

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 60043 / June 4, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13502

In the Matter of

Merchant Capital, L.L.C.,

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE AND
CEASE-AND-DESIST PROCEEDINGS
PURSUANT TO SECTIONS 15(b), 15B(c)(2) 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), 15B(c)(2), and 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Merchant Capital, L.L.C. (“Merchant Capital” 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 Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b), 15B(c)(2) 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 Respondent’s Offer, the Commission finds that:

SUMMARY

1. These proceedings arise out of Merchant Capital’s violations of the gifts and gratuities, fair dealing and supervisory rules of the Municipal Securities Rulemaking Board

(“MSRB”) by paying for travel and entertainment expenses of family members, friends or associates of senior officials at two public finance clients (the “Issuers”) and later receiving reimbursement for such expenses from the Issuers, and, in certain instances, directly from the proceeds of bond offerings made by the Issuers. From 2003 through 2005, the Issuers obtained bond insurance and credit ratings for their bond offerings from bond insurance firms and credit rating agencies based in New York City. In connection with the Issuers’ efforts to obtain bond insurance and favorable credit ratings, officials of the Issuers traveled with Merchant Capital’s investment bankers to New York City on several occasions to meet with analysts from the bond insurance firms and credit rating agencies. Issuer officials brought family members, friends or associates, some of whom were employed by the Issuers, on these trips who, although they did not attend business meetings, incurred expenses for airfare, car service, meals at upscale restaurants, and tickets to Broadway shows and various sporting events. Based on input from representatives of the Issuers, Merchant Capital organized the activities for these trips, and advanced the payment for nearly all of the expenses incurred by the Issuer officials and their family members, friends or associates. Merchant Capital then sought and obtained, with the knowledge and approval of the senior officials of the Issuers who participated in the trips, reimbursement for expenses incurred on the trips.

RESPONDENT

2. Merchant Capital, L.L.C. (“Merchant Capital”), an Alabama corporation, has been registered with the Commission as a broker and dealer since 1985, with the Financial Industry Regulatory Authority (or its predecessor) since April 12, 1971 and with the MSRB as a municipal securities dealer since December 29, 1975. Merchant Capital is primarily owned by Merchant Capital Investments, Inc., the firm’s parent company.

FACTS

BACKGROUND

3. Over the past ten years, Merchant Capital has underwritten several bond issues through which the Issuers raised capital for various infrastructure projects. From 2003 through 2005, Merchant Capital investment bankers and Issuer officials took trips to New York City to discuss planned bond issues with bond insurers and credit rating agencies.

4. Several Issuer officials took family members, friends or associates on these trips. The travel and entertainment expenses incurred by these family members, friends or associates, some of whom were employed by the Issuers, were advanced by Merchant Capital and subsequently reimbursed by the Issuers from the proceeds of bond offerings associated with the trips. Merchant Capital did not adequately consider whether the officials reimbursed the Issuers for those expenses. In fact, the Issuer officials made no effort to reimburse the Issuers for the expenses incurred by their family members, friends or associates.

5. On each of these trips, Issuer officials coordinated with Merchant Capital in planning and organizing the trips’ various activities. Merchant Capital scheduled meetings with

the bond insurers and credit rating agencies, paid for airline tickets of Issuer officials as well as their family members and friends or associates, made hotel reservations for all of the trip participants and reserved a car service to transport Issuer officials and their family members, friends or associates around New York City for business purposes and non-business excursions. Issuer officials typically advised Merchant Capital regarding restaurants and entertainment activities they had selected for the trips, and thereafter Merchant Capital made the necessary reservations, paid for meals, and advanced the funds to purchase the requested entertainment tickets for Issuer officials as well as their family members and friends or associates.

6. Merchant Capital later invoiced the Issuers for the travel and entertainment expenses incurred on the trips along with other expenses associated with the relevant bond offerings, such as: (1) third-party bond registration-related fees; (2) printing and mailing costs; and (3) a credit rating agency fee. Merchant Capital's underwriting fee, known as an underwriter's discount, was not included on the invoices, but instead was set forth in underwriter's agreements associated with each bond offering. The expenses incurred on the trips to New York City were billed to the Issuers under a single line-item called "rating trip expenses" on the underwriting invoices. This line item included the travel and entertainment expenses incurred by Issuer officials and their family, friends or associates on the rating trips associated with the invoiced bond offerings as well as the travel and entertainment expenses incurred by Merchant Capital bankers on those trips. Merchant Capital obtained reimbursement for the invoiced travel and entertainment expenses.

