17(a), which is to "encourag[e] individuals to report to the Commission," [Adopting Release at p. 201], and violate Rule 21F-17(a) by impeding individuals from communicating directly with the Commission staff about possible securities law violations.

Remedial Actions

11. In determining to accept BlackRock's Offer, the Commission considered its voluntary decision to revise its separation agreements before being contacted by the Commission staff and the remedial actions described in paragraphs 12 and 13 below.

12. BlackRock now provides all employees with mandatory yearly trainings that include a summary of and link to a document entitled, "Global Policy for Reporting Illegal or Unethical Conduct" ("Policy"). The Policy summarizes several of the rights the employee possesses under the Commission's Whistleblower Program, including an employee's rights to: (i) report potential violations of law to the Commission or other federal or state agencies or self-regulatory authorities without permission from or notice to his or her employer, (ii) report possible violations anonymously and to provide disclosures that are protected or required under whistleblower laws, and (iii) cooperate voluntarily with or respond to any inquiry from the Commission or other federal or state agencies or self-regulatory organizations. The Policy also states that employees have the right not to be retaliated against for reporting possible securities

law violations. BlackRock has agreed to notify the Chief(s) of the Asset Management Unit of the Division of Enforcement, with a copy to the Chief of the Office of the Whistleblower, at least sixty (60) days in advance of discontinuing these mandatory yearly trainings.

13. BlackRock has updated its Code of Business Conduct and Ethics as well as other relevant agreements, policies, and procedures to ensure that employees understand that there is no restriction on their rights under Rule 21F-17.

Violation

14. Through its conduct described above, BlackRock violated Rule 21F-17 under the Exchange Act.

Undertaking

15. BlackRock has agreed that, within 60 days from the date the Commission enters this Order, it will make reasonable efforts to contact BlackRock former employees who signed separation agreements from October 14, 2011 through March 31, 2016, and provide them with an Internet link to the order[2] and a statement that BlackRock does not prohibit former employees from seeking and obtaining a whistleblower award from the Securities and Exchange Commission pursuant to Section 21F of the Exchange Act. In determining whether to accept the Offer, the Commission has considered this undertaking.

16. BlackRock has agreed to certify, in writing, compliance with the undertaking set forth above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and BlackRock agrees to provide such evidence. The certification and supporting material shall be submitted to Anthony S. Kelly, Co-Chief, Asset Management Unit, with a copy to the Office of the Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of the completion of the undertakings.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent BlackRock's Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent BlackRock cease and desist from committing or causing any violations and any future violations of Rule 21F-17 under the Exchange Act;

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[2] BlackRock further agrees to provide a paper copy of the Order to any former employee who requests it.

B. Respondent BlackRock shall, within ten (10) days of the entry of this Order, pay a civil money penalty in the amount of $340,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury in accordance with Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717. Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or
(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying BlackRock as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Anthony S. Kelly, Co-Chief, Asset Management Unit, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-5012.

By the Commission.

Brent J. Fields
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 78528 / August 10, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17371

In the Matter of **BlueLinx Holdings Inc.,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against BlueLinx Holdings Inc. ("BlueLinx" or "Respondent").

II.

In anticipation of the institution of these proceedings, BlueLinx has submitted an Offer of Settlement (the "Offer"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Respondent

1. BlueLinx is a Delaware corporation with its headquarters located in Atlanta, Georgia. BlueLinx's common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and trades on the New York Stock Exchange. BlueLinx files periodic reports, including reports on Forms 10-K and 10-Q, with the Commission pursuant to Section 13(a) of the Exchange Act and related rules thereunder. BlueLinx has approximately 1,700 employees.

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Facts

A. Statutory and Regulatory Framework Protecting Whistleblowers

2. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010, amended the Exchange Act by adding Section 21F, "Whistleblower Incentives and Protection." The congressional purpose underlying these provisions was "to encourage whistleblowers to report possible violations of the securities laws by providing financial incentives, prohibiting employment-related retaliation, and providing various confidentiality guarantees."[2]

3. Congress explicitly noted the importance of providing financial incentives to promote whistleblowing to the SEC as it determined that "a critical component of the Whistleblower Program is the minimum payout that any individual could look towards in determining whether to take the enormous risk of blowing the whistle in calling attention to fraud."[3]

4. To fulfill this Congressional purpose, the Commission adopted Rule 21F-17, which provides in relevant part:

> (a) No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications.

Rule 21F-17 became effective on August 12, 2011.

B. BlueLinx's Severance Agreements

5. Beginning prior to August 12, 2011, and continuing through the present, BlueLinx entered into agreements with certain employees who were leaving the company and who were receiving severance or other post-employment consideration from BlueLinx. A severance agreement is a contract between an employer and a former employee documenting the rights and responsibilities of both parties incidental to the employee's departure.

6. During the period from August 12, 2011 through the present, BlueLinx used several forms of severance agreements, variously termed: (1) "Confidential Severance Agreement and General Release ("Termination Agreement"); (2) Separation Agreement; (3) Settlement Agreement and Full and Final Release of Claims ("Settlement Agreement"); (4) Release Agreement; and (5) a Letter Agreement that was a severance agreement in the form of a letter to the departing employee (collectively, "Severance Agreements"). The vast majority of non-

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[2] *See "Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934,"* Release No. 34-64545, at p.197 (Aug. 12, 2011) ("*Adopting Release*").

