STATE OF ILLINOIS

SECRETARY OF STATE

SECURITIES DEPARTMENT

In the matter of :	)	
	)	**File No 0700578**
MORGAN ASSET MANAGEMENT, INC.	)	
at all relevant times, a wholly owned	)	
subsidiary of MK Holding, Inc. at all relevant	)	
times, a wholly owned subsidiary of Regions	)	
Financial Corporation;	)	
	)	
MORGAN KEEGAN & COMPANY, INC.	)	
at all relevant times, a wholly owned	)	
subsidiary of Regions Financial Corporation,	)	
	)	
Respondents.		

NOTICE OF HEARING

TO THE RESPONDENTS:

Morgan Asset Management, Inc.
Morgan Keegan & Company, Inc.
c/o John N. Bolus
Maynard Cooper & Gale, PC
2400 Regions/Harbert Plaza
1901 Sixth Avenue North
Birmingham, Alabama 35203

You are hereby notified that pursuant to Section 11.F of the Illinois Securities Law of 1953, [815 ILCS 5/1 et seq.] (the "Act") and 14 Ill. Adm. Code 130, Subpart K, a public hearing will be held at 300 W. Jefferson St., Suite 300A, Springfield, Illinois 62702, on the 20th day of June, 2012 at the hour of 10:00 a.m., or as soon thereafter as counsel may be heard, before Jon K. Ellis, or such other duly designated Hearing Officer of the Secretary of State. A copy of the Rules under the Act pertaining to contested cases is attached to this Notice.

Said hearing will be held to determine whether an Order should be entered against Morgan Asset Management, Inc and Morgan Keegan & Company, Inc. (the "Respondents") in the State of Illinois and granting such other relief as may be authorized under the Act including but not limited to imposition of a monetary fine in the maximum amount pursuant to Section 11 of the Act, payable within ten (10) days of the entry of the Order.

The grounds for such proposed action are as follows:

RESPONDENTS AND PERSONS/ENTITIES AFFILIATED WITH THE RESPONDENTS

1. Respondent **Morgan Keegan & Company, Inc.** ("MKC") (CRD No. 4161), a Tennessee corporation, is a registered broker-dealer with the Department and the SEC, as well as a federally registered investment adviser with the SEC. At all relevant times MKC was properly registered and notice-filed with the Department. MKC was at all relevant times a wholly owned subsidiary of Regions Financial Corporation ("RFC") which is headquartered in Birmingham, Alabama. MKC's primary business address is 50 Front Street, Morgan Keegan Tower, Memphis, Tennessee 38103-9980.

2. Respondent **Morgan Asset Management, Inc.** ("MAM"), a Tennessee corporation, is a federally registered investment adviser with the SEC (CRD No. 111715) and at all relevant times was properly notice-filed with the Department. MAM was at all relevant times a wholly owned subsidiary of MK Holding, Inc., which at all relevant times was a wholly owned subsidiary of RFC. MAM is headquartered in Alabama with a principal business address of 1901 6th Avenue North, 4th Floor, Birmingham, Alabama 35203.

3. **Wealth Management Services** ("WMS"), a division of MKC, developed, recommended, and implemented asset allocation strategies for MKC and was to perform due diligence on traditional and alternative funds and fund managers for the benefit of MKC, its Financial Advisers (alternatively referred to as "FAs", "sales force" or "agents"), and certain investor clients.

4. **James C. Kelsoe, Jr.** ("Kelsoe") (CRD No. 2166416) was Senior Portfolio Manager of the Funds, as defined in paragraph II.5 below, and was responsible for selecting and purchasing the holdings for the Funds. Kelsoe was an employee of MAM and registered through MKC.

5. The seven (7) funds at issue are Regions Morgan Keegan Select Intermediate Bond Fund ("Intermediate Bond Fund"), Regions Morgan Keegan Select High Income Fund ("Select High Income Fund"), Regions Morgan Keegan Advantage Income Fund ("Advantage Income Fund"), Regions Morgan Keegan High Income Fund ("High Income Fund"), Regions Morgan Keegan Multi-Sector High Income Fund ("Multi-Sector High Income Fund"), Regions Morgan Keegan Strategic Income Fund ("Strategic Income Fund"), and Regions Morgan Keegan Select Short Term Bond Fund ("Short Term Bond Fund") (collectively, the "Funds").