7. For the relevant time period, Merchant Capital did not have adequate compliance policies and procedures in place to prevent violations of the rules that prohibit any broker, dealer, or municipal securities dealer from, directly or indirectly, giving or permitting to be given any thing or service of value in excess of \$100 per year to Issuer officials.

TRIPS ON BEHALF OF ISSUER A

June 2003 Trip

8. In June 2003, Merchant Capital investment bankers and officials from one of the Issuers ("Issuer A") went to New York City to meet with three bond insurers to discuss upcoming bond offerings by Issuer A.

9. One Issuer official brought his wife and two other family members on the trip. Although his wife was an employee of Issuer A, she was not involved in the bond issuance process and did not attend any of the bond insurer meetings. The other two family members were not Issuer A employees and also did not attend any meetings. Instead, the Issuer official's wife and other family members attended the Broadway shows "Gypsy" and "Hairspray" and dined at the Gotham Bar & Grill and other New York City restaurants.

10. This same Issuer official also invited his aunt and uncle to join him on the June 2003 trip. His aunt and uncle did not attend any of the meetings with bond insurers. Instead, they visited a college where their son had recently been accepted for admission. They also attended the

above-referenced Broadway shows, dined at fine restaurants, and attended a New York Yankees game.

11. Another official of Issuer A also attended the June 2003 trip as an important participant in the meetings with the bond insurers. This Issuer official brought an adult child on the trip. The Issuer official's adult child did not attend any of the meetings with bond insurers. Merchant Capital arranged for the adult child to attend two Broadway shows. The adult child also dined at three upscale restaurants.

12. Merchant Capital provided car service for the Issuer officials' family members in New York City.

13. Six of the eight individuals who went on the June 2003 trip with the investment bankers were family members of Issuer officials. Although some of these individuals were employed by Issuer A, they were unnecessary participants on the trip. Merchant Capital paid and was subsequently reimbursed for the expenses incurred on behalf of the six individuals, including airfare, car service, meals and entertainment.

14. Merchant Capital invoiced Issuer A to seek reimbursement for the expenses it incurred during this June 2003 trip, including those expenses it advanced on behalf of the Issuer officials' family members. Merchant Capital billed the expenses for the June 2003 trip in a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, the Issuer paid the invoices, which included \$8,969 in travel and entertainment expenses improperly advanced on behalf of the unnecessary participants on the trip. These expenses were paid out of the proceeds of Issuer A's bond sales in 2003 as a cost of the issuances.

September 2003 Trip

15. Merchant Capital investment bankers and officials from Issuer A made a second trip to New York City in September 2003, this time to meet with credit rating agencies. One Issuer official brought his wife, also an employee of Issuer A, on this trip. His wife did not attend any credit rating agency meetings. Instead, she attended the Broadway show "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club. The same Issuer official also invited his friend along, who was a part-time employee of Issuer A. The part-time employee took his wife along. The part-time employee's wife did not attend any credit rating agency meetings. Instead, she also saw "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club.

16. Two other officials of Issuer A also went on this trip. One brought her boyfriend; the other brought his wife. Although the boyfriend was an employee of Issuer A, neither the boyfriend nor the wife attended any credit rating agency meetings on this trip. Instead, they saw "Chicago" and dined at Smith & Wollensky and the Manhattan Ocean Club.

17. Four of the eight individuals who went on the September 2003 trip with the investment bankers were family members, friends or associates of Issuer officials. Although some were employees of Issuer A, they were unnecessary participants on the trip. Merchant Capital paid

and was subsequently reimbursed for expenses incurred on behalf of the four individuals, including airfare, car service, meals and entertainment.

18. Merchant Capital invoiced Issuer A to seek reimbursement for expenses it incurred during this September 2003 trip, including those expenses it advanced on behalf of the Issuer officials' family members, friends or associates. Merchant Capital billed the expenses under a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, when Issuer A's 2003 bond offerings closed, it paid the invoices directly out of the proceeds of the bond offerings as a cost of the issuances. The invoices included \$4,549 in travel and entertainment expenses improperly advanced on behalf of the unnecessary participants on the trip.

19. In total, the expenses incurred for these individuals during the June and September 2003 rating trips accounted for approximately eight percent of Issuer A's 2003 bond issuance costs, excluding the underwriter's discount.

November 2004 Trip

20. Merchant Capital investment bankers made a third trip to New York City on behalf of Issuer A in November 2004 to meet with bond insurers and credit rating agencies. Several Issuer officials' family members went on this trip.