[3] *See The Restoring American Financial Stability Act of 2010,* Committee on Banking, Housing, and Urban Affairs Report (April 30, 2010).

management employees who left BlueLinx during the relevant period and who received severance payments were asked to sign Letter Agreements.

7. Although the Severance Agreements differed in certain respects, most of them, other than the Letter Agreements, contained some form of a provision that prohibited the employee from sharing with anyone confidential information concerning BlueLinx that the employee had learned while employed by the company, unless compelled to do so by law or legal process. The confidentiality provisions also required employees either to provide written notice to the company or to obtain written consent from the company's legal department prior to providing confidential information pursuant to such legal process. None of the confidentiality provisions contained an exemption permitting an employee to provide information voluntarily to the Commission or other regulatory or law enforcement agencies.

8. For example, the Termination Agreements defined "Confidential Information" as "data and information relating to the business of BlueLinx which is or has been disclosed to the Employee or of which the Employee became aware as a consequence of or through his relationship to BlueLinx," and contained the following provision:

> Employee has not and in the future will not use or disclose to any third party Confidential Information, unless compelled by law and after notice to BlueLinx. * * * If the Employee has any question regarding what data or information would be considered by BlueLinx to be information subject to this provision, the Employee agrees to contact BlueLinx's Legal Department in writing for written clarification.

9. Similarly, the Release Agreements, the Separation Agreements, and the Settlement Agreements each contained the following confidentiality provision:

> [The employee shall] hold in a fiduciary capacity for the benefit of the Company [ ] all Confidential Information….For a period of two years, following the [employee's] Termination Date, Executive shall not, without the prior written consent of the Company or as may otherwise be required by law or legal process, communicate or divulge Confidential Information.

10. While several forms of the Severance Agreements included a restriction on the disclosure of confidential information, BlueLinx did not add such a provision to the Letter Agreements until mid-2013.

11. Between September 2011 and mid-2013, approximately eighteen BlueLinx employees signed Severance Agreements that included one of the confidentiality provisions referred to in paragraphs 8 and 9, above.

12. In or about June 2013 – nearly two years after the Commission had adopted Rule 21F-17 – BlueLinx reviewed and revised each of its Severance Agreements, including the Letter Agreement, and either added or amended a number of provisions that a departing employee was required to accept as a condition for receiving monetary severance payments and other consideration from BlueLinx.

13. Specifically, BlueLinx added a confidentiality clause to its form Letter Agreement that was similar to those that had been included in its other Severance Agreements even prior to the effective date of Rule 21F-17. The added confidentiality clause provided:

> [The Employee shall not] disclose to any person or entity not expressly authorized by the Company any Confidential Information or Trade Secrets….Anything herein to the contrary notwithstanding, you shall not be restricted from disclosing or using Confidential Information or Trade Secrets that are required to be disclosed by law, court or other legal process; provided, however, that in the event disclosure is required by law, you shall provide the Company's Legal Department with prompt written notice of such requirement in time to permit the Company to seek an appropriate protective order or other similar protection prior to any such disclosure by you.

14. At the same time, BlueLinx amended all of the Severance Agreements, including the Letter Agreement, by adding a clause to the general release provision specifically addressing interactions with governmental agencies and associated financial incentives. The new clause provided that:

> Employee further acknowledges and agrees that nothing in this Agreement prevents Employee from filing a charge with…the Equal Employment Opportunity Commission, the National Labor Relations Board, the Occupational Safety and Health Administration, <u>the Securities and Exchange Commission</u> or any other administrative agency if applicable law requires that Employee be permitted to do so; <u>however, Employee understands and agrees that Employee is waiving the right to any monetary recovery in connection with any such complaint or charge that Employee may file with an administrative agency</u>. (Emphasis added.)

15. Approximately 160 BlueLinx employees have signed Severance Agreements that contained the provisions described in paragraphs 13 and 14, above.

16. By including those clauses in its Severance Agreements, BlueLinx raised impediments to participation by its employees in the SEC's whistleblower program. By requiring departing employees to notify the company's Legal Department prior to disclosing any financial or business information to any third parties without expressly exempting the Commission from the scope of this restriction, BlueLinx forced those employees to choose between identifying themselves to the company as whistleblowers or potentially losing their severance pay and benefits.

17. Further, by requiring its departing employees to forgo any monetary recovery in connection with providing information to the Commission, BlueLinx removed the critically important financial incentives that are intended to encourage persons to communicate directly with the Commission staff about possible securities law violations.

18. Restrictions on the ability of employees to share confidential corporate information regarding possible securities law violations with the Commission and to accept financial awards for providing information to the Commission, such as those contained in the Severance Agreements, undermine the purpose of Section 21F, which is to "encourage individuals to report to

the Commission,"[4] and violate Rule 21F-17(a) by impeding individuals from communicating directly with the Commission staff about possible securities law violations.

Violation

19. Through its conduct described above, BlueLinx violated Exchange Act Rule 21F-17.

Undertaking

20. BlueLinx undertakes that, from the date of the issuance of this Order, it will include the following provision in all of its Severance Agreements and/or any other agreements with its employees that include prohibitions on the use or disclosure of confidential information relating to the company:

> "<u>Protected Rights</u>. Employee understands that nothing contained in this Agreement limits Employee's ability to file a charge or complaint with the Equal Employment Opportunity Commission, the National Labor Relations Board, the Occupational Safety and Health Administration, the Securities and Exchange Commission or any other federal, state or local governmental agency or commission ("Government Agencies"). Employee further understands that this Agreement does not limit Employee's ability to communicate with any Government Agencies or otherwise participate in any investigation or proceeding that may be conducted by any Government Agency, including providing documents or other information, without notice to the Company. This Agreement does not limit Employee's right to receive an award for information provided to any Government Agencies."