6. Six (6) of the seven (7) Funds were largely invested in mezzanine and lower subordinated "tranches," or slices, of structured debt instruments, which carry more risk than the senior tranches.[1] The Funds were comprised of many of the same holdings. On June 30, 2007, approximately two-thirds (2/3) of the holdings of the four (4) closed-end funds and the Select High Income Fund were substantially identical. Approximately one quarter (1/4) of the Intermediate Bond Fund's holdings corresponded to the holdings of the five (5) high yield Funds. The Funds were highly correlated, meaning they behaved like each other under similar market conditions. The combination of subordinated tranche holdings and the high correlation of

[1] The seventh, the Short Term Bond Fund, had significant investments in mezzanine and subordinated tranches of structured debt instruments.

the Funds caused investors owning more than one (1) of these funds to have a heightened risk of over concentration.

7. The Funds were created and managed by Kelsoe, MAM Senior portfolio manager. Kelsoe was also principally responsible for the purchase and sale of all of the holdings in the Funds.

8. When WMS ceased reporting and dropped its coverage of the Select Intermediate Bond Fund and Select High Income Fund in July 2007, it failed to announce the drop in coverage in writing until November, 2007. WMS did not publish a withdrawal of its prior analysis or recommend the Funds' replacement.

9. On January 19, 2007, WMS announced it was reclassifying the Intermediate Bond Fund on the Select List from "Fixed Income" to "Non-Traditional Fixed Income." Meanwhile, WMS profiles for the Intermediate Bond Fund continued to label it as the "Intermediate Gov't/Corp Bond."

10. Certain of the Funds' annual, semi-annual, and quarterly reports filed with the SEC did not adequately disclose the risks of subordinated tranches and the quantity of subordinated tranches held within the Funds.

11. MAM produced quarterly glossies for all seven (7) Funds. In the glossies, MAM did not adequately describe the risks of owning the lower tranches of structured debt instruments or the quantity of such holdings within the Funds.

12. MKC, through WMS, produced quarterly Fund Profiles for the Intermediate Bond Fund, the Select High Income Fund, and the Short Term Bond Fund that did not adequately describe the risks of owning the lower tranches of structured debt instruments or the quantity of such holdings within the Funds.

13. In SEC filings and state notice filings of March and June 2007 involving the Funds, Four Hundred Million Dollars ($400,000,000.00) of what MAM characterized as corporate bonds and preferred stocks were, in fact, the lower, subordinated tranches of asset-backed structured debt instruments. MAM eventually reclassified certain of these structured debt instruments in the March 2008 Form N-Q Holdings Report for the three (3) open-end funds.

14. In SEC filings, MAM compared the four (4) closed-end funds and the Select High Income Fund (collectively the "RMK high-yield funds"), which contained approximately two-thirds (2/3) structured debt instruments, to the Lehman Brothers U.S. High Yield Index ("Lehman Ba Index"). The Lehman Ba Index is not directly comparable to the RMK high-yield funds given the fact that the Lehman Ba Index contained only corporate bonds and no structured debt instruments.

15. Certain marketing materials and reports minimized the risks and volatility associated with investing in funds largely comprised of structured debt instruments. In the June 30, 2007 glossy, and in previous quarterly glossies created by MAM, MAM and MKC marketed the Intermediate Bond Fund as a fund appropriate for "Capital Preservation & Income." MAM later revised the Intermediate Bond Fund glossy in September 2007 by removing the caption "Capital Preservation & Income" and replacing it with "Income & Growth," and by removing the word "stability," which had previously been used to describe the fund.

16. The Intermediate Bond Fund glossies dated June 30, 2007, and September 30, 2007, stated that the Intermediate Bond Fund "...does not invest in speculative derivatives." However, the Intermediate Bond Fund did use derivatives, including interest-only strips, and collateralized debt obligations (CDOs), which are derived from the mezzanine and lower tranches of other debt securities.

