

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-13673

<p>In the Matter of</p> <p>J.P. MORGAN SECURITIES INC.</p> <p>Respondent.</p>
--

PROPOSED PLAN OF DISTRIBUTION

This proposed Plan of Distribution (“Distribution Plan”) provides for the distribution of the disgorgement and civil penalty paid by J.P. Morgan Securities Inc. (“J.P. Morgan Securities” or “Respondent”) in settlement of the above-referenced administrative proceeding.

Background and Settlement Description

1. On November 4, 2009, the Securities and Exchange Commission (“Commission”) issued an Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Section 8A of the Securities Act of 1933, and 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”) against Respondent. J.P. Morgan Securities, Inc., Securities Act Release No. 9078 (November 4, 2009).¹

2. Among other things, the Order found that J.P. Morgan Securities, through two of its managing directors, made over \$8.2 million in undisclosed payments in 2002 and 2003 to local firms whose principals or employees were friends of Jefferson County, Alabama (“the County”) public officials. The County officials were instrumental in selecting J.P. Morgan Securities as underwriter, and its affiliated bank as the swap provider, on over \$5 billion in bond underwriting and interest rate swap agreement business

¹ Concurrently with the settlement of this administrative proceeding, the Commission filed a civil injunctive action against two former J.P. Morgan Securities managing directors that participated in making the undisclosed payments described in the Order, *SEC v. Charles E. LeCroy and Douglas W. MacFaddin*, Case No. 2:09-cv-02238-AKK (N.D. Ala., filed November 4, 2009) (the “Injunctive Action”).

awarded by the County. In the Order, the Commission found that J.P. Morgan Securities willfully violated Sections 17(a)(2) and 17(a)(3) of the Securities Act of 1933 (“Securities Act”), Section 15B(c)(1) of the Securities Exchange Act of 1934 (“Exchange Act”), and Municipal Securities Rulemaking Board (“MSRB”) Rule G-17.

3. Pursuant to the Order, J.P. Morgan Securities was censured and ordered to cease and desist from committing or causing any violations and any future violations of the charged provisions. The Commission further ordered J.P. Morgan Securities to pay \$1 in disgorgement and a \$25 million civil penalty, and authorized the creation of a Fair Fund pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, to distribute the disgorgement and civil penalty paid by Respondent (the “Fair Fund”). Under the terms of the settlement, J.P. Morgan Securities also agreed to: (1) comply with a voluntary undertaking by making an immediate \$50 million payment to the County; and (2) terminate any and all obligations of the County to make any payments to its affiliated bank under the swap agreements.

4. On November 10, 2009, J.P. Morgan Securities paid \$25,000,001 to the Securities and Exchange Commission and, subsequently, the funds were transferred to the U.S. Department of Treasury Bureau of Public Debt (“BPD”) and have been invested in short-term U.S. Treasury bills. The assets of the Fair Fund are subject to the continuing jurisdiction and control of the Commission. This Plan is subject to approval by the Commission, and the Commission retains jurisdiction over the implementation of the Plan.

Administration of the Distribution Plan

5. Purpose. The Distribution Plan has been developed pursuant to the Order and the SEC Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1100, *et seq.* (the “Rules”). The purpose of the Distribution Plan is to distribute the Fair Fund to any investor or other party harmed by the conduct described in the Order (“Eligible Recipient”).

6. Plan Administrator. Rule 1105 provides that the Commission “shall have the discretion to appoint any person, including a Commission employee, as administrator of a plan of disgorgement or a Fair Fund and to delegate to that person responsibility for administering the plan.” Nichola L. Timmons, Assistant Chief Litigation Counsel in the Enforcement Division’s Office of Collections and Distributions, is proposed to act as the fund administrator for the Distribution Plan (“Plan Administrator”). As a Commission employee, the Plan Administrator shall receive no compensation, other than her regular salary, for her services in administering the Fair Fund. The Plan Administrator shall be responsible for, among other things, overseeing the administration of the Fair Fund, preparing accountings, cooperating with the Tax Administrator in providing the information necessary to accomplish income tax compliance, distributing the Fair Fund to the Eligible Recipient(s) in accordance with the Distribution Plan, and preparing a final accounting.

7. Bond. Because the Plan Administrator is a Commission employee, no bond is required pursuant to Rule 1105(c).

Distribution Plan and Procedures

8. Receipt of Additional Funds. Rule 1101(b)(1) provides, among other things, that a distribution plan shall include “[p]rocedures for the receipt of additional funds.” The Fair Fund has been deposited at the BPD for investment in short-term government obligations. The Fair Fund will from time to time receive interest from these investments. In the event the defendants in the Injunctive Action are ordered by the District Court to pay disgorgement with prejudgment interest, those funds may, but are not required to be, deposited into this Fair Fund, and distributed in accordance with the Distribution Plan.

