

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

**SECURITIES ACT OF 1933**  
**Release No. 8967 / September 29, 2008**

**INVESTMENT COMPANY ACT OF 1940**  
**Release No. 28417 / September 29, 2008**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-13258**

**In the Matter of**

**S3 INVESTMENT  
COMPANY, INC.,**

**Respondent.**

**ORDER INSTITUTING CEASE-AND-DESIST AND EXEMPTION SUSPENSION PROCEEDINGS, MAKING FINDINGS, IMPOSING A CEASE-AND-DESIST ORDER, AND PERMANENTLY SUSPENDING THE REGULATION E EXEMPTION AS TO S3 INVESTMENT COMPANY, INC., PURSUANT TO SECTION 9(f) OF THE INVESTMENT COMPANY ACT OF 1940 AND RULE 610(c) OF REGULATION E**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist and exemption suspension proceedings be, and hereby are, instituted pursuant to Section 9(f) of the Investment Company Act of 1940 (“Investment Company Act”) and Rule 610(c) of Regulation E against S3 Investment Company, Inc. (“S3” 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 Cease-and-Desist and Exemption Suspension Proceedings, Making Findings, Imposing a Cease-and-Desist Order, and Permanently Suspending the Regulation E Exemption as to S3 Investment Company, Inc., Pursuant to Section 9(f) of the Investment Company Act of 1940 and Rule 610(c) of Regulation E (“Order”), as set forth below.

### III.

On the basis of this Order and Respondent's Offer, the Commission finds<sup>1</sup> that:

#### **Summary**

1. Since electing to be regulated as a business development company ("BDC") in April 2004, S3 has, among other things, issued rights to purchase its securities without expiration to non-security holders, issued stock with unequal voting rights, issued securities for services or property other than cash, and issued stock below net asset value. As a result, S3 violated Sections 18(d), 18(i), and 23(b) respectively, of the Investment Company Act. In addition, S3 failed to obtain a fidelity bond as required under Section 17(g) of the Investment Company Act and Rule 17g-1 thereunder, and it also failed to appoint a chief compliance officer as required under Investment Company Act Rule 38a-1. Finally, S3 failed to comply with Rule 609 of Regulation E because it did not file an offering status report on Form 2-E in connection with securities offerings under Regulation E commenced in April and September 2004.

#### **Respondent**

2. S3 is a California corporation with its principal offices located in Temecula, California. It elected to be regulated as a BDC on April 12, 2004, and withdrew its BDC election on April 6, 2006. Prior to its BDC election, S3 was an operating company known as Axtion Foods, Inc., which was in the business of wholesale groceries and related products sales. S3's securities were registered under Section 12(g) of the Securities Exchange Act of 1934 from June 4, 2002 until June 6, 2007.

#### **Issuing Senior Securities and Convertible Securities with Unequal Voting Rights**

3. On March 18, 2004, S3 issued 8.3 million shares of Series-A convertible preferred stock ("Series-A preferred") to two of its officers. The Series-A preferred was not entitled to receive dividends and had no voting rights, except to elect two members of the board of directors. Each Series-A preferred share was convertible into one common share at any time, or automatically upon liquidation. Under Section 61(b) of the Investment Company Act, a BDC must comply with Section 61 at the time it becomes subject to Sections 55 through 65 of the Investment Company Act ("the BDC provisions"), "as if it were issuing a security of each class which it has outstanding at such time." When S3 became subject to the BDC provisions on April 12, 2004, the Series-A preferred was outstanding.

4. Between December 1, 2003, and June 30, 2004, S3 issued \$729,000 in convertible debentures to investors. The debentures included an 8% annual interest rate, and a maturity date six months from issuance. They were convertible into common stock at a price equal to 50% of the

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<sup>1</sup> 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.

market value on the conversion date. Between April 1, 2004, and October 13, 2004, S3 issued approximately 96 million common shares to debenture holders who had elected to convert \$719,000 in convertible debentures.

5. Between April 13, 2004 and September 16, 2004, S3 issued 4.7 million Series B convertible preferred shares (“Series-B preferred”) to an officer and to three other individuals. The Series-B preferred was convertible into Series-A preferred. Each Series-B preferred was entitled to vote on all matters and had voting rights equal to 100 shares of common stock

6. Section 18 of the Investment Company Act is made applicable to BDCs by Section 61(a) of the Investment Company Act, subject to certain exceptions. Section 18(d), as applicable to BDCs, generally prohibits registered management companies from issuing “any warrant or right to subscribe to or purchase a security of which such company is the issuer, except in the form of warrants or rights to subscribe expiring not later than one hundred and twenty days after their issuance and issued exclusively and ratably to a class or classes of such company's securities holders.” The conversion feature of S3’s Series-A and -B preferred, which constituted rights to subscribe to or purchase securities, did not provide that the conversion feature would expire within 120 days after their issuance as required under Section 18(d).

