

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES ACT OF 1933**  
**Release No. 8585 / July 8, 2005**

**INVESTMENT ADVISERS ACT OF 1940**  
**Release No. 2404 / July 8, 2005**

**INVESTMENT COMPANY ACT OF 1940**  
**Release No. 26986 / July 8, 2005**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-11976**

**In the Matter of**

**GERALD KLEIN &  
ASSOCIATES, INC. AND  
KLEIN PAVLIS &  
PEASLEY FINANCIAL,  
INC.,**

**Respondents.**

**ORDER INSTITUTING  
ADMINISTRATIVE AND CEASE-AND-  
DESIST PROCEEDINGS PURSUANT TO  
SECTION 8A OF THE SECURITIES ACT  
OF 1933, SECTION 203(e) OF THE  
INVESTMENT ADVISERS ACT OF 1940,  
AND SECTIONS 9(b) AND 9(f) OF THE  
INVESTMENT COMPANY ACT OF 1940,  
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 Section 8A of the Securities Act of 1933 (“Securities Act”), Section 203(e) of the Investment Advisers Act of 1940 (“Advisers Act”), and Sections 9(b) and 9(f) of the Investment Company Act of 1940 (“Investment Company Act”) against Gerald Klein & Associates, Inc. (“GKA”) and Klein Pavlis & Peasley Financial, Inc. (“KPP”) (collectively, “Respondents”).

## **II.**

In anticipation of the institution of these proceedings, Respondents have submitted an Offer of Settlement (“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 them and the subject matter of these proceedings, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Section 203(e) of the Investment Advisers Act of 1940, and Sections 9(b) and 9(f) of the Investment Company Act of 1940, 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, the Commission finds that:

### **SUMMARY**

1. This matter involves registration violations in connection with the offering of interests in two hedge funds: Invest Talk Partners I, L.P. (“Fund I”) and Invest Talk Partners II, L.P. (“Fund II”). These hedge funds were organized and operated by two affiliated registered investment advisers, Gerald Klein & Associates, Inc. (“GKA”) and Klein Pavlis & Peasley, Financial, Inc. (“KPP”). These investment advisers established the hedge funds to accommodate investors who wanted to be clients in GKA’s separately managed account program but did not qualify due to GKA’s \$250,000 account minimum. The hedge funds were therefore offered to “retail” investors. The offer, sale, and operation of these hedge funds were not exempt from, and therefore resulted in the violation of, the registration provisions of the Securities Act and the Investment Company Act because of general solicitation through seminars, the radio, and the Internet, and because the offerings should have been integrated.

### **RESPONDENTS**

2. GKA is a California corporation with its principal place of business in Monarch Beach, California. GKA is an investment adviser that has been registered with the Commission since December 24, 1998. The firm provides investment management services on a discretionary basis to individuals and family trusts. It currently has approximately 109 client accounts and approximately \$38 million in assets under management.

3. KPP is a Nevada corporation with its principal place of business in Dana Point, California. KPP is an investment adviser that has been registered with the Commission since February 2, 1994. The firm provides mutual fund asset allocation services to clients on a discretionary basis. It currently has approximately 350 client accounts and just over \$25 million in assets under management.

## **FORMATION AND OFFERING OF THE HEDGE FUNDS**

4. In early 2000, GKA and KPP decided to start a hedge fund that would employ essentially the same investment strategies that GKA used for its separately managed client accounts, but would accommodate investors who did not have the \$250,000 minimum to become a direct GKA client. The hedge fund was designed to accept non-accredited investors with as little as \$50,000 to invest.

5. In November 2000, GKA and KPP formed Fund I as a limited partnership and Invest Talk, Inc. (“Invest Talk”) to be its general partner. In December 2000, Invest Talk began offering interests in Fund I to investors. In 2002, GKA and KPP formed a second hedge fund, Fund II. In June 2002, Invest Talk began offering interests in Fund II to investors. Invest Talk managed the portfolios of Fund I and Fund II. In late 2003, KPP assumed all investment management decisions for Fund I. Fund II was liquidated in 2004 and the proceeds were returned to investors.

## **THE OFFERINGS INCLUDED A GENERAL SOLICITATION**

6. At all relevant times, GKA and KPP marketed their investment advisory services through radio programs, investment seminars, and the Internet. While the interests in Fund I and Fund II were being offered to investors, GKA and KPP principals talked about these hedge funds, including the reason for starting the Funds, the investment strategies, and minimum investment amounts, during at least one radio program. During the same offering period, the hedge funds were also discussed by GKA and KPP principals during one or more investment seminars. In addition, performance figures for the hedge funds, fund strategy, and contact information were posted for a brief period in the fall of 2002 on the advisers’ shared website, which was accessible to the general public. Accordingly, as a result of these marketing activities, the offerings of the hedge funds included a general solicitation.