21. BlueLinx undertakes that, within sixty (60) days from the date the Commission enters this Order, it will make reasonable efforts to contact BlueLinx former employees who signed any of the Severance Agreements from August 12, 2011 to the present, and provide them with an Internet link to the Order[5] and a statement that BlueLinx does not prohibit former employees from: (1) providing information to, or communicating with, Commission staff without notice to the Company; or (2) accepting a whistleblower award from the Commission pursuant to Section 21F of the Exchange Act.

22. BlueLinx undertakes to certify, in writing, its compliance with the undertakings set forth above. The certification shall identify each undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Antonia Chion, Associate Director, with a copy to the Office of the

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4 *See Adopting Release*, at 201.

5 BlueLinx further agrees to provide a paper copy of the Order to any former employee who requests it.

Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of completion of the undertakings.

23. In determining whether to accept the Offer, the Commission has considered each of the undertakings set forth above.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent BlueLinx's Offer.

Accordingly, it is hereby ORDERED that**:**

A. Pursuant to Section 21C of the Exchange Act, Respondent BlueLinx cease and desist from committing or causing any violations and any future violations of Exchange Act Rule 21F-17;

B. Respondent shall pay a civil money penalty in the amount of $265,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury in accordance with Exchange Act Section 21F(g)(3) pursuant to the terms of the payment schedule set forth in paragraph C below. Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying BlueLinx as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Antonia Chion, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549.

C. BlueLinx shall pay the penalty due of $265,000.00 in four installments to the Commission according to the following schedule:

(1) $25,000.00 within five (5) days of entry of this Order;

(2) $60,000.00 within ninety (90) days of entry of this Order;
(3) $80,000.00 within one hundred eighty (180) days of entry of this Order;
(4) $100,000.00 within two hundred seventy (270) days of entry of this Order.

Payments shall be deemed made on the date they are received by the Commission and shall be applied first to post order interest, which accrues pursuant to 31 U.S.C. § 3717 on any unpaid amounts due after twenty-one (21) days of the entry of the Order. Prior to making the final payment set forth herein, BlueLinx shall contact the staff of the Commission for the amount due for the final payment. If BlueLinx fails to make any payment by the date agreed and/or in the amount agreed according to the schedule set forth above, all outstanding payments under this Order, including post-order interest, minus any payments made, shall become due and payable immediately at the discretion of the staff of the Commission without further application to the Commission.

D. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within thirty (30) days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 78590 / August 16, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17396

In the Matter of **Health Net, Inc.,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Health Net, Inc. ("Health Net" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

<u>Respondent</u>

1. Health Net, Inc. is a Delaware corporation headquartered in Woodland Hills, California. Until April 4, 2016, Health Net's common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and, until March 24, 2016, traded on the New York

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[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Stock Exchange. While registered with the Commission, Health Net filed periodic reports, including reports on Forms 10-K and 10-Q, with the Commission pursuant to Section 13(a) of the Exchange Act and related rules thereunder. As of December 31, 2015, Health Net and its subsidiaries had approximately 8,541 employees.

Facts

A. Statutory and Regulatory Framework Protecting Whistleblowers

2. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010, amended the Exchange Act by adding Section 21F, "Whistleblower Incentives and Protection." The purpose of these provisions was to encourage whistleblowers to report possible securities law violations by providing, among other things, financial incentives and various confidentiality guarantees.

3. Congress explicitly noted the critical importance of providing financial incentives to promote whistleblowing to the SEC as it determined that "a critical component of the Whistleblower Program is the minimum payout that any individual could look towards in determining whether to take the enormous risk of blowing the whistle in calling attention to fraud." *See* "The Restoring American Financial Stability Act of 2010" report from the Committee on Banking, Housing, and Urban Affairs (April 30, 2010).

4. To fulfill this Congressional purpose, the Commission adopted Rule 21F-17, which provides in relevant part:

> (a) No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications.

Rule 21F-17 became effective on August 12, 2011.

B. Health Net's Severance Agreements

5. Beginning prior to August 12, 2011, and continuing through October 22, 2015, Respondent entered into voluntary severance agreements with employees who were leaving the company. A severance agreement is a contract between an employer and a former employee documenting the rights and responsibilities of both parties incidental to the employee's departure. Respondent continues to enter into voluntary severance agreements with departing employees, but on October 22, 2015, it amended those agreements to strike the language at issue below.

6. Respondent's severance agreements included a Waiver and Release of Claims that listed various potential claims against Respondent that a departing employee waived as a condition of being paid monetary severance payments and receiving other voluntarily provided consideration from Respondent.

7. In August 2011 – after the Commission adopted Rule 21F-17 – and as part of a regular periodic review and update of its agreements, Respondent amended the Waiver and

Release of Claims. Among other things, Respondent amended the Waiver and Release of Claims to specify that, while not prohibited by the severance agreement from participating in a government investigation, the former employee who executed the Waiver and Release of Claims was prohibited from filing an application for, or accepting, a whistleblower award from the Commission.

8. In particular, Paragraph 4 of Respondent's Waiver and Release of Claims expressly required an employee to waive:

> the right to file an application for award for original information submitted pursuant to Section 21F of the Securities Exchange Act of 1934.