7. Section 61(a)(3) allows a BDC, notwithstanding Section 18(d), to issue warrants, options, or rights to subscribe or convert to voting securities that are accompanied by securities if, among other things, the BDC’s shareholders authorize, and a majority of the BDC’s disinterested directors approves, the proposal to issue such securities; the exercise or conversion price is not less than the current market value at the date of issuance.

8. S3’s shareholders did not authorize the issuance of the Series-A or -B preferred. Furthermore, in light of the 50% discount, the debenture’s conversion price was less than the market price of S3’s common stock at the date of issuance.

9. With certain exceptions not relevant here, Section 18(i) of the Investment Company Act provides that every share of stock issued by a BDC shall be a voting stock and have equal voting rights with every other outstanding voting stock. Here, S3’s preferred stock did not have voting rights equal to that of its common stock.

#### **Issuance of Shares for Services or Below Net Asset Value**

10. Section 23(b) of the Investment Company Act, which Section 63 of the Investment Company Act makes applicable to BDCs, generally prohibits any closed-end company from issuing shares below net asset value (“NAV”) without the consent of the majority of stockholders. During the quarter ending March 31, 2005, S3 issued 437,250,000 shares of common stock at prices between \$.001 and \$.002 per share for cash of \$448,405 and a subscription receivable of \$73,000. At the time of these stock sales, the NAV per share was between \$.003 and \$.006. For the period ending June 30, 2005, S3 issued an additional 80,000,000 shares at prices below NAV. S3 did not receive shareholder approval to sell shares below NAV.

### **Failure to Appoint a Chief Compliance Officer**

11. On December 17, 2003, the Commission adopted Rule 38a-1 under the Investment Company Act, which requires each registered investment company and BDC to adopt and implement written policies and procedures reasonably designed to prevent violations of federal securities laws. These policies and procedures must be approved by the BDC's board of directors (including a majority of disinterested directors) and reviewed annually. Furthermore, each BDC must appoint a chief compliance officer to administer the policies and procedures and fulfill certain reporting duties to the board. The compliance deadline for this rule was October 5, 2004. S3 did not appoint a chief compliance officer.

### **Failure to Provide and Maintain a Fidelity Bond**

12. Section 17(g) of the Investment Company Act and Rule 17g-1 thereunder, which Section 59 makes applicable to BDCs, require each BDC to provide and maintain a bond issued by a reputable fidelity insurance company against larceny and embezzlement by officers and employees of the BDC. S3 did not provide and maintain a fidelity bond.

### **Violations**

13. As a result of the conduct described above, S3 violated Sections 17(g), 18(d), 18(i), and 23(b) of the Investment Company Act and Rules 17g-1 and 38a-1 thereunder.

### **Failure to Comply with Requirements of Regulation E**

14. On April 13, 2004, and September 21, 2004, S3 filed Form 1-E notification of stock issuance pursuant to the securities-registration exemption under Securities Act of 1933 Regulation E. The filings included an offering circular, which provided certain disclosures regarding the offering.

15. Rule 609 of Regulation E requires that, within 30 days after the end of each six-month period following the date of the original offering circular, or upon the termination of the offering, whichever is earlier, an issuer must file a report on Form 2-E, providing certain information regarding the status of the offering. S3 did not file the Form 2-E that was due within 30 days after October 13, 2004, for the April 13, 2004 Regulation E offering and never filed any Forms 2-E for the September 21, 2004 Regulation E offering. Therefore, S3 failed to comply with Rule 609.

16. Under Regulation E, Rule 610(c), the Commission may, at any time after notice of and opportunity for hearing, enter an order permanently suspending the Regulation E exemption, if the Commission has reason to believe, among other things, that any of the terms or conditions of Regulation E have not been complied with, including failure to include in the offering circulars the required financial information as required by Rule 605 or failure to file any report as required by Rule 609.

### **Respondent's Remedial Efforts**

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

#### **IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent S3's Offer.

Accordingly, pursuant to Section 9(f) of the Investment Company Act and Rule 610(c) of Regulation E, it is hereby ORDERED that:

A. Respondent S3 cease and desist from committing or causing any violations and any future violations of Sections 17(g), 18(d), 18(i), and 23(b) of the Investment Company Act and Rules 17g-1 and 38a-1 thereunder.

B. The Regulation E exemption as to Respondent S3 be, and hereby is, permanently suspended.

By the Commission.

Florence E. Harmon  
Acting Secretary