17. Respondent MKC through WMS labeled the Intermediate Bond Fund with varying names. None of the three labels "Taxable Fixed Income", "Enhanced Low-Correlation" and "Intermediate Gov't/Corp Bond" used by MKC adequately portrayed the nature of the Intermediate Bond Fund, of which approximately two-thirds (2/3) of the portfolio was invested in the mezzanine or lower subordinated tranches of structured debt instruments. The label "Gov't/Corp Bond," which first appeared on the December 31, 2006 profile sheet, was never changed after that date.

A. SUPERVISION AND SUPERVISORY DUE DILIGENCE

18. During the period January 1, 2007 through July 31, 2007, preceding the collapse of the subprime market, MAM made 262 downward price adjustments for the purpose of adjusting the net asset value of the Funds. In some instances, MAM's communications led MKC, through its sales force, to actively discourage investors from selling the Funds—even while fund prices continued to decline -- by advising investors to "hold the course." Some members of MKC, MAM, and their management personnel continued during this period to advise FAs and investors to buy the Funds through, *inter alia*, statements that characterized the decline as "a buying opportunity."

19. MKC and MAM failed to adequately supervise the flow of information to the MKC sales force concerning the Funds. For example, in conference calls with the sales force, the senior portfolio manager for the Funds cited sub-prime fears and liquidity as the primary factors for a decline in the net asset value of the Funds without fully explaining the market impact on certain securities held by the Funds.

20. WMS did not complete a thorough annual due diligence report of the open-end funds and the management of the open-end funds in 2007. A fixed income analyst for WMS,

attempted to complete an annual due diligence review of the open-end funds and the management of the open-end funds in the summer of 2007, but was unsuccessful due to Kelsoe's and MAM's failure to provide sufficient information and Kelsoe's failure to be available for a meeting during normal operating hours. Subsequently, WMS failed to notify the MKC sales force of WMS's failure to complete the annual on-site due diligence review. An incomplete draft of WMS's annual due diligence report for internal use only was submitted by the WMS analyst, but it was neither completed nor released to the sales force.

21. On July 31, 2007, WMS dropped coverage of all proprietary products, which included the funds for which WMS could not produce a thorough report. This fact was not disclosed in writing to the sales force until November 2007.

22. Based on WMS's one (1) page, one (1) paragraph report of the August 18, 2006 on-site due diligence review, the due diligence visits by the WMS fixed income analysts were not "detailed, thorough, and exhaustive," as advertised by MKC. There are two (2) WMS profiles of the Intermediate Bond Fund dated September 30, 2006. The sections titled "investment philosophy" in the profile sheets contain substantial differences. The first WMS profile for the Intermediate Bond Fund, based on the information for the quarter ending September 30, 2006, is titled "Taxable Fixed Income." The first profile, much like previous quarterly profiles, does not refer to any of the holdings as "inferior tranches." Neither does it mention potential lack of demand and lack of liquidity. Further, it includes the statement that "The fund does not use derivatives or leverage."

23. WMS's changing of the Intermediate Bond Fund profile label indicated WMS's inability and lack of supervision in the creation of these marketing pieces to accurately

categorize the Intermediate Bond Fund. Within one (1) quarter, WMS identified the Intermediate Bond Fund three (3) different ways:

September 30, 2006 - Taxable Fixed Income
September 30, 2006 - Enhanced Low Correlations Fixed Income
December 31, 2006 - Intermediate Gov't/Corp Bond

24. The "Gov't/Corp Bond" label implied that the Intermediate Bond Fund holdings were predominately government and corporate bonds carrying a certain degree of safety. This improper labeling indicates a failure to conduct proper due diligence, a duty of MKC.

25. In addition, all profiles for the Intermediate Bond Fund from March 31, 2006, through June 30, 2007, stated that Kelsoe was joined by Rip Mecherle ("Mecherle") as assistant portfolio manager. Mecherle left MAM in 2004. The failure to detect the errors in promotional materials relating to management does not reflect the "detailed, thorough, and exhaustive due diligence" claimed by MKC in its sales and promotional material distributed to investors.