9. While Paragraph 8 of the Waiver and Release of Claims stated that nothing in the Release precludes an employee from participating in any investigation before any federal agency, that same Paragraph required the employee to waive his or her right to any monetary recovery related to any such investigation.

10. In particular, Paragraph 8 provided that "nothing in this Release precludes Employee from participating in any investigation or proceeding before any federal or state agency, or governmental body . . . however, while Employee may file a charge and participate in any such proceeding, by signing this Release, Employee waives any right to bring a lawsuit against the Company, and waives any right to any individual monetary recovery in any such proceeding or lawsuit or in any proceeding brought based on any communication by Employee to any federal, state, or local government agency or department."

11. Approximately 600 employees signed agreements that contained the above language, which was used by Respondent from approximately August 2011 to June 2013.

12. In June 2013, again as part of a regular periodic review and update of its agreements, Respondent further amended the Waiver and Release of Claims. Respondent removed the language expressly prohibiting employees from applying for whistleblower awards pursuant to Exchange Act Section 21F. Respondent also added Paragraph 4.a. which provided that "[n]othing herein shall be construed to impede the employee from communicating directly with, cooperating with or providing information to any government regulator." However, Respondent retained restrictions in the Waiver and Release of Claims that removed the financial incentive for its former employees who executed that agreement to communicate with Commission staff concerning possible securities law violations at Health Net. Paragraph 5 of the revised Waiver and Release of Claims stated that: "nothing in this Release precludes Employee from participating in any investigation or proceeding before any federal or state agency or governmental body . . .however, while Employee may file a charge, provide information, or participate in any investigation or proceeding, by signing this Release, Employee, to the maximum extent permitted by law . . . waives any right to any individual monetary recovery . . . in any proceeding brought based on any communication by Employee to any federal, state or local government agency or department."

13. Though the Commission is unaware of any instances in which (i) a former employee of Respondent who executed the above noted agreements did not communicate directly with Commission staff about potential securities law violations or (ii) Respondent took action to enforce those provisions or otherwise prevent such communications, Respondent – by use of both

the 2011 and 2013 agreements – directly targeted the SEC's whistleblower program by removing the critically important financial incentives that are intended to encourage persons to communicate directly with the Commission staff about possible securities law violations. Such restrictions on accepting financial awards for providing information regarding possible securities law violations to the Commission undermine the purpose of Section 21F and Rule 21F-17(a), which is to "encourag[e] individuals to report to the Commission," [Adopting Release at p. 201], and violate Rule 21F-17(a) by impeding individuals from communicating directly with the Commission staff about possible securities law violations.

Violation

14. Through its conduct described above, Health Net violated Rule 21F-17 under the Exchange Act.

Undertaking

15. Health Net has agreed that, within 60 days from the date the Commission enters this Order, it will make reasonable efforts to contact Health Net former employees who signed the Waiver and Release of Claims from August 12, 2011 to October 22, 2015, and provide them with an Internet link to the order[2] and a statement that Health Net does not prohibit former employees from seeking and obtaining a whistleblower award from the Securities and Exchange Commission pursuant to Section 21F of the Exchange Act. In determining whether to accept the Offer, the Commission has considered this undertaking.

16. Health Net has agreed to certify, in writing, compliance with the undertaking set forth above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Antonia Chion, Associate Director, with a copy to the Office of the Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of completion of the undertakings.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Health Net's Offer.

Accordingly, it is hereby ORDERED that**:**

A. Pursuant to Section 21C of the Exchange Act, Respondent Health Net cease and desist from committing or causing any violations and any future violations of Rule 21F-17 of the Exchange Act;

B. Respondent shall, within thirty (30) days of the entry of this Order, pay a civil money penalty in the amount of $340,000 to the Securities and Exchange Commission for

[2] Health Net further agrees to provide a paper copy of the Order to any former employee who requests it.

transfer to the general fund of the United States Treasury in accordance with Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Health Net as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Antonia Chion, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549.

By the Commission.

Brent J. Fields
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 78957 / September 28, 2016

ACCOUNTING AND AUDIT ENFORCEMENT
Release No. 3808 / September 28, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17586

In the Matter of **ANHEUSER-BUSCH INBEV SA/NV,** **Respondent.**	**ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS, PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be and hereby are instituted pursuant to Section 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Anheuser-Busch InBev SA/NV ("AB InBev" or "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

1. This matter concerns AB InBev's violations of the books and records and internal controls provisions of the Foreign Corrupt Practices Act of 1977 ("FCPA"), which occurred at its Indian wholly owned subsidiary, Crown Beers India Private Limited ("Crown"). From 2009 to 2012, AB InBev held a 49% interest in an Indian joint venture, InBev India International Private Limited ("IIIPL"), which managed the marketing and distribution of Crown beer. During this period, IIIPL used third-party sales promoters to make improper payments to Indian government officials to obtain beer orders and to increase brewery hours for Crown in 2011. IIIPL invoiced Crown for reimbursement for certain of these expenses, and Crown paid or accrued them. In doing so, Crown recorded certain of these expenses in its books as legitimate promotional costs. During this period, Crown had inadequate internal accounting controls to detect and prevent these improper payments and to ensure that transactions involving these promoters were recorded properly in its books. As a result, Crown's books, which were consolidated into AB InBev's books and records, did not accurately and fairly reflect the nature of the promoters' transactions.

2. Furthermore, in December 2012, AB InBev entered into a separation agreement with a former Crown employee containing language that impeded the employee from communicating directly with the Commission staff about possible securities law violations. AB InBev had also used the same or similar language in other separation agreements in the past.

