

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 59830 / April 28, 2009

ADMINISTRATIVE PROCEEDING
File No. 3-13456

In the Matter of

**Royal Alliance Associates,
Inc.,**

Respondent.

**ORDER INSTITUTING
ADMINISTRATIVE PROCEEDINGS,
MAKING FINDINGS, AND IMPOSING
REMEDIAL SANCTIONS PURSUANT
TO SECTION 15(b)(4) OF THE
SECURITIES EXCHANGE ACT OF
1934**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b)(4) of the Securities Exchange Act of 1934 (“Exchange Act”) against Royal Alliance Associates, Inc. (“Royal Alliance” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Royal Alliance has submitted an Offer of Settlement 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 Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings, Making Findings, and Imposing Remedial Sanctions Pursuant to Section 15(b)(4) of the Securities Exchange Act of 1934 (“Order”), as set forth below.

III.

On the basis of this Order and Respondent’s Offer, the Commission finds that¹:

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.

Summary

1. Respondent failed reasonably to supervise David L. McMillan (“McMillan”) with a view to preventing and detecting his violations of the federal securities laws during the period January 1999-December 2004. During at least this time period, McMillan operated a Ponzi scheme and defrauded at least 28 investors by lying about purchases and sales of securities, by misappropriating funds for his personal use, and by sending certain investors falsified statements relating to their investment accounts.

Respondent

2. Royal Alliance is a Delaware corporation with its main office in New York, New York. Royal Alliance has been registered with the Commission as a broker-dealer since November 1984.

Other Relevant Persons

3. McMillan, age 43, was a registered representative with Royal Alliance from 1994 through 2004, and with another brokerage firm from January 2005 through October 2005 until his fraud was uncovered. McMillan operated a one-man satellite office in Bullhead City, Arizona, which was located about 200 miles from the Office of Supervisory Jurisdiction (“OSJ”) office in Phoenix where his immediate supervisor Brad Parish (“Parish”) was located.

Commission’s Civil Action Against McMillan

4. On April 4, 2006, the Commission filed an injunctive action in the United States District Court for the District of Arizona alleging that McMillan committed securities fraud by telling clients he had invested their money in particular investments when in fact he either used the funds for his personal use or to repay earlier investors. The Commission charged McMillan with violating Sections 206(1) and (2) of the Investment Advisers Act of 1940 (“Advisers Act”), Section 17(a) of the Securities Act of 1933 (“Securities Act”), and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The court entered a temporary restraining order and asset freeze against McMillan on April 4, 2006 and a preliminary injunction on April 13, 2006. McMillan did not answer the Commission’s complaint and the Court entered a default against McMillan on August 29, 2006.

McMillan’s Misconduct

5. During at least 1999 through October 2005, McMillan defrauded at least 28 investors, many of whom had brokerage accounts with Royal Alliance, out of at least \$3 million through the offer and sale of fictitious investments in annuities, fictitious loans to a real estate developer, and real estate loans that were to be secured by fraudulent first

deeds of trust. McMillan falsely represented to investors that their money would continue to be invested in securities when, in fact, he misappropriated their funds either to repay other investors, for his own personal use, or to fund a new outside business activity. He also sent certain investors falsified statements relating to their investments in the fraudulent securities.

Royal Alliance's Failure to Supervise

Royal Alliance Failed to Establish Adequate Procedures For the Review of Operational Bank Records of Satellite Offices in 1999

6. Although Royal Alliance prohibited registered representatives from depositing customer checks in a bank account owned or controlled by the registered representative, Royal Alliance did not have a written supervisory policy requiring the review of bank records prior to 2000. During 1999, customers of Royal Alliance had checks relating to the fraud that were deposited in McMillan's operating account. A review of McMillan's bank records for his operating account in 1999 would have uncovered these transactions. Thus, if Royal Alliance had developed policies for the review of bank records in 1999, the firm likely could have prevented and detected McMillan's violations of the federal securities laws.