B. SUITABILITY OF RECOMMENDATIONS

26. Respondent MAM indicated that risks and volatility were minimized in the Intermediate Bond Fund portfolio. In the June 30, 2007 glossy, and previous quarterly glossies created by MAM, Respondents marketed the Intermediate Bond Fund's broad diversification of asset classes three (3) times on the first page of each of the glossies, when in fact, approximately two-thirds (2/3) of the Intermediate Bond Fund portfolio was composed of structured debt instruments which included risky assets. The four (4) closed-end funds also advertised diversification among asset classes, despite the similarities in asset classes as set forth in Section C below.

27. Furthermore, the glossies emphasized the Select High Income Fund's net asset value as being less volatile than typical high-yield funds. The glossies failed to state that a reason for any lower volatility was that the structured debt instruments within the Select High Income

Fund were not actively traded, and that the daily fair value adjustments of certain holdings were imprecise in a market that became illiquid.

28. In certain cases, MKC and its sales force failed to obtain adequate suitability information regarding risk tolerance that was necessary to determine suitability for using the Funds for regular brokerage account customers. New account forms for regular brokerage accounts provided a menu of four (4) investment objectives to choose from: Growth, Income, Speculation, and Tax-Advantaged. Risk tolerance was not addressed by the form, was not noted by the sales force whose records were examined during the investigation, and may not have been taken into consideration when the sales force made its recommendations.

29. In at least one instance, an agent of MKC provided a customer with a self-made chart assuming the hypothetical growth of One Hundred Thousand Dollars ($100,000.00) over five (5) years, and comparing the rate of return on CDs to the return on the Intermediate Bond Fund. The chart failed to address any risks of investing in the fund, save the caption "Not FDIC Insured."

C. ADVERTISEMENTS BY RESPONDENTS

30. Marketing glossies prepared by MAM for the Intermediate Bond Fund and Select High Income Fund contained allocation pie charts dividing the categories of holdings by percentages of the total portfolio. Between June 2004 and March 2005, the pie charts for both funds changed significantly: MAM divided the category originally titled "asset-backed securities" into multiple categories. These changes indicated that the holdings of these Funds were more diversified than they actually were because the majority of the portfolios continued to be invested in asset-backed securities.

a. In the Intermediate Bond Fund glossy dated June 30, 2004, the Asset-Backed Securities (ABS) and Commercial Mortgage Backed Securities (CMBS) are listed under a single heading comprising seventy percent (70%) of the portfolio.

b. In the Intermediate Bond Fund glossy dated December 31, 2004, the pie chart was revised and the ABS and CMBS are shown as separate categories, but together still comprise seventy-six percent (76%) of the portfolio.

c. The Intermediate Bond Fund glossies dated March 31, 2005, show the ABS category further split into six (6) categories that, together with CMBS, comprised seventy-seven percent (77%) of the portfolio. Those six (6) categories were: "Manufactured Housing Loans," "Home Equity Loans," "Franchise Loans," "Collateralized Debt Obligations," "Collateralized Equipment Leases," and "Other." Subsequent glossies continue to show the ABS split into six (6) categories.

d. In the Select High Income Fund glossy dated June 30, 2004, the ABS and CMBS are listed under a single heading comprising sixty percent (60%) of the portfolio.

e. In the Select High Income Fund glossy dated December 31, 2004, the pie chart was revised and the ABS and CMBS are shown as separate categories, but together still comprise fifty-nine percent (59%) of the portfolio.

f. The Select High Income Fund glossy dated March 31, 2005, shows the ABS category further split into six (6) categories which, together with CMBS, comprised sixty-four (64%) of the portfolio. Those six (6) categories were: "Collateralized Debt Obligations," "Manufactured Housing Loans," "Collateralized Equipment Leases," "Franchise Loans," "Home Equity Loans," and "Other." Subsequent glossies continue to show the ABS split into six (6) categories.

31. The pie charts in the glossies for the High Income Fund were also changed in a similar manner between June 2004 and March 2005.

32. Similar changes were also made to pie charts in glossies for the Advantage Income Fund and the Strategic Income Fund between December 2004 and March 2005.

33. Respondent MKC used different index comparisons in the Select High Income Fund "Profile" sheets produced by WMS. These profile sheets compared the Select High Income Fund to the Credit Suisse First Boston High Yield Index, as well as the Merrill Lynch US High Yield Cash BB Index. These two indices only contain corporate bonds and no structured debt instruments. The Select High Income Fund contained substantially different risks than the portfolios within either of the two indices, and therefore these benchmarks were not directly comparable.