Respondent

3. **AB InBev**, a global brewer, is a Belgian company headquartered in Leuven, Belgium. AB InBev was formed in November 2008 through the merger of Anheuser-Busch Companies Inc. ("Anheuser-Busch") and InBev SA/NV ("InBev"). AB InBev's American Depositary Receipts trade on the New York Stock Exchange and have been registered with the Commission pursuant to Section 12(b) of the Exchange Act since September 16, 2009. AB InBev has, through various direct and indirect subsidiaries and affiliates, approximately 155,000 employees based in 25 countries around the world. AB InBev files annual reports with the Commission on Form 20-F.

Other Relevant Entities

4. **Crown** is a wholly owned subsidiary of AB InBev and is headquartered in Hyderabad, Andhra Pradesh, India. Crown's financial results are consolidated into AB InBev's financial statements, which are filed with the Commission.

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[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

5. **IIIPL**, a defunct company formerly based in Gurgaon, India, was a joint venture between AB InBev and RJ Corp, an Indian corporation. InBev (AB InBev's predecessor) and RJ Corp formed IIIPL in 2007 to brew and sell beer in India and Nepal. Prior to its dissolution in early 2015, RJ Corp and AB InBev owned 51% and 49% of IIIPL, respectively. AB InBev and RJ Corp each had the right to appoint four IIIPL directors, with RJ Corp having the right to appoint the Chairman, who cast the tie-breaking vote on all but certain specified matters. RJ Corp appointed the IIIPL CEO, who had the power to appoint the other members of the IIIPL management team, except for the CFO, whom AB InBev appointed. Throughout the relevant period, the top financial officer at Crown acted as the top financial officer at IIIPL. From mid-2011 through early 2014, Crown's in-house counsel also acted as IIIPL's in-house counsel.

Facts

A. Background

6. AB InBev's predecessor corporate entities, Anheuser-Busch and InBev, independently entered the Indian beer market before the two companies merged in November 2008. Anheuser-Busch entered the Indian market in 2007 through a joint venture with Crown and subsequently bought out its partner, making Crown a wholly owned subsidiary. InBev entered the Indian market in 2007 through IIIPL. Post-merger, AB InBev continued to operate in India through both Crown and IIIPL.

7. Pre-merger, Crown controlled the marketing, distribution, and sale of the beer it brewed. The Anheuser-Busch/InBev merger, however, triggered a provision in the IIIPL joint venture shareholders' agreement that required IIIPL to manage the marketing, distribution, and sale of beer brewed by Crown. Thereafter, IIIPL controlled the third-party sales promoters that were used to facilitate the sale and marketing of Crown's beers in both Andhra Pradesh and Tamil Nadu. Among other tasks, these promoters administered retail promotional programs and liaised with Indian state government authorities.

8. The sale of beer in India is predominantly regulated by individual states. In the state of Andhra Pradesh, the Andhra Pradesh Beverages Corporation Limited ("APBCL"), an instrumentality of the government of Andhra Pradesh, purchases beer directly from brewers and sells beer directly to private retailers. In the state of Tamil Nadu, the Tamil Nadu State Marketing Corporation ("TASMAC"), an instrumentality of the government of Tamil Nadu, controls both wholesale and retail beer sales, purchasing beer from brewers and selling to consumers through TASMAC retail outlets.

B. Third-Party Promoters of AB InBev's and IIIPL's Beers Provided Improper Benefits and Payments to Indian Government Officials

9. In early 2009, IIIPL's CEO and his appointed executives formulated a plan to increase IIIPL's market share in Andhra Pradesh by providing improper benefits and payments to government officials through third-party sales promoters.

Promoter Company A

10. In 2009, IIIPL hired a promoter for the state of Andhra Pradesh, Promoter Company A. Promoter Company A had no experience in the alcohol industry. Promoter Company A received excessive commissions and reimbursements for questionable promotional charges. For example, Promoter Company A sought reimbursement from IIIPL of certain "display" charges that had no substantiation and were billed on a "per case" basis rather than based on the actual amount spent on the display. Promoter Company A used these excessive commissions and reimbursements to make improper payments to government officials at APBCL.

11. There was no executed contract in place to govern the relationship between Promoter Company A and IIIPL. Neither IIIPL nor Crown conducted any due diligence on Promoter Company A. Instead, the contractual terms of IIIPL's agreement with Promoter Company A were documented only in two short internal emails between IIIPL employees. Promoter Company A was replaced by a successor entity in April 2012, but neither IIIPL nor Crown conducted any due diligence on the successor entity at that time. Even though Crown's in-house counsel forwarded AB InBev's FCPA due diligence forms to IIIPL staff and offered to help complete them, the due diligence forms were never completed. Neither company executed a written contract with the successor entity until September 2012.

12. In December 2009, AB InBev received an internal complaint regarding compliance and internal control issues at IIIPL, including potential FCPA issues related to Promoter Company A. In response, AB InBev expedited an already-planned internal audit of IIIPL, which AB InBev staff conducted in early 2010. This audit did not scrutinize Promoter Company A's activities or expenses. Still, the 2010 audit identified various deficiencies at IIIPL, including (a) a lack of documented business policies and procedures for significant functions such as procurement, vendor selection, and expense reimbursement; (b) a lack of awareness about FCPA compliance; and (c) inadequate information technology controls regarding financial processes and expense payments. AB InBev did not rectify many of the issues identified in the audit until 2011 or early 2012.