Royal Alliance Failed to Develop a Reasonable System to Implement Its Procedures for Conducting Exams in Satellite Offices

7. Royal Alliance required the OSJ manager, in this case Parish, to conduct at least one exam each year of every satellite office and to complete a workbook documenting various aspects of the exam. However, Royal Alliance failed to establish a reasonable system to review the findings of the satellite exam, including whether all sections of the satellite exam workbook were completed. In 2000, Royal Alliance changed its satellite exam workbook to include a review of bank records. During that year, Parish failed to review McMillan's business bank records and left that section of the satellite exam workbook blank. Parish's failure to complete the required review of the business bank records went undetected because of Royal Alliance's failure to establish a reasonable system to adequately review the findings of satellite exams after 2000. Had Parish conducted the required review of McMillan's bank records in 2000, the fraud likely would have been uncovered because large checks were reflected to and from McMillan's customers in that account, which was in violation of firm policy.

Royal Alliance's Procedures for Conducting Exams In Satellite Offices Were Inadequate Because They Failed to Address Red Flags Relevant to Satellite Offices

8. Royal Alliance failed to establish reasonable policies and procedures to address red flags relevant to satellite offices, such as how an office was funded in light of a registered representative's declining commissions. McMillan's commission income from Royal Alliance dropped substantially from 2000 through 2004. McMillan earned \$149,000 in 2000, \$93,000 in 2001, \$40,000 in 2002, \$71,000 in 2003, and \$13,000 in

2004. McMillan's primary business banking account showed expenses of roughly \$90,000 a year during this period, meaning McMillan appeared to be operating at loss for the last three of five years unless he was generating income from other sources. Despite declining income, McMillan continued to employ two support staff during this period. This substantial drop in commissions, especially when combined with continuing high expenses, was a red flag. Royal Alliance had no reasonable procedures to review whether commissions generated from Royal Alliance together with any income separately earned by its registered representative from other businesses were adequate to support the operations of the satellite office.

9. For example, Royal Alliance's procedures could have required limited questioning of the support staff in response to declining commissions. Questioning of McMillan's support staff would have likely prevented or detected the fraud because they were involved in many administrative aspects of these fraudulent investments from 1999-2004, although they did not know the investments were fraudulent. Specifically, the assistants printed checks to investors on the office computer from McMillan's personal bank account, they deposited clients' monthly interest checks from the fraudulent investments in the clients' personal bank accounts at various banks, they handed out checks to investors from McMillan's personal bank account relating to the fraudulent investments, they deposited investor checks into McMillan's personal bank account, and they created account statements on an office computer relating to McMillan's fraudulent investments. These activities violated Royal Alliance policies and procedures, which if known by Royal Alliance, would have raised red flags requiring further investigation. Moreover, the assistants kept a very detailed check register for the bank account used to perpetrate the fraud. If they had been asked about what bank accounts McMillan used to operate his business, the assistants likely would have disclosed this account, enabling Royal Alliance to examine the account and detect the fraud.

Royal Alliance Failed to Develop Systems to Implement Its Procedure Requiring the First Line Supervisor to Investigate and Respond to Surveillance Inquiries Related to Registered Representatives

10. The Royal Alliance Sales Practices Manual made the first line supervisor responsible for investigating and responding to surveillance inquiries directed to representatives under his or her supervision. However, Royal Alliance failed to adequately implement this procedure and instead, the registered representative who was the subject of the inquiry was generally responsible for providing a response. In 2000, Royal Alliance's surveillance system forwarded an exception report relating to a large annuity withdrawal by a customer to McMillan for his response. The first line supervisor, Parish, who was copied on this inquiry, was not asked to and did not follow up on the inquiry. McMillan sent a response disclosing that the client liquidated the annuity to purchase a First Deed of Trust. In fact, the First Deed of Trust was a nonexistent and fraudulent investment created by McMillan. The client eventually incurred significant losses in connection with McMillan's scheme.

