

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-11538

In the Matter of

J. MICHAEL SCARBOROUGH and
ROYAL ALLIANCE ASSOCIATES, INC.

Respondents.

PROPOSED PLAN OF DISTRIBUTION

1. *Purpose and Background.* This Proposed Plan of Distribution (the "Plan") has been developed pursuant to the Commission's Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Section 8A of the Securities Act of 1933 and Section 15(b) of the Securities Exchange Act of 1934 (Rel. Nos. 33-8438 and 34-49982) against J. Michael Scarborough ("Scarborough") and Royal Alliance Associates, Inc. ("Royal Alliance") (collectively, "Respondents"), dated July 8, 2004 (the "Order"). The Plan provides for the distribution of the disgorgement, prejudgment interest, and civil monetary penalties provided for in the Order to those customers of Royal Alliance who would have paid lower commissions and fees and enjoyed higher overall returns but for the conduct described in the Order. Simultaneously with the entry of the Order, the Commission accepted settlement offers from Scarborough and Royal Alliance in which they consented to the entry of the Order without admitting or denying the Order's findings.

The Order found, among other things, that Scarborough was the manager of the Annapolis, Maryland branch office of Royal Alliance, a broker-dealer registered with the Commission. The Order further found that, from 1998 through early 2000, Scarborough, through the registered representatives under his supervision, sold Class B mutual fund shares to customers of Royal Alliance in amounts that would have entitled the customers to "breakpoint" sales charge discounts had they purchased Class A shares of the same mutual funds. Discounts were available for large purchases (usually \$100,000 or more) of Class A shares, often increasing at various investment levels, or "breakpoints." Although Scarborough, along with the registered representatives, disclosed the different characteristics of Class A shares and Class B shares to customers, they did not tell customers that Class A shares generally produce higher returns than Class B shares of the same mutual fund when purchased in amounts of \$100,000 or more. Between 1998 and early 2000, of the 406 Royal Alliance customers who qualified for a

breakpoint at the \$100,000 level or above, 399 customers, or 98 percent, purchased Class B shares even though all of these customers would have paid lower commissions and fees and enjoyed higher overall returns had they purchased Class A shares. If all of the customers who purchased Class B shares in amounts of \$100,000 or more had purchased Class A shares instead, they would have paid, and Scarborough and Royal Alliance would have received, \$1.7 million less in commissions.

As a result of this conduct, the Order found that Scarborough willfully violated Sections 17(a)(2) and 17(a)(3) of the Securities Act of 1933. The Order also found that Scarborough failed reasonably to supervise the registered representatives at the Annapolis branch office who engaged in this conduct under his direction, with a view to preventing their violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. Similarly, Royal Alliance failed reasonably to supervise Scarborough, its branch manager, as well as the registered representatives, with a view to preventing these violations of the securities laws.

The Order provided that Scarborough pay disgorgement and prejudgment interest in the total amount of \$2,111,084, and pay a civil monetary penalty in the amount of \$50,000, and that Royal Alliance pay \$1 in disgorgement and a civil monetary penalty in the amount of \$150,000.

In accordance with the Order, on August 18 and 24, 2004, Respondents paid a total of \$2,311,085 in disgorgement, prejudgment interest, and civil monetary penalties to the Commission. Pursuant to the Order, a Fair Fund was established for these funds. The assets of the Fair Fund are subject to the continuing jurisdiction and control of the Commission. The Fair Fund is currently on deposit at the U.S. Treasury's Bureau of Public Debt and has been invested in short-term U.S. Treasury securities.

This Plan is subject to approval by the Commission, and the Commission retains jurisdiction over the implementation of the Plan.

2. *Fund Administrator.* David S. Horowitz, an Assistant Regional Director in the Commission's Division of Enforcement, is proposed to act as the administrator of the Fair Fund (the "Fund Administrator"). As a Commission employee, the Fund Administrator shall receive no compensation, other than his regular salary as a Commission employee, for his services in administering the Fair Fund. In accordance with Rule 1105(c), no bond is required since the Fund Administrator is a Commission employee.