13. From April 2009 until March 2012, IIIPL generally incurred the initial costs of marketing and selling Crown's beer and then sent invoices to Crown for reimbursement. Crown, in turn, recorded certain of these costs as expenses on its books and records. Crown thus either incurred or accrued certain of Promoter Company A's expenses and recorded them as legitimate commissions or promotional costs, even though some of those amounts included improper payments to government officials.

14. Despite the internal complaint and the 2010 audit results, Crown personnel did not verify that a contract was in place with Promoter Company A and did not ensure that IIIPL personnel had performed due diligence on Promoter Company A. As a result, Crown recorded certain Promoter Company A expenses on its books in a manner that failed to accurately and fairly reflect their true nature and purpose.

Promoter Company B

15. In or about 2011, IIIPL began working with an individual (the "Principal") who had connections in Andhra Pradesh, including to the son-in-law of the Andhra Pradesh Excise Minister. The Principal used his local connections to secure extra brewing hours for Crown after the Andhra Pradesh Excise Commissioner limited Crown's production time to 8 hours per day. On April 1, 2011, before the Principal was hired in any capacity by IIIPL or Crown, and before the Principal had entered into any contract, the Principal emailed IIIPL a signed order from the Andhra Pradesh Excise Commissioner that gave Crown an additional 7.5 brewing hours per day. The Principal helped IIIPL obtain further authorizations from the Andhra Pradesh Excise Commissioner to operate for an additional 7.5 hours per day in May 2011, and an additional 7 hours per day in June 2011. Neither IIIPL nor Crown held any contractual relationship with, or had performed any due diligence on, the Principal when he helped secure the additional brewing hours.

16. Around the same time, IIIPL engaged the Principal to assist in generating beer orders from TASMAC in Tamil Nadu. In April 2011, the Principal secured orders of more than 534,000 cases of beer in Tamil Nadu, resulting in gross profits of approximately $637,000 to Crown. This was the first and only time that IIIPL ever sold Crown beer in Tamil Nadu.

17. IIIPL utilized the Principal's company, Promoter Company B, to promote beer in Tamil Nadu despite the fact that Promoter Company B had no experience, staff, or infrastructure in Tamil Nadu.

18. IIIPL personnel did not conduct due diligence on the Principal or Promoter Company B before they began performing work for IIIPL. To conceal this fact, IIIPL employees subsequently completed and backdated Promoter Company B's due diligence forms to make it appear as though they were completed in April 2011, when IIIPL initially engaged Promoter Company B. In addition, IIIPL employees allowed the Principal to complete the due diligence forms in the first instance, and then altered his responses to make them more suitable.

19. Neither Crown nor IIIPL had a written agreement in place with the Principal or Promoter Company B. Rather, the basic terms of the engagement were first set out in an internal email between IIIPL employees in June 2011, several months after IIIPL had begun to sell beer in Tamil Nadu and after Promoter Company B had already invoiced IIIPL for its services. The terms included an inflated commission rate, which Promoter Company B used to make improper payments to TASMAC officials. IIIPL employees subsequently drafted and backdated a contract with Promoter Company B to create the appearance that the contract had been executed on the date that IIIPL initially engaged Promoter Company B. In reality, IIIPL did not execute a formal contract with Promoter Company B until approximately January 2012.

20. Although they were on notice of internal controls issues at IIIPL and had received a complaint about the Principal and Promoter Company B, Crown personnel did not verify the existence of a written contract with Promoter Company B and did not confirm that IIIPL personnel performed due diligence on Promoter Company B.

C. AB InBev's Separation Agreement Contained Language that Impeded the Crown Employee's Communication with the Commission

21. In 2010 and 2011, a Crown employee (the "Crown Employee") informed AB InBev personnel that, among other things, IIIPL may have been using Promoter Company A to make improper payments to government officials. The Crown Employee also raised concerns to AB InBev about Promoter Company B, questioning its lack of sales experience, staff, and infrastructure. The Crown Employee reported to AB InBev personnel that the Principal had a local reputation for "taking care of" government officials and suggested that AB InBev perform due diligence on him.

22. During the relevant period, the Crown Employee was employed by an AB InBev subsidiary.

23. In early 2012, AB InBev's subsidiary terminated the Crown Employee's employment. The Crown Employee and AB InBev's subsidiary subsequently engaged in mediation regarding potential employment law claims related to this termination. In late 2012, the Crown Employee and AB InBev's subsidiary entered into a Confidential Agreement and General Release (the "Separation Agreement") that resolved the Crown Employee's claims.

24. Paragraph 7.A of the Separation Agreement includes the following language:

> [The Crown Employee] agrees to keep in strict secrecy and confidence any and all unique, confidential and/or proprietary information and material belonging or relating to [the AB InBev subsidiary] that is not a matter of common knowledge or otherwise generally available to the public including, but not limited to, business, government affairs, communications, financial, trade, technical or technological information. [The Crown Employee] acknowledges and agrees that [the Crown Employee] remains subject to the "Employment Agreement as to Intellectual Property and Confidentiality," which [the Crown Employee] previously signed and is incorporated into the Agreement by reference.

25. Paragraph 7.C of the Separation Agreement includes the following language:

> [The Crown Employee] agrees not to disclose, directly or indirectly, any information regarding the substance of this Agreement to any person other than [the Crown Employee's] spouse, attorney, or financial or tax advisor, except to the extent such disclosure may be required for accounting or tax purposes or as otherwise required by law.