21. One Issuer official took his wife, also an employee of the Issuer, and three other relatives, two of whom were Issuer employees, on this trip. None of these family members had any business purpose for accompanying the Issuer official to New York City, and, accordingly, none of them attended any of the bond insurer or credit rating agency meetings.

22. Instead, the Issuer official's family members attended the Radio City Music Hall Christmas Spectacular, saw the Broadway show "Wicked" and dined at the Blue Water Grill. Additionally, two of the family members saw the Broadway show "Avenue Q," while two others attended a world heavyweight championship boxing match at Madison Square Garden.

23. Another Issuer official brought an adult child on this November 2004 trip. The adult child did not attend any bond insurer or credit rating agency meetings. Instead, the Issuer official's adult child attended the Radio City Music Hall Christmas Spectacular and saw two Broadway shows.

24. A third employee of Issuer A made this trip and brought her husband. The husband was an employee of Issuer A, but he had no role in the bond issuance process and, accordingly, did not attend any bond insurer or credit rating agency meetings during the trip. Instead, the husband attended the Radio City Music Hall Christmas Spectacular, saw "Wicked" and dined at the Blue Water Grill. The husband also went to the world heavyweight championship boxing match.

25. In all, six of the ten individuals who went on the November 2004 trip with the investment bankers were family members of Issuer officials and, although some were employed by the Issuer, they did not attend any meetings and were unnecessary participants on the trip.

Merchant Capital advanced and was subsequently reimbursed for expenses incurred on behalf of the six family members, including airfare, car service, meals and entertainment.

26. Merchant Capital invoiced Issuer A to seek reimbursement for most of the expenses it incurred during this November 2004 trip, including most of the expenses it advanced on behalf of the Issuer officials' family members. Merchant Capital billed the expenses under a single line-item entitled "rating trip expenses" on the underwriting invoices. Thereafter, when Issuer A's 2005 bond offerings closed, Merchant Capital sought and obtained reimbursement for the November 2004 rating trip expenses directly out of the proceeds of the bond offerings as a cost of the issuances. In total, Merchant Capital improperly advanced \$8,925 in travel and entertainment expenses on behalf of the family members of the Issuer officials and subsequently obtained reimbursement for at least \$7,809 of those expenses.

27. In total, the expenses incurred for these family members during the November 2004 rating trip accounted for approximately seven percent of Issuer A's 2005 bond issuance costs, excluding the underwriter's discount.

28. The state government travel laws and Issuer A's guidelines and policies in effect during the relevant time period required officials of Issuer A to: (1) obtain advance approval for their out of state travel; (2) provide an itemization of expenses to identify those that are actual and necessary and subject to reimbursement; and (3) identify, in advance, the source of the funds that would be used to pay for the trip. The Issuer officials who attended the out-of-state rating trips did not comply with these state travel laws, guidelines and policies. Moreover, the relevant state travel laws and Issuer guidelines and policies contain no provisions that would allow Issuer officials to permit the travel expenses of friends or associates and family members who accompany them on official out-of-state business to be advanced by a municipal securities dealer and later reimbursed by the Issuer.

29. After it advanced the funds for the Issuer officials' family members, friends or associates, Merchant Capital did not adequately consider whether the officials reimbursed the Issuer for those expenses. In fact, the officials did not reimburse Issuer A for the travel and entertainment expenses incurred by their family members, friends or associates on the July 2003, September 2003 or November 2004 trips.

30. In total, Merchant Capital paid and was subsequently reimbursed at least \$21,327 for travel and entertainment expenses incurred by family members, friends or associates in connection with the June 2003, September 2003 and November 2004 trips to New York City on behalf of Issuer A.

TRIPS ON BEHALF OF ISSUER B

June 2004 Trip

31. In June 2004, Merchant Capital investment bankers, an official from another of the Issuers ("Issuer B"), and an advisor to Issuer B went to New York City to meet with credit rating

agencies and bond insurers in connection with an upcoming bond issuance. The advisor brought his wife and two children, and the Issuer official brought his wife.

32. The Issuer's advisor traveled to New York City with his wife and two children on a Friday, three days prior to the meetings scheduled for the following Monday. The advisor paid personally for his family's airfare and hotel costs.

33. None of the Issuer official's or advisor's family members attended any of the meetings with credit rating agencies or bond insurers. Rather, the family members enjoyed meals at Oceana, Estiatorio Milos and the Gotham Bar & Grill. They also attended the Broadway show "Mamma Mia" and a New York Mets game.