9. Identifying the Eligible Recipient(s) of the Fair Fund. Rule 1101(b)(2) provides that a distribution plan shall include a “[s]pecification of categories of persons potentially eligible to receive proceeds from the fund.” As stated in the Order, the Commission found that J.P. Morgan Securities made undisclosed payments to local firms whose principals were friends of Jefferson County public officials involved in the selection of firms for the County’s municipal securities business. The enforcement action concerned conduct and payments in connection with three County bond offerings and three security-based swap agreements between October 2002 and November 2003, totaling approximately \$5 billion.² Accordingly, the pool of potential recipients include the County, which was a counterparty to the relevant interest rate swap agreements, and the individuals and entities that purchased bonds in the relevant bond offerings.

The staff engaged the assistance of the Commission’s Division of Risk, Strategy and Financial Innovation (“RiskFin”) to determine whether the County and/or any of the original bond holders suffered economic harm directly related to the improper payment scheme. RiskFin conducted an analysis based upon a detailed review of, among other things, the relevant transactions, findings in the Order and allegations in the Injunctive Action complaint, and market data. RiskFin determined that the County suffered direct economic harm caused by the scheme. This conclusion was based on the findings in the Order and allegations in the Injunctive Action complaint that J.P. Morgan Securities passed on the costs of the improper payments to the County in the form of inflated fixed interest rates on the swaps. These inflated fixed interest rates directly harmed the County by increasing the swap payments it had to make over what it would have paid absent the improper payment scheme. Additionally, commencing in March 2008, the County could no longer continue to make payments under the swap agreements and entered into a series of forbearance agreements until March 2009, at which time J.P. Morgan Securities’ affiliated bank notified the County that it was terminating the swap agreements and triggering the obligation to pay all outstanding payments (including the inflated interest), totaling over \$647 million. That obligation was not extinguished until November 2009, in

² These transactions are: (1) \$839 million sewer bond offering that closed on October 24, 2002; (2) \$1.1 billion sewer bond offering that closed on May 1, 2003 (“the 2003-B bonds”); (3) \$1.05 billion sewer bond offering that closed on August 7, 2003 (“the 2003-C bonds”); (4) \$1.1 billion swap agreement executed in connection with the 2003-B bonds; (5) \$789 million swap agreement executed in connection with the 2003-C bonds; and (6) \$111 million swap agreement executed on November 7, 2003 with an effective date of May 1, 2004.

connection with J.P. Morgan Securities' agreement to settle the above-referenced administrative action, but by then the County suffered additional harm to its reputation, credit rating and ability to refinance these obligations.

RiskFin further concluded that, as to the original bond holders (1) there was no evidence or information that the interest rates bond holders received was affected by the improper payment scheme; and (2) the harm suffered by original bond holders was largely the result of the failures of the markets for variable rate demand warrants and auction rate warrants, and there is no evidence to indicate that these failures were caused by the improper payment scheme. Accordingly, the staff, in consultation with RiskFin, has concluded that the Eligible Recipient of the Fair Fund is the County.

10. Notifying the Eligible Recipient. Rule 1101(b)(3) provides that a plan shall include “[p]rocedures for providing notice to such persons of the existence of the fund and their potential eligibility to receive proceeds of the fund.” Because the Eligible Recipient of the Fair Fund is the County, it is proposed that the Plan Administrator notify the Eligible Recipient of the Distribution Plan by contacting the current president of the County Commission with (a) a notification of the Distribution Plan, and (b) the proposed distribution amount to be paid to the Eligible Recipient. The Plan Administrator will provide such notice by United States Postal Service and will request from the Eligible Recipient such information necessary to accomplish the distribution, including confirmation of: (i) tax identification number, if applicable, (ii) payment address, and (iii) wiring instructions. If the Eligible Recipient fails to respond to such notice within twenty-one (21) days from the mailing of the notice, the Plan Administrator will send a second written notice by mail. If the Eligible Recipient does not respond to the second notice within twenty-one (21) days, the Plan Administrator will make two attempts to contact the Eligible Recipient telephonically.

11. No Claims Process. Rule 1101(b)(4) provides, among other things, that a plan shall include “[p]rocedures for making and approving claims, procedures for handling disputed claims, and a cut-off date for the making of claims.” Since this Fair Fund is not being distributed according to a claims-made process, the procedures for providing notice and for making and approving claims are not applicable.

12. Qualified Settlement Fund. The Fair Fund constitutes a Qualified Settlement Fund under Section 468B(g) of the Internal Revenue Code, 26 U.S.C. §468B(g), and related regulations, 26 C.F.R. §§ 1.468B-1 through 1.468B-5.