Royal Alliance Failed To Develop Systems to Implement its Procedure Requiring Maintenance of Complete and Accurate Customer Transaction Reports

11. Royal Alliance's written supervisory procedures required the first line supervisor to monitor customer transactions by reviewing transaction reports that were based in part on data manually entered by registered representatives. McMillan failed to input a number of transactions by one or more customers who sold legitimate securities and used the money to invest in his fraudulent scheme. Royal Alliance failed to adequately implement its procedure requiring the reports to include all customer transactions, and therefore failed to detect customers' sales of securities that generated funds which McMillan recommended customers invest in his fraud.

Conclusions

12. Under Section 15(b)(4)(E) of the Exchange Act, broker-dealers are responsible for reasonably supervising, with a view to preventing violations of the federal securities laws, persons subject to their supervision. Royal Alliance was responsible for supervising McMillan.

13. The Commission has repeatedly emphasized that the "responsibility of broker-dealers to supervise their employees by means of effective, established procedures is a critical component in the federal investor protection scheme regulating the securities markets." *Dean Witter Reynolds, Inc.*, Exchange Act. Rel. 46578 (October 1, 2002). Section 15(b)(4)(E) provides that a broker-dealer may discharge this responsibility by having "established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect" such violations. "Where there has been an underlying violation of the federal securities laws, the failure to have or follow compliance procedures has frequently been found to evidence a failure reasonably to supervise the primary violator." *In the Matter of William V. Giordano*, Exchange Act Rel. No. 36742 (January 19, 1996). In addition to adopting effective procedures for supervision, broker-dealers "must provide effective staffing, sufficient resources, and a system of follow up and review to determine that any responsibility to supervise delegated to compliance officers, branch managers, and other personnel is being diligently exercised." *In the Matter of Mabon, Nugent & Co.*, Exchange Act Rel. No. 19424 (January 13, 1983).

14. Because McMillan violated Sections 206(1) and (2) of the Advisers Act, Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Royal Alliance failed to establish and implement systems and procedures that would reasonably be expected to prevent and detect such violations, Royal Alliance failed reasonably to supervise McMillan for purposes of Section 15(b)(4)(E) of the Exchange Act.

Royal Alliance's Remedial Efforts

15. In determining to accept Royal Alliance's Offer, the Commission considered the remedial acts promptly undertaken by Royal Alliance to make significant improvements to its supervisory system, and the cooperation afforded the Commission staff.

Undertakings

16. Royal Alliance has represented to the staff of the Denver Regional Office that, following the discovery of McMillan's violations, Royal Alliance utilized an outside consultant to recommend improvements to its supervisory and compliance practices, and that it has implemented, or is in the process of implementing, these recommendations for improvement. Among the improvements, Royal Alliance has strengthened its satellite exam procedures as well as its supervision of those exams, it has enhanced its surveillance system, and it has increased its training for examiners and non-registered personnel in branch offices. When these improvements have been fully implemented, Royal Alliance will provide written certification of that fact to the Commission staff.

IV.

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

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

A. Royal Alliance is hereby censured;

B. Royal Alliance shall, within ten days of the entry of this Order, pay disgorgement of \$1 and a civil money penalty in the amount of \$500,000 to the Clerk of the Court, U.S. District Court for the District of Arizona, to be held in such Court's Registry Investment system account established for the Matter of *Securities and Exchange Commission v. David L. McMillan*, Case No. CV-06-0951-PCT-SMM, until further order of such Court. Such payment shall be made by United States postal money order, certified check, bank cashier's check, or bank money order and submitted under cover letter that identifies Royal Alliance 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 Donald Hoerl, Regional Director, Securities and Exchange Commission, 1801 California Street, Suite 1500, Denver, CO 80202.

C. Such civil money penalty may be distributed pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002 ("Fair Fund distribution"). Regardless of whether any such Fair Fund distribution is made, 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 tax purposes. To preserve the deterrent effect of this civil penalty,

Royal Alliance agrees that it shall not argue that it is entitled to, nor shall it further benefit by offset or reduction 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 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 United States Treasury. 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 Royal Alliance 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.

Elizabeth M. Murphy
Secretary