34. Four of the eight individuals who went on the June 2004 trip with the investment bankers were family members, did not participate in any of the meetings, and were unnecessary participants on the trip. Merchant Capital advanced and was subsequently reimbursed for expenses incurred on behalf of the four family members, including car service, meals, and entertainment.

35. Merchant Capital invoiced Issuer B to seek reimbursement for the expenses it advanced during this June 2004 trip, including those expenses it advanced on behalf of the Issuer official's and the advisor's family members. Thereafter, the Issuer paid the invoice, which included \$2,247 in travel and meal expenses improperly advanced on behalf of the official's wife and the advisor's family members.

36. In total, the expenses incurred by the family members during the June 2004 rating trip accounted for approximately fifteen percent of Issuer B's 2004 bond issuance costs, excluding the underwriter's discount.

May 2005 Trip

37. In May 2005, Merchant Capital investment bankers and the officials from Issuer B made another trip to New York City to meet with credit rating agencies. One of the Issuer officials brought his wife.

38. Merchant Capital paid and was subsequently reimbursed for expenses advanced on behalf of the wife, including airfare and a meal at the Blue Water Grill.

39. Merchant Capital invoiced Issuer B to seek reimbursement for certain expenses it incurred during this May 2005 trip, including those expenses it advanced on behalf of the Issuer official's wife. Thereafter, the Issuer paid the invoice, which included \$543 in travel and meal expenses improperly advanced on behalf of the official's wife.

40. After it advanced the funds for the Issuer official's wife and the advisor's family members, Merchant Capital did not adequately consider whether the official or the advisor reimbursed the Issuer for those expenses. In fact, the Issuer B official and advisor did not reimburse the Issuer for the travel and entertainment expenses advanced by Merchant Capital and

paid by Issuer B in connection with the June 2004 and May 2005 trip.

41. In total, Merchant Capital paid and was subsequently reimbursed \$2,790 for travel and entertainment expenses incurred by family members in connection with the June 2004 and May 2005 trips to New York City on behalf of Issuer B.

42. Since the time of the above-referenced rating trips, Merchant Capital has taken significant steps to improve the way it organizes and oversees rating trips taken by its clients, including the implementation of employee training programs.

VIOLATIONS

43. Section 15B(b) of the Exchange Act established the MSRB and empowered it to propose and adopt rules with respect to transactions in municipal securities by brokers, dealers, and municipal securities dealers. Section 15B(c)(1) prohibits a broker, dealer or municipal securities dealer from using the mails or any instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security in violation of any MSRB rule. As a municipal securities dealer, Merchant Capital was subject to Section 15B(c)(1) of the Exchange Act and the MSRB rules.

44. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-17, which requires municipal securities dealers to deal fairly with all persons and not to engage in any deceptive, dishonest, or unfair practice.

45. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-20(a), which prohibits any broker, dealer, or municipal securities dealer from, directly or indirectly, giving or permitting to be given any thing or service of value, including gratuities, in excess of \$100 per year to a person other than an employee or partner of such broker, dealer, or municipal securities dealer, if such payments or services are in relation to the municipal securities activities of the recipient's employer.

46. As a result of the conduct set forth above, Merchant Capital violated MSRB Rule G-27, which requires, among other things, that (a) each broker, dealer and municipal securities dealer supervise the conduct of its municipal securities business and the municipal securities activities of its associated persons to ensure compliance with MSRB rules as well as the applicable provisions of the Exchange Act and the rules promulgated thereunder; and (b) each broker, dealer and municipal securities dealer to adopt, maintain, and enforce written supervisory procedures reasonably designed to ensure compliance with the same rules and Exchange Act provisions.

47. As a result of Merchant Capital's violations of MSRB Rules G-17, G-20, and G-27, Merchant Capital willfully¹ violated Section 15B(c)(1) of the Exchange Act.

¹ 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.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer. Accordingly, pursuant to Sections 15(b), 15B(c)(2) and 21C of the Exchange Act, it is hereby ORDERED that:

A. Respondent cease and desist from committing or causing any violations and any future violations of Section 15B(c)(1) of the Exchange Act, and MSRB Rules G-17, G-20 and G-27.

B. Respondent shall be, and hereby is, censured.

C. Respondent shall, within 10 days of the date of entry of this Order, pay a civil money penalty in the amount of \$55,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Such payment shall be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Merchant Capital, L.L.C. as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Gerald W. Hodgkins, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549.

By the Commission.

Elizabeth M. Murphy,
Secretary

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)).