13. Implementation of the Fair Fund; Financial Management Service; Validation and Approval of Disbursement of the Fair Fund. The Fair Fund disbursement to the Eligible Recipient will be implemented through the United States Department of the Treasury's Financial Management Service (“FMS”), which will electronically transfer funds through the Automated Clearing House (“ACH”) or mail a check to the payee. Commission staff will provide the Plan Administrator with appropriate proprietary software for compiling the information necessary to be submitted to FMS. The Plan Administrator will compile the information into the specified file format and submit this

electronic file to the assigned Commission staff. The Plan Administrator will validate the payee and amount in the file to the Commission staff. The validation will state that the electronic file was compiled in accordance with the Plan and provides all information necessary for FMS to make disbursement through the ACH or by check. The Plan Administrator will coordinate with the appropriate Commission staff to ensure the electronic file passes all system edits for a timely distribution. Upon receipt of a properly validated file, the Commission staff will obtain authorization from the Commission to disburse pursuant to SEC Rule 1101(b)(6). When the electronic file and validation are approved and the order to disburse is entered, the Commission will transmit the electronic file to FMS for the transfer of funds pursuant to the following FMS procedures.

Within 48 hours of receipt by FMS, funds will be transferred by the ACH or a check will be mailed. FMS will notify the Commission, which, in turn, will notify the Plan Administrator of any returned item due to non-delivery, insufficient addresses, and/or other deficiencies. The Plan Administrator is responsible for researching and reconciling all errors that result in non-delivery and shall submit a supplemental electronic file for payment of the returned items.

The Plan Administrator also is responsible for accounting for all payments. In the event that any distribution is in the form of a paper check in lieu of an electronic transfer, the check will state on its face that it is valid for one year. After one year from the date on the distribution check, FMS shall notify the Commission, which, in turn, will notify the Plan Administrator of the uncashed check. FMS will credit the SEC account for the Fair Fund for the amount of the uncashed check.

14. Expenses of Administration. Fees and other expenses of administering the Distribution Plan shall be paid first from the interest earned on the funds and, if the interest is not sufficient, then from the corpus.

15. Tax Administrator. The Commission has appointed Damasco & Associates as the tax administrator for the Fair Fund (the "Tax Administrator"). See J.P. Morgan Securities Inc., Order Appointing Tax Administrator, Exchange Act Release No. 61028 (November 19, 2009). The Plan Administrator will cooperate with the Tax Administrator in providing information necessary to accomplish the income tax compliance, ruling and advice work assigned to the Tax Administrator by the Commission. The Tax Administrator shall be compensated first from the interest earned on the funds, and if that interest is not sufficient, then from the corpus.

16. Accountings. The Plan Administrator will submit a final accounting on the standardized accounting form provided by the Commission staff for approval of the Commission prior to termination of the Fair Fund and discharge of the Plan Administrator. Since the funds are being held at the BPD, and a Tax Administrator has been appointed, no interim accounting will be conducted.

17. Termination of the Fair Fund. The Fair Fund shall be eligible for termination, and the Plan Administrator shall be discharged, after all of the following have occurred: (1) the Final Accounting has been submitted by the Plan Administrator for approval of, and has been approved by, the Commission; (2) all taxes fees, and expenses have been paid; and (3) any amount remaining in the Fair Fund has been received by the Commission. When the Commission has approved the final accounting, the staff shall seek an order from the Commission to approve the termination of the Fair Fund and discharge of the Plan Administrator.

18. Amendments and Procedural Deadline Extensions. The Plan Administrator shall take reasonable and appropriate steps to distribute the Fair Fund according to the Distribution Plan. Where the Plan Administrator deems necessary, after agreement with Commission staff, the Plan Administrator may implement immaterial changes to the Distribution Plan to effectuate its general purposes. If a change is deemed material by Commission staff, Commission approval is required prior to implementation by amending the Distribution Plan, which may be done upon the motion of any party, the Plan Administrator, or upon the Commission's own motion.

For good cause shown, the Commission staff may extend any of the procedural deadlines set forth in this Plan.

Notice of Proposed Distribution Plan

19. In accordance with Rule 1103, notice of the proposed Distribution Plan shall be published in the SEC Docket and on the Commission's website [<http://www.sec.gov>]. Any person or entity wishing to comment on the Plan may do so by submitting their comments, in writing, within thirty (30) days of the publication date of the Notice to the Office of the Secretary, United States Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090; by using the Commission's Internet comment form (www.sec.gov/litigation/admin.shtml); or by sending an e-mail to rule-comments@sec.gov, including the appropriate Administrative Proceeding File Number in the subject line. Comments received will be publicly available. Persons should submit only information that they wish to make publicly available.