D. REQUIRED EXAMINATIONS OF CUSTOMER ACCOUNTS TO DETECT AND PREVENT IRREGULARITIES OR ABUSES

34. While the models for WMS managed accounts limited the use of the Intermediate Bond Fund to certain percentages, usually no more than fifteen percent (15%) of any client's portfolio, there was no such limitation for non-managed accounts. Additionally, no guidance was provided to the FAs regarding limiting concentrations of the Intermediate Bond Fund in

non-managed accounts. As a result, certain customer accounts contained in excess of a twenty percent (20%) concentration of the Intermediate Bond Fund.

35. The four closed-end funds, the Select High Income Fund and the Intermediate Bond Fund were all highly correlated. However, MKC provided limited guidance to the FAs regarding limiting concentrations of combinations of the Funds in non-managed accounts.

36. Up until six (6) months before the collapse of the fund, WMS classified the Intermediate Bond Fund as "Core Plus" in the Fixed Income section of the Select List. At that time it was reclassified as "Alternative Fixed Income" in the Non-Traditional section of the Select List. Yet MKC's concentration for many of its non-WMS managed accounts continued to be above twenty percent (20%) which could indicate its use as a core holding. An e-mail chai from Gary S. Stringer of WMS states as follows:

> **From:** Stringer Gary [Gary.Stringer@morgankeegan.com]
> **Sent:** Tuesday, May 15, 2007 4:10 PM
> **To:** Hennek, Roderick
> **Subject:** Re: RMK Intermediate Bond Fund
>
> Rod,
>
> I did notice that you didn't cc anyone on your email, and I aperciate that. We've always had good, candid conversation.
>
> You have a good point in that we have some low correlation equity strategies on the Traditional side. What worries me about this bond fund is the tracking error and the potential risks associated with all that asset-backed exposure. **Mr & Mrs Jones don't expect that kind of risk from their bond funds. The bond exposure is not supposed to be where you take risks. I'd bet that most of the people who hold that fund have no idea what's it's actually invested in. I'm just as sure that most of our FAs have no idea what's in that fund either.** They think the return are great because the PM is so smart. He definately is smart, but it's the same as thinking your small cap manager is a hero because he beat the S&P for the last 5 years.
>
> **If people are using RMK as their core, or only bond fund, I think it's only a matter of time before we have some very unhappy investors.**
>
> (Emphasis added.).

Certain MKC brokers and branch managers interviewed during the investigation stated that they received limited or no guidance as to appropriate concentrations of the Funds to use within clients' accounts.

E. REQUIREMENT TO CONDUCT AN ADEQUATE AND THOROUGH CORRESPONDENCE REVIEW

37. An agent of MKC provided one known customer with a self-made chart assuming the hypothetical growth of One Hundred Thousand Dollars ($100,000.00) over five (5) years, and comparing the rate of return on CDs to the return on the Intermediate Bond Fund. The chart failed to address any risks of investing in the fund, save the caption "Not FDIC Insured."

38. The MKC agent referred to in the preceding paragraph created a sales illustration in which he compared the returns for the Intermediate Bond Fund to the returns for traditional bank CDs. The agent used the illustration in order to market the Intermediate Bond Fund to bank customers. The agent stated that he created the illustration and that the illustration was not reviewed or approved by appropriate supervisory personnel of MKC. The chart fails to address any risks of investing in the Intermediate Bond Fund, save the caption "Not FDIC Insured."

F. SUPERVISION

39. Carter Anthony, President of MAM from 2001 until the end of 2006, has testified under oath that he conducted performance reviews of all MAM mutual fund managers that included reviews of their portfolios and trading. However, he testified that he did not conduct the same supervisory review and oversight of Kelsoe and the Funds because he was instructed to "leave Kelsoe alone." MAM denies that any such instruction was given.

40. In December 2001, Kelsoe signed a new account form as branch manager, when he, in fact, was never a branch manager nor held any supervisory/compliance licenses. Proper supervision of Kelsoe's activities would have detected such an unauthorized action on his part.