## **THE TWO HEDGE FUNDS WERE NEARLY IDENTICAL AND SHOULD HAVE BEEN INTEGRATED**

7. In its offering materials, Fund I’s stated investment strategy was to take long positions in stocks of domestic companies which exhibited recent trends of advancing prices, and short positions in stocks with recent trends of declining prices. Fund II’s stated investment strategy was almost identical, but included an intention to also invest a minimum of 15% of its net assets in fixed income securities. In the actual management of Fund I and Fund II, however, GKA and KPP caused both funds to hold essentially the same investment portfolios. For example, as of November 2002, 23 of the 24 long equity positions held by Fund II were also held by Fund I, and both funds had one short position in the same security. Because the two funds were nearly identical, their offerings should have been integrated, i.e., combined. See In the Matter of George W. Meyers, Advisers Act Release No. 1640 (June 23, 1977); see also In the Matter of Kenneth Von Kohorn, Advisers Act Release No. 1471 (February 22, 1995).

8. As of November 2002, Fund I had approximately \$10.3 million in assets, 40 accredited investors, and 34 non-accredited investors. At that same time, Fund II had approximately \$3.4 million in assets, 30 non-accredited investors, and eight accredited investors. The funds as integrated therefore had a total of 112 investors, including 64 non-accredited investors.

### **REMEDIAL ACTIONS**

9. In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondents and cooperation afforded the Commission staff.

### **VIOLATIONS**

10. Sections 5(a) and 5(c) of the Securities Act generally prohibit any person from offering or selling a security unless an appropriate registration statement is in effect or a valid exemption from registration exists. In the offer and sale of Fund I and Fund II, no registration statement was in effect, and because the offerings included a general solicitation and were made to over 35 non-accredited investors, there was no valid exemption from registration. Accordingly, GKA and KPP willfully violated Sections 5(a) and 5(c) of the Securities Act.

11. Section 7(a) of the Investment Company Act generally prohibits any investment company from engaging in the business of buying and selling securities unless it has registered with the Commission or has a valid exemption from registration. Section 3(c)(1) of the Investment Company Act generally excludes from the definition of investment company an issuer whose outstanding securities are beneficially owned by not more than 100 persons, and which is not making and does not presently propose to make a public offering of its securities. Similarly, Section 3(c)(7) of the Investment Company Act generally excludes from the definition of investment company an issuer whose outstanding securities are owned by persons who, at the time of acquisition, are qualified purchasers, and which is not making and does not presently propose to make a public offering of its securities. Because Fund I and Fund II on an integrated basis had 112 investors, because not all investors were qualified purchasers at the time of acquisition of the securities, and because the hedge funds were offered by means of a general solicitation, the hedge funds violated Section 7(a) of the Investment Company Act. Because GKA and KPP were responsible for forming, offering, and selling the hedge funds, these entities willfully aided and abetted and caused the hedge funds' violation of Section 7(a) of the Investment Company Act.

### **UNDERTAKINGS**

12. GKA and KPP have undertaken to:

a. Within 10 days after the entry of this Order, GKA and KPP will engage an Independent Consultant, who is not unacceptable to the Commission staff, to conduct quarterly compliance reviews of GKA's and KPP's investment advisory operations for a period of three years, commencing with the calendar-year quarter beginning on July 1, 2005. Within a reasonable time following completion of each quarterly review by the Independent Consultant, but not later than 30 days after such completion, GKA and KPP will provide the Pacific Regional

Office with a report on the results of the compliance review, along with a description of any actions taken or to be taken by GKA and/or KPP in response to findings by the Independent Consultant.

b. GKA and KPP will require the Independent Consultant to enter into an agreement that provides that for the period of engagement, and for a period of two years from completion of the engagement, the Independent Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with GKA, KPP, or any of their present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the Independent Consultant will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the Independent Consultant in performance of his/her duties under this Order shall not, without prior written consent of the Commission staff, enter into any employment, consultant, attorney-client, auditing or other professional relationship with GKA, KPP, or any of their present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

#### IV.

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

Accordingly, pursuant to Section 8A of the Securities Act, Section 203(e) of the Investment Advisers Act of 1940, and Sections 9(b) and 9(f) of the Investment Company Act, it is hereby ORDERED that:

- A. GKA and KPP are censured;
- B. GKA and KPP shall cease and desist from committing or causing any violations and any future violations of Sections 5(a) and 5(c) of the Securities Act, and from causing any violations and any future violations of Section 7(a) of the Investment Company Act;
- C. GKA and KPP shall each, within 60 days of the entry of this Order, pay a civil money penalty in the amount of \$20,000 to the United States Treasury. 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 GKA and KPP as Respondents in these proceedings, the file number of these proceedings, a copy of which cover letter and money orders or checks shall be sent to Michele Wein Layne, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 5670 Wilshire Boulevard, 11<sup>th</sup> Floor, Los Angeles, CA 90036; and

D. GKA and KPP shall comply with the undertakings enumerated in Section III. above.

By the Commission.

Jonathan G. Katz  
Secretary