The Fund Administrator will, among other things: oversee the administration of the Fair Fund, obtain accurate mailing information for shareholders, prepare accountings, cooperate with the tax administrator in providing the information necessary to accomplish income tax compliance, and, as described below, distribute money from the Fair Fund in accordance with this Plan.

3. *Persons Eligible to Participate in the Fair Fund.* The staff of the Commission previously identified approximately 400 Royal Alliance customers who, between 1998 and early 2000, qualified for a breakpoint at the \$100,000 level or above, and who purchased Class B mutual fund shares even though these customers would have paid approximately \$1.7 million less in commissions had they purchased Class A shares. The staff's determination was based on

breakpoint discounts that could have been received through single purchases, rights of accumulation and/or letters of intent.¹ The Fund Administrator shall distribute Plan funds to these identified Royal Alliance customers harmed by the conduct described in the Order (individually, each “Eligible Customer,” and collectively, the “Eligible Customers”).

4. *No claims-made process.* This Fair Fund is not being distributed according to a claims-made process, so the procedures for providing notice and for making and approving claims are not applicable.

5. *Qualified Settlement Fund.* The Fair Fund constitutes a Qualified Settlement Fund (“QSF”) 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.

6. *Intentions of Distribution.* The intention of the Plan is to distribute the Fair Fund to approximately 400 Royal Alliance customers, each of whom is an Eligible Customer, who paid excessive commissions to Scarborough and Royal Alliance from 1998 through early 2000, as a result of the conduct described in the Order.

7. *Methodology for Determining Distribution Amounts.* The Fund Administrator will determine the amount to be distributed to each Eligible Customer in the following manner. First, the Fund Administrator will determine what percentage of Eligible Customers’ total excess commissions paid is represented by each Eligible Customer’s excess commissions. Next, for each Eligible Customer, the Fund Administrator will multiply this percentage by the total amount paid by the Respondents, plus any accrued interest and less any taxes, fees or other expenses of administering the Plan. This amount will represent each Eligible Customer’s distribution amount. In the view of the Fund Administrator, this methodology constitutes a fair and reasonable allocation of the Fair Fund. Based on this methodology, the anticipated distribution to each Eligible Customer will average approximately \$5,000, and will range from approximately \$700 to approximately \$23,000.

8. *Financial Management Service; Validation and Approval of Disbursement of the Fair Fund.* The Fair Fund disbursement to investors 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 each payee. Commission staff will provide the Fund Administrator with appropriate proprietary software for compiling the information necessary to be submitted to FMS. The Fund Administrator will compile the information into the specified file format and submit this electronic file to the assigned Commission staff. The Fund Administrator will validate the

¹ In addition to single large purchases, investors could qualify for breakpoint discounts pursuant to a “letter of intent,” an agreement to make multiple purchases of Class A shares issued by the same fund or fund complex over a 13-month (or similar) period which, when aggregated, equaled an amount that qualified for a breakpoint discount. Breakpoints were also available through “rights of accumulation,” under which an investor, or an eligible group of related investors, could aggregate the value of their existing holdings to determine the reduced sales charge applicable to subsequent purchases of Class A shares.

payees and amounts 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 Fund 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 checks will be mailed. FMS will notify the Commission staff, which, in turn, will notify the Fund Administrator of any returned items due to non-delivery, insufficient addresses, and/or other deficiencies. The Fund 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 Fund 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, each 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 staff, which, in turn, will notify the Fund Administrator of all uncashed checks. FMS will credit the SEC account for the Fair Fund for the amount of all uncashed checks.

9. *Information mailing to accompany payments.* All payments shall be preceded by a communication that includes, as appropriate: (a) a statement characterizing the distribution; (b) a description of the tax information reporting required of the QSF and related tax consequences; (c) a statement that checks will be void after one year; and (d) the name of a person to contact, to be used in the event of any questions regarding the distribution. Any such information letter or other communication about this distribution plan shall be submitted to the assigned Commission staff for review and approval. Distribution checks, on their face, or in the accompanying mailing, will clearly indicate that the money is being distributed from a Fair Fund established by the SEC.