G. MAINTENANCE OF REQUIRED BOOKS AND RECORDS

41. MAM's Fund Management fundamental and qualitative research was touted in marketing and research material.

42. MAM, through its Portfolio Managers, selected securities for investments by the Funds' portfolios. MAM was consulted regarding the fair valuation of certain securities held by the portfolios. Adequate documentation was not retained as to pricing adjustments recommended by MAM to be made to certain of the securities.

43. WMS performed annual due diligence reviews of certain of the Funds and Fund management (MAM and Kelsoe). In mid-2007, MAM and Kelsoe did not provide sufficient information to allow completion of the 2007 annual due diligence review conducted by MKC through WMS. Kelsoe did not make himself available for a meeting during normal operating hours, further delaying the completion of WMS's on-site due diligence review. As a consequence, the report for two of the open-end funds was not completed. By August 2007, WMS dropped coverage of proprietary products and a report for 2007 was never released to the MKC sales force.

H. RESPONSIBILITIES AND CONDUCT OF JAMES KELSOE

44. In addition to his duties regarding management of the Funds and selection of investments, Kelsoe was responsible for reviewing information regarding holdings of the Funds to be included in marketing materials and filings with the SEC. Kelsoe also was responsible for supervising his staff's involvement with these processes, as well as their interaction with third parties. Kelsoe had the most knowledge at MAM about the nature of the holdings of the Funds, including the types of securities being purchased or sold for the Funds, the risks associated with the holdings, and the correlation of the holdings among the Funds. Kelsoe and his staff provided information for the preparation of regulatory filings, marketing materials,

reports and communications about the Funds. Kelsoe contributed to and delivered commentaries for the Funds and management discussions of fund performance. The SEC filings for the Funds, for which Kelsoe and his staff furnished information regarding holdings of each of the Funds, were provided to Kelsoe for his review prior to filing.

45. Kelsoe contributed to and was aware of the usage of the glossies and certain other marketing materials for the Funds by MAM, as described above, including the descriptions of the Funds, the allocation pie charts, the use of benchmarks, and characterizations of risks and features of the Funds.

46. Kelsoe's involvement in the fair valuation process for securities held by the Funds during the period from January 1, 2007 to July 31, 2007, including influencing some dealer confirmations that were returned, contributed to certain inaccurate valuations of selected holdings on various dates during that period.

47. From January 1, 2007 through July 31, 2007, Kelsoe did not retain documentation relating to his recommendations of price changes of certain securities held by the Funds. These recommendations were used on occasion in the calculation of the daily net asset values of the Funds.

48. From January 1, 2007 through July 31, 2007, Kelsoe failed to review and approve certain emails and other communications of his staff that characterized the downturn of the market for certain securities contained within the Funds as a "buying opportunity," which were circulated to certain MKC FAs.

49. The Department is responsible for the enforcement of laws governing the issuance, sale, and other transactions relative to securities pursuant to Illinois Securities Law of

1953, [815 ILCS 5/1, et seq.] and the Regulations under Illinois Securities Law of 1953 [14 Ill.Adm.Code 130.100 et seq.].

50. In violation of Sections 8.E.1(b) and 8.E.1(e) of the Act, MKC and/or MAM conducted and participated in the following practices:

a. MAM failed to adequately disclose in quarterly, semi-annual and annual reports filed with the SEC prior to late 2007 some of the risks associated with investment in the Funds.

b. In SEC disclosure filings, MAM classified approximately Four Hundred Million Dollars ($400,000,000.00) of asset-backed securities as corporate bonds and preferred stocks, when they were the lower tranches of asset-backed structured debt instruments.

c. MKC and MAM used industry benchmarks not directly comparable to the Funds.

d. In certain marketing and disclosure materials, MKC and MAM did not correctly characterize the Funds and their holdings.

e. In certain instances, MKC and MAM failed to adequately disclose to retail customers the Funds' risks of volatility and illiquidity.

f. In certain instances, MKC, through some of its FAs, inappropriately compared the returns of the Intermediate Bond Fund to the returns of certificates of deposit and other low risk investments.

g. In certain marketing materials, MKC and MAM used charts and visual aids that demonstrated a level of diversification in the Funds that did not exist.