26. Paragraph 7.D of the Separation Agreement includes the following language:

> [The Crown Employee] agrees that, if [the Crown Employee] violates in any way any of the terms and conditions of paragraph 7, [the Crown Employee] shall be liable to [the AB InBev subsidiary], and shall

> immediately pay to [the AB InBev subsidiary] as liquidated damages and not as a penalty, the total sum of $250,000.00 which represents reasonable compensation for the loss incurred by [the AB InBev subsidiary] as a result of such breach….

27. After signing the Separation Agreement, the Crown Employee, who was previously voluntarily communicating directly with the Commission staff, stopped doing so. The Crown Employee stopped doing so because he believed that he was prohibited by the recently executed Separation Agreement and any violation of the Separation Agreement would risk triggering the Separation Agreement's liquidated damages provision. Only after the Commission issued an administrative subpoena for testimony and documents did the Crown Employee resume communicating directly with the Commission staff.

28. AB InBev has used the same or similar language in other agreements in the past.

Document Destruction at IIIPL

29. In or about May 2013, Commission staff learned of IIIPL's plans to destroy or hide documents. The Commission staff informed AB InBev immediately thereafter, but the company took no immediate corrective action. In September 2013, AB InBev notified the Commission staff of a meeting in which several IIIPL managers instructed top IIIPL employees to remove potentially inculpatory data from their offices and computers. Crown and IIIPL's in-house counsel attended the meeting, but never alerted AB InBev management to the document removal instructions. Other IIIPL employees reported that they had helped or observed IIIPL managers take several binders out of the building to destroy or move to a "secret location."

AB InBev's Investigation and Remedial Efforts

30. AB InBev did not report the 2009 and 2011 complaints to the Commission staff before the Commission first contacted AB InBev in October 2011. During the investigation, AB InBev did not respond to subpoenas in a timely manner, and made broad assertions of privilege that required significant resources from the Commission staff to address and delayed the production of responsive, non-privileged documents. The timeliness of AB InBev's responses to the Commission's requests for documents and information improved over time.

31. After the 2010 internal audit, AB InBev did improve some internal controls at Crown and IIIPL, including by adopting AB InBev's own policies, due diligence questionnaires, and checklists; more sound controls over expenses and cash; and tighter controls over IIIPL's accounting software, and the eventual replacement in 2012 of a flawed accounting system with a more sophisticated system. However, IIIPL employees were still able to circumvent many of these controls between 2010 and 2012. AB InBev also conducted FCPA training at both IIIPL and Crown, albeit over a year and a half after it received the first complaint regarding potential FCPA violations.

32. Additionally, AB InBev and RJ Corp terminated their joint venture and dissolved IIIPL in early 2015. AB InBev now operates in India solely through its wholly owned subsidiary,

Crown, and has consolidated its Indian production, sales, and marketing functions at Crown. Following the dissolution of IIIPL in 2015, AB InBev conducted extensive FCPA training for Crown's staff, and implemented improved compliance policies and controls at Crown, including policies and controls relating to third-party due diligence and contracts. AB InBev also has hired a dedicated India compliance manager who reports to a new India Legal Counsel and Head of Compliance.

33. In September 2015, AB InBev amended its separation agreements that impose confidentiality restrictions on departing employees of its United States entities to make clear that they do not prohibit the employees from reporting possible violations of law to governmental agencies. Those separation agreements now include the following language: "I understand and acknowledge that notwithstanding any other provision in this Agreement, I am not prohibited or in any way restricted from reporting possible violations of law to a governmental agency or entity, and I am not required to inform the Company if I make such reports."

Legal Standards and Violations

34. Under Section 21C(a) of the Exchange Act, the Commission may impose a cease-and-desist order upon any person who is violating, has violated, or is about to violate any provision of the Exchange Act or any rule or regulation thereunder, and upon any other person that is, was, or would be a cause of the violation, due to an act or omission the person knew or should have known would contribute to such violation.

35. Under Section 13(b)(2)(A) of the Exchange Act, issuers are required to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and disposition of the assets of the issuer.

36. Section 13(b)(2)(B) of the Exchange Act requires issuers with a class of securities registered pursuant to Section 12 of the Exchange Act to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that, among other things, transactions are (a) executed in accordance with management's general or specific authorization; (b) recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or any other applicable criteria; and (c) recorded as necessary to maintain accountability for assets; and access to assets is permitted only in accordance with management's general or specific authorization.

37. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010, amended the Exchange Act by adding Section 21F, "Whistleblower Incentives and Protection." The Commission adopted Rule 21F-17(a), which provides that, "No person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing, or threatening to enforce, a confidentiality agreement . . . with respect to such communications." Rule 21F-17(a) became effective on August 12, 2011.

38. As a result of the conduct described above, AB InBev violated Section 13(b)(2)(A) of the Exchange Act, because its books and records did not, in reasonable detail, accurately and fairly reflect the true nature and purpose of Promoter Company A's illicit expenses.

39. AB InBev also violated Section 13(b)(2)(B) of the Exchange Act by failing to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that Crown executed transactions in accordance with management's general or specific authorization.

40. In addition, AB InBev violated Rule 21F-17(a) because the Separation Agreement contained language that impeded the Crown Employee from communicating directly with the Commission staff. Such restrictions on providing information regarding possible securities law violations to the Commission undermine the purpose of Section 21F, which is to "encourage[e] individuals to report to the Commission" [Adopting Release at p. 201], and violate Rule 21F-17(a) by impeding individuals from communicating directly with the Commission staff about possible securities law violations.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent AB InBev's Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent shall cease and desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B), and Rule 21F-17, of the Exchange Act.