10. *Tax Administrator.* The Commission has appointed Damasco & Associates as the Tax Administrator ("Tax Administrator") of the Fair Fund (Rel. No. 34-54838, November 29, 2006). The Fund Administrator and Respondents 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 by the Fair Fund.

11. *Tax Provisions.* The Fund Administrator will ensure that all required information shall be made available to the Tax Administrator. The Fund Administrator shall use the assets and earnings of the Fair Fund to provide payments to Eligible Customers and to provide the Tax Administrator with assets to pay tax liabilities and tax compliance fees and costs.

12. *Accountings.* Once all funds are disbursed through FMS of the U.S. Treasury, the Fund Administrator will submit a final accounting for approval by the Commission prior to termination of the Fair Fund and discharge of the Fund Administrator.

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

14. *Assistance by Respondents.* Royal Alliance and Scarborough will assist the Fund Administrator by providing requested information necessary for the administration and implementation of the Plan.

15. *Notice of Proposed Plan and Opportunity for Comment.* Notice of this Plan shall be published in the SEC Docket and on the Commission website [<http://www.sec.gov>]. Any person or entity wishing to comment on the Plan must do so in writing by submitting their comments within thirty (30) days of the date of the notice (i) by sending a letter to the Office of the Secretary, United States Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090; (ii) by using the Commission's Internet comment form (www.sec.gov/litigation/admin.shtml); or (iii) by sending an e-mail to rule-comments@sec.gov. Comments submitted by e-mail or via the Commission's website should include the Administrative Proceeding File Number (Admin. Proc. File No. 3-11538) in the subject line. Comments received will be available to the public. Commenters should only submit information that they wish to make publicly available.

16. *Order Approving the Proposed Plan and Order of Disbursement.* At the end of the thirty (30) day notice and plan publication period, the staff of the Commission will seek an order approving the Plan. The staff will seek an order of disbursement of the disgorgement funds within thirty (30) days of plan approval.

17. *Amendments and Procedural Deadline Extensions.* The Fund Administrator will inform the Commission staff of any changes in the Plan. If a change is determined to be material, Commission approval is required prior to implementation by amending the Plan, which may be done upon the motion of the Fund Administrator, or upon the Commission's own motion.

18. *Procedures for the Receipt of Additional Funds.* This Fair Fund has been deposited at the Bureau of Public Debt for investment in government obligations. Other than interest from these investments, it is not anticipated that the Fair Fund will receive additional funds.

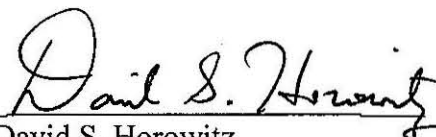
19. *Disposition of Undistributed Funds.* A residual account within the Fair Fund is established for any amounts remaining after all assets have been distributed. The residual account may include funds reserved for future taxes and related expenses, distributions from checks that have not been cashed, from checks that were not delivered or from funds returned to the Fund Administrator, tax refunds for overpayment or for waiver of penalties. All

undistributed funds in the residual account will be transferred to the U.S. Treasury after the final accounting is approved by the Commission.

20. *Termination of the Fair Fund.* Upon distribution of the funds, the Fund Administrator shall make arrangement for the final payment of taxes and Tax Administrator fees and shall submit a final accounting to the Commission. The Fair Fund shall be eligible for termination after all of the following have occurred: (1) the Final Accounting by the Fund Administrator has been submitted and approved by the Commission, (2) all taxes and fees have been paid, and (3) all remaining funds or any residual amounts have been transferred to the U.S. Treasury. Staff shall seek an order from the Commission to (1) approve the Final Accounting; (2) approve sending the remaining residual amounts to the United States Treasury after the final tax payment has been made; and (3) authorize the Secretary of the Commission, upon receipt of notice from the staff assigned to this matter that all funds have been expended, to terminate the Fair Fund and discharge the Fund Administrator.

21. *Distribution Timing.* The Fund Administrator will use his best efforts to start the distribution within thirty (30) days of plan approval and to complete the distribution within sixty (60) days of the distribution start date.

Submitted on February 3, 2009

By: 
David S. Horowitz
Assistant Regional Director
Philadelphia Regional Office