51. In violation of 8.E.1(e) of the Act, MKC and/or MAM failed to reasonably supervise their agents, employees and associated persons in the following manner:

a. In certain instances, MKC and MAM allowed the Funds' manager, Kelsoe, to operate outside of the firm organizational supervisory structure.

b. In certain instances, MAM and MKC failed to perform adequate supervisory reviews of Kelsoe.

c. MKC, through WMS, and MAM failed to perform sufficient due diligence reviews of the Funds.

d. MAM and MKC allowed Kelsoe to improperly influence the net asset value calculations of the Funds in certain instances during the period from January through July of 2007.

e. MKC failed to assure adequate training and supervision of certain agents in the composition and true nature of the funds.

f. MKC allowed agents to recommend (or in discretionary accounts, to purchase) an overconcentration of the Funds in some client accounts.

52. In violation of Section 130.850 of the Regulations, MKC and/or MAM failed to make suitable recommendations to some investors as demonstrated by the following:

a. MKC allowed agents to recommend (or in discretionary accounts, to purchase) an overconcentration of the Funds in some client accounts.

b. MAM and MKC recommended and sold the Intermediate Bond Fund and the Short Term Bond Fund to clients as a low risk, stable principal, liquid investment opportunity.

c. In a number of instances, MKC sold or recommended investments to retail investors without determining the risk tolerances of the investors.

53. In violation of Section 8.E.1(e) of the Act, MKC failed to enforce their supervisory procedures in the following manner:

a. MKC failed to review certain customer accounts for over concentration and proper diversification.

b. MKC failed to adequately determine suitability of the Funds as it related to the investment needs of certain of their clients.

54. In violation of 8.E.1(e) of the Act, MKC and/or MAM in many instances failed to review correspondence and marketing materials used by associated persons to sell the Funds:

a. MKC failed to discover that an agent used a comparison of the return of the Intermediate Bond Fund to the returns of a bank certificate of deposit.

b. MAM and MKC allowed marketing materials containing inaccurate representations relating to the composition of the Funds to be used by their agents.

c. MAM and MKC allowed marketing materials that represented that no derivative products were contained in the Select Intermediate Fund to be used by agents, when in fact some derivative products were contained in the Fund.

55. In violation of Section 130.853 of the Regulations, in certain cases, MAM and MKC inappropriately recommended the purchase of the Funds for client portfolios without reasonable justification that said recommendation was suitable for the client.

56. In violation of Section 8.E.1(f) and 8.E.1(g) of the Act, MKC permitted distribution of marketing materials and MAM permitted distribution of disclosure materials that were inaccurate:

a. MAM failed to adequately disclose in quarterly, semi-annual and annual reports filed with the SEC prior to late 2007 some of the risks associated with investment in the Funds.

b. In SEC disclosure filings, MAM classified approximately Four Hundred Million Dollars ($400,000,000.00) of asset-backed securities as corporate bonds and preferred stocks, when they were the lower tranches of asset-backed structured debt instruments.

c. MKC and MAM used industry benchmarks not directly comparable to the Funds.

d. In certain marketing and disclosure materials, MKC and MAM did not correctly characterize the Funds and their holdings.

e. In certain instances, MKC, through some of its FAs, inappropriately compared the returns of the Intermediate Bond Fund to the returns of certificates of deposit and other noncomparable lower risk investments.

You are further notified that you are required pursuant to Section 130.1104 of the Rules and Regulations (14 Ill. Adm. Code 130) (the "Rules"), to file an answer to the allegations outlined above or a Special Appearance pursuant to Section 130.1107 of the Rules, or other responsive pleading within thirty days of the receipt of this notice. Your failure to do so within the prescribed time shall be deemed an admission of the allegations contained in the Notice of Hearing and waives your right to a hearing.

Furthermore, you may be represented by legal counsel; may present evidence; may cross-examine witnesses and otherwise participate. A failure to so appear shall constitute default.

Delivery of notice to the designated representative of any Respondent constitutes service upon such Respondents.

Dated this 4th day of June, 2012.

Jesse White
Secretary of State
State of Illinois

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