B. Respondent shall, within thirty (30) days of the entry of this Order, pay disgorgement of $2,712,955, prejudgment interest of $292,381, and a civil penalty of $3,002,955, for a total payment of $6,008,291 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury in accordance with Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 and 31 U.S.C. § 3717.

Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying AB InBev as the Respondent in these proceedings, and the file number of these proceedings. A copy of the cover letter and check or money order must be sent to Ansu Banerjee, Assistant Regional Director, Los Angeles Regional Office, Division of Enforcement, United States Securities and Exchange Commission, 444 S. Flower Street, Suite 900, Los Angeles, CA 90071.

C. During a two-year term from the date the Order is issued, Respondent agrees, as set forth below, to cooperate fully and truthfully with respect to this action and any other enforcement litigation or investigation commenced by the Commission or to which the Commission is a party into potential violations of the FCPA or Section 21F(h)(1)(A) of the Exchange Act and Rule 21F-17 promulgated under the Exchange Act (the "Proceedings"). In addition, during this two-year term, Respondent agrees to cooperate fully and truthfully, when directed by the Commission, in an official investigation or proceeding by the United States Department of Justice into potential violations of the FCPA ("Other Proceedings"). The full, truthful, and continuing cooperation of Respondent during this two-year term shall include, but not be limited to:

(1) producing, in a responsive and prompt manner, all non-privileged documents, information, and other materials to the Commission as requested by the Commission's staff, wherever located, in the possession, custody, or control of the Respondent, including translations of any of the foregoing;

(2) using its best efforts to secure the full, truthful, and continuing cooperation of current and former directors, officers, employees and agents, including making these persons available, when requested to do so by the Commission's staff, at Respondent's expense, for interviews and the provision of testimony in the investigation, trial and other judicial proceedings in connection with the Proceedings or Other Proceedings; and

(3) entering into tolling agreements, when requested to do so by the Commission.

D. During a two-year term as set forth below, Respondent shall report to the Commission staff on the operation of AB InBev's FCPA and anti-corruption compliance program. If Respondent discovers credible evidence, not already reported to the Commission staff, that: (1) questionable or corrupt payments or questionable or corrupt transfers of property or interests may have been offered, promised, paid, or authorized by Respondent, or any entity or person while working directly for Respondent, to any government official; (2) that related false books and records have been maintained; or (3) that Respondent's internal controls failed to detect and prevent such conduct, Respondent shall promptly report such conduct to the Commission staff.

E. During this two-year period:

(1) Respondent shall submit to the Commission staff a written report within one year of the entry of this Order on the operation of AB InBev's FCPA and anti-corruption compliance program (the "Initial Report"). The Initial Report shall be transmitted to Ansu Banerjee, Assistant Regional Director, Los Angeles Regional Office, Division of Enforcement, United States Securities and Exchange Commission, 444 S. Flower Street, Suite 900, Los Angeles, CA 90071. Respondent may extend the time period for issuance of the Initial Report with prior written approval of the Commission staff.

(2) Respondent shall undertake one follow-up review, incorporating any comments provided by the Commission staff on the Initial Report, to further monitor and assess the operation of its FCPA and anti-corruption compliance program and whether Respondent's policies and procedures are reasonably designed to detect and prevent violations of the FCPA and other applicable anti-corruption laws (the "Final Report").

(3) The Final Report shall be completed by no later than one year after the Initial Report, and shall be transmitted to Ansu Banerjee, Assistant Regional Director, Los Angeles Regional Office, Division of Enforcement, United States Securities and Exchange Commission, 444 S. Flower Street, Suite 900, Los Angeles, CA 90071. Respondent may extend the time period for issuance of the Final Report with prior written approval of the Commission staff.

(4) The reports submitted by Respondent will likely include proprietary, financial, confidential, and competitive business information. Public disclosure of the reports could discourage cooperation, impede pending or potential government investigations, or undermine the objectives of the reporting requirement. For these reasons, among others, the reports and the contents thereof are intended to remain and shall remain non-public, except (a) pursuant to court order, (b) as agreed by the parties in writing, (c) to the extent that the Commission staff determines in its sole discretion that disclosure would be in furtherance of the Commission's discharge of its duties and responsibilities, or (d) is otherwise required by law.

(5) During this two-year period of review, Respondent shall provide its external auditors with its annual internal audit plan and reports of the results of internal audit procedures and its assessment of its FCPA compliance policies and procedures.

(6) During this two-year period of review, Respondent shall provide the Commission staff with any written reports or recommendations provided by Respondent's external auditors in response to Respondent's annual internal audit plan, reports of the results of internal audit procedures, and its assessment of its FCPA compliance policies and procedures.

F. AB InBev has agreed that, within 60 days from the date the Commission enters this Order, it will make reasonable efforts to contact the former employees of AB InBev's United States entities previously identified by the Commission staff, and provide them with a copy of this Order and a statement that AB InBev does not prohibit former employees from contacting the Commission regarding possible violations of federal law or regulation.

G. AB InBev has agreed to certify, in writing, compliance with the undertaking set forth in Paragraph IV.F above. The certification shall identify the undertaking, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Ansu Banerjee, Assistant Regional Director, Los Angeles Regional Office, with a copy to the Office of the Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of completion of the undertaking.

H. In determining to accept the Offer, the Commission considered the remedial acts described above, cooperation afforded to the Commission staff, and this undertaking.

By the Commission.

Brent J. Fields
Secretary